# Disclosure Statement.

For the nine months ended 31 March 2013.

Kiwibank.

Number 47

# 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 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 nine months ended 31 March 2013, in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2013 (the "Order"). Words and phrases defined by the Order have the same meanings when used in this Disclosure Statement.

## Address for service

The address for service is: Kiwibank Limited, New Zealand Post House, Level 12, 7 Waterloo Quay, Wellington 6011, New Zealand.

## Ultimate holding company

The ultimate holding company of Kiwibank is New Zealand Post Limited ("NZP") whose address for service is: New Zealand Post House, Level 12, 7 Waterloo Quay, Wellington 6011, New Zealand.

## Voting securities and power to appoint directors

There are 360 million voting securities of Kiwibank. Kiwi Group Holdings Limited ("KGHL") is the registered and beneficial holder of all those voting securities. KGHL, NZP and the Crown (being those ministers who hold shares in NZP on behalf of the Crown) are the only holders of a direct or indirect qualifying interest in the voting securities of Kiwibank. KGHL does not guarantee any of the obligations of Kiwibank or any member of the Banking Group. For details of the guarantees provided by NZP and the Crown, see "Guarantees" on page 2.

KGHL has the ability to directly appoint 100% of the board of directors of Kiwibank. NZP, as the immediate parent of KGHL and the ultimate holding company of Kiwibank, has the ability to indirectly appoint 100% of the board of directors of Kiwibank. No appointment of any director, chief executive officer, or executive, who reports or is accountable directly to the chief executive officer, shall be made in respect of Kiwibank unless:

1. the RBNZ has been supplied with a copy of the curriculum vitae of the proposed appointee; and
2. the RBNZ has advised that it has no objection to that appointment.

## Other material matters

Kiwibank's directors are of the opinion that there are no matters relating to the business or affairs of Kiwibank, 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.

## Pending proceedings or arbitration

Kiwibank's directors are of the opinion that there are no pending legal proceedings or arbitration concerning Kiwibank, whether in New Zealand or elsewhere, that may have a material adverse effect on Kiwibank or the Banking Group.

# Credit ratings

On 21 May 2013, Standard & Poor's (Australia) Pty Limited ("S&P") affirmed Kiwibank's credit rating of A+. On the same date, they also revised the outlook to negative from stable. On 30 October 2012, S&P granted Kiwibank a credit rating of A+ with a stable outlook for long-term senior unsecured obligations payable in New Zealand, in New Zealand dollars. This credit rating is a one notch downgrade from Kiwibank's previous rating of AA- granted on 29 November 2001 and reaffirmed on 31 January 2012, at which time the outlook was revised to negative from stable.

On 12 November 2010, Moody's Investors Service granted Kiwibank a credit rating of Aa3 for long-term senior unsecured obligations payable in New Zealand in New Zealand dollars.

On 13 June 2012, Fitch Ratings granted Kiwibank a credit rating of AA+ for senior unsecured debt obligations payable in New Zealand dollars and a credit rating of AA for unsecured debt obligations payable in other currencies.

# Guarantees

As at the date the directors signed this Disclosure Statement, the payment obligations of Kiwibank have the benefit of certain guarantees: a deed poll guarantee by Kiwibank's ultimate holding company NZP (the "NZP Guarantee") and (in relation to the fixed rate bonds issued by Kiwibank on 20 October 2009) a Crown deed of guarantee entered into by the New Zealand Government under the New Zealand wholesale funding guarantee scheme (the "Crown Wholesale Guarantee"). Details of each guarantee are set out below.

## NZP Guarantee

NZP supports Kiwibank as a registered bank. By way of example, NZP has contracted with Kiwibank to offer banking services through NZP's existing retail network for an unlimited period.

All 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 are guaranteed pursuant to the NZP Guarantee. The following is a summary of the features of the NZP Guarantee as at 31 March 2013:

i. The address for service of NZP is New Zealand Post House, Level 12, 7 Waterloo Quay, Wellington, New Zealand.

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

iii. The NZP Guarantee is an unsecured guarantee of 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 month's 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.

iv. There are no limits on the amount of the payment obligations guaranteed.

v. There are no material conditions applying to the NZP Guarantee.

vi. There are no material legislative or regulatory restrictions, which would have the effect of subordinating the claims under the NZP Guarantee of any of the creditors of Kiwibank on the assets of NZP, to other claims on NZP, in a winding up of NZP.

The net tangible assets of NZP were $943m as recorded in NZP's most recent Annual Report for the financial year ended 30 June 2012. There were no qualifications in the audit report accompanying the Annual Report.

NZP has a credit rating applicable to its long term unsecured obligations payable in New Zealand, in New Zealand dollars, from Standard & Poor's (Australia) Pty Limited of A+, granted on 30 October 2012. On 21 May 2013 the outlook was revised to negative from stable. This credit rating is a one notch downgrade from NZP's previous rating of AA- granted on 29 November 2001. The AA-rating was reaffirmed on 29 June 2012 with the outlook negative.

For an explanation of Standard & Poor's (Australia) Pty Limited's credit rating scale see page 3.

## Crown Wholesale Guarantee

On 1 November 2008 the New Zealand Government announced details of a wholesale funding guarantee facility (the "Facility") to investment-grade financial institutions that have substantial New Zealand borrowing and lending operations, giving institutions the ability to opt-in to the guarantee either by institution or by instrument. The credit ratings applicable to the Crown are set out below.

