RESULTS FOR THE YEAR ENDED 30 SEPTEMBER 2004

GROUP PERFORMANCE OVERVIEW

OVERVIEW [1]

Group performance

Year to 30 September 2004

Whilst economic conditions were reasonable in each of the National's markets, the Group result for the year was poor.

Cash earnings before significant items of $3,461 million decreased 15.0% from the prior year result of $4,070 million. The strength of the Australian dollar has reduced the contribution from offshore operations and this has particularly affected earnings in Australian dollar terms from Financial Services Europe and Corporate & Institutional Banking. At constant exchange rates, cash earnings before significant items decreased 13.0%.

Performance was impacted by a range of factors with a deterioration in underlying operating performance in major areas of the business:

- a 6.6% decline in earnings for Australia;
- a 32.9% decline in earnings for Europe;
- a 29.5% decline in earnings for Corporate & Institutional Banking (excluding the foreign currency options trading losses, which are shown as a significant item).

Further details are discussed below.

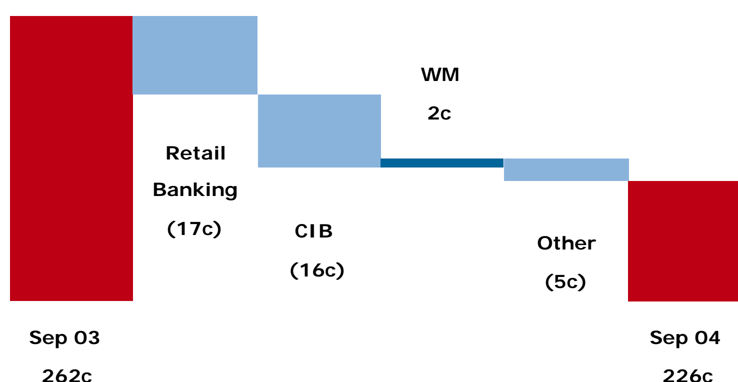
Net profit attributable to members of the Company of $3,177 million was 19.7% below the prior year. This included a breakeven Wealth Management revaluation outcome compared with the prior year loss of $200 million.

Cash earnings after significant items of $3,077 million was 24.4% below the prior year. This included the following (after-tax) significant items which resulted in a loss of $384 million:

- foreign currency options trading loss $(252) million;
- writedown of impaired application software $(307) million;
- increase in the general provision for doubtful debts of $(204) million;
- profit on sale of strategic shareholdings $315 million; and
- reversal of HomeSide provision $64 million.

Diluted cash earnings per share before significant items decreased 36 cents (13.8%) from 262 cents to 226 cents.

Diluted cash earnings per share before significant items (cents)



The full year dividend has increased 3 cents to 166 cents per share compared with the prior year and will be 100% franked.

The major components of the result, discussed further below, are:

- a 16.5% deterioration in cash earnings from Total Banking; and
- a 9.4% improvement in Wealth Management's results (before revaluation profit/loss).

[1] *Unless otherwise specified, the discussion on the following three pages relates to results before significant items. For a reconciliation to net profit refer to page 9.*

Half year to 30 September 2004

Cash earnings before significant items of $1,611 million decreased 12.9% on the March half year. This was consistent with the guidance provided to the market in July 2004 when the Group advised that September half cash earnings were expected to be 10% to 15% lower than the March half.

Total Banking cash earnings were 12.0% lower and Wealth Management operating profit after tax was 14.9% lower than the March half. In line with the full year results, the major second half performance deteriorations were in Australia, Europe and Corporate & Institutional Banking.

Cash earnings after significant items of $1,100 million for the half year were 44.4% lower than the March half.

The September half included a $307 million after-tax writedown of impaired application software and a $204 million after-tax charge to provide for doubtful debts which have been classified as significant items, compared with significant items in the March half of positive $127 million.

Banking performance

Total Banking includes Retail Banking, Corporate & Institutional Banking and Other (including Group Funding & Corporate Centre). It excludes Wealth Management.

Banking operations generated $3,239 million of total Group cash earnings, a decrease of 16.5% on the prior year, or 13.3% at constant exchange rates. Income decreased by 1.7% with a flat outcome for Retail Banking and a 7.4% reduction in Corporate & Institutional Banking. Expense growth was excessive, as pension fund expenses, particularly in Europe, grew significantly and other expenses grew 8.1%. The charge to provide for doubtful debts was 9.3% lower due to a decline in specific provisions and flat general provisions.

