Disclosure Statement.

For the six months
ended 31 December 2019

Number 70

Kiwibank.

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 2019, in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (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, Level 9, 20 Customhouse Quay, Wellington 6011, New Zealand.

Address for service

The address for service is: Kiwibank Limited, Level 9, 20 Customhouse 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 other 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.

Outcome of the RBNZ Capital Review

On 5 December 2019, the RBNZ published its final decisions in respect of their proposals to reform the amount of regulatory capital required of banks incorporated in New Zealand.

The key changes to the regulatory capital requirements for the Banking Group are:

- Increase in the Common Equity Tier 1 capital ratio required to 11.5%
- Increase in Tier 1 capital ratio required to 14%
- Increase in the Total Capital ratio required to 16%

These changes are being phased in over a seven-year transition period. Kiwibank is already compliant with the Common Equity Tier 1 capital ratio requirement and expects to meet the other capital requirements through a combination of growth in retained earnings and the issuance of qualifying capital instruments over the transition period.

Pending proceedings or arbitration

The Board is not aware of any 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.

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	Current credit rating	Rating outlook
S&P Global Ratings ("**S&P**")	A	Outlook Positive
Moody's Investors Service ("**Moody's**")	A1	Outlook Stable
Fitch Ratings ("**Fitch**")	AA	Outlook Stable

General matters continued

Conditions of registration

Changes in conditions of registration

There have been no changes to the Kiwibank conditions of registration from those which were in force at 30 June 2019.

Non-compliance with conditions of registration

As previously reported in the Bank's Disclosure Statement for the year ended 30 June 2019, the Bank is undertaking a review of its compliance with its conditions of registration. As a result of the review and related activities, in the six months ending 31 December 2019 the Bank identified a number of minor errors in its calculations of the regulatory liquidity ratios required under condition of registration 13. The errors impacted regulatory ratio calculations but the Bank has remained above all Board and RBNZ ratio requirements at all times. The largest impact on the one-week and one-month mismatch ratios was in October 2019 and reduced the ratios by 12 basis points and the largest impact on the core funding ratio was in August 2019 and reduced the ratio by 8 basis points. The review is ongoing and further updates will be provided if necessary. Kiwibank is working on system and process improvements to ensure these errors do not arise again.

Condition of registration 24 requires that the Bank complies with the Reserve Bank document Outsourcing Policy (BS11) dated September 2017. The Bank did not enter some outsourcing arrangements in the compendium as required by BS11 for the period commencing from 1 October 2019. The Bank remediated this issue in January 2020.

Directorate

Susan Carrel Macken resigned as a director on 28 November 2019.

Jonathan Peter Hartley was appointed as a director and Chair of Kiwibank on 28 November 2019.

David James Walsh resigned as a director on 30 September 2019.

There have been no other changes in the Board for the six months ended 31 December 2019.

Responsible persons

Jonathan Peter Hartley and Alistair Bruce Ryan 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:

Jonathan Peter Hartley

Kevin Mark Malloy

Ian Cameron Blair

Scott John Pickering

Michael Charles John O'Donnell

Alistair Bruce Ryan

Carol Anne Campbell

Auditor

The auditor whose review opinion is referred to in this disclosure statement is Michele Embling assisted by PricewaterhouseCoopers, acting as agent on behalf of the Office of the Auditor General. Her address for service is PricewaterhouseCoopers, PwC Centre, 10 Waterloo Quay, Wellington 6011, New Zealand.

Guarantees

As at the date the Board approved this Disclosure Statement, payment obligations of Kiwibank in relation to certain debt securities issued by Kiwibank have the benefit of a guarantee by Kiwi Covered Bond Trustee Limited (the "**Covered Bond Guarantee**"). Also, the payment obligations of Kiwibank owed as at 28 February 2017 and still outstanding have the benefit of a deed poll guarantee by New Zealand Post Limited (the "**NZP Guarantee**").

Further details on the NZP Guarantee can be obtained by referring to Kiwibank's Disclosure Statement for the year ended 30 June 2019 which is available at **www.kiwibank.co.nz**.

On 31 October 2016, New Zealand Post Limited ("**NZP**") gave notice of the termination of the NZP Guarantee (with an effective date of withdrawal of 28 February 2017). This termination did not affect any payment obligations of Kiwibank that were already guaranteed at the time the guarantee was terminated. A summary of the details of each guarantee are set out below.

NZP GUARANTEE

NZP continues to support Kiwibank as a registered bank through the NZP Guarantee to the extent of guaranteed payment obligations that existed as at 28 February 2017.

The following is a summary of the main features of the NZP Guarantee effective for payment obligations that existed as at 28 February 2017:

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 owing as at 28 February 2017 and still outstanding. The NZP Guarantee has no expiry date in relation to the payment obligations that continue to be guaranteed.

iv. There are no material legislative or regulatory restrictions in New Zealand, 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 $607m as calculated from NZP's most recent publicly available audited financial statements for the year ended 30 June 2019 and as disclosed in the Director's Report in the NZ Post Group Finance Limited Annual Report for the year ended 30 June 2019. There were no modifications 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 S&P of A with 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 (as amended); and
   - II. the Disclosure Statement is not false or misleading.
2. During the period ended 31 December 2019:
   - i. Kiwibank has complied with the conditions of registration applicable during the period except as noted on page 2;
   - 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 Jonathan Peter Hartley and Alistair Bruce Ryan as directors and responsible persons on behalf of all the directors listed in the Directorate of this Disclosure Statement:

18 February 2020

Interim financial statements

Income statement

For the six months ended 31 December 2019

Dollars in millions	Note	Unaudited 6 months ended 31/12/19	Unaudited 6 months ended 31/12/18	Audited year ended 30/06/19
Interest income		**461**	462	933
Interest expense		**(236)**	(239)	(488)
Net interest income		**225**	223	445
Net gains on financial instruments at fair value	2	**6**	2	3
Gross fee and other income		**98**	97	185
Direct fee expenses		**(52)**	(49)	(95)
Net fee and other income	3	**46**	48	90
Total operating income		**277**	273	538
Operating expenses		**(207)**	(183)	(375)
Profit before credit impairment and taxation		**70**	90	163
Credit impairment losses	5	**(5)**	(4)	(12)
Profit before taxation		**65**	86	151
Income tax expense		**(14)**	(24)	(43)
Profit after taxation		**51**	62	108

Statement of comprehensive income

For the six months ended 31 December 2019

Dollars in millions	Unaudited 6 months ended 31/12/19	Unaudited 6 months ended 31/12/18	Audited year ended 30/06/19
Profit after taxation	**51**	62	108
Other comprehensive income			
Net gain/(loss) from changes in reserves that may subsequently be reclassified to profit or loss			
- Fair value reserve (net of tax)	**(5)**	2	6
- Cash flow hedge reserve (net of tax)	**9**	-	(12)
Other comprehensive income for the period/year	**4**	2	(6)
Total comprehensive income for the period/year	**55**	64	102

From 1 July 2019, the Banking Group has applied NZ IFRS 16 in the preparation of the Income Statement and Statement of Comprehensive Income. See note 25 for more details of the related changes in accounting policies and impact of adoption.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these financial statements.

Statement of changes in equity

For the six months ended 31 December 2019

Dollars in millions	Fully Paid Ordinary Shares	Retained Earnings	Fair Value Reserve	Cash Flow Hedge Reserve	Total Shareholder's Equity
Audited balance at 30 June 2018	737	755	5	(10)	1,487
Balance adjusted for adoption of NZ IFRS 9 and NZ IFRS 15	-	(4)	-	-	(4)
Opening balance as at 1 July 2018	737	751	5	(10)	1,483
Unaudited 6 months ended 31 December 2018					
Unaudited profit for the period	-	62	-	-	62
Other comprehensive income					
Movement in fair value of investment securities (net of tax)	-	-	2	-	2
Cash flow hedges (net of tax)	-	-	-	-	-
Total other comprehensive income	-	-	2	-	2
Total comprehensive income	-	62	2	-	64
Transactions with owners					
Dividends paid on ordinary shares	-	(14)	-	-	(14)
Distributions to holder of perpetual capital	-	(5)	-	-	(5)
Unaudited balance at 31 December 2018	737	794	7	(10)	1,528
Audited year ended 30 June 2019					
Audited profit for the year	-	108	-	-	108
Other comprehensive income					
Movement in fair value of investment securities (net of tax)	-	-	6	-	6
Cash flow hedges (net of tax)	-	-	-	(12)	(12)
Total other comprehensive income	-	-	6	(12)	(6)
Total comprehensive income	-	108	6	(12)	102
Transactions with owners					
Dividends paid on ordinary shares	-	(25)	-	-	(25)
Distributions to holder of perpetual capital	-	(11)	-	-	(11)
Audited balance at 30 June 2019	737	823	11	(22)	1,549
Balance adjusted for adoption of NZ IFRS 16	**-**	**1**	**-**	**-**	**1**
Opening balance as at 1 July 2019	**737**	**824**	**11**	**(22)**	**1,550**
Unaudited 6 months ended 31 December 2019					
Unaudited profit for the period	**-**	**51**	**-**	**-**	**51**
Other comprehensive income					
Movement in fair value of investment securities (net of tax)	**-**	**-**	**(5)**	**-**	**(5)**
Cash flow hedges (net of tax)	**-**	**-**	**-**	**9**	**9**
Total other comprehensive income	**-**	**-**	**(5)**	**9**	**4**
Total comprehensive income	**-**	**51**	**(5)**	**9**	**55**
Transactions with owners					
Dividends paid on ordinary shares	**-**	**(11)**	**-**	**-**	**(11)**
Distributions to holder of perpetual capital	**-**	**(5)**	**-**	**-**	**(5)**
Unaudited balance at 31 December 2019	**737**	**859**	**6**	**(13)**	**1,589**

From 1 July 2019, the Banking Group has applied NZ IFRS 16 in the preparation of the Statement of Changes in Equity. See note 25 for more details of the related changes in accounting policies and impact of adoption.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these financial statements.

