FIPS

FINANCIAL INSTITUTIONS PERFORMANCE SURVEY

DECEMBER 2015 QUARTERLY RESULTS

EXECUTIVE SUMMARY

Despite some softening in interest margins this quarter due to competitive pressures prevailing in a falling interest rate environment, the banking sector continues to deliver strong results on the back of growing loan books fuelled by a still buoyant property market.

Decrease in profits underpinned by lower interest margins and decrease in non-interest income

The December 2015 quarter saw a reduction of profitability for the banking industry from $1,266 million in the September 2015 quarter to $1,107 million in the December 2015 quarter driven mainly by falling interest margins for most survey participants and a reduction of non-interest income due to unfavourable movements in fair value of financial instruments and a decrease in trading income. Despite the reduction of profits for the banking sector, there have been positives during this quarter with lending increasing by $7.32 billion, funding conditions continuing to be favourable resulting in a reduction of the interest expense by 5.42% despite interest bearing liabilities growing by 1.43%, operating expenses decreasing by $17.7 million or 1.46% and impaired asset expense reducing by $1.9 million.

The December 2015 quarter saw a reduction of profitability for the banking sector

Of the major banks, Kiwibank, CBA and Westpac had a combined $16 million increase in net profit after tax (NPAT), while ANZ, and BNZ combined for a $169 million decrease.

Total assets at a record high

Total assets continue to grow at a steady pace, increasing from $440.97 billion in September 2015 to $443.01 billion in December 2015. All the survey participants continue to increase the value of their loan books with no signs of slowing down. This was driven mainly by the continued momentum of the housing market and falling dairy prices which continue to put pressure on cash flows and the ability to service debt for farmers with loan repayments slowing and additional drawings occurring.

Total assets continue to grow at a steady pace

The latest Reserve Bank of New Zealand (RBNZ) data related to lending showed that the year-on-year growth in agriculture and business sectors was 8.4% and 6.9%, respectively, as at February 2016 with housing lending increasing by 7.9%.

Economic outlook

The global sharemarkets experienced their worst start to a year on record in 2016, with stock sell-offs amidst global growth concerns and falling oil prices. However, the major indices recovered to varying degrees and by the end of

March 2016 the US indices returned to broadly the same levels as before year end, while European and Asian indices were slower to recover with most still down by circa 5-10% on previous levels.

Global economic outlook remains uncertain

Global economic outlook remains uncertain. As China experiences slowing growth and undergoes economic rebalancing of its highly indebted local government and private sector, Standard & Poor's became the second rating agency to downgrade China's credit rating outlook from stable to negative in April 2016, saying this was due to China's economic rebalancing being likely to proceed more slowly than expected. The US Federal Reserve has expressed caution towards hiking interest rates to reduce upward pressure on the USD, with strengthening employment data and growing household spending weighing against adverse impacts of slowing global growth on manufacturing and net exports. In Australia, declines experienced in mining investments and falling terms of trade were to some extent mitigated by low interest rates and a weaker currency.

The New Zealand economy continues to be buoyant relative to its global counterparts, still delivering growth at circa 2-3% for the past five years, with Moody's having recently announced the economy's credit rating as Aaa with a stable outlook, pointing to moderate growth, a below median ratio of government debt to GDP, and the focus on foreign trade mitigated to some degree by the diversity of products within its largest segment of exports.

ANZ has reported diminishing business confidence in its March 2016 Business Outlook Survey, with a net 3% of respondents feeling optimistic about the economic outlook, compared to 23% in December and a 10-year average of +10%. Concerns remain around global growth prospects and recent turbulence in major sharemarkets as businesses look forward to what the 2016 year may bring.

The local economy continues to be buoyant relative to its global counterparts

The latest Real Estate Institute of New Zealand (REINZ) statistics show that the Auckland median house price reached an all-time high of $820,000 in March, up by 9.3% compared to February 2016. Nationally, sales volumes were reported at 9,527, which was 8.22% up on volumes last March. Sales volumes in Auckland were 66.8% up compared to February 2016. The building consents data released in March has shown a seasonally adjusted 11% uplift in new dwellings consented for February 2016.

The outlook for the dairy sector continues to be gloomy caused by low global dairy prices as they continue to be subdued by large volumes of milk produced around the world and particularly in Europe. At the last Global Dairy Trade (GDT) auction whole milk powder prices climbed by 7.5% with the GST price index gaining 3.8%, however prices continue to be low by historical levels. The longer term outlook for the global dairy industry remains positive with expected annual growth in global demand estimated at circa 2-3%, but uncertainty remains as to just how long dairy prices will remain at these lower levels.

The outlook for the dairy sector continues to be gloomy caused by low global dairy prices driven by developments in the wider global dairy market

Fonterra has reported a 123% increase in its half-year profit, up to $409 million, which was largely attributable to lower input costs due to low milk prices and a focus on higher margin products. Consequently, Fonterra has forecast a full-year dividend of 40¢, which would bring the total forecast cash payout to $4.30/kgMS for a farmer who is a full shareholder. Fonterra has made the decision to pay dividends earlier to aid cash strapped farmers, as opposed to further extending the interest-free loans which are expected to total about $383 million by April 2016. Additionally, as some of the banks have reduced floating rates for rural borrowers after the latest RBNZ Official Cash Rate (OCR) cut, this may bring some relief and ease the cash flow pressures for highly leveraged farmers.

Regulation

The regulatory landscape continues to evolve, with the RBNZ having completed its Regulatory Stocktake involving a review of the prudential requirements applying to registered banks and licensed Non-bank Deposit Takers (NBDTs) and about to commence follow-on implementation work. The RBNZ is currently reviewing quarterly disclosure requirements and is planning a follow-up consultation

on its 'Dashboard' option for quarterly disclosures, with the consultation process expected to take place in mid-2016.