Banking cash earnings decreased 12.0% on the March 2004 half year. At constant exchange rates cash earnings decreased 13.6%. This also reflected lower income levels and higher expenses, partly offset by lower specific provisioning charges.

The 2004 efficiency targets established under Positioning for Growth (PfG) are set out below.

		Half Year to		
Cost to income ratio by banking division	**2004 Target**	**Sep 04 %**	**Mar 04 %**	**Sep 03 %**
Financial Services Australia	46.0	**50.8**	45.0	45.8
Financial Services Europe (excluding pension costs)	48.0	**59.8**	55.1	51.4
Financial Services Europe (including pension costs)		**65.5**	61.5	54.7
Financial Services New Zealand	48.0	**50.8**	49.6	49.7
Corporate & Institutional Banking	36.0	**60.3**	41.4	38.7
Total Banking (including pension fund expense)		**57.3**	50.9	49.6

This clearly represents an unsatisfactory performance. The move to a regional structure is in part a response to this, and is designed to create clearer accountability for the end-to-end value chain aligned to a customer perspective, resulting in improved revenue and cost performance.

Wealth Management performance

Wealth Management reported an operating profit of $409 million growing 9.4% from the 2003 year. This result was underpinned by the performance of both the Insurance business up 11.8% and the Investments business up 33.1%. Average funds under management and administration grew $8.1 billion, or 11.9%, over the year, reflecting improved investment market conditions and strong wholesale sales, which offset more subdued retail sales in Australia. Improved equity market performance contributed to higher earnings on shareholders' retained profits and capital. However, overall results were depressed by prior year adjustments of $50 million, primarily in the second half of the year.

Wealth Management efficiency targets	2004 Target	Year to Sep 04	Year to Sep 03
Cost to premium income ratio (%) [1]	21	**18**	20
Cost to funds under management (basis points) [2]	65	**56**	60

(1) *Excludes volume-related expenses*

(2) *Excludes the NAFiM investor compensation and enforceable undertakings and volume-related expenses.*

Regional performance

Full year cash earnings for Australia were down 6.6%, with Retail Banking flat, Corporate & Institutional Banking down 14.9%, Wealth Management up 11.0% and increased deficits in Group Funding and Corporate Centre. In the September half, results in Retail Banking and Corporate & Institutional Banking continued to decline and Wealth Management was adversely impacted by a $40 million prior year adjustment impacting policyholder liabilities.

European cash earnings declined 32.9% (26.8% before exchange rate movements) from the previous year. Retail Banking income levels fell (primarily in the first half) and costs increased with the impact of defined benefit pension fund expense growth, investment in the business and regulatory projects. Corporate & Institutional Banking results deteriorated significantly, particularly in the second half, with lower Markets risk and trading income and reduced Specialised Finance deal flows.

New Zealand, United States and Asian cash earnings all declined, reflecting shortfalls in Corporate & Institutional Banking results.

Asset Quality

The credit environment in which the National operates in has continued to remain favourable notwithstanding that in the past twelve months interest rates have tightened.

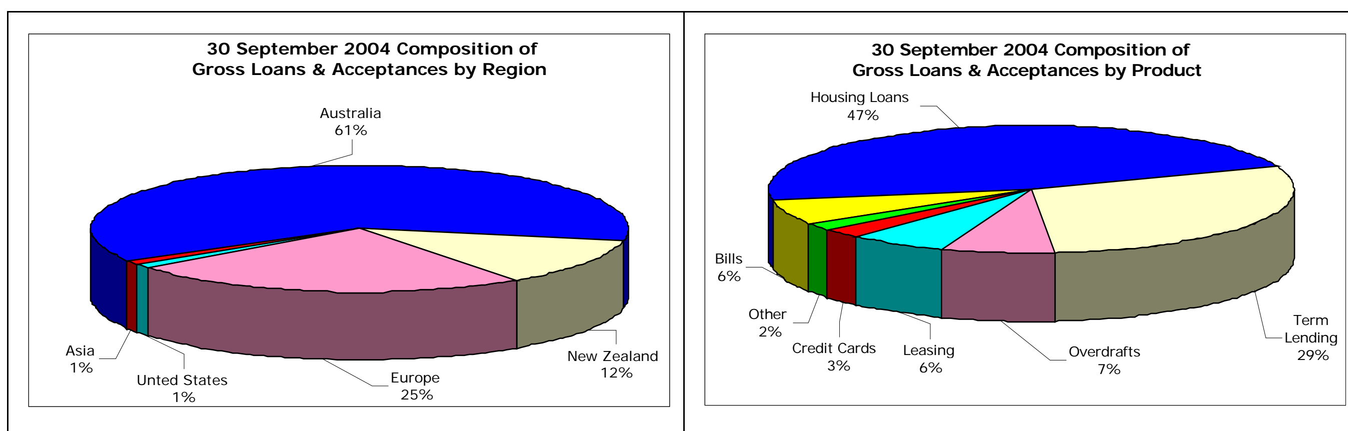
During the September 2004 year the Group's lending portfolio remained largely secured and/or in the highest credit quality bandings of the Group's internal risk rating system. Offshore impaired credit exposures reduced. The trends observed in the asset quality of the Group's portfolio include:

