

CREDIT RISK MANAGEMENT MERRILL LYNCH PRESENTATION

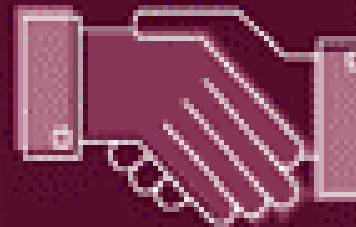
29 November 2002

> profitability

> asset quality

> support

> dynamic credit



Credit Risk Management

Overview

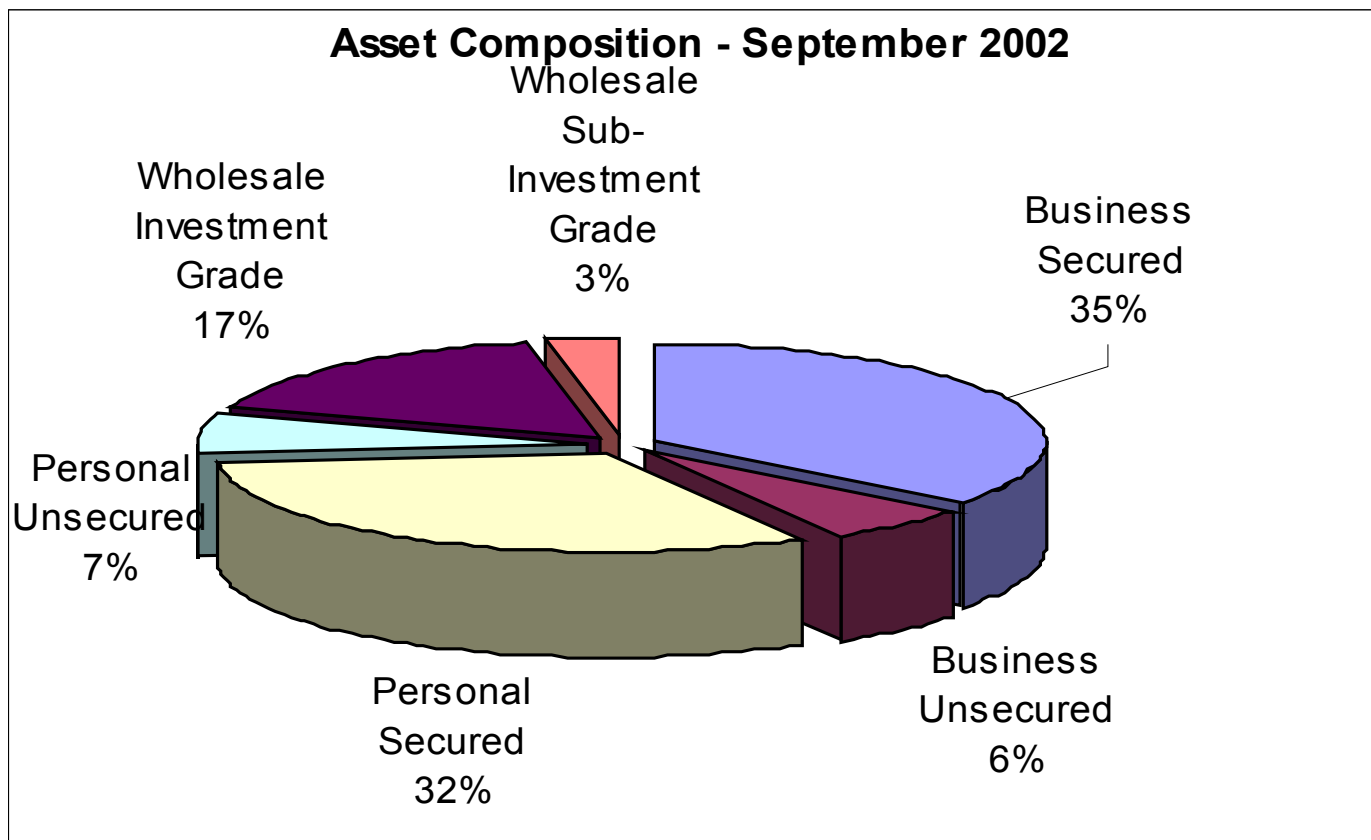
FYE 2002 presented some unique challenges:

- Spill-over effects of September 11;
- Managing the “fallen angels” phenomena
- General uncertainty with respect to the credit environment;
- On-going need for Banks to achieve a better balance between risk and return

Against this background the Group has achieved:

- Good earnings growth but not at the expense of Asset quality;
- Asset quality remains strong;
- Stressing testing of housing indicates risks are within acceptable bounds

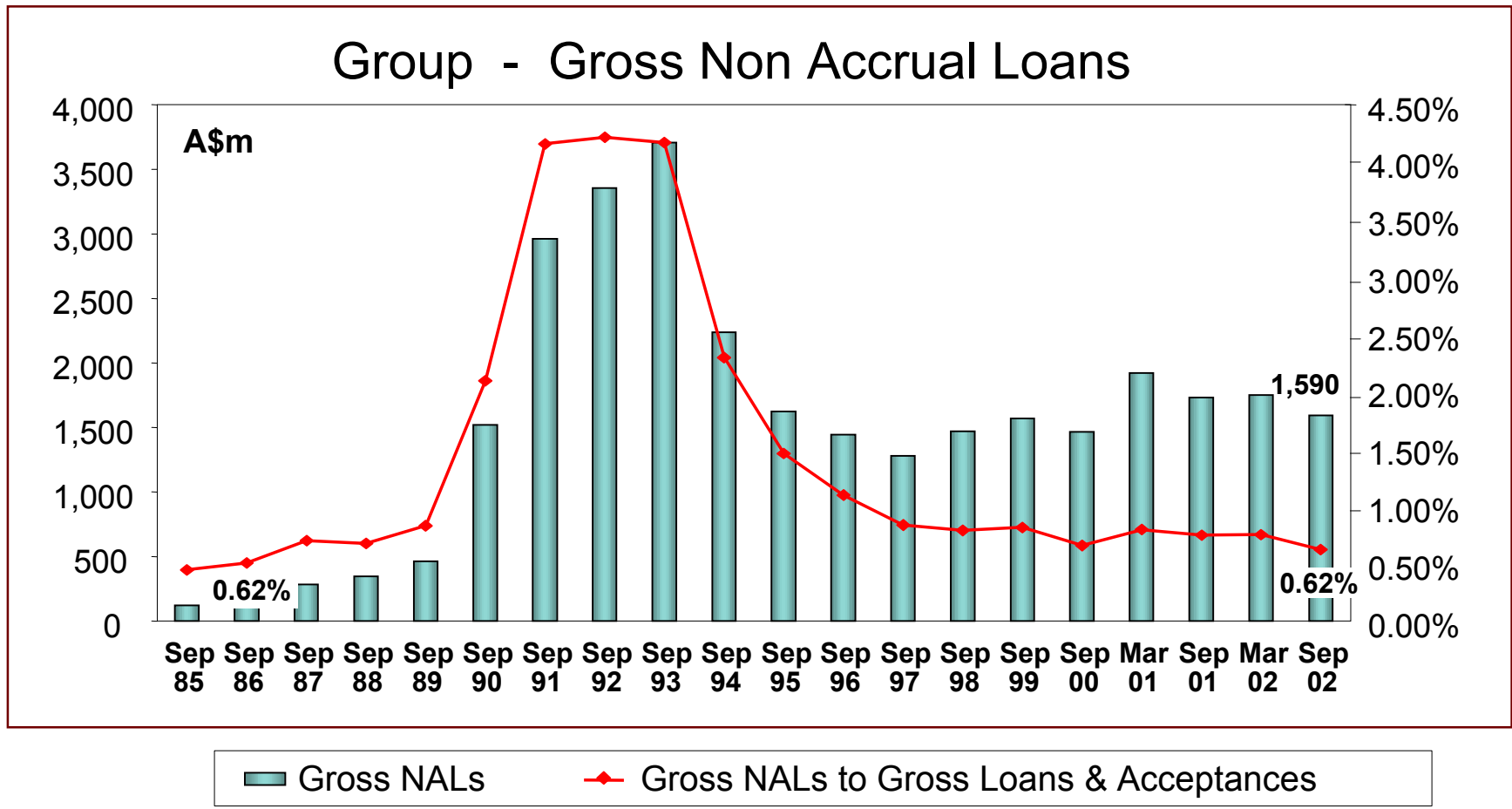
Portfolio Composition by Security / Rating Grade