In the months leading up to November 2015, when the new loan-to-value ratio (LVR) speed limits were imposed, trends in new mortgage lending published by the RBNZ show a marked reduction in greater than 70% LVR lending to investors as a proportion of total new investor lending from 50.8% in June 2015 to 32.0% by October 2015. February 2016 data shows greater than 70% LVR new investor loans at 35.0%; however, data reported thus far has not disaggregated Auckland investors into a separate category. The full impacts of the new LVR restrictions remain to be seen as more property market data becomes available over the coming months.

With regards to capital adequacy, recent Basel Committee consultations have prompted the RBNZ to review parts of its capital adequacy framework, including its approach to both operational and credit risk (this includes both the Standardised and the Internal Ratings Based Approach framework). The RBNZ will also review its liquidity policy in relation to Basel liquidity requirements and the Liquidity Coverage Ratio (LCR).

In March, the RBNZ has commenced public consultation on a crisis management regime for systemically important financial market infrastructures (SIFMIs), being channels through which financial institutions, governments, businesses and individuals transmit money and financial instruments. The proposed crisis management regime has two parts: (i) SIFMIs would be required to maintain business continuity plans and recovery and wind-down plans; and (ii) the RBNZ and Financial Markets Authority (FMA) could call on proposed new statutory powers when these plans are inadequate to manage a crisis.

TABLE 1: Movement in Interest Margin	31 Dec 15 Quarter Ended (%)	Movement During the Quarter (bps)	Movement for the 6 Months (bps)	Movement for the 12 Months (bps)
ANZ Banking Group	2.22%	-1	1	-1
Bank of New Zealand	2.21%	-9	-15	-13
Commonwealth Bank of Australia	2.12%	-1	-9	-15
Heartland Bank	5.18%	37	35	27
Kiwibank Limited	2.07%	-6	0	-5
Southland Building Society	2.63%	-4	-23	-30
The Co-operative Bank	2.71%	-6	-10	-9
TSB Bank Limited	2.08%	-6	-4	-12
Westpac Banking Corporation	2.17%	-11	-15	-9
Average	**2.21%**	**-4**	**-7**	**-8**

TABLE 2: Movement in Impaired Asset Expense/Average Gross Loans	31 Dec 15 Quarter Ended (%)	Movement During the Quarter (bps)	Movement for the 6 Months (bps)	Movement for the 12 Months (bps)
ANZ Banking Group	0.09%	3	-1	2
Bank of New Zealand	0.22%	-16	12	-4
Commonwealth Bank of Australia	0.14%	5	6	0
Heartland Bank	0.34%	-22	-40	-10
Kiwibank Limited	0.07%	-1	4	-1
Southland Building Society	0.33%	-29	2	-46
The Co-operative Bank	0.08%	4	-8	3
TSB Bank Limited	0.08%	155	1	4
Westpac Banking Corporation	-0.01%	-2	-9	-8
Average	**0.11%**	**0**	**2**	**-2**

What else is happening?

In April, NZ Post has announced its intention to sell a 45% share in Kiwibank to NZ Super Fund (25%) and the ACC (20%) for a total of $495 million, with this deal reportedly valuing the whole Kiwibank at $1.1 billion. However, this is still in

early stages with discussions and due diligence currently underway.

The latest OCR cut of 25 basis points (bps) by the RBNZ was reported to have surprised 80% of the market, and led to a circa 20 bps drop in one and two-year swap rates in a single day. The swap curve has continued to shift downward since, with the more pronounced falls observed in the one and two-year rates, down by 8 bps to 2.19% and 5 bps to 2.21%, respectively, by the end of March, having approached near all-time lows.

Widening credit spreads have also been at the forefront of attention, with a notable spike of 170 bps observed in mid-February for five-year investment grade corporate credit default swaps, which has since eased to 118 bps by early April. Credit spreads have nearly doubled from circa 70 bps last year and given prevailing low interest rates, these have become a more significant component of overall funding costs for banks. Recent local currency debt issuances include $625 million raised by ANZ in March, $475 million raised by ASB in March and $500 million raised by BNZ in February.

QUARTERLY ANALYSIS

Decrease in profits underpinned by lower interest margins and decrease in non-interest income

The banking sector experienced a 12.57% decline in profitability during the December quarter, attributable to a weaker interest margin yielding to competitive pressures, down by 4 bps to 2.21%, with record low interest rates being offered by banks and a marked reduction in non-interest income, down by $252.63 million or 31.05%.

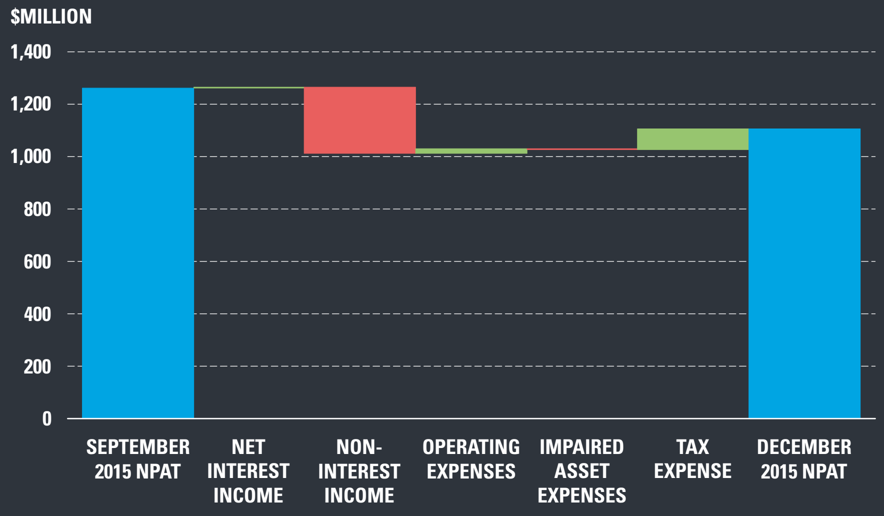
The reduction in non-interest income for this quarter is attributable mostly due to a decline in trading income and unfavourable fair value movements of financial instruments (see Figure 1) experienced by ANZ and BNZ which accounted for $265 million.