- reductions in the level of non-accrual loans;
- continued improvement in the credit rating of customers across the Group's portfolio;
- increase in the security/collateral coverage across the business;
- low net write offs; and
- the level of 90 days past due loans has increased following the revision of data collection procedures and definitional differences arising from the consolidation of all mortgage loans onto the National's primary banking system.

The Group has re-classified a large Australian exposure as non-accrual from September 2001. Details are below.

Asset composition

Housing loans are the largest product in the Group's lending portfolio and comprise 47% of total loans (an increase from 44% at 30 September 2003). The Australian operations hold 61% of the Group's total loan portfolio.



Credit policy and strategic framework

The Group maintains a credit policy and sets appropriate credit standards that aim to:

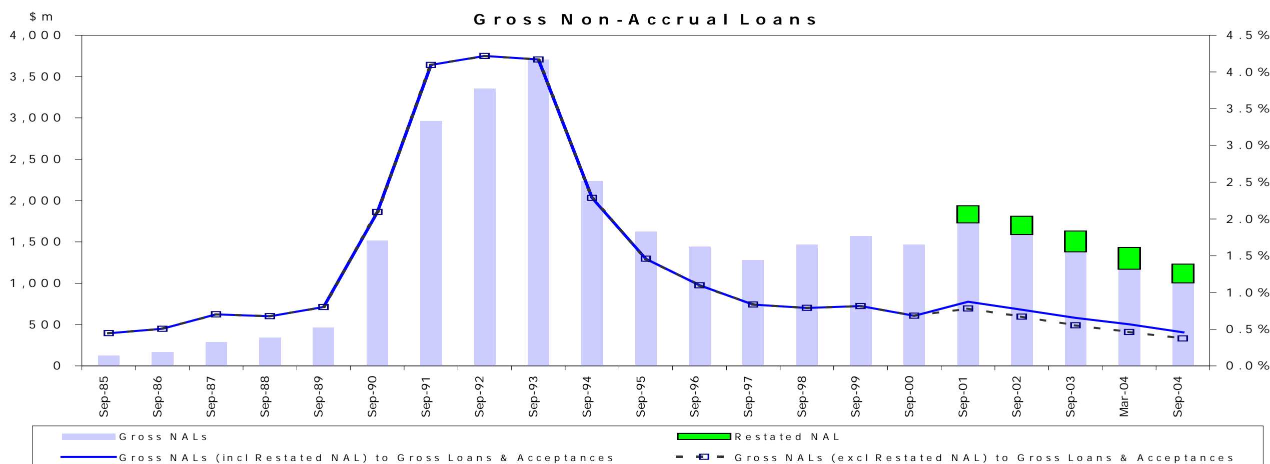
- Support the credit risk appetite of the National's business units;
- Manage asset quality by ensuring customers are rated in accordance with policy and the applicable customer rating system;
- Identify loans showing signs of deteriorating credit quality via early warning indicators, which include two internal categories, 'watch' or 'substandard'. This enables pro-active management of these exposures;
- Manage a limit framework covering country, industry and individual exposures; and
- Provide information to the Board Risk Committee and executive management on asset quality and credit policy compliance.

Non-accrual loans

The National has re-classified an exposure for one large client from 90 days past due to non-accrual over the period from 30 September 2001 to 31 March 2004.

This has increased the balance of non-accrual loans by $207 million at 30 September 2001 rising to $263 million at 31 March 2004. The balance at 30 September 2004 of $226 million reflects the write back of $38 million of previously capitalised interest to the profit and loss during the September 2004 half-year.