On 24 March 2009, Kiwibank was accepted into the scheme by the New Zealand Government.

On 30 April 2010 the Crown wholesale funding guarantee scheme was withdrawn by the New Zealand Government. However, the Crown Wholesale Guarantee still applies in relation to fixed rate bonds issued by Kiwibank on 20 October 2009.

A guarantee fee was charged for each guarantee issued under the Facility, differentiated by the credit rating of the issuer and the term of the security being guaranteed. The maximum term of securities guaranteed is five years.

The following is a summary of the features of the Crown Wholesale Guarantee:

a) The guarantor under the Crown Wholesale Guarantee is Her Majesty the Queen in right of New Zealand acting by and through the Minister of Finance (the "Crown").

# Guarantees continued

b) Any demand under the guarantee must be delivered by hand to the Minister of Finance, Parliament Buildings, Wellington, New Zealand with a copy to The Treasurer, The New Zealand Debt Management Office, 1 The Terrace, Wellington 6011, New Zealand.

c) The Crown guarantees the payment by Kiwibank of any liability of Kiwibank to pay principal and interest in respect of the debt securities for which the Crown has issued a Guarantee Eligibility Certificate (being the fixed rate bonds issued by Kiwibank on 20 October 2009); and

d) Undertakes that if Kiwibank does not pay any such liability on the date on which it becomes due, the Crown shall within 5 business days of a demand being made in accordance with the Crown Wholesale Guarantee and following the expiry of any applicable grace period, pay such liability.

e) The Crown Wholesale Guarantee does not extend to debt securities held by related parties. Related parties of Kiwibank include KGHL's subsidiaries and its ultimate parent, NZP.

f) Additional information on the Crown Wholesale Guarantee scheme and the Crown's most recent audited financial statements are available, free of charge and at all reasonable times, on the New Zealand Treasury's website: www.treasury.govt.nz/economy/guarantee/wholesale.

g) There are no material conditions applicable to the guarantee.

h) The minimum Tier 1 capital ratio under the Crown Wholesale Guarantee is 6% of risk weighted exposures.

i) The Crown has the following credit ratings applicable to its long term obligations payable in New Zealand dollars:

- Standard & Poor's (Australia) Pty Limited: AA+
- Fitch Ratings Limited AA+
- Moody's Investors Services Aaa

The following table describes the steps in the applicable rating scales for each rating agency:

| | Standard & Poor's | Moody's Investors Services | Fitch Ratings |
|---|---|---|---|
| Highest credit quality – ability to repay debt obligations is extremely strong | AAA | Aaa | AAA |
| High quality, low credit risk – ability to repay debt obligations is very strong | AA | Aa | AA |
| High quality – ability to repay is strong although may be susceptible to adverse changes in circumstances or in economic conditions | A | A | A |
| Low credit risk – satisfactory ability to repay debt obligations though changes in circumstances or in economic conditions are likely to impair this capacity | BBB | Baa | BBB |
| Ability to repay debt obligations is only adequate and likely to be affected by adverse economic change which might affect timeliness of repayment | BB | Ba | BB |
| Risk of default due to greater vulnerability | B | B | B |
| Significant risk of default. Repayment of debt obligations requires favourable financial conditions | CCC | Caa | CCC |
| Poor protection, highest risk of default | CC to C | Ca to C | CC to C |
| Obligations currently in default | D | – | RD to D |

Credit ratings between AA – CCC by Standard & Poor's and Fitch Ratings may be modified by the addition of a plus or minus sign (signalling higher and lower end of the scale respectively).

Moody's Investor Services applies numeric modifiers 1,2 and 3 to each generic rating classification with a 1 indicating a higher rating and a 3 indicating a lower rating within that generic rating category.

# Conditions of registration

These conditions apply on and after 31 March 2013, except as provided otherwise.

The registration of Kiwibank 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 percent;
   b) the tier 1 capital ratio of the Banking Group is not less than 6 percent;
   c) the Common Equity Tier 1 capital ratio of the Banking Group is not less than 4.5 percent;
   d) the Total capital of the Banking Group is not less than NZ$30 million; and
   e) the process in Subpart 2H of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated March 2013 is followed for the recognition and repayment of capital.

   For the purposes of this condition of registration, capital, the Total capital ratio, the Tier 1 capital ratio, and the Common Equity Tier 1 capital ratio must be calculated in accordance with the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated March 2013.

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 (Standardised Approach)" (BS2A) dated March 2013; and
   c) the Bank determines an internal capital allocation for each identified and measured "other material risk".

1B. 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 purpose 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 (Standardised Approach)" (BS2A) dated March 2013.

   This condition of registration applies on and after 1 January 2014.

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.

# Conditions of registration continued

4. That 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 |

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 exposure policy" (BS8) dated March 2013.

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 March 2011.

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 March 2011.

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

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.)

# Conditions of registration continued

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 decisions 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 March 2011 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.

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.

In these conditions of registration, -

"Banking Group" means Kiwibank Limited's financial reporting group (as defined in section 2(1) of the Financial Reporting Act 1993);

"generally accepted accounting practice" has the same meaning as in section 2 of the Financial Reporting Act 1993.

# Amendments to conditions of registration

With effect from 1 January 2013, the Bank's conditions of registration were amended to implement the Reserve Bank's Basel III policy. The changes include a requirement to maintain a Common Equity Tier 1 capital ratio of not less than 4.5% from 1 January 2013, and the requirement to ensure a buffer ratio of 2.5% with effect from 1 January 2014.