Interim financial statements continued

Balance sheet

As at 31 December 2019

Dollars in millions	Note	Unaudited 31/12/19	Unaudited 31/12/18	Audited 30/06/19
Assets				
Cash and cash equivalents		**561**	447	421
Due from related parties	16	**79**	82	85
Due from other financial institutions	7	**246**	342	71
Investment securities		**1,116**	1,333	1,176
Derivative financial instruments		**308**	326	358
Loans and advances	4	**21,523**	19,316	20,443
Property, plant and equipment		**51**	50	51
Right-of-use assets	25	**80**	-	-
Current tax asset		**-**	21	-
Deferred taxation		**19**	15	21
Intangible assets	15	**64**	81	74
Other assets		**39**	27	34
Total assets		**24,086**	22,040	22,734
Total interest earning and discount bearing assets		***23,391***	*21,394*	*22,081*
Liabilities				
Due to other financial institutions		**141**	150	126
Due to related parties	16	**4**	5	9
Deposits and other borrowings	8	**19,217**	17,430	18,240
Derivative financial instruments		**296**	289	343
Debt securities issued	9	**2,463**	2,253	2,078
Current tax liability		**4**	-	7
Other liabilities		**117**	105	102
Contract liabilities		**24**	27	27
Lease liabilities	25	**81**	-	-
Subordinated debt	10	**150**	253	253
Total liabilities		**22,497**	20,512	21,185
Total interest and discount bearing liabilities		***19,144***	*17,788*	*18,325*
Shareholder's equity				
Share capital		**737**	737	737
Reserves		**852**	791	812
Total shareholder's equity		**1,589**	1,528	1,549
Total liabilities and shareholder's equity		**24,086**	22,040	22,734

From 1 July 2019, the Banking Group has applied NZ IFRS 16 in the preparation of the Balance Sheet. See note 25 for more details of the related changes in accounting policies and impact of adoption.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these financial statements.

Interim financial statements continued

Cash flow statement

For the six months ended 31 December 2019

Dollars in millions	Unaudited 6 months ended 31/12/19	Unaudited 6 months ended 31/12/18	Audited year ended 30/06/19
Cash flows from operating activities			
Interest received	**477**	478	967
Interest paid	**(250)**	(223)	(470)
Fees and other income received	**98**	119	185
Direct fee expenses paid	**(52)**	(48)	(95)
Operating expenses paid	**(174)**	(165)	(340)
Taxes paid	**(17)**	(35)	(29)
Net cash flows from operating activities before changes in operating assets and liabilities	**82**	126	218
Net changes in operating assets and liabilities			
Decrease/(increase) in investment securities	**55**	(111)	53
Increase in loans and advances	**(1,089)**	(1,026)	(2,185)
Decrease in net amounts due from related parties	**1**	2	3
(Increase)/decrease in balances due from other financial institutions	**(175)**	(210)	61
Increase in deposits and other borrowing	**987**	1,240	2,047
Increase/(decrease) in balances due to other financial institutions	**15**	22	(2)
(Decrease)/increase in contract liabilities	**(3)**	-	21
Net cash flows provided by operating activities	**(127)**	43	216
Cash flows from investing activities			
Purchase of property, plant and equipment	**(6)**	(11)	(18)
Purchase of intangible assets	**(1)**	(13)	(21)
Net cash flows from investing activities	**(7)**	(24)	(39)
Cash flows from financing activities			
Payment of principal portion of lease liabilities	**(6)**	-	-
Increase/(decrease) in debt securities issued	**396**	-	(167)
Repayment of subordinated debt	**(100)**	-	-
Dividends paid on ordinary shares	**(11)**	(14)	(25)
Distributions paid to holder of perpetual capital	**(5)**	(5)	(11)
Net cash flows from financing activities	**274**	(19)	(203)
Increase/(decrease) in cash and cash equivalents	**140**	-	(26)
Cash and cash equivalents at beginning of the period/year	**421**	447	447
Effect of exchange translation adjustments	**-**	-	-
Cash and cash equivalents at end of the period/year	**561**	447	421

From 1 July 2019, the Banking Group has applied NZ IFRS 16 in the preparation of the Cash flow statement. See note 25 for more details of the related changes in accounting policies and impact of adoption.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these financial statements.

Notes to the interim financial statements

1. Summary of significant accounting policies

1.1 Reporting entity

These consolidated interim financial statements are presented for the “Banking Group”, which consists of Kiwibank Limited (“Kiwibank” or the “Bank”) and its subsidiaries. Kiwibank is a for-profit 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 banking products and services to individuals and small to medium-sized businesses.

Kiwibank's immediate parent company is Kiwi Group Holdings Limited (“KGHL”). KGHL is owned by New Zealand Post Limited (“NZP”) (53%), NZSF Tui Investments Limited ("NZSF") (25%) and Accident Compensation Corporation ("ACC") (22%). The ultimate holding company of Kiwibank is NZP whose address for service is: Ground Floor, New Zealand Post House, 7 Waterloo Quay, Wellington 6011, New Zealand. 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 2019 and have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand, as appropriate for for-profit 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 (as amended) (the “Order”). These interim financial statements should be read in conjunction with the Banking Group’s financial statements for the year ended 30 June 2019.

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 the following assets and liabilities:

- Derivative financial instruments – held at fair value through profit or loss
- Debt securities issued – commercial paper held at fair value through profit or loss
- Investment securities – held at fair value through other comprehensive income

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 2019, except for the adoption of new standards and interpretations effective as of 1 July 2019.

The Banking Group has applied, for the first time, the following new standards and amendments:

- NZ IFRS 16: Leases

The above standard was adopted without restatement of comparative amounts. Note 25 includes a description of the nature and effect of the changes made in accounting policies due to the adoption of the above standard and includes a disclosure of the financial impact of adoption.

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 2019, using the acquisition method. Subsidiaries are entities that are controlled by Kiwibank.

1.5 Functional and presentation currency

The Banking Group’s interim financial statements are presented in New Zealand dollars which is the Bank’s functional and presentation currency. All amounts are expressed in millions of New Zealand dollars, unless otherwise stated.

1.6 Comparative amounts

Certain amounts in the comparative information have been reclassified or amended to ensure consistency with the current period’s presentation. Changes are disclosed within impacted notes where relevant.

2. Net gains on financial instruments at fair value

Dollars in millions	Unaudited 6 months ended 31/12/19	Unaudited 6 months ended 31/12/18	Audited year ended 30/06/19
Derivative financial instruments held for trading	-	(1)	(1)
Financial instruments held for trading	-	-	(1)
Net ineffectiveness on qualifying fair value and cash flow hedges	-	-	-
Cumulative gain transferred from fair value reserve	3	1	-
Cumulative loss transferred from cash flow hedge reserve	-	-	-
Net foreign exchange gains	3	2	5
Total net gains on financial instruments at fair value	**6**	2	3

Net ineffectiveness on qualifying cash flow hedges is $0.0m (31 December 2018: $0.0m; 30 June 2019: $0.0m). Net ineffectiveness on qualifying fair value hedges is $0.4m (31 December 2018: $0.0m; 30 June 2019: $0.0m).

3. Net fee and other income and contracts with customers

	Unaudited 6 months ended 31/12/19		
Dollars in millions	Personal	Business	Total
Major service categories			
Lending services	4	2	6
Card services	57	1	58
Transactional account and other services	16	3	19
Agency services	2	1	3
Total revenue from contracts with customers	**79**	**7**	**86**
Other income	12	-	12
Gross fee and other income	**91**	**7**	**98**

The Banking Group sold the Prezzy card business to epay New Zealand Limited on 29 November 2019 with a transitional agreement in place whereby Kiwibank will operate parts of the business on behalf of epay for an ongoing fee until epay takes on the full operation and issuance of the cards. epay will manage Marketing and Distribution of the Prezzy card from the sale date. $12.0m has been recognised in the period ended 31 December 2019 within other income above in relation to the gain on sale.

Reconciliation to segment reporting

	Unaudited 6 months ended 31/12/19		
Dollars in millions	Personal	Business	Total
Net interest income	144	81	225
Net gains on financial instruments at fair value	1	5	6
Gross fee and other income	91	7	98
Direct fee expenses	(51)	(1)	(52)
Total revenue (as reported in segment analysis in note 18)	**185**	**92**	**277**

Notes to the interim financial statements continued

3. Net fee and other income and contracts with customers continued

Dollars in millions	Unaudited 6 months ended 31/12/18 Personal	Business	Total
Major service categories			
Lending services	3	1	4
Card services	55	-	55
Transactional account and other services	20	3	23
Agency services	3	10	13
Total revenue from contracts with customers	81	14	95
Other income	1	1	2
Gross fee and other income	82	15	97

Reconciliation to segment reporting

Dollars in millions	Unaudited 6 months ended 31/12/18 Personal	Business	Total
Net interest income	145	78	223
Net gains on financial instruments at fair value	-	2	2
Gross fee and other income	82	15	97
Direct fee expenses	(45)	(4)	(49)
Total revenue (as reported in segment analysis in note 18)	182	91	273

Dollars in millions	Audited year ended 30/06/19 Personal	Business	Total
Major service categories			
Lending services	7	3	10
Card services	107	1	108
Transactional account and other services	41	7	48
Agency services	4	12	16
Total revenue from contracts with customers	159	23	182
Other income	2	1	3
Gross fee and other income	161	24	185

Reconciliation to segment reporting

Dollars in millions	Audited year ended 30/06/19 Personal	Business	Total
Net interest income	290	155	445
Net gains on financial instruments at fair value	(1)	4	3
Gross fee and other income	161	24	185
Direct fee expenses	(89)	(6)	(95)
Total revenue (as reported in segment analysis in note 18)	361	177	538

Notes to the interim financial statements continued

4. Loans and advances

Dollars in millions	Unaudited as at 31/12/19	Unaudited as at 31/12/18	Audited as at 30/06/19
Overdrafts	**98**	78	94
Credit card outstandings	**461**	407	398
Term loans - housing	**18,799**	17,071	17,977
Other term lending	**2,010**	1,632	1,837
Other lending	**196**	164	177
Gross loans and advances	**21,564**	19,352	20,483
Provision for credit impairment	**(41)**	(36)	(40)
Fair value hedge adjustments	**-**	-	-
Total net loans and advances	**21,523**	19,316	20,443
Current	**1,744**	1,291	1,507
Non-current	**19,779**	18,025	18,936

The table above presents gross loans and advances by type of product. Total gross residential mortgage loans at 31 December 2019 were $19,725m (31 December 2018: $17,952m, 30 June 2019: $18,894m). This includes *term loans – housing* and other residentially secured lending included within *other term lending*.