Inclusive of the restatement, the level of gross non-accrual loans has decreased from $1,633 million at 30 September 2003 to $1,230 million at 30 September 2004.



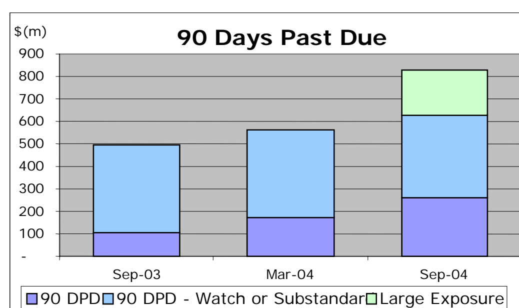
Since 31 March 2004 there has been a large reduction in non-accrual loans through a program to exit impaired exposures in the United States power and utility sector. This was performed through asset sales for US$162 million with a low impact on write-offs. The level of non-accrual loans in the United States as a proportion of gross loans and acceptances has decreased from 10.32% at 31 March 2004 to 4.32% at 30 September 2004.

Accruing loans past due – 90 days or more

90 day past due loans are well secured loans that accrue interest, but are in arrears 90 days or more. These loans are not classified as impaired assets.

The Group has revised its data collection procedures used to establish its 90 day past due exposures.

This process now includes loans that are identified by the internal categories, 'watch' or 'substandard', and are in arrears 90 days or more. One large Australian 90 day past due exposure of $204 million was settled in October 2004.



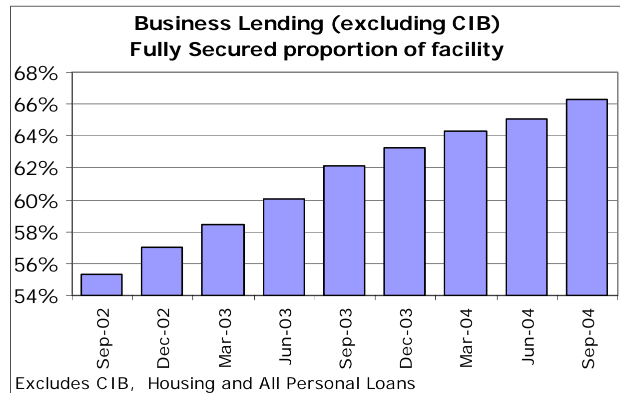
The consolidation of all mortgage loans onto the National's primary banking system has also given rise to an increase in 90 days past due loans as a result of definitional differences between the systems. 90 day past due loans at 30 September 2003 and 31 March 2004 have been restated to reflect the revised data collection process and definitions.

Trends in the level of secured lending

At the Retail Business Banking level the Group continues to focus on building and retaining its core of well-secured customers. The level of well-secured business increased from 64% at 31 March 2004 to 66% at 30 September 2004.

The Group considers a loan to be well secured when it is allocated a lending category A or B.

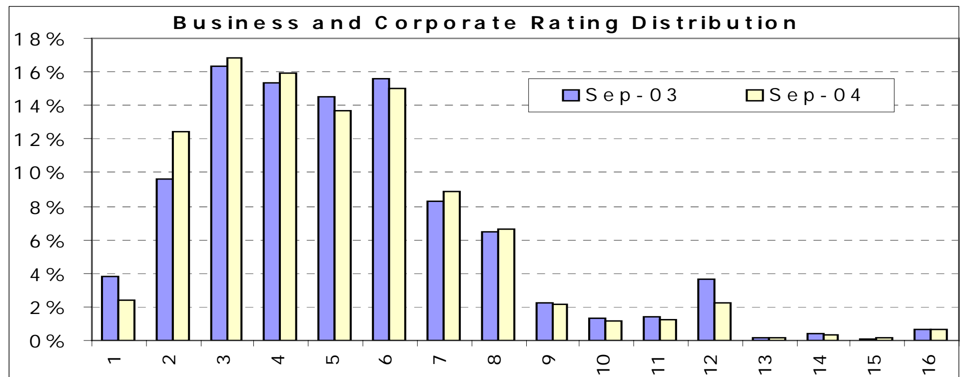
- Category A applies to facilities where Bank security is greater than 142% of the facility.
- Category B applies to facilities where Bank security is greater than 100% of the facility, but less than 142% of the facility.