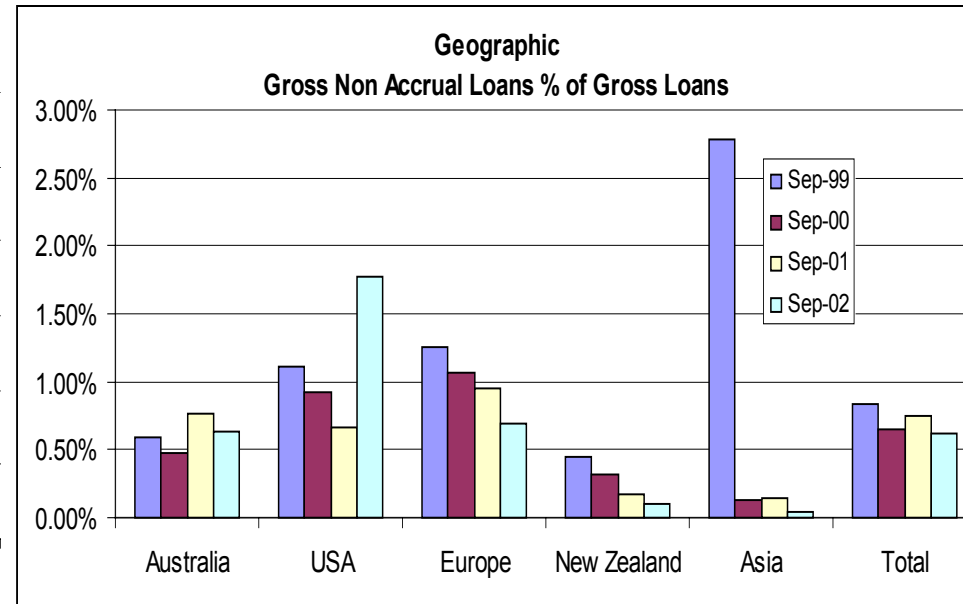
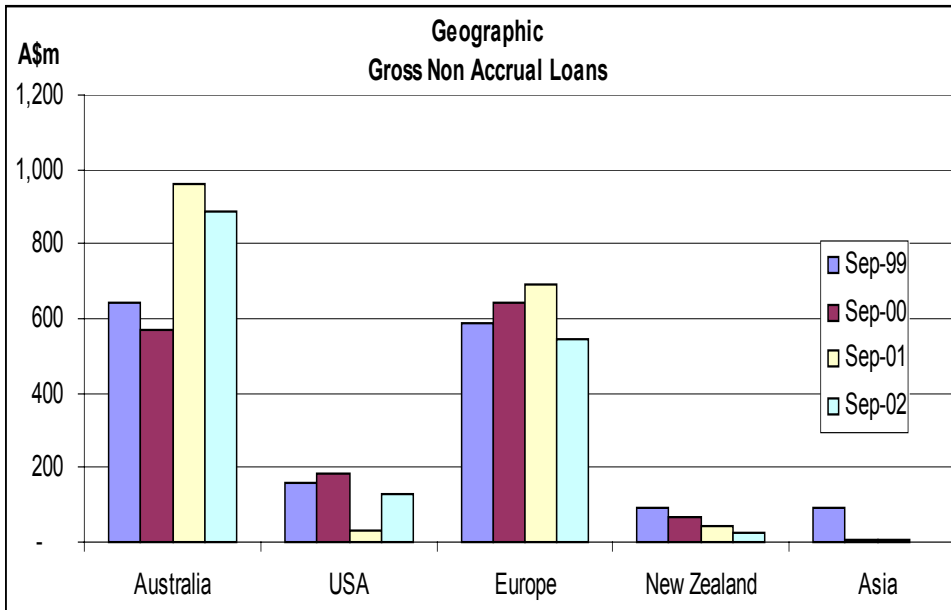
- The National's book is predominantly concentrated in investment grade; and
- Well secured