With effect on and from 31 March 2013 the Bank's conditions of registration were amended to put into effect the Reserve Bank's Basel III enhanced risk coverage policy.

# Directorate

There have been no changes to the composition of the Bank's Board of Directors since 30 June 2012.

As at the date of signing of the Disclosure Statement, the directors of Kiwibank were:

| | |
|---|---|
| Robert William Bentley Morrison | Hon. Sir. Michael John Cullen |
| Alison Rosemary Gerry | Murray Ian David Gribben |
| Grant Andrew Paterson | Brian Joseph Roche |
| Catherine Maria Savage | David Stephen Willis |

Mark David Yeoman (as alternate director for Brian Joseph Roche)

# Directors' statement

Each director of Kiwibank after due enquiry by them, believes that:

1. As at the date on which this Disclosure Statement is signed:
   i. this Disclosure Statement contains all the information that is required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2013; and
   ii. this Disclosure Statement is not false or misleading.
2. During the nine months ended 31 March 2013:
   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 other directors listed in the Directorate section of this Disclosure Statement.

22 May 2013

# Interim Financial Statements

# Interim financial statements

## Consolidated statement of profit or loss and other comprehensive income

**For the nine months ended 31 March 2013**

| | | The Banking Group | | |
|---|---|---|---|---|
| Dollars in millions | Note | **Unaudited 9 months ended 31/03/13** | Unaudited 9 months ended 31/03/12 | Audited 12 months ended 30/06/12 |
| Interest income | | **595** | 574 | 773 |
| Interest expense | | **(388)** | (386) | (516) |
| **Net interest income** | | **207** | 188 | 257 |
| Gains on financial instruments at fair value | | **-** | 3 | 5 |
| Other income | | **126** | 119 | 157 |
| **Total operating income** | | **333** | 310 | 419 |
| Operating expenses | | **(216)** | (198) | (273) |
| Impairment losses on loans and advances | 6 | **(2)** | (27) | (35) |
| **Profit before taxation** | | **115** | 85 | 111 |
| Income tax expense | | **(32)** | (24) | (32) |
| **Profit after taxation** | | **83** | 61 | 79 |
| **Attributable to:** | | | | |
| Owners of the parent | | **83** | 61 | 79 |
| Non controlling interest | | **-** | - | - |
| **Other comprehensive income** | | | | |
| **Net (loss)/gain from changes in reserves that may be subsequently reclassified to profit or loss** | | | | |
| Available-for-sale reserve (net of tax) | | **(1)** | **2** | 5 |
| Cash flow hedge reserve (net of tax) | | **16** | **16** | 15 |
| **Other comprehensive income for the period** | | **15** | **18** | 20 |
| **Total comprehensive income for the period** | | **98** | **79** | 99 |
| **Attributable to:** | | | | |
| Owners of the parent | | **98** | **79** | 99 |
| Non controlling interest | | **-** | **-** | - |

The notes on pages 13 to 18 form part of these interim financial statements.

# Interim financial statements continued

## Consolidated statement of changes in equity

**For the nine months ended 31 March 2013**

| The Banking Group<br>Dollars in millions | Fully Paid Ordinary Shares | Retained Earnings | Available-For-Sale Reserve | Cash Flow Hedge Reserve | Non Controlling Interest | Total |
|---|---|---|---|---|---|---|
| Balance at 1 July 2011 | 310 | 187 | 3 | (42) | 150 | 608 |
| **Unaudited 9 months ended 31 March 2012** | | | | | | |
| Unaudited profit for the period | - | 61 | - | - | - | 61 |
| **Other comprehensive income** | | | | | | |
| Available-for-sale financial assets (net of tax) | - | - | 2 | - | - | 2 |
| Cash flow hedges (net of tax) | - | - | - | 16 | - | 16 |
| **Total other comprehensive income** | **-** | **-** | **2** | **16** | **-** | **18** |
| **Total comprehensive income** | **-** | **61** | **2** | **16** | **-** | **79** |
| **Transactions with owners** | | | | | | |
| Issue of share capital | 50 | - | - | - | - | 50 |
| Transaction with non controlling interest | - | - | - | - | (1) | (1) |
| Dividends paid to non controlling interest | - | (7) | - | - | - | (7) |
| **Unaudited balance at 31 March 2012** | **360** | **241** | **5** | **(26)** | **149** | **729** |
| **Audited year ended 30 June 2012** | | | | | | |
| Audited profit for the year | - | 79 | - | - | - | 79 |
| **Other comprehensive income** | | | | | | |
| Available-for-sale financial assets (net of tax) | - | - | 5 | - | - | 5 |
| Cash flow hedges (net of tax) | - | - | - | 15 | - | 15 |
| **Total other comprehensive income** | **-** | **-** | **5** | **15** | **-** | **20** |
| **Total comprehensive income** | **-** | **79** | **5** | **15** | **-** | **99** |
| **Transactions with owners** | | | | | | |
| Issue of share capital | 50 | - | - | - | - | 50 |
| Transaction with non controlling interest | - | - | - | - | (1) | (1) |
| Dividends paid to non controlling interest | - | (9) | - | - | - | (9) |
| Audited balance at 30 June 2012 | 360 | 257 | 8 | (27) | 149 | 747 |
| **Unaudited 9 months ended 31 March 2013** | | | | | | |
| Unaudited profit for the period | - | 83 | - | - | - | 83 |
| **Other comprehensive income** | | | | | | |
| Available-for-sale financial assets (net of tax) | - | - | (1) | - | - | (1) |
| Cash flow hedges (net of tax) | - | - | - | 16 | - | 16 |
| **Total other comprehensive income** | **-** | **-** | **(1)** | **16** | **-** | **15** |
| Total comprehensive income | - | 83 | (1) | 16 | - | 98 |
| **Transactions with owners** | | | | | | |
| Transaction with non controlling interest | - | - | - | - | 1 | 1 |
| Dividends paid to non controlling interest | - | (7) | - | - | - | (7) |
| Unaudited balance at 31 March 2013 | 360 | 333 | 7 | (11) | 150 | 839 |

The notes on pages 13 to 18 form part of these interim financial statements.