5. Asset quality

Credit impairment (losses)/reversals recognised in income statement

Dollars in millions	Unaudited 6 months ended 31/12/19			
	Retail unsecured lending	Residential mortgage loans	Business exposures	Total
(Charged)/credited to the income statement for collectively assessed provisions	**(1)**	**1**	**(2)**	**(2)**
Credited to the income statement for individually assessed provisions	**-**	**-**	**(1)**	**(1)**
Amounts written off directly to the income statement	**(4)**	**-**	**-**	**(4)**
Recovery of amounts previously written off	**2**	**-**	**-**	**2**
Total credit impairment (losses)/reversals per income statement	**(3)**	**1**	**(3)**	**(5)**

Dollars in millions	Unaudited 6 months ended 31/12/18			
	Retail unsecured lending	Residential mortgage loans	Business exposures	Total
Credited/(charged) to the income statement for collectively assessed provisions	2	(1)	(2)	(1)
Credited/(charged) to the income statement for individually assessed provisions	(3)	-	-	(3)
Amounts written off directly to the income statement	(2)	-	-	(2)
Recovery of amounts previously written off	2	-	-	2
Total credit impairment (losses)/reversals per income statement	(1)	(1)	(2)	(4)

The comparative prior period amounts in the table above have been reclassified to align with the categories used in the current period's presentation.

5. Asset quality continued

Dollars in millions	Audited year ended 30/06/19 Retail unsecured lending	Residential mortgage loans	Business exposures	Total
Credited/(charged) to the income statement for collectively assessed provisions	1	(2)	(6)	(7)
Credited to the income statement for individually assessed provisions	1	-	1	2
Amounts written off directly to the income statement	(10)	(1)	-	(11)
Recovery of amounts previously written off	4	-	-	4
Total credit impairment (losses)/reversals per income statement	**(4)**	**(3)**	**(5)**	**(12)**

Recovery of amounts previously written off are recognised directly in the income statement and there is no related movement in provisions when amounts are recovered.

Summary of lending

Dollars in millions	Unaudited as at 31/12/19 Retail unsecured lending	Residential mortgage loans	Business exposures	Total
Neither past due nor impaired	460	19,651	1,325	21,436
Past due but not impaired	21	73	32	126
Impaired	-	1	1	2
Gross loans and advances	**481**	**19,725**	**1,358**	**21,564**
Provision for credit impairment	(11)	(14)	(16)	(41)
Fair value hedge adjustments	-	-	-	-
Net loans and advances	**470**	**19,711**	**1,342**	**21,523**

Loans and advances past due but not impaired

Dollars in millions	Unaudited as at 31/12/19 Retail unsecured lending	Residential mortgage loans	Business exposures	Total
Past due less than 30 days	17	53	22	92
Past due 30 - 59 days	3	6	5	14
Past due 60 - 89 days	1	4	1	6
Past due 90 days or greater	-	10	4	14
Total past due but not impaired	**21**	**73**	**32**	**126**

5. Asset quality continued

Movement in provision for credit impairment - retail unsecured lending exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Balance at beginning of period - retail unsecured lending	5	5	-	-	10
Transfers between stages:					
- Transferred to Stage 1	1	(1)	-	-	-
- Transferred to Stage 2	-	-	-	-	-
- Transferred to Stage 3	-	-	-	-	-
- Transferred to Stage 3 individually assessed	-	-	-	-	-
Total transfers between stages	1	(1)	-	-	-
(Credited)/charged to income statement for collectively assessed provisions					
- Net remeasurement of loss allowances	(1)	2	-	-	1
- Changes due to additions and deletions	-	1	-	-	1
- Changes due to amounts written off	-	(1)	-	-	(1)
- Other changes	-	-	-	-	-
Total (credited)/charged to income statement for collectively assessed provisions	(1)	2	-	-	1
Charged/(credited) to income statement for individually assessed provisions					
- New and increased provisions	-	-	-	-	-
- Write-back of provisions no longer required	-	-	-	-	-
Total charged/(credited) to income statement for individually assessed provisions	-	-	-	-	-
Amounts written off from individually assessed provisions	-	-	-	-	-
Balance at end of period - retail unsecured lending	5	6	-	-	11

Impact of changes in gross carrying amount on ECL - retail unsecured lending exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Gross carrying amount - retail unsecured lending					
Balance at the beginning of period	311	119	1	-	431
Net transfers between stages	14	(14)	-	-	-
Additions	146	32	-	-	178
Deletions	(102)	(22)	-	-	(124)
Amounts written off	-	(4)	-	-	(4)
Balance at the end of period - retail unsecured lending	369	111	1	-	481

Impact of changes in gross carrying amount on ECL - retail unsecured lending exposures

An explanation of how significant changes in the gross carrying amount of financial assets for retail unsecured lending exposures during the year have contributed to changes in the provision for credit impairment is outlined below.

Overall, credit impairment provisions for retail unsecured lending exposures increased by $1m.

5. Asset quality continued

- *Stage 1 collectively assessed* – no material change in provisions. New lending of $146m was largely offset by repayments of $102m. $14m of gross balances moved from stage 2 to stage 1 during the year to date which increased stage 1 ECL by $1m. However, the $1m increase was balanced by credit quality improvements within stage 1.
- *Stage 2 collectively assessed* – while total stage 2 balances decreased by a net $8m, provisions increased by $1m. A $2m additional ECL provision resulted from credit deterioration as exposures moved to stage 2 while there was another $1m impact from additional lending within that stage. $4m of gross balances were written off from stage 2 releasing $1m of stage 2 lifetime ECL in the year to date.
- *Stage 3 collectively assessed & stage 3 individually assessed* – stable with no material movement in gross balances during the year to date.

Movement in provision for credit impairment – residential mortgage loan exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Balance at beginning of period - residential mortgage loans	8	3	3	2	16
Transfers between stages:					
- Transferred to Stage 1	1	(1)	-	-	-
- Transferred to Stage 2	-	-	-	-	-
- Transferred to Stage 3	-	-	-	-	-
- Transferred to Stage 3 individually assessed	-	-	-	-	-
Total transfers between stages	1	(1)	-	-	-
(Credited)/charged to income statement for collectively assessed provisions					
- Net remeasurement of loss allowances	(1)	1	-	-	-
- Changes due to additions and deletions	1	-	(2)	-	(1)
- Changes due to amounts written off	-	-	-	-	-
- Other changes	-	-	-	-	-
Total charged/(credited) to income statement for collectively assessed provisions	-	1	(2)	-	(1)
Charged/(credited) to income statement for individually assessed provisions					
- New and increased provisions	-	-	-	-	-
- Write-back of provisions no longer required	-	-	-	-	-
Total charged/(credited) to income statement for individually assessed provisions	-	-	-	-	-
Amounts written off from individually assessed provisions	-	-	-	(1)	(1)
Balance at end of period - residential mortgage loans	9	3	1	1	14

Impact of changes in gross carrying amount on ECL - residential mortgage loan exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Gross carrying amount - residential mortgage loans					
Balance at the beginning of period	18,263	610	18	3	18,894
Net transfers between stages	(55)	55	-	-	-
Additions	2,877	47	-	-	2,924
Deletions	(1,999)	(84)	(8)	(1)	(2,092)
Amounts written off	-	-	-	(1)	(1)
Balance at the end of period - residential mortgage loans	19,086	628	10	1	19,725

Notes to the interim financial statements continued

5. Asset quality continued

An explanation of how significant changes in the gross carrying amount of financial assets for residential mortgage loan exposures during the year have contributed to changes in the provision for credit impairment is outlined below.

Overall, credit impairment provisions for residential mortgage loan exposures decreased by a net $2m.

- *Stage 1 collectively assessed* - provisions increased by $1m largely due to net lending growth of $823m. Due to improvements in underlying risk, exposures with $1m of provisions transitioned to stage 1 from other stages, allowing most of that provision to be released.
- *Stage 2 collectively assessed* – there was no net change in the provisions in this stage despite a small net $18m increase in stage 2 balances. While $55m of exposures were transferred into stage 2, along with $47m of additional lending, the related provisions were largely offset by a reduction of provisions through repayment of exposures already in stage 2.
- *Stage 3 collectively assessed* – lending balances within this stage reduced from $18m to $10m in the year to date resulting in provisions reducing by $2m.
- *Stage 3 individually assessed* – individually assessed provisions reduced to $1m on $1m of gross impaired residential mortgage lending. Total impaired mortgage balances reduced by $2m during the year to date through repayments and write-offs.