1 SEE FIGURE 1 – PAGE 5

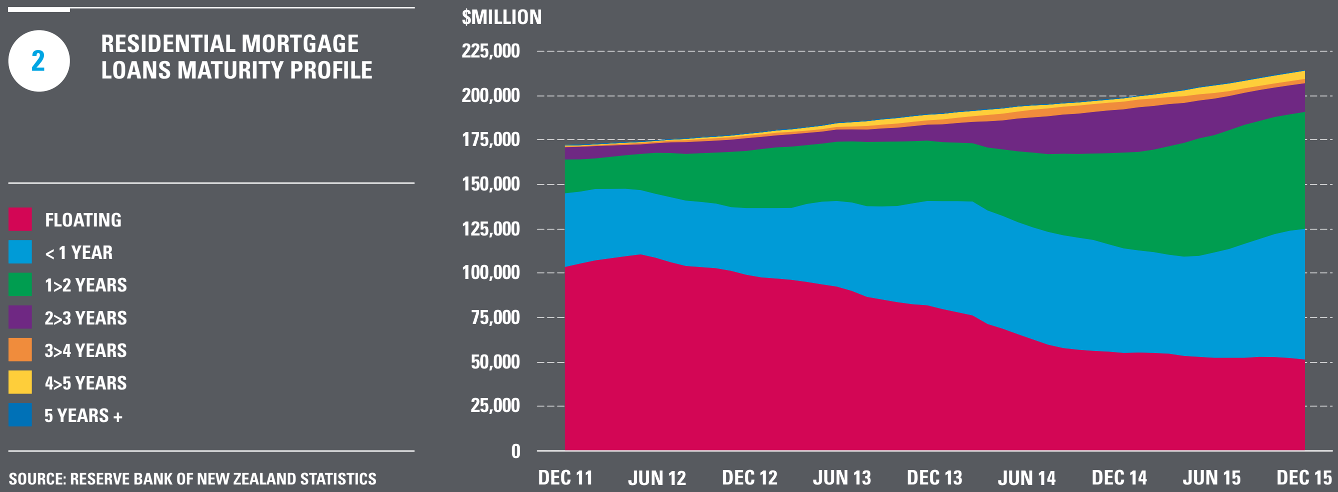
The decline in profits for the sector during the December quarter has been driven by the weak quarter experienced by ANZ, BNZ and TSB with the rest of the survey participants improving their quarterly financial performance. Heartland Bank was the standout performer of this quarter achieving a 49.25% or $5.1 million increase followed by Kiwibank with 15.15% or $5.0 million uplift to their bottom line. Westpac and CBA maintained their profitability at broadly consistent levels, with CBA reporting a 3.85% increase or $9.0 million,

TABLE 3: Analysis of Gross Loans	Quarterly Analysis			Annual Analysis		
	31 Dec 15 Quarter Ended $Million	30 Sep 15 Quarter Ended $Million	% Increase	31 Dec 15 Quarter Ended $Million	31 Dec 14 Quarter Ended $Million	% Increase
ANZ Banking Group	116,573	114,844	1.51%	116,573	108,018	7.92%
Bank of New Zealand	70,039	68,430	2.35%	70,039	65,569	6.82%
Commonwealth Bank of Australia	72,644	70,854	2.53%	72,644	66,066	9.96%
Heartland Bank	2,951	2,415	22.19%	2,951	2,159	36.67%
Kiwibank Limited	16,402	16,001	2.51%	16,402	15,111	8.54%
Southland Building Society	2,813	2,756	2.04%	2,813	2,351	19.62%
The Co-operative Bank	1,757	1,686	4.23%	1,757	1,532	14.67%
TSB Bank Limited	3,745	3,581	4.57%	3,745	3,235	15.77%
Westpac Banking Corporation	70,959	69,991	1.38%	70,959	66,561	6.61%
Total	**357,883**	**350,559**	**2.09%**	**357,883**	**330,602**	**8.25%**

1 MOVEMENT IN NET PROFIT AFTER TAX

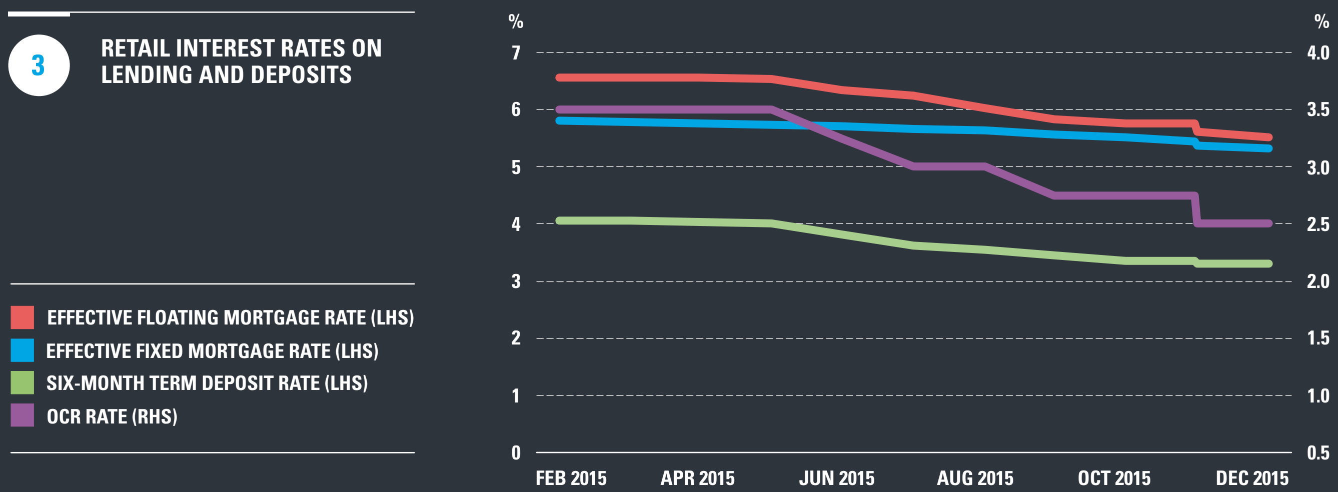


2 RESIDENTIAL MORTGAGE LOANS MATURITY PROFILE



SOURCE: RESERVE BANK OF NEW ZEALAND STATISTICS

3 RETAIL INTEREST RATES ON LENDING AND DEPOSITS



followed by Westpac with 0.80% or $2.0 million.