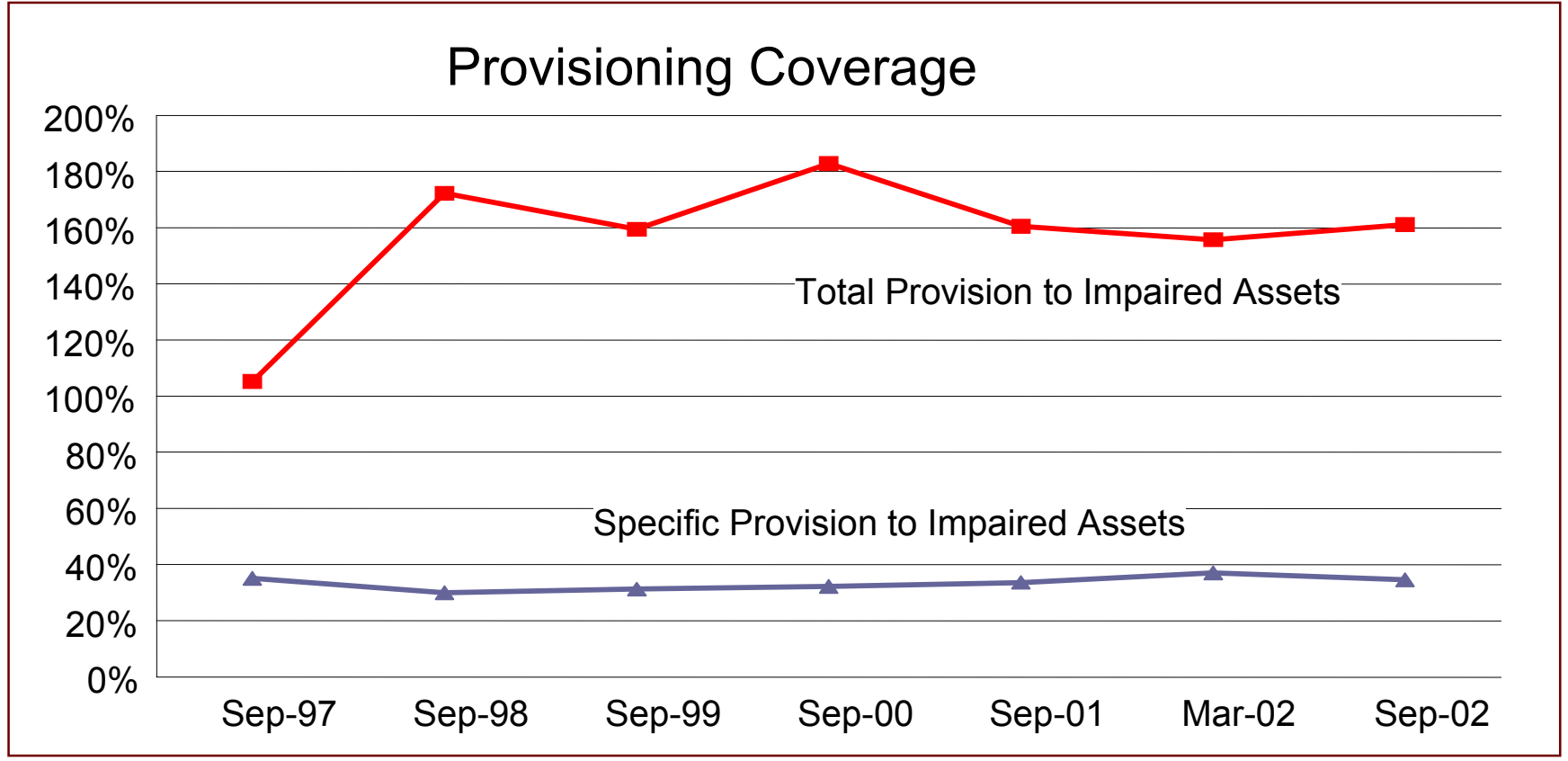
Gross Non Accrual Loans



Gross Non Accrual Loans by Geography

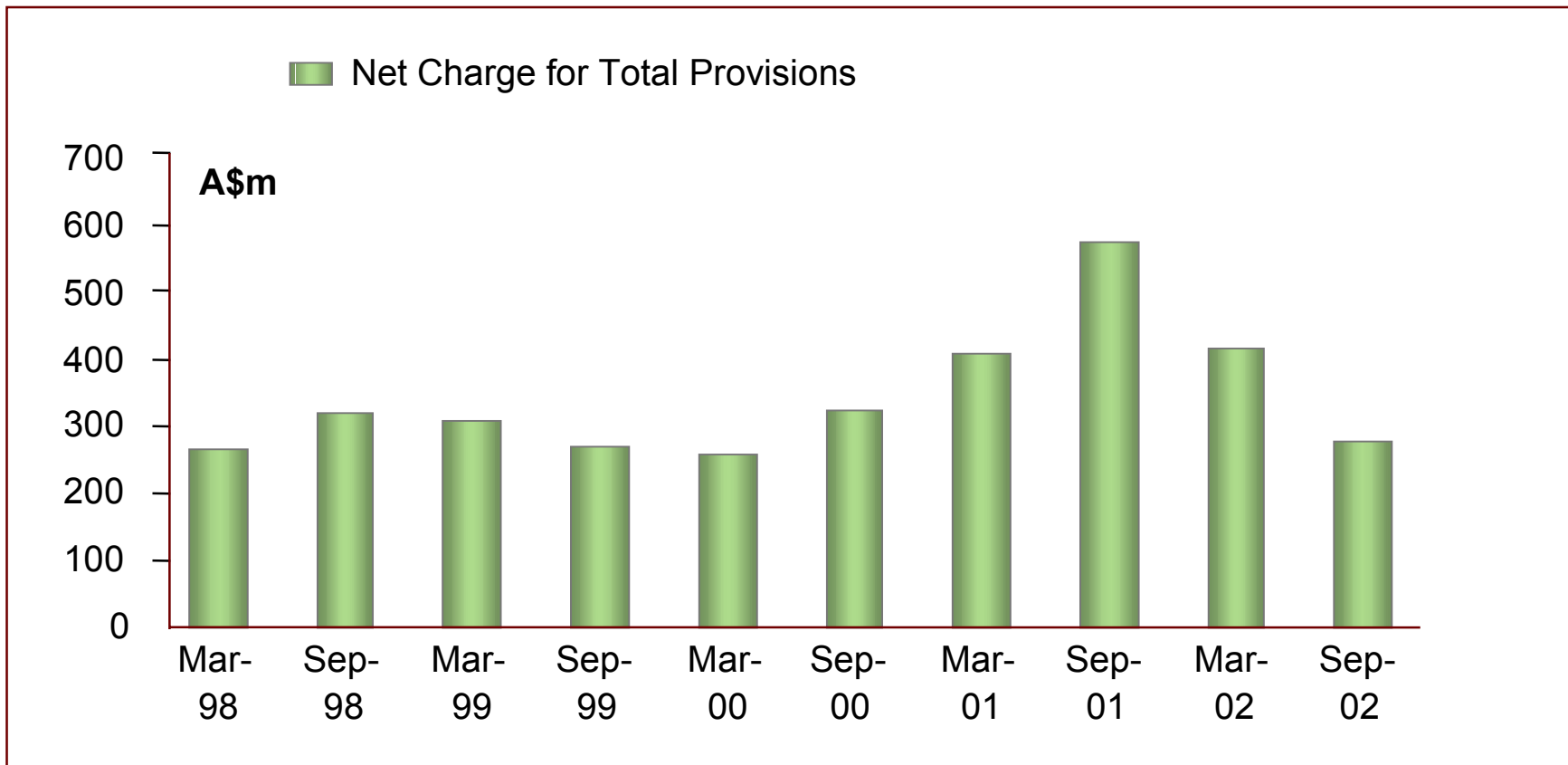


Coverage Ratios





Provision Charges - Half Yearly Periods



Statistical Provisioning Principles

Background

Statistically-based provisioning is an approach to establishing a general loan loss provision. Key feature of provision:

- Established at the outset of the transaction,
- Reassessed and re-calculated monthly, and
- Able to be used to fund the creation of specific provisions if and when a exposure is classified as non-accrual.