Trends in the ratings of exposures

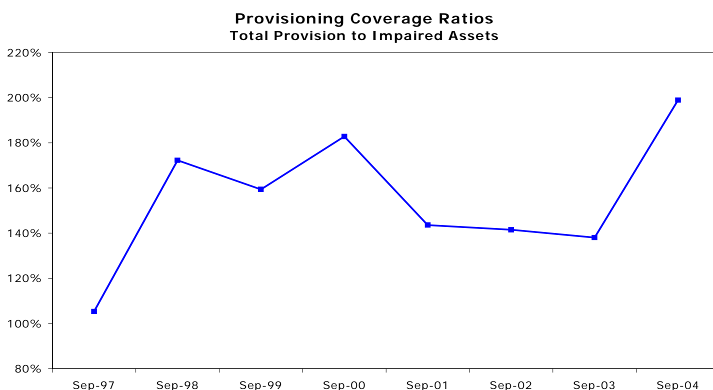
Business and Corporate & Institutional Banking exposures in the 1-6 band of internal risk ratings have increased by 1% since 30 September 2003 to 76% at 30 September 2004.

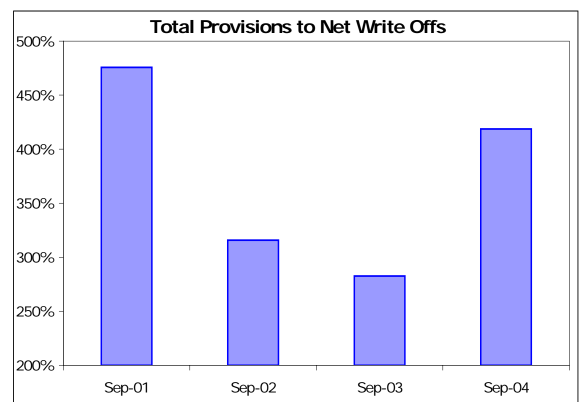
A rating of 1 represents the highest level of credit quality. The lowest level of credit quality is assigned a rating of 16.



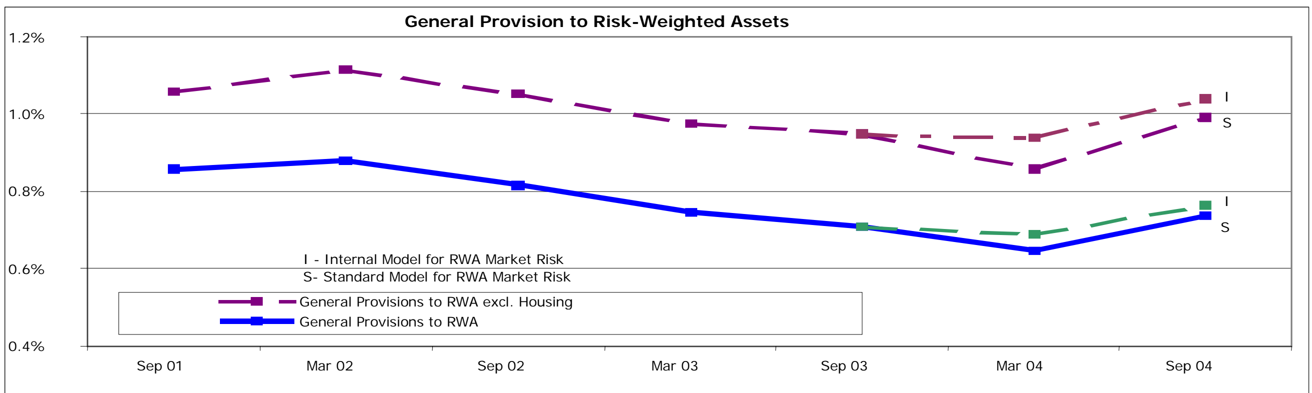
Provisioning coverage

The total provision to impaired assets has improved from 138% at 30 September 2003 to 198% at 30 September 2004. The coverage ratios have been negatively impacted by the re-classification of the previously mentioned Australian exposure to non-accrual status. The improvement in the ratio is mostly due to a reduction in the level of non-accrual loans during the year, but has also been impacted by the increase in the general provision. Total provisions as a proportion of net write-offs have improved to provide a level of cover of 4.2 times at 30 September 2004.