Heartland improved its profitability on the back of a stronger net interest margin up by 37 bps to 5.18%, reduced operating costs relative to operating income down from 49.94% to 45.69%, and improved asset quality with impaired asset expense decreasing by 30.31% or $1.0 million this quarter.

Kiwibank's strong quarter was driven by an increase in non-interest income by $2.0 million, while also improving operating cost efficiencies having reduced operating costs relative to operating income from 59.84% to 59.35%. Meanwhile, its slightly weaker interest margin, down by 6 bps to 2.07%, was mitigated by 2.51% growth in its loan book.

For TSB the 49.53% or $12.52 million decrease in net profit was driven by a $13.70 million increase in its impaired asset expense, which arose due to a $13.0 million write-back recorded in the previous quarter.

ANZ and BNZ reported the more notable reductions in non-interest income, down by $178 million and $87 million, respectively serving as key drivers for reduced profitability this quarter (see Figure 13).

13 SEE FIGURE 13 – PAGE 15

For ANZ the $178 million reduction in non-interest income was mostly attributable to an $89 million unfavourable movement in fair value gains or losses on hedging, and a $53 million unfavourable movement in trading income. For BNZ the $87 million reduction in non-interest income was mostly due to a $79 million unfavourable movement in gains or losses on financial instruments (see Figure 10).

10 SEE FIGURE 10 – PAGE 14

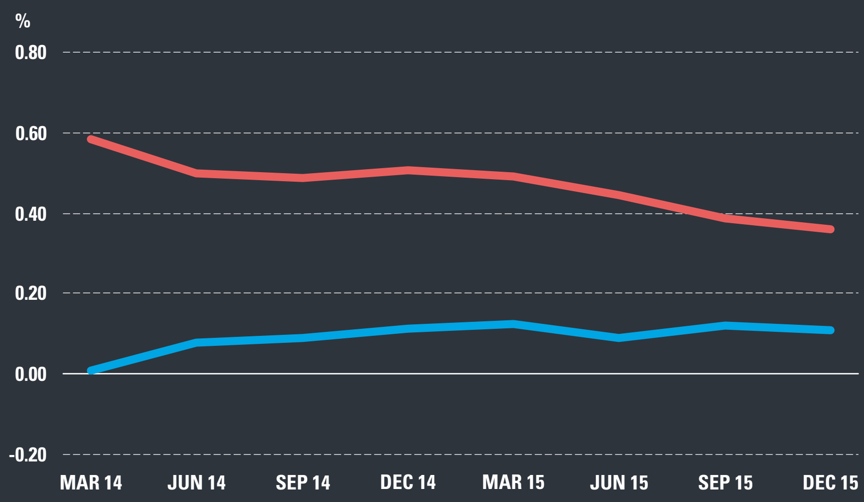
The NZD has depreciated against the USD in the latter half of 2015, falling by approximately 10¢ from the peak 0.77 in late April 2015 to 0.67 by March 2016. Volatility in exchange rates has been considerable during the December quarter and leading up to March 2016, with peaks and

TABLE 4: Movement in Over 80% LVR Lending (On and Off Balance Sheet)

	Quarterly Analysis				Six Month Analysis			
Quarterly Analysis	31 Dec 15 $Million	30 Sep 15 $Million	Movement During the Quarter $Million	% Change	31 Dec 15 $Million	30 Jun 15 $Million	Movement During the Six Month Period $Million	% Change
ANZ Banking Group	8,286	8,650	-364	-4.21	8,286	8,871	-585	-6.59
Bank of New Zealand	3,201	3,304	-103	-3.12	3,201	3,347	-146	-4.36
Commonwealth Bank of Australia	7,688	8,013	-325	-4.06	7,688	8,153	-465	-5.70
Heartland Bank	22	17	5	30.57	22	19	3	17.07
Kiwibank Limited	1,943	1,858	85	4.57	1,943	2,053	-110	-5.36
Southland Building Society	325	392	-67	-17.09	325	377	-52	-13.84
The Co-operative Bank	186	184	2	1.16	186	183	4	2.04
TSB Bank Limited	388	381	7	1.93	388	386	2	0.55
Westpac Banking Corporation	7,722	7,855	-133	-1.69	7,722	7,960	-238	-2.99
Total	**29,762**	**30,655**	**-892**	**-2.91**	**29,762**	**31,349**	**-1,587**	**-5.06**