# Interim financial statements continued

## Consolidated statement of financial position

**As at 31 March 2013**

| | | The Banking Group | | |
|---|---|---|---|---|
| Dollars in millions | Note | **Unaudited 31/03/13** | Unaudited 31/03/12 | Audited 30/06/12 |
| **Assets** | | | | |
| Cash and cash equivalents | | **326** | 238 | 315 |
| Due from NZP related parties | 7 | **62** | 45 | 58 |
| Due from other financial institutions | 3 | **390** | 254 | 171 |
| Financial assets held for trading | | **231** | 285 | 104 |
| Available-for-sale assets | | **1,149** | 1,310 | 1,401 |
| Loans and advances | 2 | **13,013** | 12,309 | 12,445 |
| Derivative financial instruments | | **88** | 100 | 138 |
| Property, plant and equipment | | **16** | 21 | 19 |
| Intangible assets | | **60** | 48 | 49 |
| Deferred taxation | | **22** | 31 | 31 |
| Other assets | | **14** | 11 | 14 |
| **Total assets** | | **15,371** | 14,652 | 14,745 |
| **Liabilities** | | | | |
| Due to other financial institutions | | **219** | 269 | 334 |
| Due to NZP related parties | 7 | **3** | 1 | 4 |
| Deposits and other borrowings | 4 | **12,237** | 11,488 | 11,565 |
| Derivative financial instruments | | **132** | 140 | 156 |
| Debt securities issued | | **1,660** | 1,909 | 1,806 |
| Current taxation payable | | **10** | 6 | 16 |
| Other liabilities | | **57** | 47 | 53 |
| Term subordinated debt | 5 | **214** | 63 | 64 |
| **Total liabilities** | | **14,532** | 13,923 | 13,998 |
| **Equity attributable to owners of the parent** | | | | |
| Share capital | | **360** | 360 | 360 |
| Reserves | | **329** | 220 | 238 |
| **Total equity attributable to owners of the parent** | | **689** | 580 | 598 |
| **Non controlling interest** | | **150** | 149 | 149 |
| **Total equity** | | **839** | 729 | 747 |
| **Total liabilities and shareholder's equity** | | **15,371** | 14,652 | 14,745 |

The notes on pages 13 to 18 form part of these interim financial statements.

# Interim financial statements continued

## Consolidated statement of cash flows

**For the nine months ended 31 March 2013**

| | The Banking Group | | |
|---|---|---|---|
| Dollars in millions | **Unaudited 9 months ended 31/03/13** | Unaudited 9 months ended 31/03/12 | Audited 12 months ended 30/06/12 |
| **Cash flows from operating activities** | | | |
| Interest income | **602** | 580 | 762 |
| Fees and other income | **126** | 118 | 157 |
| Operating expenses paid | **(197)** | (174) | (233) |
| Interest paid | **(363)** | (391) | (525) |
| Taxes paid | **(34)** | (27) | (28) |
| **Net cash flows from operating activities before changes in operating assets and liabilities** | **134** | 106 | 133 |
| **Net changes in operating assets and liabilities:** | | | |
| (Increase)/decrease in financial assets held for trading | **(126)** | 42 | 223 |
| Decrease/(increase) in available-for-sale assets | **257** | (183) | (270) |
| Increase in loans and advances | **(537)** | (893) | (1,043) |
| Increase in amounts due from related parties | **(4)** | (45) | (57) |
| (Increase)/decrease in balances due from other financial institutions | **(218)** | 186 | 269 |
| Increase in deposits and other borrowings | **648** | 902 | 984 |
| Decrease in balances due to other financial institutions | **(115)** | (526) | (462) |
| **Net cash flows from operating activities** | **39** | (411) | (223) |
| **Cash flows from investing activities** | | | |
| Purchase of property, plant and equipment | **(3)** | (2) | (3) |
| Purchase of intangible software assets | **(23)** | (13) | (18) |
| **Net cash flows from investing activities** | **(26)** | (15) | (21) |
| **Cash flows from financing activities** | | | |
| Issue of ordinary shares | **-** | 50 | 50 |
| Issue of shares to non controlling interest | **-** | 1 | 1 |
| (Decrease)/increase in debt securities issued | **(145)** | 324 | 296 |
| Issue/(redemption) of subordinated debt | **150** | - | (75) |
| Dividend paid to non controlling interest | **(7)** | (7) | (9) |
| **Net cash flows from financing activities** | **(2)** | 368 | 263 |
| **Increase /(decrease) in cash and cash equivalents** | **11** | (58) | 19 |
| Cash and cash equivalents at beginning of the period | **315** | 296 | 296 |
| **Cash and cash equivalents at end of the period** | **326** | 238 | 315 |

The notes on pages 13 to 18 form part of these interim financial statements.