Key points:

- Provides an unambiguous signal to external stake-holders of the Group's asset quality and
- Statistical provisioning affects only the timing of the recognition of loan losses.

Statistical Provisioning

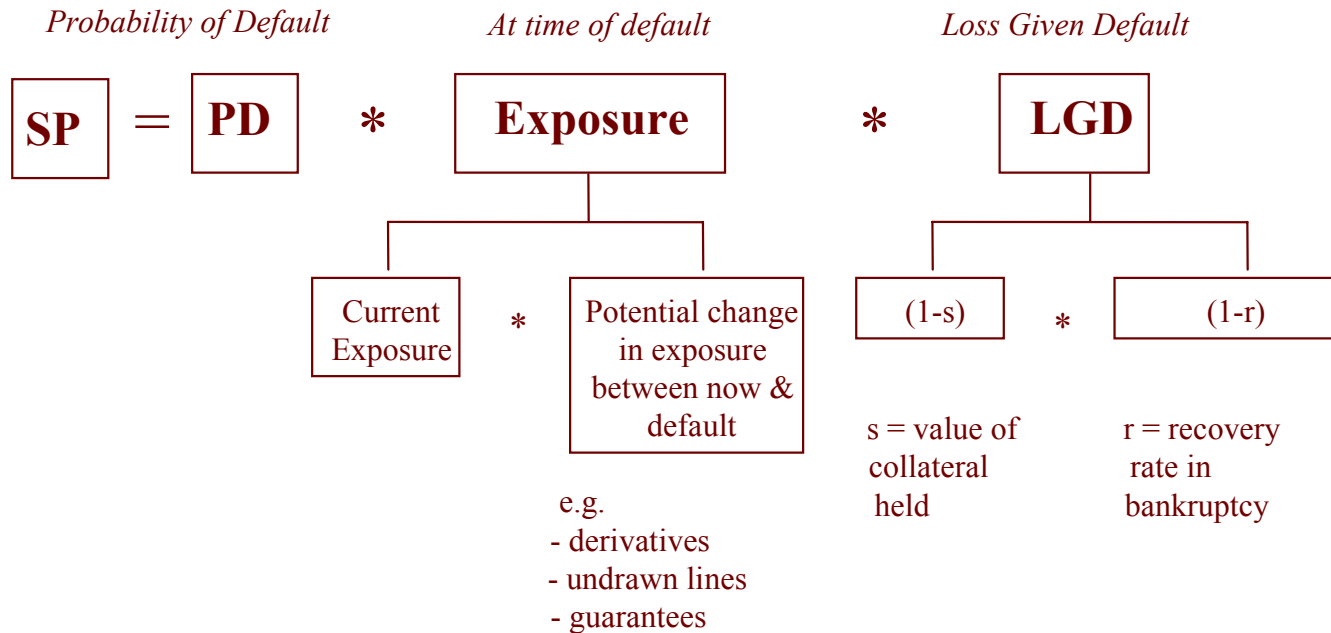
Key Principles

- Lending Assets should reflect their expected net realisable value;
 - This means that deducting “expected loss” from outstanding
 - From a statistical perspective “expected loss” captures the inherent credit risk on the balance sheet and is the required provision
 - The calculation of expected loss based on actual losses of the Group and the various legal entities therein
- Disclosure of lending assets on a net expected realisable value basis:
 - makes the Group’s asset quality more **transparent**; and
 - internally drives behaviours that **improves shareholder value**

Statistical Provisioning

Statistical Provision (SP) is calculated based on the following:

Key drivers of Statistical Provisioning:



- Credit Exposure of the borrower
- Credit rating of the borrower (drives PD)
- Lending category (drives LGD)
- Term to maturity of the loan
- Calculated monthly