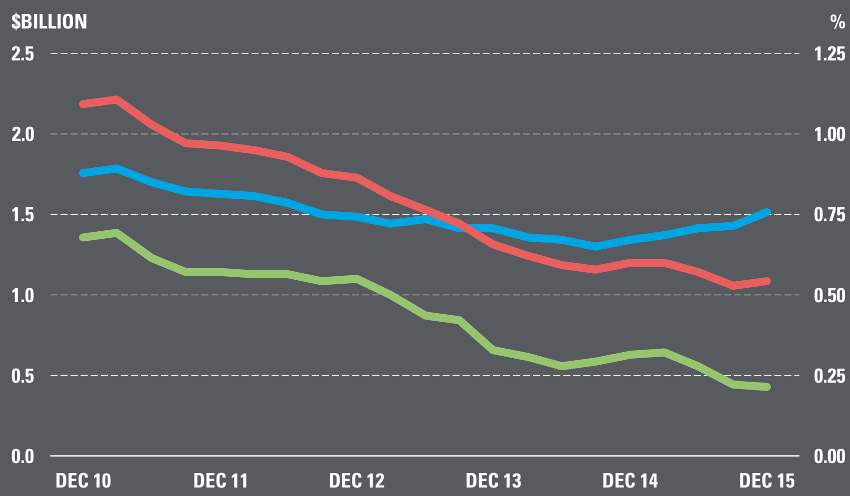
4 MAJOR BANKS: GROSS IMPAIRED VS IMPAIRED ASSET EXPENSE

- GROSS IMPAIRED LOANS/GROSS LOANS AND ADVANCES
- IMPAIRED ASSET EXPENSE/AVERAGE GROSS LOANS AND ADVANCES



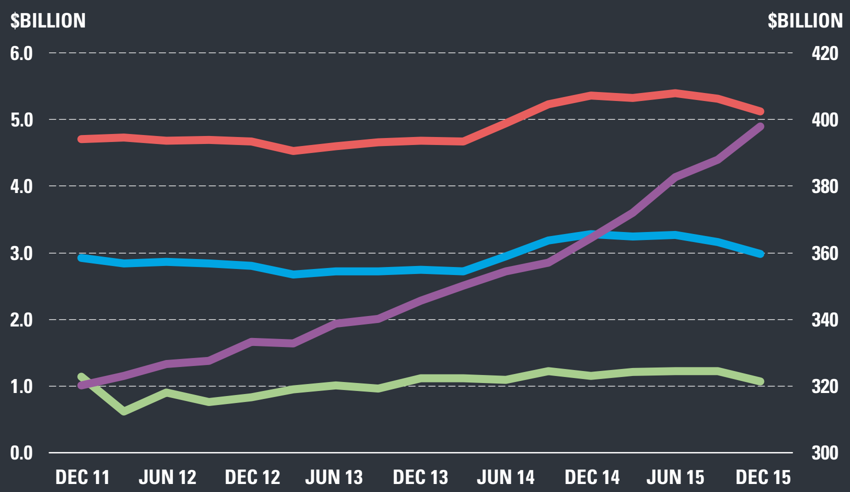
5 MOVEMENT IN PROVISIONING

- TOTAL PROVISION FOR DOUBTFUL DEBTS/ GROSS LOANS AND ADVANCES (RHS)
- COLLECTIVE PROVISION (LHS)
- INDIVIDUAL PROVISION (LHS)



6 MAJOR BANKS: INTEREST EARNING ASSETS COMPARED TO INTEREST INCOME AND EXPENSE

- INTEREST INCOME (LHS)
- INTEREST EXPENSE (LHS)
- NET PROFIT (LHS)
- INTEREST EARNING ASSETS (RHS)



troughs of circa 4-5¢ observed within the space of weeks, which could have contributed to more sizeable trading gains or losses on financial instruments.

A summary of the financial performance of the survey participants is as follows:

- Net interest income marginally improved by 42 bps or $95,000
- Non-interest income decreased by 31.05% or $252.6 million
- Operating expenses dropped by 1.46% or $17.7 million
- Impaired asset expense reduced by 2.01% or $1.9 million
- Tax expense decreased by 15.92% or $77.7 million.

Margins continue to be tight in a highly competitive environment

Continued competitive pressures in the banking sector led to a further 4 bps weakening in interest margins down to 2.21% in December, with eight of the nine survey participants having reported reductions in their margins. The overall interest margin of 2.21% is the lowest it has been since December 2010, when it was reported at 2.16%. A consistent theme appears to have emerged this quarter, with all survey participants, except for Heartland, having reported declines in interest income, most ranging between 2-4%, despite having increased their interest earning asset base by an overall 2.68%. Annualised interest income earned over average interest earning assets decreased by 28 bps from 5.54% to 5.26% this quarter (see Figure 6).

6 SEE FIGURE 6 – PAGE 7

Falling interest rates also led to lower funding costs, with the overall interest expense having reduced by 5.42%, while interest bearing liabilities grew by 1.43% reflective of the favourable funding conditions experienced in 2015. Annualised interest costs over average interest earning liabilities reduced by 22 bps from 3.72% to 3.50%. However, we noted that in early 2016, markets became more volatile with Executives commenting about an increase in wholesale funding costs for banks.

Among the major banks (see Figure 11), Westpac experienced the most notable easing in net interest margins at 11 bps down to 2.17%, followed by BNZ reporting a decrease of 9 bps down to 2.21%, and Kiwibank with a 6 bps decrease down to 2.07%. Meanwhile ANZ and CBA broadly maintained their margins this quarter, showing only a 1 bp drop, down to 2.22% and 2.12% respectively.

11 SEE FIGURE 11 – PAGE 14

Heartland Bank remained the front-runner and not only continued to report the highest net interest margin in the sector at 5.18%, but also having bucked the trend and lifted its margin by a further 37 bps since September 2015. Heartland Bank achieved this on the back of higher interest income relative to interest earning assets, up by 120 bps to 9.97%, and a 22.19% growth in its gross loans and advances. Heartland Bank has recently amalgamated with Heartland New Zealand, effective from 31 December 2015.