# Notes to the interim financial statements

## 1. Statement of accounting policies

### Reporting entity and statutory base

In these interim financial statements, the reporting entity is Kiwibank Limited ("Kiwibank"). The Banking Group consists of Kiwibank and its subsidiaries. Kiwibank is registered 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.

These interim financial statements are for the Banking Group for the nine months ended 31 March 2013. They have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand as appropriate for profit oriented entities, the requirements of NZ IAS 34 *Interim Financial Reporting* and the Order, and should be read in conjunction with the Banking Group's financial statements for the year ended 30 June 2012. These financial statements comply with International Accounting Standard 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board.

### Accounting Policies

The accounting policies and methods of computation adopted by the Banking Group are consistent with those adopted and disclosed in the previous full year Disclosure Statement.

The following amendment to a standard relevant to the Banking Group has been adopted from 1 July 2012 and applied in the preparation of these interim financial statements.

NZ IAS 1 – *Presentation of financial statements:* The revised standard was adopted on 1 July 2012. Separate presentation is now required of items presented in other comprehensive income into two groups, based on whether they may be recycled to profit or loss in the future and those items which will not be recycled. Adoption of this revised accounting standard has not resulted in any material change to the Banking Group's reported result or financial position.

### 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.

### Currency of presentation

All amounts are expressed in millions of New Zealand dollars, unless otherwise stated.

| | The Banking Group | | |
|---|---|---|---|
| Dollars in millions | **Unaudited as at 31/03/13** | Unaudited as at 31/03/12 | Audited as at 30/06/12 |
| **2. Loans and advances** | | | |
| Loans and advances designated upon initial recognition at fair value through profit or loss | **-** | 179 | 44 |
| Loans and advances at amortised cost | **13,088** | 12,222 | 12,492 |
| Allowance for impairment losses (note 6) | **(75)** | (92) | (91) |
| **Total net loan and advances** | **13,013** | 12,309 | 12,445 |
| **Current** | **1,080** | 1,083 | 1,036 |
| **Non-current** | **11,933** | 11,226 | 11,409 |
| **3. Due from other financial institutions** | | | |
| Unsettled receivables | **206** | 68 | - |
| Short term advances due from other financial institutions | **155** | 154 | 145 |
| Collateralised loans | **29** | 32 | 26 |
| **Total – current** | **390** | 254 | 171 |

As at 31 March 2013, included within the balance above, is $29m of collateral pledged by Kiwibank in respect of its credit support annex obligations to derivative counterparties (31 March 2012: $32m; 30 June 2012: $26m).

# Notes to the interim financial statements continued

| Dollars in millions | The Banking Group<br>Unaudited as at 31/03/13 | Unaudited as at 31/03/12 | Audited as at 30/06/12 |
|---|---|---|---|
| **4. Deposits and other borrowings** | | | |
| Demand deposits non-interest bearing | **899** | 713 | 745 |
| Demand deposits bearing interest | **2,249** | 2,083 | 2,078 |
| Term deposits | **9,089** | 8,692 | 8,742 |
| **Total deposits from customers** | **12,237** | 11,488 | 11,565 |
| **Current** | **11,911** | 11,165 | 11,189 |
| **Non current** | **326** | 323 | 376 |

In the event of the liquidation of Kiwibank, deposit holders will rank equally with all other unsecured 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 a deed poll guarantee (the “Guarantee”) provided by Kiwibank’s ultimate parent company, NZP.

The Kiwibank PIE Unit Trust, established under the Unit Trusts Act 1960 in May 2008, operates three funds; the PIE Term Deposit Fund, the PIE Notice Saver and the PIE Online Call Fund. Kiwibank Investment Management Limited is the issuer and manager of the Unit Trust.

Trustees Executors Limited is the trustee of the Unit Trust. Kiwibank is the promoter of the Trust. Units in the Trust do not directly represent deposits or liabilities of Kiwibank, however the Unit Trust is invested exclusively in term and call deposits with Kiwibank. At 31 March 2013, $3,396m of PIE funds were invested in Kiwibank’s own products or securities (31 March 2012: $3,020m; 30 June 2012: $2,980m).

Kiwibank guarantees the payment obligations of the manager and any amounts owing to Unit Holders under the Trust Deed in respect of their Units and agrees to pay to Unit Holders 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.

| Dollars in millions | The Banking Group<br>Unaudited as at 31/03/13 | Unaudited as at 31/03/12 | Audited as at 30/06/12 |
|---|---|---|---|
| **5. Term subordinated debt** | | | |
| Face value | **210** | 60 | 60 |
| Interest accrued | **5** | - | 1 |
| Transaction costs | **(2)** | - | - |
| Fair value hedge adjustment | **1** | 3 | 3 |
| **Total term subordinated debt (non-current)** | **214** | 63 | 64 |

During the period $150m of term subordinated debt was issued by the Banking Group. The terms and conditions of the term subordinated debt issued are as follows:

| Issue date | Amount $ million | Coupon rate | Call date | Maturity date |
|---|---|---|---|---|
| 30 September 2008 | 60 | 8.75% | 30 September 2013 | 30 September 2018 |
| 15 December 2012 | 150 | 5.80% | 15 December 2017 | 15 December 2022 |

The term subordinated debt issue is subordinate to all other general liabilities of the Banking Group and is denominated in New Zealand dollars. The 30 September 2008 issue carried an A credit rating and the 15 December 2012 issue carried a BB+ credit rating from Standard & Poor’s Pty Limited as at reporting date.