Movement in provision for credit impairment – business exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Balance at beginning of period - business exposures	6	6	1	1	14
Transfers between stages:					
- Transferred to Stage 1	1	(1)	-	-	-
- Transferred to Stage 2	-	-	-	-	-
- Transferred to Stage 3	-	-	-	-	-
- Transferred to Stage 3 individually assessed	-	-	-	-	-
Total transfers between stages	1	(1)	-	-	-
(Credited)/charged to income statement for collectively assessed provisions					
- Net remeasurement of loss allowances	(1)	1	-	-	-
- Changes due to additions and deletions	2	(1)	1	-	2
- Changes due to amounts written off	-	-	-	-	-
- Other changes	-	-	-	-	-
Total charged/(credited) to income statement for collectively assessed provisions	1	-	1	-	2
Charged/(credited) to income statement for individually assessed provisions					
- New and increased provisions	-	-	-	1	1
- Write-back of provisions no longer required	-	-	-	-	-
Total charged/(credited) to income statement for individually assessed provisions	-	-	-	1	1
Amounts written off from individually assessed provisions	-	-	-	(1)	(1)
Balance at end of period - business exposures	8	5	2	1	16

5. Asset quality continued

Impact of changes in gross carrying amount on ECL – business exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Gross carrying amount - business exposures					
Balance at the beginning of period	1,102	52	2	2	1,158
Net transfers between stages	(7)	7	-	-	-
Additions	430	9	3	1	443
Deletions	(227)	(13)	(1)	(1)	(242)
Amounts written off	-	-	-	(1)	(1)
Balance at the end of period - business exposures	**1,298**	**55**	**4**	**1**	**1,358**

An explanation of how significant changes in the gross carrying amount of financial assets for business exposures during the year have contributed to changes in the provision for credit impairment is outlined below.

Overall, credit impairment provisions for business exposures increased a net $2m.

- *Stage 1 collectively assessed* – provisions increased by $2m driven by a net increase of $196m in gross balances. Exposures moving from stage 2 to stage 1 due to improvements in credit quality allowed $1m of provisions to be released.
- *Stage 2 collectively assessed* – provisions decreased by $1m despite a $3m increase in balances within stage 2. The decrease of $1m reflects lower provisions due to repayments and a change in the mix of assets now in stage 2.
- *Stage 3 collectively assessed* – provisions increased by $1m due to $2m of net growth in lending balances.
- *Stage 3 individually assessed* – individually assessed provisions did not materially change with impaired lending balances reducing by $1m year to date through repayments and amounts written off.

Notes to the interim financial statements continued

5. Asset quality continued

Movement in provision for credit impairment – total exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Balance at beginning of period - total exposures	19	14	4	3	40
Transfers between stages:					
- Transferred to Stage 1	3	(3)	-	-	-
- Transferred to Stage 2	-	-	-	-	-
- Transferred to Stage 3	-	-	-	-	-
- Transferred to Stage 3 individually assessed	-	-	-	-	-
Total transfers between stages	3	(3)	-	-	-
(Credited)/charged to income statement for collectively assessed provisions					
- Net remeasurement of loss allowances	(3)	4	-	-	1
- Changes due to additions and deletions	3	-	(1)	-	2
- Changes due to amounts written off	-	(1)	-	-	(1)
- Other changes	-	-	-	-	-
Total charged/(credited) to income statement for collectively assessed provisions	-	3	(1)	-	2
Charged/(credited) to income statement for individually assessed provisions					
- New and increased provisions	-	-	-	1	1
- Write-back of provisions no longer required	-	-	-	-	-
Total charged/(credited) to income statement for individually assessed provisions	-	-	-	1	1
Amounts written off from individually assessed provisions	-	-	-	(2)	(2)
Balance at end of period - total exposures	22	14	3	2	41

Impact of changes in gross carrying amount on ECL – total exposures

	Unaudited 6 months ended 31/12/19				
	Stage 1	Stage 2	Stage 3		
Dollars in millions	Collectively assessed	Collectively assessed	Collectively assessed	Individually assessed	Total
Gross carrying amount - total exposures					
Balance at the beginning of period	19,676	781	21	5	20,483
Net transfers between stages	(48)	48	-	-	-
Additions	3,453	88	3	1	3,545
Deletions	(2,328)	(119)	(9)	(2)	(2,458)
Amounts written off	-	(4)	-	(2)	(6)
Balance at the end of period - total exposures	20,753	794	15	2	21,564

Asset quality of loans and advances

There were no real estate or other assets acquired through the enforcement of security/collateral held at 31 December 2019 (31 December 2018: nil; 30 June 2019: nil). There were no assets under administration as at 31 December 2019 (31 December 2018: nil; 30 June 2019: nil). Other assets under administration are those loans that are not impaired or past due, but where the customer is in receivership, liquidation, bankruptcy, statutory management, a not asset procedure, voluntary administration or any other form of administration in New Zealand.

5. Asset quality continued

The aggregate amount of undrawn balances on lending commitments to counterparties for whom drawn balances are classified as individually impaired was $0.8m for business exposures at 31 December 2019 (31 December 2018: $0.2m; 30 June 2019: $0.4m). There were no undrawn balances on lending commitments to counterparties for whom drawn balances are classified as individually impaired for residential mortgage loan exposures and other retail exposures at 31 December 2019 (31 December 2018: nil; 30 June 2019: nil).

Credit quality of loans and advances 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 assessed on a combination of debt servicing ability, demographic characteristics and loan-to-valuation ("LVR") ratios. Non-retail advances are individually risk-graded against similar characteristics. The behavioural credit 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.

Credit quality of other financial assets

In addition to assessing impairment for loans and advances, the Banking Group has assessed impairment for cash and cash equivalents, due from other financial institutions, due from related parties, investment securities and other financial assets. All of these financial assets are considered of high credit quality and are neither past due nor impaired. The identified impairment loss for all other financial assets, excluding loans and advances, was immaterial.

Credit risk related adjustments on financial assets at fair value

Credit impairment losses of $0.0m were recognised through other comprehensive income in relation to expected credit losses on Investment Securities held at fair value through other comprehensive income in the period ended 31 December 2019 (31 December 2018: $0.0m; 30 June 2019: $0.0m).

Credit Valuation Adjustments (CVA) and Debit Valuation Adjustments (DVA) are included in the valuations of Derivative Financial Instruments and these adjustments are recognised within net gains on financial instruments at fair value on the income statement. ($0.1m) was recognised in the income statement related to CVA and DVA during the period ended 31 December 2019 (31 December 2018: $0.4m; 30 June 2019: $0.3m).

Notes to the interim financial statements continued

6. 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:

	Unaudited as at 31/12/19		
Dollars in millions	Financial assets	Off-balance sheet commitments	Total credit exposure
New Zealand			
Government, local authorities and services	967	1	968
Finance, investment and insurance	543	13	556
Households	19,292	3,051	22,343
Transport and storage	192	9	201
Professional, scientific and technical services	62	21	83
Electricity, gas and water	5	20	25
Construction	237	170	407
Property and business services	1,258	136	1,394
Agriculture	17	3	20
Health and community services	118	22	140
Personal and other services	128	33	161
Retail and wholesale trade	160	40	200
Food & other manufacturing	127	36	163
Overseas			
Finance, investment and insurance	768	9	777
Total credit exposure	23,874	3,564	27,438
Less provision for credit impairment	(41)	-	(41)
Other financial assets	20	-	20
Total	23,853	3,564	27,417

6. Concentration of credit risk continued

	Unaudited as at 31/12/19				
Dollars in millions	Financial assets	Off-balance sheet commitments	Maximum exposure to credit risk	Collateral	Net credit exposure
Credit risk relating to on-balance sheet assets					
Loans and advances	21,564	-	21,564	(21,091)	473
Due from other financial institutions	246	-	246	-	246
Due from related parties	79	-	79	-	79
Derivative financial instruments	308	-	308	(61)	247
Investment securities	1,116	-	1,116	-	1,116
Cash and cash equivalents	561	-	561	-	561
Other financial assets	20	-	20	-	20
Total on-balance sheet credit risk	23,894	-	23,894	(21,152)	2,742
Less provision for credit impairment	(41)	-	(41)	-	(41)
Total financial assets	23,853	-	23,853	(21,152)	2,701
Credit risk relating to off-balance sheet commitments					
Undrawn credit commitments	-	3,564	3,564	-	3,564
Total off-balance sheet credit risk	-	3,564	3,564	-	3,564
Total	23,853	3,564	27,417	(21,152)	6,265

The table above represents the maximum net credit risk exposure of the Banking Group at 31 December 2019. The exposures set out are based on net carrying amounts as reported in the balance sheet. Australian and New Zealand Standard Industrial Classification ("**ANZSIC**") 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 90% of the total maximum exposure (31 December 2018: 89%; 30 June 2019: 91%).

The preceding table 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 credit commitments (note 23) for an amount equal to the undrawn balance.

7. Due from other financial institutions

Dollars in millions	Unaudited as at 31/12/19	Unaudited as at 31/12/18	Audited as at 30/06/19
Short term advances due from other financial institutions	176	277	-
Collateral paid	70	65	71
Total amounts due from other financial institutions - current	246	342	71

As at 31 December 2019, included within the balance above, is $69.9m of collateral pledged by Kiwibank in respect of its credit support annex obligations to derivative counterparties (31 December 2018: $64.9m; 30 June 2019: $70.6m).

8. Deposits and other borrowings

Dollars in millions	Unaudited as at 31/12/19	Unaudited as at 31/12/18	Audited as at 30/06/19
Demand deposits non-interest bearing	**2,813**	2,287	2,314
Demand deposits bearing interest	**3,891**	3,401	3,498
Term deposits	**12,513**	11,742	12,428
Total deposits from customers	**19,217**	17,430	18,240
Current	**18,694**	16,808	17,625
Non-current	**523**	622	615

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 covered by the NZP Guarantee that existed at the time the NZP Guarantee was terminated on 28 February 2017 are guaranteed under the NZP Guarantee but only to the extent of those obligations.

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 Supervisor 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 2019, $4,557m of the Trust's funds were invested in Kiwibank products or securities (31 December 2018: $4,182m; 30 June 2019: $4,438m).

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.