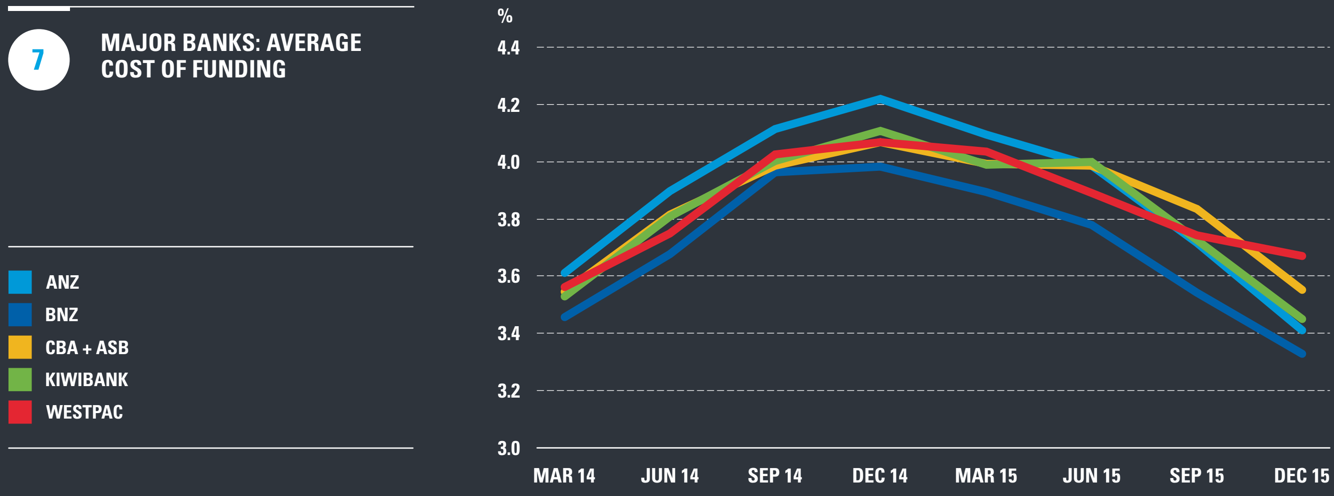
Overall net interest income remained unchanged since the September quarter at $2.25 billion, despite a $7.32 billion or 2.09% growth in gross loans and advances, which has been reflective of the current highly competitive environment experienced by the banks. ANZ led the way having reported an $8.0 million increase in net interest income largely on the back of reduced funding costs, having reduced its interest costs relative to interest bearing liabilities by 31 bps to 3.41%. Meanwhile, Westpac reported the most notable reduction in net interest income, down by $15.0 million or 3.27%, with reduced funding costs not fully mitigating for the reduced interest income earned on a growing asset base.

Returns on interest earning assets have continued to decline for a fourth consecutive quarter (being annualised interest income over average interest earning assets), with a further 28 bps reduction this quarter contributing to a total 71 bps reduction for the 2015 year. This continues to be reflective of not only continued margin pressures, but also diminishing returns as banks' asset bases continue to grow.

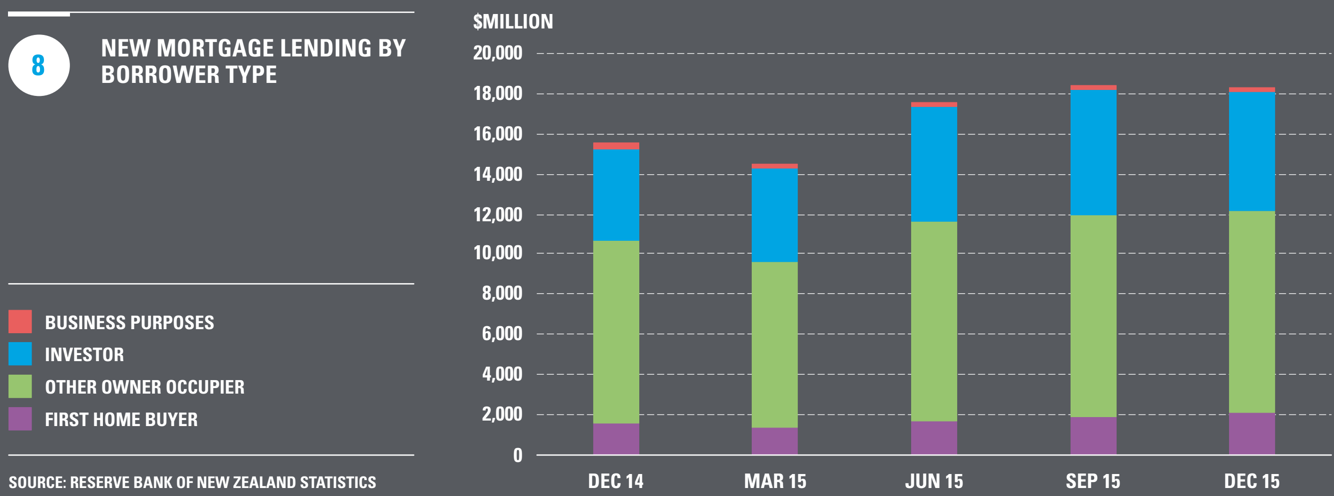
Funding costs continue to be low

Favourable funding conditions resulting in lower funding costs were reported by all participants this quarter, with the exception of Heartland Bank that reported an increase of 96 bps to 5.44%. Of the remaining participants, ANZ enjoyed the largest reduction of 31 bps down to 3.41%, while Westpac reported the smallest reduction of 7 bps down to 3.67%. The others