All the term subordinated debt qualifies as Tier 2 capital for Capital Adequacy calculation purposes. The contractual terms of the term subordinated debt expressly provide that they do not have the benefit of a deed poll guarantee (“the NZP Guarantee”) provided by the Banking Group’s ultimate parent company, (NZP). The debt is also not covered by the Crown Guarantee scheme.

# Notes to the interim financial statements continued

## 6. Asset quality

| Dollars in millions | The Banking Group Unaudited as at 31/03/13 | Unaudited as at 31/03/12 | Audited as at 30/06/12 |
|---|---|---|---|
| **Allowance for impairment losses in statement of financial position** | | | |
| Collective allowance for impairment losses | **42** | 48 | 50 |
| Allowance for individually impaired assets | **33** | 44 | 41 |
| **Total allowance for impairment losses** | **75** | 92 | 91 |

| Dollars in millions | Unaudited for period ended 31/03/13 | Unaudited for period ended 31/03/12 | Audited for year ended 30/06/12 |
|---|---|---|---|
| **Impairment (credit)/losses per statement of comprehensive income** | | | |
| Collective impairment (credit)/losses on loans not at fair value through profit or loss | **(6)** | 14 | 16 |
| Charge to statement of comprehensive income for individually impaired assets | **8** | 13 | 19 |
| **Total impairment losses per statement of comprehensive income** | **2** | 27 | 35 |

| Dollars in millions | Residential unsecured lending | Residential mortgage loans | Corporate exposures | Total |
|---|---|---|---|---|
| **Unaudited as at 31 March 2013** | | | | |
| **Collective allowance for impairment loss** | (4) | (18) | (20) | **(42)** |
| **Past due assets > 90 days but not impaired** | 2 | 17 | 1 | **20** |
| **Impaired assets** | | | | |
| Gross impaired assets | 1 | 23 | 37 | **61** |
| Individual allowance for impaired assets | (1) | (9) | (23) | **(33)** |
| **Total net impaired assets** | - | 14 | 14 | **28** |
| **Unaudited 9 months ended 31 March 2013** | | | | |
| **Impairment losses per statement of comprehensive income** | | | | |
| Collective allowance credit | - | (2) | (4) | **(6)** |
| Individual allowance charge | 1 | 4 | 3 | **8** |
| **Total impairment losses/(credit)** | 1 | 2 | (1) | **2** |

The cumulative change in fair value arising from changes in credit risk for loans and advances designated at fair value through profit or loss is nil (31 March 2012: $0.1m; 30 June 2012: $0.03m)

# Notes to the interim financial statements continued

## 7. Related parties

The table below shows balances with individual companies within the NZP group and other related parties as at reporting date.

| | The Banking Group | | |
|---|---|---|---|
| Dollars in millions | **Unaudited 31/03/13** | Unaudited 31/03/12 | Audited 30/06/12 |
| **9 months ended 31 March 2013** | | | |
| NZP | **32** | 29 | 39 |
| Other subsidiaries within the NZP Group | **1** | 1 | 1 |
| **Expenditure** | | | |
| NZP | **51** | 44 | 60 |
| Other subsidiaries within the NZP Group | **10** | 10 | 14 |
| Associates of the NZP Group | **6** | 5 | 6 |
| **As at 31 March 2013** | | | |
| **Outstanding balances** | | | |
| Due to NZP related parties | **3** | 1 | 4 |
| Presented as deposits | **22** | 36 | 23 |
| **Total balances due to related parties** | **25** | 37 | 27 |
| **Receivables** | | | |
| Due from NZP related parties | **62** | 45 | 58 |
| Presented as loans and advances | **4** | 4 | 2 |
| **Total related party receivables** | **66** | 49 | 60 |

NZP has a credit facility with the Banking Group, allowing NZP to drawdown 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 March 2013 the amount owed by NZP to Kiwibank was $62m (31 March 2012: $45m; 30 June 2012: $58m). This does not exceed the 15% of Tier 1 capital requirement.

The Crown has entered into a $300m uncalled capital facility with NZP where it 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.

## 8. Liquidity

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 both items classified as cash and cash equivalents and those classified as operating assets in the consolidated statement of cash flow.

| Dollars in millions | **Unaudited as at 31/03/13** |
|---|---|
| The Banking Group's liquidity portfolio is based on the amount required to meet its liquidity policy. | |
| Cash on hand and with central banks | **286** |
| Certificate of deposit | **126** |
| Government bonds and treasury bills | **580** |
| Local body stock and bonds | **69** |
| Other bonds | **789** |
| **Total** | **1,850** |

# Notes to the interim financial statements continued

## 9. Credit exposure concentrations

### Credit exposure to individual counterparties

Credit exposure concentration 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), equaled or exceeded 10% of the Banking Group's shareholder's equity as at reporting date.

## 10. Fiduciary activities

### 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 and Kiwibank KiwiSaver scheme, 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 market or distribute its own insurance products.

### Covered bond

On 23 January 2013, the Kiwi Covered Bond Trust (the "Trust") was established to hold Kiwibank housing loans and to provide guarantees to certain debt securities issued by the Bank. Guarantees provided by the Trust have a prior claim over the assets of the Trust. On 19 February 2013, selected Kiwibank housing loans were transferred to the Trust in order to establish and facilitate the Bank's covered bond programme. The Trust is consolidated within the Banking Group.