9. Debt securities issued

Dollars in millions	Unaudited as at 31/12/19	Unaudited as at 31/12/18	Audited as at 30/06/19
Short-term debt			
Certificates of deposit	**531**	155	495
Long-term debt			
Medium term notes	**1,677**	1,854	1,319
Covered bonds	**230**	226	230
Fair value hedge adjustment	**25**	18	34
Total debt securities issued	**2,463**	2,253	2,078
Current	**909**	875	878
Non-current	**1,554**	1,378	1,200

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 that existed at the time the NZP Guarantee was terminated on 28 February 2017, 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.
Further information on the guarantee arrangements and other details relating to covered bonds are disclosed in note 17.

Kiwibank has not had any defaults of principal, interest or other breaches with respect to debt securities issued during the period (period ended 31 December 2018: none; year ended 30 June 2019: none).

10. Subordinated debt

Dollars in millions	Unaudited as at 31/12/19	Unaudited as at 31/12/18	Audited as at 30/06/19
Kiwibank bonds	-	104	104
Perpetual capital bonds	**150**	149	149
Total subordinated debt	**150**	253	253
Current	-	3	104
Non-current	**150**	250	149

On 15 July 2019 Kiwibank fully repaid $100m of Kiwibank bonds at the first call date (period ended 31 December 2018: nil; year ended 30 June 2019: nil). The Kiwibank Bonds had a maturity date of 15 July 2024, however, Kiwibank elected to make an early repayment on 15 July 2019 after obtaining the consent of the RBNZ.

As at 31 December 2019 nil of the subordinated debt qualified as Tier 2 capital for Capital Adequacy calculation purposes (31 December 2018: $100m; 30 June 2019: $100m). The contractual terms of subordinated debt instruments on issue expressly provide that they do not have the benefit of the NZP Guarantee. The NZP Guarantee was terminated with an effective date of 28 February 2017.

The Banking Group has not issued any subordinated debt nor had any defaults of principal, interest or other breaches with respect to these liabilities during the period (period ended 31 December 2018: none; year ended 30 June 2019: 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)	Coupon rate	Call date	Maturity date
Perpetual capital bonds	27 May 2015	150	7.25% p.a.	27 May 2020	None

The classification of subordinated debt as non-current is based on the contractual maturity date of the instruments because the Banking Group is not contractually obliged to make any early repayment and early repayment is subject to the RBNZ's consent being obtained prior to repayment.

The Perpetual Capital Bonds have no maturity date, however, Kiwibank may elect to make an early repayment on 27 May 2020 after obtaining the consent of the RBNZ.

Notes to the interim financial statements continued

11. 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.

Investment securities

Estimates of fair value for investment 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.

	Unaudited as at 31/12/19			
Dollars in millions	Level 1	Level 2	Level 3	Total
Financial assets				
Investment securities	519	597	-	1,116
Derivative financial instrument assets	-	308	-	308
Total financial assets at fair value	519	905	-	1,424
Financial liabilities				
Derivative financial instrument liabilities	-	296	-	296
Debt securities issued	-	-	-	-
Total financial liabilities at fair value	-	296	-	296

Notes to the interim financial statements continued

11. Financial instruments continued

Dollars in millions	Unaudited as at 31/12/18 Level 1	Level 2	Level 3	Total
Financial assets				
Investment securities	477	856	-	1,333
Derivative financial instrument assets	-	326	-	326
Total financial assets at fair value	477	1,182	-	1,659
Financial liabilities				
Derivative financial instrument liabilities	-	289	-	289
Debt securities issued	-	-	-	-
Total financial liabilities at fair value	-	289	-	289

Dollars in millions	Audited as at 30/06/19 Level 1	Level 2	Level 3	Total
Financial assets				
Investment securities	475	701	-	1,176
Derivative financial instrument assets	-	358	-	358
Total financial assets at fair value	475	1,059	-	1,534
Financial liabilities				
Derivative financial instrument liabilities	-	343	-	343
Debt securities issued	-	-	-	-
Total financial liabilities at fair value	-	343	-	343

There have been no transfers between levels 1 and 2 during the period ended 31 December 2019 (period ended 31 December 2018: no transfers; year ended 30 June 2019: no transfers). There were also no transfers into/out of level 3 during the period ended 31 December 2019 (period ended 31 December 2018: no transfers; year ended 30 June 2019: no transfers).

	Unaudited as at 31/12/19		Unaudited as at 31/12/18		Audited as at 30/06/19	
Dollars in millions	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Assets						
Due from related parties	**79**	**79**	82	82	85	85
Investment securities	**1,116**	**1,116**	1,333	1,333	1,176	1,176
Derivative financial instruments	**308**	**308**	326	326	358	358
Loans and advances	**21,523**	**21,565**	19,316	19,355	20,443	20,481
Liabilities						
Due to related parties	**4**	**4**	5	5	9	9
Derivative financial instruments	**296**	**296**	289	289	343	343
Deposits and other borrowings	**19,217**	**19,234**	17,430	17,443	18,240	18,264
Debt securities issued	**2,463**	**2,472**	2,253	2,264	2,078	2,090
Subordinated debt	**150**	**153**	253	261	253	260

11. Financial instruments continued

The carrying values of the following financial instruments are considered a reasonable approximation of fair value because 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.

12. Credit exposure concentrations

Unaudited

CREDIT EXPOSURES TO INDIVIDUAL COUNTERPARTIES

Credit exposure concentrations to individual counterparties at the reporting date are disclosed on the basis of actual credit exposures. Peak end-of-day aggregate credit exposures are disclosed on the basis of actual credit exposures and have been calculated gross of set-offs using the Banking Group's common equity tier 1 capital ("CET1 capital") at the end of the period.

The individual counterparty exposures included in the following table exclude exposures to:

- connected persons;
- the central government or central bank of any country with a long-term credit rating of A- or A3 or above, or its equivalent; and
- any supranational or quasi-sovereign agency with a long-term credit rating of A- or A3 or above, or its equivalent.

	As at 31/12/19	Peak end-of-day over 6 months ended 31/12/19
Exposures to banks		
Total number of exposures to banks that are greater than 10% of CET1 capital	-	3
With a long-term credit rating of A- or A3 or above, or its equivalent	-	3
- 10% to less than 15% of CET1 capital	-	2
- 15% to less than 20% of CET1 capital	-	1
- 20% to less than 25% of CET1 capital	-	-
- 25% to less than 30% of CET1 capital	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-
Exposures to non-banks		
Total number of exposures to non-banks that are greater than 10% of CET1 capital	-	-
With a long-term credit rating of A- or A3 or above, or its equivalent	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-

Inclusion of prior period disclosure of credit exposures to individual counterparties

The Banking Group incorrectly excluded exposures to banks in prior period disclosures of credit exposures to individual counterparties. The disclosure error was made in the June 2018, December 2018 and June 2019 Disclosure Statements. The comparative period disclosures have been included on the following page for June 2019 and December 2018.

12. Credit exposure concentrations continued

	As at 31/12/18	Peak end-of-day over 6 months ended 31/12/18
Exposures to banks		
Total number of exposures to banks that are greater than 10% of CET1 capital	2	5
With a long-term credit rating of A- or A3 or above, or its equivalent	2	5
- 10% to less than 15% of CET1 capital	1	3
- 15% to less than 20% of CET1 capital	1	2
- 20% to less than 25% of CET1 capital	-	-
- 25% to less than 30% of CET1 capital	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-
Exposures to non-banks		
Total number of exposures to non-banks that are greater than 10% of CET1 capital	-	-
With a long-term credit rating of A- or A3 or above, or its equivalent	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-

	As at 30/06/19	Peak end-of-day over 6 months ended 30/06/19
Exposures to banks		
Total number of exposures to banks that are greater than 10% of CET1 capital	-	3
With a long-term credit rating of A- or A3 or above, or its equivalent	-	3
- 10% to less than 15% of CET1 capital	-	1
- 15% to less than 20% of CET1 capital	-	2
- 20% to less than 25% of CET1 capital	-	-
- 25% to less than 30% of CET1 capital	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-
Exposures to non-banks		
Total number of exposures to non-banks that are greater than 10% of CET1 capital	-	-
With a long-term credit rating of A- or A3 or above, or its equivalent	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-

13. Concentration of funding

Dollars in millions	Unaudited as at 31/12/19
Analysis by industry sector	
New Zealand	
Transport and storage	154
Finance, investment and insurance	3,650
Electricity, gas and water	22
Food & other manufacturing	221
Construction	224
Communications	32
Government, local authorities and services	309
Agriculture	59
Health and community services	204
Personal and other services	358
Property and business services	502
Education	157
Retail and wholesale trade	90
Households	14,914
Overseas	
Finance, investment and insurance	1,046
Households	329
	22,271
Lease liabilities	81
Other financial liabilities	77
Total financial liabilities	**22,429**

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

14. Dividends paid

Unaudited

During the period ended 31 December 2019, Kiwibank paid ordinary dividends of $11m to KGHL (period ended 31 December 2018: $14m; year ended 30 June 2019: $25m).

15. Intangible assets

	Unaudited as at 31/12/19		
	Internally developed		
Dollars in millions	Computer software	Computer software work in progress	Total
Cost at beginning of year	256	11	267
Accumulated amortisation at beginning of period	(193)	-	(193)
Carrying value at beginning of period	**63**	**11**	**74**
Additions & Transfers with computer software work in progress	5	1	6
Amortisation	(11)	-	(11)
Amortisation released on disposal	1	-	1
Written off or disposed	(2)	(4)	(6)
Carrying value at end of period	**56**	**8**	**64**
Cost at end of period	259	8	267
Accumulated amortisation at end of year	(203)	-	(203)
Carrying value at end of period	**56**	**8**	**64**

Intangible assets are assessed for impairment on at least an annual basis and whenever events or changes in circumstances indicate that the carrying amount of intangible assets may exceed their recoverable amount. Any impairment loss or write-off is recognised in the income statement as an operating expense. Write-offs and disposals of $6.5m of intangible assets were recognised in the period ended 31 December 2019 (31 December 2018: ($0.1m); 30 June 2019: $2.1m). Included within write-offs of intangible assets for the period ended 31 December 2019 was an individual write-off of $3.7m relating to computer software work in progress that no longer aligns with the Banking Group's long-term technology strategy.