7 MAJOR BANKS: AVERAGE COST OF FUNDING

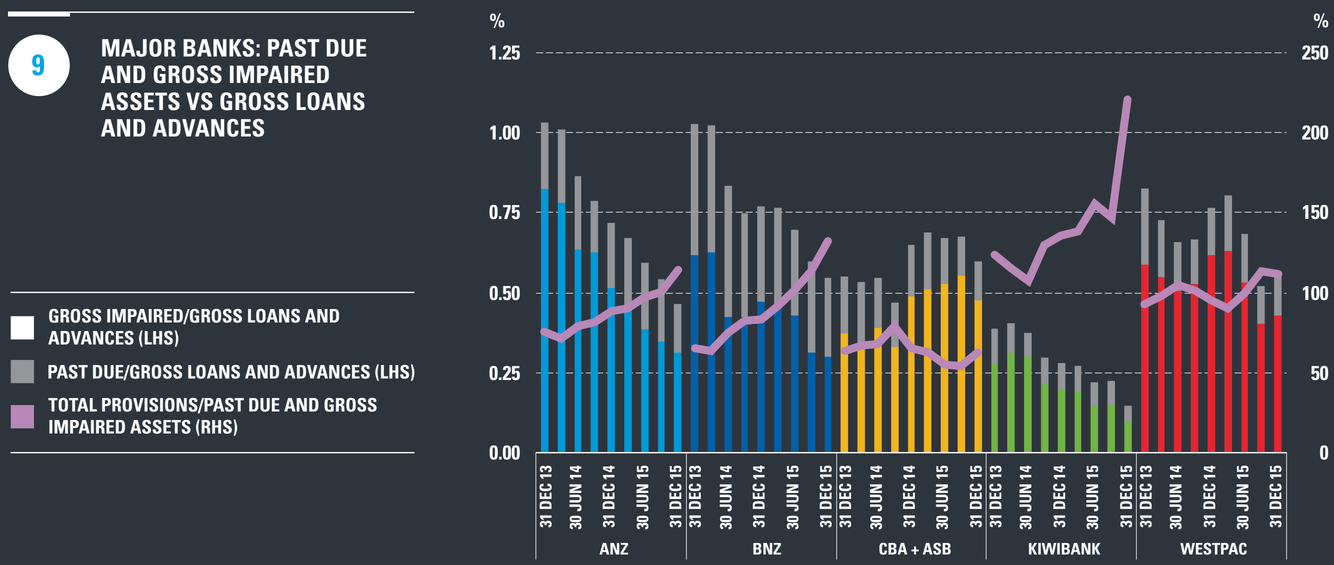


8 NEW MORTGAGE LENDING BY BORROWER TYPE



SOURCE: RESERVE BANK OF NEW ZEALAND STATISTICS

9 MAJOR BANKS: PAST DUE AND GROSS IMPAIRED ASSETS VS GROSS LOANS AND ADVANCES



reported decreases ranging between circa 20-30 bps. See Figure 7.

7 SEE FIGURE 7 – PAGE 9

Looking at short-term funding and local deposits, the latest RBNZ data shows that the six-month deposit rates continued on a downward trend, having fallen by a further 8 bps down to 3.28% in February, and down by 78 bps since March 2015 (see Figure 3).

3 SEE FIGURE 3 – PAGE 5

Since the December 2014 peak funding costs have continued to fall during 2015, following four consecutive OCR cuts by the RBNZ, with the latest in March 2016. The RBNZ has cut the OCR by 25 bps in a surprise move on the 10th March, which resulted in the markets reacting with a 19 bps drop in one-year swap rates in a single day, down from 2.45% to 2.26%. However, perceived cheaper funding stemming from falling swap rates continues to be offset by rising spreads experienced by the New Zealand banks over the past 15 months, with spreads on five-year bank senior bonds having nearly doubled from circa 67 bps in September 2014 to circa 117 bps in early 2016, and are well above the pre-global financial crisis (GFC) levels of circa 20 bps.

The Core Funding Ratio of 85.6% in February 2016 remains well above the regulatory minimum of 75.0% and still provides New Zealand banks with a substantial buffer to seek alternative sources of funding.

Lending

The banking sector has continued to grow its loan books this quarter, with the five major banks contributing 88.71% of the total $7.32 billion increase in lending (see Figure 12).

12 SEE FIGURE 12 – PAGE 14

Among the major banks, CBA led the way achieving both the highest dollar value and percentage increase of $1.79 billion or 2.53%. BNZ followed with a 2.35% increase or $1.61 billion, ANZ reported a 1.51% increase or $1.73 billion, and Westpac reported a 1.38% increase or $0.97 billion. Heartland Bank reported the highest percentage growth in its loan book, up by 22.19% or $535.82 million this quarter.

RBNZ data released continues to show rising annual growth rates in agricultural and business sector lending with growth rates reported in February 2016 at 8.4% and 6.9%. In February 2016, lending for the agricultural sector totalled $59.01 billion; meanwhile, housing loans year on year growth at the end of February was 7.9% topping $214.2 billion.

For residential mortgages, borrowers continued to display a preference for shorter fixed terms, with the one-year fixed mortgages increasing further, up to 34.41% in December, while mortgages on floating rates eased from 25.05% to 23.87% (see Figure 2).

2 SEE FIGURE 2 – PAGE 5

Figure 8 shows that new mortgage lending by borrower type has remained broadly consistent with the previous quarter, with lending to first home buyers and owner occupiers comprising 67% of new mortgage lending for the December quarter.

8 SEE FIGURE 8 – PAGE 9

Asset quality remains strong

Overall asset quality metrics reported in December remain broadly consistent with those reported in the previous quarter, with the impaired asset expense relative to gross loans and advances remaining stable at 0.11% or $98.64 million (see Figures 4 and 15).

4 SEE FIGURE 4 – PAGE 7

15 SEE FIGURE 15 – PAGE 15

The banking sector achieved further growth in loan books, while still managing to reduce both gross impaired assets (see Figure 4),

down by 4.64% to $1.29 billion, and past due assets, down by 11.74% to $568.56 million (see Figure 9).

9 **SEE FIGURE 9 – PAGE 9**

Total provisioning relative to gross loans and advances remained at 0.54% (see Figure 5). However, this was underpinned by an improvement in specific provisions, down from 0.13% to 0.12% of gross loans, offset by an increase in collective provisions, up from 0.41% to 0.42% of gross loans. Levels of collective provisioning continue to be consistent with the two year average of 0.42%.

5 **SEE FIGURE 5 – PAGE 7**

Dairy industry exposures continue to be closely monitored by the banks and RBNZ, but thus far there does not appear to be a significant deterioration of asset quality reported.

Stress tests conducted by the major dairy lenders revealed that on the existing dairy exposures currently totalling circa $38 billion or 10% of banks' loan books, the projected loan losses could amount to around 8% or $3 billion. The RBNZ said that the stress tests showed that most of the impact on bank profitability would occur in the first three years and expected that these losses could be absorbed through earnings, as opposed to eroding capital.[1]

1. Bulletin article 'Summary of the dairy portfolio stress testing exercise' published on 16 March 2016 by the Reserve Bank.

Operating expenses/ Operating income

The banking sector has experienced some deterioration in the overall operating costs ratio relative to operating income, which has increased by 293 bps to 42.45% this quarter. However, when removing the impacts of the $252.63 million reduction in non-interest income which largely comprised trading losses and unfavourable fair value movements in financial instruments, then the increase in the operating costs ratio only amounted to 40 bps. Despite the banks having achieved a reduction in overall operating costs, down by $17.69 million or 1.46%, the increase in the operating costs ratio was a result of lower interest income, due to falling interest rates combined with the abovementioned considerable reduction in non-interest income.