Substantially all of the assets of the Trust are made up of certain housing loans originated by the Bank and highly rated short-dated securities together which are security for the guarantee by Kiwi Covered Bond Trustee Limited as trustee of the Trust of issuances of covered bonds by the Bank. The assets of the 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 Trust (if any) after all prior ranking creditors of the Trust have been satisfied. The Banking Group continues to recognise the assets of the 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.

### RMBS

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 RBNZ. As at 31 March 2013, included within the Banking Group's loans and advances to customers were housing loans with a carrying value of $600m held by the RMBS Trust (31 March 2012 and 30 June 2012: $600m). These housing loans do not qualify for de-recognition from the Kiwibank Limited financial statements as the Bank retains substantially all of the risks and rewards of ownership. The RMBS Trust is consolidated within the Banking Group.

## 11. 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 2012.

# Notes to the interim financial statements continued

## 12. Segment analysis

| Dollars in millions | Personal market | Business market | Payment services | Total |
|---|---|---|---|---|
| **Unaudited 9 months ended 31 March 2013** | | | | |
| External revenues | **298** | **(12)** | **47** | **333** |
| Intersegment revenues | **(96)** | **96** | **-** | **-** |
| **Total revenues** | **202** | **84** | **47** | **333** |
| **Profit before taxation** | **68** | **37** | **10** | **115** |
| **Unaudited 9 months ended 31 March 2012** | | | | |
| External revenues | 298 | (35) | 47 | 310 |
| Intersegment revenues | (110) | 110 | - | - |
| **Total revenues** | 188 | 75 | 47 | 310 |
| **Profit before taxation** | 55 | 18 | 12 | 85 |
| **Audited 12 months ended 30 June 2012** | | | | |
| External revenues | 396 | (39) | 62 | 419 |
| Intersegment revenues | (143) | 143 | - | - |
| **Total revenues** | 253 | 104 | 62 | 419 |
| **Profit before taxation** | 70 | 26 | 15 | 111 |

There have been no changes to the segments as defined in the financial statements for the year ended 30 June 2012.

## 13. Interest earning and discount bearing assets and liabilities

| | The Banking Group | | |
|---|---|---|---|
| Dollars in millions | **Unaudited as at 31/03/13** | Unaudited as at 31/03/12 | Audited as at 30/06/12 |
| Interest earning and discount bearing assets | **15,171** | 14,465 | 14,522 |
| Interest and discount bearing liabilities | **13,226** | 12,998 | 13,006 |

## 14. Capital expenditure commitments

Capital expenditure commitments contracted for as at 31 March 2013, but not provided for in these interim financial statements, total $0.7m, (31 March 2012: $3.0m; 30 June 2012: $0.7m). All such commitments are due no later than one year from reporting date.

## 15. Contingent liabilities

There are no material contingent liabilities as at 31 March 2013 (31 March 2012: nil; 30 June 2012: nil).

## 16. Events subsequent to reporting period date

On 23 April 2013, Kiwibank Ltd issued covered bonds to the value of CHF 150 million with a maturity of 23 December 2020. The covered bond issuance is guaranteed by Kiwi Covered Bond Trustee Limited. Guarantees provided by the Trust have a prior claim over the assets of the Trust. The Trust is consolidated within the Banking Group.

On 21 May 2013, Standard & Poor's (Australia) Pty Limited affirmed Kiwibank's credit rating of A+. On the same date, they also revised the outlook to negative from stable.

# Capital adequacy

Kiwibank is subject to the capital adequacy requirements for registered banks as specified by the Reserve Bank of New Zealand (RBNZ). Following an internationally agreed framework (commonly known as Basel III) developed by the Basel committee on Banking supervision, the RBNZ has set minimum acceptable regulatory capital requirements and provided methods for estimating or measuring the risks incurred by the Bank. As a bank adopting a standardised approach under the Basel III regime, Kiwibank applies the RBNZ's BS12 – Guidelines on Internal Capital Adequacy Assessment Process (ICAAP) as a basis for estimating adequate prudential capital and BS2A – Capital Adequacy Framework, Standardised Approach for calculating regulatory capital requirements. In accordance with changes to Kiwibank's banking conditions of registration, from 1 January 2013, Kiwibank applies the RBNZ's Basel III framework which requires a strengthened and more conservative approach to capital adequacy.

Regulatory capital adequacy ratios are calculated by expressing capital as a percentage of risk weighted exposures. As a condition of registration, the Bank must comply with the following minimum capital requirements set by the RBNZ:

- Total capital ratio must not be less than 8% of risk weighted exposures.
- Tier 1 capital ratio must not be less than 6% of risk weighted exposures.
- The Common Equity Tier 1 capital ratio is not less than 4.5%.
- Capital of the Banking Group must not be less than NZ$30m.

## Regulatory capital

The Basel III standards for bank capital distinguish between Tier 1 and Tier 2 capital. Tier 1 capital is permanently and freely available to absorb losses without the bank being obliged to cease trading, while Tier 2 capital generally only absorbs losses in a winding up. Within Tier 1 capital, Common Equity (CET 1) has greater loss absorbing capability than the other Tier 1 instruments referred to as Additional Tier 1 (AT 1) capital.