	Unaudited as at 31/12/18		
	Internally developed		
Dollars in millions	Computer software	Computer software work in progress	Total
Cost at beginning of year	237	11	248
Accumulated amortisation at beginning of period	(170)	-	(170)
Carrying value at beginning of period	67	11	78
Additions & Transfers with computer software work in progress	11	3	14
Amortisation	(11)	-	(11)
Amortisation released on disposal	-	-	-
Written off or disposed	-	-	-
Carrying value at end of period	67	14	81
Cost at end of period	248	14	262
Accumulated amortisation at end of year	(181)	-	(181)
Carrying value at end of period	67	14	81

The comparative disclosures above for 31 December 2019 have been added to align with the presentation used in the current period.

15. Intangible assets continued

Dollars in millions	Audited as at 30/06/19 Internally developed Computer software	Computer software work in progress	Total
Cost at beginning of year	237	11	248
Accumulated amortisation at beginning of year	(170)	-	(170)
Carrying value at beginning of year	67	11	78
Additions & Transfers with computer software work in progress	21	-	21
Amortisation	(25)	-	(25)
Amortisation released on disposal	2	-	2
Written off or disposed	(2)	-	(2)
Carrying value at end of year	63	11	74
Cost at end of year	256	11	267
Accumulated amortisation at end of year	(193)	-	(193)
Carrying value at end of year	63	11	74

16. Related party balances

On 25 March 2019, KGHL entered into a loan agreement with Kiwibank, allowing KGHL to drawdown $75.5m provided that the Banking Group does not exceed credit exposure to connected persons of 15% of Tier 1 capital, as required in Kiwibank's banking conditions of registration. When loans are drawn down under the loan agreement the transaction is undertaken at market interest rates. As at 31 December 2019, the balance owed by KGH to the Banking Group was $75.5m (31 December 2018: nil; 30 June 2019: $75.5m). NZP previously had a credit facility with the Banking Group which was fully repaid on 29 March 2019. As at 31 December 2019 the balance of the loan facility owed by NZP to the Banking Group was nil (31 December 2018: $75.8m; 30 June 2019: nil).

Dollars in millions	**Unaudited as at 31/12/19**	Unaudited as at 31/12/18	Audited as at 30/06/19
Outstanding balances			
Due to related parties	**4**	5	9
Included in derivative financial instruments - liabilities	**-**	2	1
Included in deposits and other borrowings	**14**	13	15
Included in subordinated debt	**150**	253	253
Total amounts due to related parties	**168**	273	278
Receivables			
Due from related parties	**79**	82	85
Included in derivative financial instruments - assets	**-**	1	1
Included in loans and advances	**2**	2	2
Total amounts due from related parties	**81**	85	88

The comparative amounts due to related parties at 30 June 2019 have been amended to include an additional $5m exposure to a related party for a deposit held with Kiwibank by an entity that is managed by a subsidiary of KGHL.

17. Fiduciary activities and securitisation

Unaudited

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.

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 Banking Group. 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 Kiwibank and highly rated short-dated securities, together which are security for the guarantee of issuances of covered bonds by the Banking Group, provided by Kiwi Covered Bond Trustee Limited as Trustee of the Covered Bond Trust.

The assets of the Covered Bond Trust are not available to creditors of Kiwibank, although the Banking Group (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 2019 is $316m (31 December 2018: $316m; 30 June 2019: $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 2019, included within Loans and advances to customers on the Banking Group's consolidated balance sheet were housing loans with a carrying value of $1,100m held by the RMBS Trust (31 December 2018: $1,100m; 30 June 2019: $1,100m). 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.

18. Segment analysis

For the purposes of determining reportable operating segments, the chief operating decision-maker has been identified as the Kiwibank Executive Committee ("**EXCO**"), which consists of the Chief Executive Officer and his direct reports. The EXCO 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 they service and the services they provide.

The EXCO 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.

18. Segment analysis continued

A summarised description of each business unit is shown below:

- Personal– Provides banking products and services to the personal banking segment.
- Business – Provides banking products and services to the business sector. Included within the segment are Business and Treasury services.

	Unaudited 6 months ended 31/12/19		
Dollars in millions	Personal markets	Business markets	Total
External revenues	251	26	277
Intersegment revenues	(66)	66	-
Total revenues	185	92	277
Profit before taxation	28	37	65

	Unaudited 6 months ended 31/12/18		
Dollars in millions	Personal markets	Business markets	Total
External revenues	256	17	273
Intersegment revenues	(74)	74	-
Total revenues	182	91	273
Profit before taxation	48	38	86

	Audited year ended 30/06/19		
Dollars in millions	Personal markets	Business markets	Total
External revenues	501	37	538
Intersegment revenues	(140)	140	-
Total revenues	361	177	538
Profit before taxation	80	71	151

19. Risk management

Unaudited

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 2019.

20. 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 items both classified as cash and cash equivalents and those classified as operating assets in the consolidated cash flow statement. Amounts below are presented net of any appropriate haircut where applicable.

Dollars in millions	Unaudited as at 31/12/19
Cash, balances with central bank, and certain foreign currency deposits	510
Certificates of deposit	72
Government bonds and treasury bills	444
Local body stock and bonds	-
Other bonds	488
Total	**1,514**

The Bank also held unencumbered internal residential mortgage backed securities which would entitle the Banking Group to enter into repurchase transactions with a value of NZ$855m at 31 December 2019 (31 December 2018: $855m, 30 June 2019: $855m).

The following table 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.

20. Liquidity continued

The Banking Group does not manage its liquidity risk on the basis of the information provided in the table below.

	Unaudited as at 31/12/19						
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	(141)	-	-	-	-	(141)	(141)
Due to related parties	(4)	-	-	-	-	(4)	(4)
Deposits and other borrowings	(8,118)	(5,367)	(5,283)	(569)	-	(19,337)	(19,217)
Debt securities issued	(45)	(114)	(800)	(1,477)	(180)	(2,616)	(2,463)
Other financial liabilities	(77)	-	-	-	-	(77)	(77)
Lease liabilities	(1)	(2)	(11)	(39)	(42)	(95)	(81)
Subordinated debt	-	-	-	-	(150)	(150)	(150)
Total financial liabilities	(8,386)	(5,483)	(6,094)	(2,085)	(372)	(22,420)	(22,133)
Assets							
Cash and cash equivalents	561	-	-	-	-	561	561
Due from related parties	3	1	2	77	-	83	79
Due from other financial institutions	145	-	101	-	-	246	246
Investment securities	52	133	192	743	25	1,145	1,116
Loans and advances	201	420	1,307	4,732	33,175	39,835	21,523
Other financial assets	20	-	-	-	-	20	20
Total financial assets	982	554	1,602	5,552	33,200	41,890	23,545
Net non-derivative cash flows	(7,404)	(4,929)	(4,492)	3,467	32,828	19,470	1,412
Derivative cash flows - net							
Interest rate derivatives	(5)	-	(27)	-	-	(32)	
Total	(5)	-	(27)	-	-	(32)	
Derivative cash flows - gross							
Foreign exchange derivatives							
Inflow	241	109	482	472	180	1,484	
Outflow	(245)	(111)	(441)	(459)	(187)	(1,443)	
Total	(4)	(2)	41	13	(7)	41	
Off balance sheet cash flows							
Capital commitments	-	(3)	-	-	-	(3)	
Undrawn credit commitments	(3,564)	-	-	-	-	(3,564)	
Total	(3,564)	(3)	-	-	-	(3,567)	
Net cash flows	(10,977)	(4,934)	(4,478)	3,480	32,821	15,912	
Cumulative net cash flows	(10,977)	(15,911)	(20,389)	(16,909)	15,912	15,912	

Notes to the interim financial statements continued

21. Interest repricing

	Unaudited as at 31/12/19						
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	561	61	500	-	-	-	-
Due from related parties	79	3	76	-	-	-	-
Due from other financial institutions	246	-	145	101	-	-	-
Investment securities	1,116	-	204	162	-	365	385
Derivative financial instruments	308	308	-	-	-	-	-
Loans and advances	21,523	70	5,489	2,091	6,140	6,427	1,306
Other financial assets	20	20	-	-	-	-	-
Total financial assets	23,853	462	6,414	2,354	6,140	6,792	1,691
Financial liabilities							
Due to other financial institutions	(141)	(14)	(127)	-	-	-	-
Due to related parties	(4)	(4)	-	-	-	-	-
Deposits and other borrowings	(19,217)	(2,813)	(10,724)	(2,888)	(2,274)	(275)	(243)
Derivative financial instruments	(296)	(296)	-	-	-	-	-
Debt securities issued	(2,463)	-	(694)	(418)	(347)	(43)	(961)
Other financial liabilities	(77)	(77)	-	-	-	-	-
Lease liabilities	(81)	(81)	-	-	-	-	-
Subordinated debt	(150)	-	-	(150)	-	-	-
Total financial liabilities	(22,429)	(3,285)	(11,545)	(3,456)	(2,621)	(318)	(1,204)
On-balance sheet gap	1,424	(2,823)	(5,131)	(1,102)	3,519	6,474	487
Net derivative notional principals	30	-	5,917	(675)	(1,407)	(4,825)	1,020
Net effective interest rate gap	1,454	(2,823)	786	(1,777)	2,112	1,649	1,507

The table above 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.

22. Capital expenditure commitments

Unaudited

Capital expenditure commitments contracted for as at 31 December 2019, but not provided for in these interim financial statements, total $3.1m (31 December 2018: $3.0m; 30 June 2019: $3.1m). The full amount is due within 12 months.

23. Contingent liabilities and credit commitments

Contingent liabilities

The Bank has uncovered disclosure issues in relation to the Credit Contracts and Consumer Finance Act and has proactively discussed these with the Commerce Commission. At this stage, the possible impact of the Commission's position cannot be determined with any certainty (31 December 2018: nil; 30 June 2019: as above).