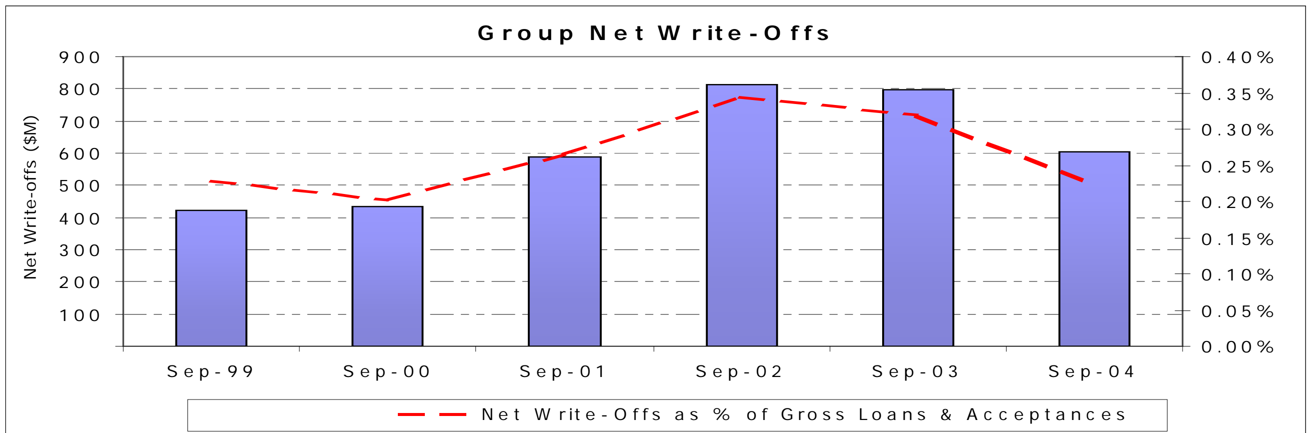


The level of general provision to risk-weighted assets has similarly increased since 31 March 2004 using both the standard and internal methods of calculation.



Net write offs

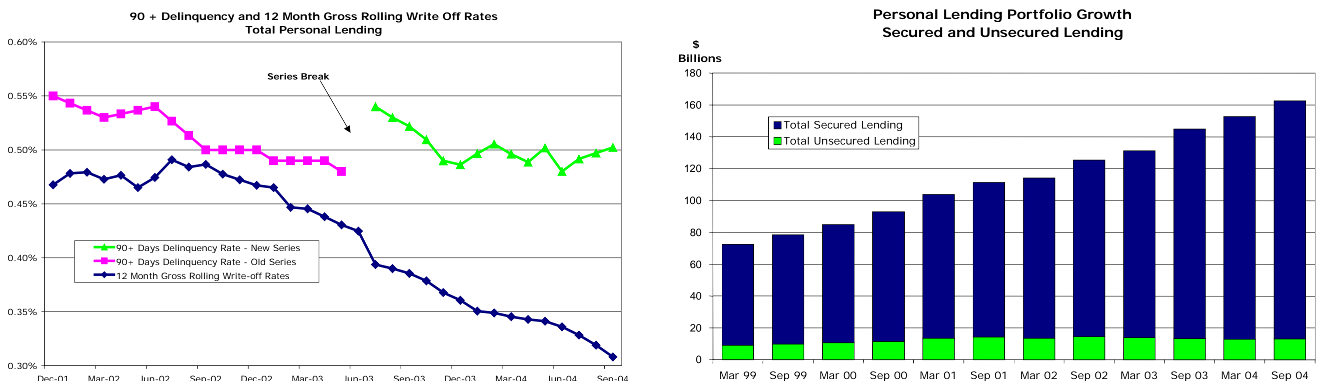
The Group incurred lower net write offs compared to the previous two years both in absolute terms and as a percentage of gross loans and acceptances. The majority of net write-offs were incurred in Australia with $311 million, followed by Europe with $227 million.



Consumer Portfolio

The definitional differences on the transition of home loans from the previous servicing system has caused a moderate increase in the 90-day delinquency rate over the three months to 30 September 2004. The increase in delinquency rates is unlikely to impact loss rates because of the sound security coverage in the housing portfolio.

The series break in the chart below is a result of changes made to systems in June 2003 to align to a Basel definition of default.



Loss rates have declined over the past 12 months. The loss rates are at historically low levels and are unlikely to reduce further because of the recent flattening in housing prices.

Unsecured personal lending comprises around 8% of the total consumer portfolio. 90-day delinquency rates and loss rates on the unsecured portfolio (ie. cards and personal lending) remain stable.