Capital ratios are used to define minimum capital requirements for each of: Common Equity, Tier 1 capital (CET 1 plus AT 1), and total capital (Tier 1 plus Tier 2), as a percentage of risk-weighted assets. From 1 January 2014, in addition to the minimum capital requirements, Basel III introduces a capital conservation buffer of 2.5 percent of risk-weighted assets. There are increasing constraints on capital distributions where a bank's capital level falls within the buffer range. The following table shows the new capital ratio requirements and conservation buffers (as a percentage of risk weighted assets).

| | Common equity | Tier 1 capital | Total capital |
|---|---|---|---|
| RBNZ minimum ratios prior to 1 January 2013 | | 4.0% | 8.0% |
| Minimum ratios from 1 January 2013 | 4.5% | 6.0% | 8.0% |
| Conservation buffer from 1 January 2014 | 2.5% | | |
| Minimum ratio plus conservation buffer from 1 January 2014 | 7.0% | 8.5% | 10.5% |

The ordinary shares, which are fully paid, are included within Common Equity Tier 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.

The perpetual preference shares, which are fully paid, are included within Additional Tier 1 capital. Their material terms and conditions are:

a) each share has no voting rights;

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

c) dividends are paid quarterly in arrears at the discretion of the directors;

d) there is a predetermined dividend rate of 8.15%;

e) there is no maturity date;

f) no provision has been made for a variation or suspension of dividend payments;

g) there are no options to be granted pursuant to any agreement; and

h) there are no dividends in arrears.

The term subordinated debt meets the definition of Tier 2 capital. This issue is subordinate to all other general liabilities of the Banking Group and is denominated in New Zealand dollars. Refer to note 5 for the material terms and conditions relating to this.

# 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 statement of financial position 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 can be summarised as follows:

Material risks with capital allocations (commonly referred to as "Pillar I" risk classes under Basel III):

- 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).

The Basel III capital adequacy regime intends to ensure that banks have adequate capital to support all material risk inherent in their business activities. Consequently, banks are required to maintain an ICAAP for assessing overall capital adequacy in relation to their risk profile. Kiwibank's ICAAP methodology requires it to hold capital against the following "other material risks" (Pillar II risks).

- Earnings risk – The current or prospective risk to earnings and growth targets arising from changes in the business environment and from adverse business decisions, improper implementation of decisions or lack of responsiveness to changes in the business environment.
- Access to capital: – The risk to the Banking Group's earnings and business objectives arising from an imbalanced internal capital structure in relation to the nature and size of the Bank, or from difficulties with raising additional capital in a timely manner.

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 the following pages summarise the composition of regulatory capital and capital adequacy ratios for the period ended 31 March 2013. Throughout the period Kiwibank and the Banking Group complied with both regulatory and internal capital adequacy requirements.

Note: New disclosure requirements under the Basel III capital adequacy regime became effective from 1 January 2013. There is no requirement to disclose the comparatives of prior periods for the off-quarter disclosures.

# Capital adequacy continued

| | The Banking Group |
|---|---|
| Dollars in millions | Unaudited as at 31/03/13 |
| **Capital** | |
| Tier 1 capital (net of all deductions and adjustments), which consists of: | |
| Common Equity Tier 1 capital | 618 |
| Additional Tier 1 capital | 146 |
| Total Tier 1 capital | 764 |
| Total Tier 2 capital | 168 |
| Total Tier 1 capital and Tier 2 capital | 932 |
| Deduction included in in calculation of capital: | |
| Deduction from Common Equity Tier 1 capital | (72) |
| Deduction from Additional Tier 1 capital | - |
| **Deduction from Tier 2 capital** | - |
| Capital adequacy ratios | |
| **Common Equity Tier 1 capital ratio** | 8.3% |
| **Additional Tier 1 capital ratio** | 2.0% |
| **Total Tier 1 capital ratio** | 10.3% |
| **Minimum Common Equity Tier 1 capital ratio requirement** | 4.5% |
| **Minimum Tier 1 capital ratio requirement** | 6.0% |
| **Minimum total capital ratio requirement** | 10.5% |
| **Total capital (Pillar I) ratio** | 12.5% |
| **Total capital ratio (Pillar I and II) ratio** | 12.0% |
| Buffer ratio | |
| Buffer ratio | 3.8% |
| Buffer ratio requirement (effective from 1 January 2014) | 2.5% |
| **Pillar I capital requirement** | |
| **On-balance sheet credit risk** | |
| Residential mortgages (including past due) | 379 |
| Corporate | 8 |
| Claims on banks | 19 |
| Other | 71 |
| **Total on-balance credit risk** | 477 |
| **Other capital requirements** | |
| Off-balance sheet credit exposures | 21 |
| Operational risk | 75 |
| Market risk | 22 |
| **Total other capital requirements** | 118 |
| **Total Pillar I capital requirement** | 595 |
| **Capital requirements for other material risk (Pillar II)** | |
| **Total capital requirement (Pillar II)** | 27 |

Capital requirements for the other material risks covers risks associated with earnings, funding and credit lending.

# Capital adequacy continued

## Residential mortgages by loan-to-value ratio

| | The Banking Group | | |
|---|---|---|---|
| **Unaudited as at 31 March 2013**<br>**Dollars in millions** | **On-balance sheet** | **Off-balance sheet** | **Total** |
| LVR 0%-80% | 9,902 | 218 | 10,120 |
| LVR > 80%-90% | 1,961 | 13 | 1,974 |
| LVR 90% + | 373 | 5 | 378 |

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 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 March 2013, of the loans with an LVR greater than 80%, $500m relates to "Welcome Home" loans, whose credit risk is mitigated by the Crown. Of the remaining portfolio with an LVR greater than 80%, Kiwibank uses lenders' mortgage insurance on selected loans.