Undrawn credit commitments as at the reporting date are as follows:

Dollars in millions	Unaudited as at 31/12/19	Unaudited as at 31/12/18	Audited as at 30/06/19
Letters of credit and performance-related contingencies	**57**	20	48
Loan commitments	**3,507**	3,184	3,363
Total undrawn credit commitments	**3,564**	**3,204**	**3,411**

The comparative prior period amounts above for 31 December 2018 have been corrected to include an additional $10m related to letters of credit and the amounts have been reclassified to align with the categories used in the current period's presentation.

24. Contingent assets

Unaudited

The Banking Group held insurance policies at the date of the Kaikoura earthquake that provided cover for Material Damage and Business Interruption. It is probable that the policies will enable the Banking Group to obtain a further reimbursement for various costs incurred as a result of the earthquake however there is insufficient information to form a reliable estimate of the financial effect.

25. Changes in accounting policies

Unaudited

This note explains the nature and effect of the changes in accounting policies for the Banking Group due to the adoption of NZ IFRS 16 *Leases* from 1 July 2019.

IMPACT OF ADOPTION OF NEW ACCOUNTING STANDARDS ON THE FINANCIAL STATEMENTS

NZ IFRS 16: *Leases*

Summary

NZ IFRS 16 *Leases* replaced guidance in NZ IAS 17 *Leases* and introduced a single, on-balance sheet accounting model for lessees that requires a lessee to recognise its right to use underlying leased assets as a right-of-use asset, and an obligation to make lease payments as a lease liability for all leases. There are recognition exemptions for short-term leases and leases of low-value items. The asset and liability are initially measured at the present value of non-cancellable lease payments and payments to be made in optional periods where it is reasonably certain that the option will be exercised.

NZ IFRS 16 has an impact on the accounting treatment of leases within operating expenses disclosed in the Banking Group's income statement. Lease payments that were previously recognised as expenses on a straight-line basis over the term of a lease have been replaced by a depreciation expense on the right-of-use asset and financing costs calculated on the outstanding balance of the lease liability that are included within interest expense in the income statement.

Depreciation and interest expense are expected to be higher in the near term than the equivalent lease expenses under NZ IAS 17. This will result in changes in certain expense and profit measures. The Banking Group's cash flow statement has also been impacted by the principal portion of the lease payments being reported as part of cash flows from financing activities rather than cash flows from operating activities.

Impact of transition

On adoption of NZ IFRS 16, the Banking Group recognised lease liabilities in relation to leases which had previously been classified as 'operating leases' under NZ IAS 17. These liabilities were measured at the present value of the remaining lease payments, discounted using the incremental borrowing rate as of 1 July 2019.

As permitted by the standard, the Banking Group measured the right-of-use asset at an amount equal to the lease liability on a lease-by-lease basis. The Banking Group has also elected not to reassess whether a contract is, or contains a lease, at the date of initial application.

25. Changes in accounting policies continued

The impact of transitional adjustments resulting from the adoption of NZ IFRS 16 have been applied retrospectively by adjusting the opening balance of right-of-use assets, lease liabilities, deferred taxation, other assets, other liabilities and reserves. The Banking Group has not restated comparatives as permitted by the standard. The change in accounting policy affected the following items in the balance sheet on 1 July 2019:

- Right-of-use assets – increase by $83.6m
- Deferred taxation – decrease by $0.3m
- Other assets – decrease by $1.4m
- Lease liabilities – increase by $83.6m
- Other liabilities – decrease by $2.5m
- Reserves – increase by $0.8m

The following table is an extract of the financial statements summarising each financial statement line item that was adjusted on 1 July 2019 upon adoption of NZ IFRS 16 *Leases*.

Dollars in millions	Audited 30/06/19	Transitional adjustments	Unaudited 1/07/2019
Assets			
Right-of-use assets	-	84	84
Deferred taxation	21	-	21
Other assets	34	(1)	33
Total assets	22,734	83	22,817
Liabilities			
Lease liabilities	-	84	84
Other liabilities	102	(2)	100
Total liabilities	21,185	82	21,267
Shareholder's equity			
Reserves	812	1	813
Total shareholder's equity	1,549	1	1,550
Total liabilities and shareholder's equity	22,734	83	22,817

Leasing activities

The Banking Group leases various office sites, branch sites, ATM sites and vehicles. The majority of leases are for branch and office property leases. Rental contracts are typically made for fixed periods but may have extension options. Lease terms are generally negotiated on an individual basis for property leases and on a group basis for vehicle leases.

The Banking Group also subleases a portion of certain shared sites to NZ Post. The subleasing income is recognised in the income statement. The Banking Group is not party to any finance leases.

Key judgements made by management

NZ IFRS 16 involves a greater use of judgement than the previous approach to accounting for leases under NZ IAS 17. The key judgements for the Banking Group are assessing whether an arrangement contains a lease, determining the terms of lease contracts with renewal and termination options and, the method applied to calculating Incremental Borrowing Rates that are used to discount future lease payments to present value in calculating the lease liability for each lease. The latter two are considered areas of significant judgement and are explained in more detail below.

Determining the terms of lease contracts

The Banking Group determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised. The Banking Group has a number of leases with extension and termination options and exercises judgement in evaluating whether it is reasonably certain whether or not to exercise the option to renew or terminate each lease. All relevant factors that create an economic incentive to exercise an option to extend or terminate a lease are considered including, but not limited to:

25. Changes in accounting policies continued

- The relevant cost of lease payments at the time of the option vs expected market rates;
- The cost of the relevant leasehold improvements and their carrying value;
- The cost of terminating and relocating; and
- The importance of the underlying leased asset to the Banking Group.

Calculating Incremental Borrowing Rates

Where the Banking Group cannot readily determine the interest rate implicit in the lease, it uses its incremental borrowing rate ("IBR") to discount future payments in measuring lease liabilities. The IBR is the rate of interest that the Banking Group would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore requires estimation when no observable rates are available or when adjustments are required to reflect the terms and conditions of the lease. The Banking Group estimates the IBR for each lease using observable inputs (such as market interest rates) when available.

The Banking Group's weighted average incremental borrowing rate applied to calculate lease liabilities on 1 July 2019 was 2.87%.

Practical expedients applied

The Banking Group applied the following practical expedients in applying NZ IFRS 16 for the first time as permitted by the standard:

- Certain leases with a remaining lease term of less than 12 months as at 1 July 2019 were treated as short-term leases
- Certain initial direct costs were excluded for the measurement of the right-of-use asset at the date of initial application
- Hindsight was used in determining the lease term where the contract contains options to extend or terminate the lease upon adoption

Reconciliation of closing operating lease commitments to opening lease liability

Dollars in millions	Unaudited 31/12/19
Operating lease commitments as at 30 June 2019	93.5
Discounted using the lessee's incremental borrowing rate at 1 July 2019	78.8
Add/(deduct):	
Short-term leases not recognised as a liability	(0.1)
Low-value leases not recognised as a liability	-
Adjustments as a result of different treatment of extension and termination options	4.9
Lease liability recognised as at 1 July 2019	**83.6**

Current period movement in right-of-use assets and lease liabilities

Dollars in millions	Unaudited 6 months ended 31/12/19
Opening lease liabilities (recognised upon adoption)	84
Additions and adjustments	3
Amortisation	(6)
Total lease liabilities as at 31 December 2019	**81**

Dollars in millions	Unaudited 6 months ended 31/12/19
Opening right-of-use assets (recognised upon adoption)	84
Additions and adjustments	3
Depreciation	(7)
Total right-of-use assets as at 31 December 2019	**80**

26. Events subsequent to the reporting date

Unaudited

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

Capital adequacy and regulatory liquidity ratios

Unaudited

The "**Banking Group**" consists of Kiwibank Limited ("**Kiwibank**" or the "**Bank**") 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, calculated 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 capital bonds

The Perpetual capital bonds, issued by the Bank on 27 May 2015, and which are fully paid, are included within Additional Tier 1 capital. The Perpetual capital 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 capital bonds constitute direct, perpetual, convertible, non-cumulative, unsecured, subordinated debt securities issued by Kiwibank;

b) interest on the Perpetual capital 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 capital 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 capital bonds do not have a maturity date, however, after obtaining the consent of the RBNZ, Kiwibank may elect to make early repayment on 27 May 2020 or any reset date thereafter (reset dates occur at 5-yearly intervals, commencing on 27 May 2020) or if a tax or regulatory event has occurred (as described in the Deed Poll); and

f) the Perpetual capital 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.

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.
- Market risk - The vulnerability of earnings to movements in interest rates, foreign currency and equity prices.
- Operational risk - The risk of loss, resulting from inadequate or failed internal processes (including legal risks), people and systems and from external events.

The capital requirements for these risk classes are calculated following the standardised risk measurement methodologies contained in 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.

Capital adequacy and regulatory liquidity ratios
continued

Unaudited

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 December 2019. Throughout the period Kiwibank and the Banking Group complied with both regulatory and internal capital adequacy requirements.