Early Warning System

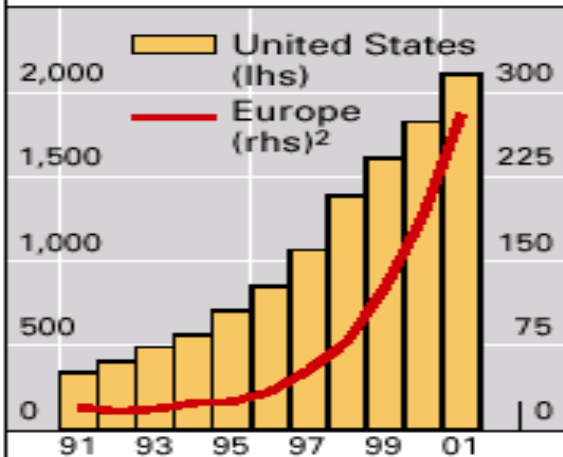
- EWS tool was developed 2 years ago to identify probability of default/impairment through Overdraft/Current Account behavioural activity trends of Business & Agribusiness Accounts >\$250k (not Wholesale or Corporate) in Australia
- Files are Stress Tested for Interest Cover, Sales, Gross Margin and Payback period
- EWS has demonstrated value in isolating potential impaired accounts - the number of EWS accounts has reduced by approx. 40% in the last 2 years.
- Business Financial Services Australia has established a Portfolio Review Team to support the proactive management of EWS accounts
- EWS will be introduced in Europe & New Zealand in 2003

Transfer of credit risk has occurred in global banking

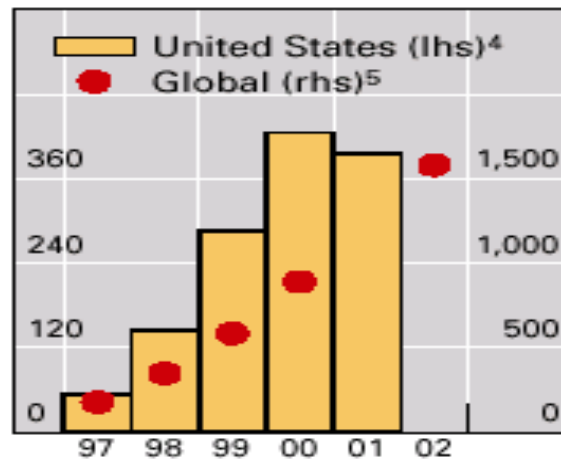
Indicators of credit risk transfer

In billions of US dollars

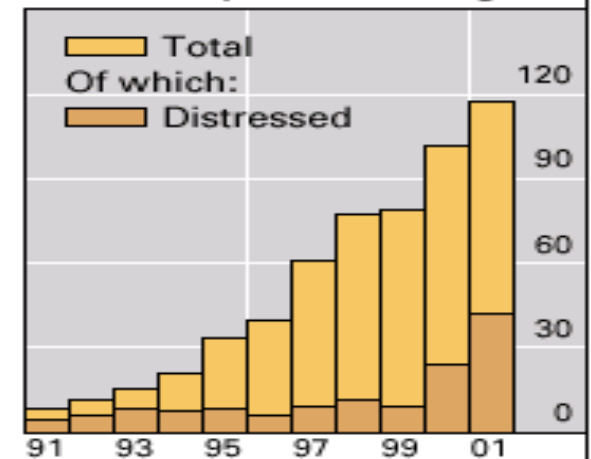
Asset-backed securities¹



Credit derivatives³



Secondary loan trading⁶



¹ Amounts outstanding. ² International bonds. ³ Notional amounts outstanding. ⁴ Commercial banks. ⁵ Market participants' estimates (BBA surveys of 1998 and 2000); for 2002, forecast. ⁶ Global; turnover data.
Sources: Board of Governors of the Federal Reserve System, *Flow of Funds Accounts*; US Office of the Comptroller of the Currency; British Bankers' Association (BBA); Loan Pricing Corporation; BIS.

Graph VII.8