Regulatory capital ratios

		The Banking Group		
	Regulatory Minima	31/12/19	31/12/18	30/06/19
Capital adequacy ratios				
Common Equity Tier 1 capital ratio	**4.5%**	**12.0%**	13.0%	12.4%
Tier 1 capital ratio	**6.0%**	**13.2%**	14.4%	13.7%
Total capital ratio	**8.0%**	**13.2%**	15.3%	14.5%
Buffer ratios				
Buffer ratio	**2.5%**	**5.2%**	7.3%	6.5%

	Kiwibank Limited		
	31/12/19	31/12/18	30/06/19
Capital adequacy ratios			
Common Equity Tier 1 capital ratio	**11.7%**	12.5%	12.1%
Tier 1 capital ratio	**12.8%**	13.8%	13.3%
Total capital ratio	**12.8%**	14.6%	14.1%

Capital adequacy and regulatory liquidity ratios
continued

Unaudited

Regulatory capital

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

Dollars in millions	The Banking Group 31/12/19	31/12/18	30/06/19
Common Equity Tier 1 capital			
Issued and fully paid up share capital	**737**	737	737
Retained earnings (net of appropriations)	**859**	794	823
Accumulated other comprehensive income and other disclosed reserves [1, 2]	**(7)**	(3)	(11)
Less deductions from Common Equity Tier 1 capital			
Intangible assets	**(64)**	(81)	(74)
Cash flow hedge reserve	**13**	10	22
Deferred tax assets	**(19)**	(15)	(21)
Receivables from affiliated insurance group and other adjustments	**(2)**	(1)	(1)
Total Common Equity Tier 1 capital	**1,517**	1,441	1,475
Additional Tier 1 capital			
Perpetual capital bonds [3]	**150**	149	149
Total Additional Tier 1 capital	**150**	149	149
Total Tier 1 capital	**1,667**	1,590	1,624
Tier 2 capital			
Subordinated debt	**-**	100	100
Total Tier 2 capital	**-**	100	100
Total capital	**1,667**	1,690	1,724

[1] Includes fair value reserve of $6m. The fair value reserve includes the cumulative net change in the fair value of investment securities until the investment is derecognised or impaired.

[2] Includes cash flow hedge reserve of ($13m). 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] Perpetual capital bonds issued by Kiwibank Limited are classified as debt of the Banking Group for financial reporting purposes.

Capital adequacy and regulatory liquidity ratios
continued

Unaudited

On-balance sheet exposures

	31/12/19			
Dollars in millions	Total exposure after credit risk mitigation	Risk weight	Risk weighted exposure	Minimum Pillar I capital requirement
On-balance sheet exposures				
Cash and gold bullion	61	0%	-	-
Sovereigns and central banks	1,029	0%	-	-
Multilateral development banks and other international organisations	326	0%	-	-
Public sector entities	-	20%	-	-
	-	100%	-	-
Banks	384	20%	77	6
	101	50%	51	4
Corporate	18	20%	4	-
	5	50%	3	-
	1,417	100%	1,417	113
Non-property investment residential mortgage loans				
<= 80% loan to value ratio ("LVR")	11,202	35%	3,921	314
80 <= 90% LVR	1,088	50%	544	44
90 <= 100% LVR	32	75%	24	2
> 100% LVR	184	100%	184	15
Non-property investment residential mortgage loans - Welcome home loans and lenders mortgage insured loans				
<= 80% LVR	303	35%	106	8
80 <= 90% LVR	386	35%	135	11
90 <= 100% LVR	19	50%	10	1
Property investment residential mortgage loans				
<= 80% LVR	6,230	40%	2,492	199
80 <= 90% LVR	77	70%	54	4
90 <= 100% LVR	37	90%	33	3
> 100% LVR	33	100%	33	3
Property investment residential mortgage loans - Welcome home loans and lenders mortgage insured loans				
<= 80% LVR	26	40%	10	1
80 <= 90% LVR	1	50%	1	-
Impaired assets	1	100%	1	-
Past due residential mortgages greater than 90 days	1	35%	-	-
	7	100%	7	1
Other past due assets	2	150%	3	-
Non-risk-weighted assets	391	0%	-	-
All other equity holdings (not deducted from capital)	-	400%	1	-
Other assets	725	100%	725	58
Total on-balance sheet exposures	24,086		9,836	787

Capital adequacy and regulatory liquidity ratios
continued

Unaudited

Off-balance sheet exposures and market related exposures

	31/12/19					
Dollars in millions	Total exposure	Credit conversion factor	Credit equivalent amount	Average risk weight	Risk weighted exposure	Minimum Pillar I capital requirement
Direct credit substitute	47	100%	47	99%	47	4
Performance-related contingency	10	50%	5	100%	5	-
Other commitments where original maturity is greater than one year	2,512	50%	1,256	48%	603	48
Other commitments where original maturity is less than or equal to one year	-	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	995	0%	-	-	-	-
Market related contracts: [1]						
(a) Foreign exchange contracts	1,303	n/a	100	43%	43	3
(b) Interest rate contracts	20,945	n/a	315	37%	117	9
(c) Credit Valuation Adjustment					102	8
Total off-balance sheet exposures	25,812		1,723		917	72

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

Residential mortgages by loan-to-value ratio

	31/12/19		
Dollars in millions	On-balance sheet	Off-balance sheet	Total
LVR 0% - 80%	17,768	982	18,750
LVR 80% - 90%	1,553	45	1,598
LVR 90% +	306	23	329
Total	19,627	1,050	20,677

The LVR classification above is calculated in compliance with the Order.

At 31 December 2019, of the loans with an LVR greater than 80%, $394m relates to "Welcome Home" loans, whose credit risk is mitigated by the New Zealand Crown (via underwriting by Housing New Zealand Corporation).

Capital adequacy and regulatory liquidity ratios
continued

Unaudited

Reconciliation of residential mortgage-related amounts

Dollars in millions	31/12/19
Residential mortgages total on-balance sheet exposures	19,627
Collective allowance for impairment	14
Deferred arrangement fees	84
Gross residential mortgage loans per asset quality (note 5)	**19,725**
Residentially secured lending included within 'Other term lending'	(926)
Gross 'term loans - housing' per loans and advances (note 4)	**18,799**

Credit risk mitigation

	31/12/19			
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
Bank	(21,728)	-	(193)	(15)
	(21,728)	-	(193)	(15)

Operational risk

	31/12/19	
Dollars in millions	Implied risk weighted exposure	Total operational risk capital requirement
Operational risk	1,419	114

Market risk

	31/12/19			
	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	677	782	54	63
- of which relates to trading book	25	33	2	3
Foreign currency risk	12	22	1	2
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 for each market risk category.

Capital adequacy and regulatory liquidity ratios
continued

Unaudited

Total capital requirements

Dollars in millions	31/12/19 Total exposure after credit risk mitigation	Risk weighted exposure or implied risk weighted exposure	Total capital requirement
Total credit risk plus equity	28,170	10,560	844
Operational risk	n/a	1,419	114
Market risk	n/a	689	55
Total Pillar I risk	**n/a**	**12,668**	**1,013**

Other material risk (Pillar II)

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), including:

- 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.
- Other risks – Including conduct and culture, project execution, and cyber risks.

The Bank has made an internal capital allocation of $63m (31 December 2018: $60m; 30 June 2019: $63m).

Regulatory liquidity ratios

The Bank calculates regulatory liquidity ratios in accordance with the RBNZ's 'Liquidity Policy' (BS13). Ratios are calculated daily and the quarterly average of the daily ratios are disclosed below.

	Three months ended 31/12/19	Three months ended 30/9/2019
Average one-week mismatch ratio	7.5%	7.8%
Average one-month mismatch ratio	7.5%	8.0%
Average core funding ratio	90.1%	88.4%

Independent review report

To the readers of Kiwibank Limited's Disclosure Statement for the six months ended 31 December 2019 (the "Disclosure Statement").

The Auditor-General is the auditor of Kiwibank Limited (the "Bank") and the entities it controlled as at 31 December 2019 or from time-to-time during the six months ended on that date (the "Banking Group"). The Auditor-General has appointed me, Michele Embling, using the staff and resources of PricewaterhouseCoopers, to carry out the annual audit of the Bank and the Banking Group, on his behalf.

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

- interim financial statements of the Banking Group on pages 5 to 39 which comprise the balance sheet as at 31 December 2019, the income statement, the statement of comprehensive income, the statement of changes in equity and the cash flow statement for the six months ended on that date, and a summary of significant accounting policies 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 2019 (the "supplementary information") and included in the balance sheet and notes 2, 5, 6, 12, 13, 17, 19, 20 and 21 of the financial statements and on pages 40 to 46.

Review conclusion

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

- the interim financial statements (excluding the supplementary information) of the Banking Group are not prepared, in all material respects, in accordance with New Zealand Equivalent to International Accounting Standard 34: *Interim Financial Reporting* (NZ IAS 34) and International Accounting Standard 34: *Interim Financial Reporting* (IAS 34);

- the supplementary information (excluding the supplementary information relating to capital adequacy and regulatory liquidity requirements) 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 and regulatory liquidity requirements disclosed on pages 40 to 46 is not, in all material respects, disclosed in accordance with Schedule 9 of the Order.

The review was completed on 19 February 2020, and this is the date at which our review conclusion is expressed.

Responsibilities of the Directors

The Directors of Kiwibank Limited (the "Directors") are responsible on behalf of the Bank for the preparation and presentation of the Disclosure Statement, which includes interim financial statements in accordance with Clause 25 of the Order.

PricewaterhouseCoopers, PwC Centre, 10 Waterloo Quay, PO Box 243, Wellington 6140, New Zealand
T: +64 4 462 7000, F: +64 4 462 7001, pwc.co.nz

The Directors are also responsible for such internal control as the Directors determine is necessary to enable the preparation of the 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 the supplementary information in the 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.

Our responsibility

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

- *on the interim financial statements (excluding the supplementary information):*
  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 NZ IAS 34 and IAS 34;

- *on the supplementary information (excluding the supplementary information relating to capital adequacy and regulatory liquidity requirements):*
  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; and

- *on the supplementary information relating to capital adequacy and regulatory liquidity requirements:*
  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 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 in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand). Accordingly, we do not express an audit opinion on the interim financial statements or on the supplementary information.

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

In addition to the review, we have carried out agreed upon procedures engagements, provided whistle-blower services and have been engaged to undertake compliance assurance engagement which are compatible with those independence requirements. 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. Other than the review, these engagements and dealings in the ordinary course of trading activities of the Bank and the Banking Group, we have no relationship with or interests in the Bank or the Banking Group.

Michele Embling
On behalf of the Auditor-General
Wellington, New Zealand

PricewaterhouseCoopers