The more notable increases in the operating expense ratios were reported by ANZ, BNZ and TSB (see Figure 14). However, this was mostly due to the large unfavourable movements in trading income and fair value gains or losses on financial instruments, thus the movements may not be indicative of operating cost efficiencies for these banks. When looking at operating costs alone, these banks managed to keep their cost bases reasonably stable, while having continued to grow their asset bases, with ANZ reporting a 0.26% reduction in operating costs, BNZ reporting an incremental increase of 0.90% and TSB reporting a 4.13% increase or $0.67 million.

14 **SEE FIGURE 14 – PAGE 15**

Operating cost management continues to be at the forefront for the banking sector, while they continue to invest in their business and stay on track with technological advancements and any new regulatory initiatives.

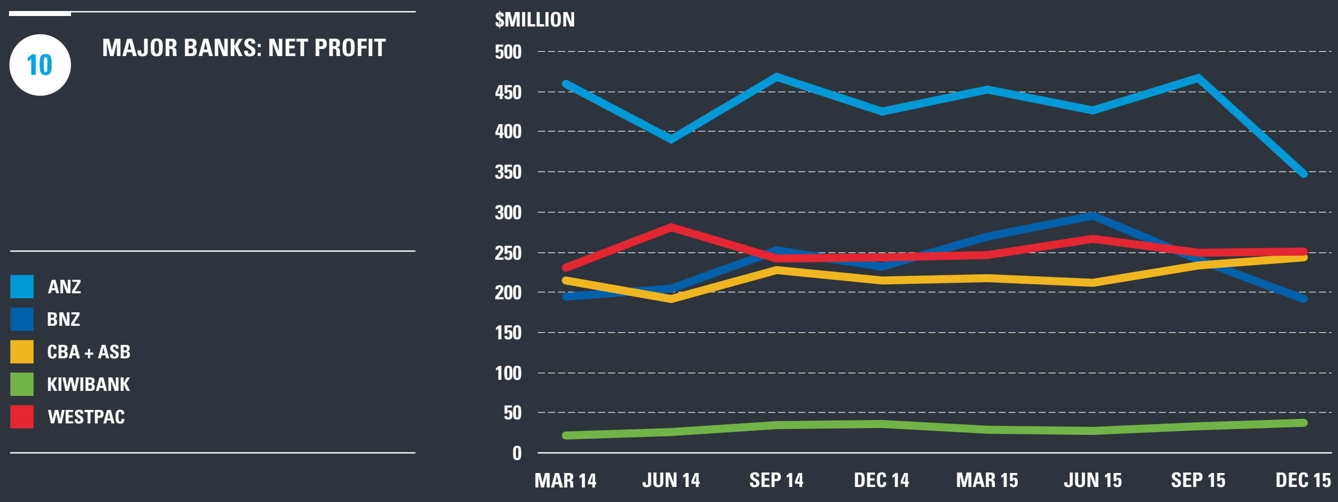
Major banks – Quarterly analysis

Entity	Size & Strength Measures							
	31 Mar 14	30 Jun 14	30 Sep 14	31 Dec 14	31 Mar 15	30 Jun 15	30 Sep 15	31 Dec 15
	Total Assets[4] ($Million)							
ANZ[2]	129,529	132,422	135,074	135,290	140,253	150,664	152,038	152,289
BNZ	76,740	75,845	79,522	79,658	81,926	85,657	86,629	86,819
CBA + ASB[2]	72,586	72,077	73,483	74,149	76,994	80,147	81,321	81,785
Heartland Bank	2,423	2,368	2,431	2,543	2,623	2,772	2,825	3,290
Kiwibank	16,344	16,590	16,882	17,064	17,948	18,228	18,686	18,858
Southland Building Society	2,784	2,786	2,825	2,826	2,858	3,094	3,163	3,286
The Co-operative Bank Limited	1,616	1,664	1,704	1,770	1,795	1,838	1,896	1,971
TSB Bank Limited	5,682	5,655	5,736	5,908	5,908	5,991	6,208	6,299
Westpac[2]	78,857	80,392	80,963	82,442	82,087	87,455	88,203	88,416
Total	**386,561**	**389,799**	**398,619**	**401,649**	**412,392**	**435,846**	**440,968**	**443,014**
	Increase in Gross Loans and Advances (%)							
ANZ[2]	0.99	1.30	1.31	1.53	1.75	3.60	0.86	1.51
BNZ	0.42	1.45	0.93	1.16	1.57	1.01	1.72	2.35
CBA + ASB[2]	0.49	0.96	1.87	1.19	2.75	2.04	2.29	2.53
Heartland Bank	-0.49	3.77	3.15	4.50	4.10	4.11	3.21	22.19
Kiwibank	2.87	1.85	0.66	2.20	2.04	1.50	2.24	2.51
Southland Building Society	0.03	-0.53	-0.10	2.88	2.50	11.34	2.71	2.04
The Co-operative Bank Limited	3.02	2.58	2.74	2.93	2.19	3.24	4.28	4.23
TSB Bank Limited	0.26	0.94	0.20	3.04	1.73	5.27	3.39	4.57
Westpac[2]	1.16	0.95	1.24	1.67	1.51	1.57	1.99	1.38
Average	**0.88**	**1.22**	**1.30**	**1.50**	**1.90**	**2.34**	**1.67**	**2.09**
	Capital Adequacy (%)							
ANZ[2, 3]	12.10	12.10	12.70	11.80	12.60	12.50	13.30	13.30
BNZ	12.13	11.82	12.04	12.28	12.90	12.59	12.67	13.26
CBA + ASB[2]	11.20	12.00	11.10	12.70	12.10	12.70	13.30	14.10
Heartland Bank	14.71	14.39	14.09	13.76	13.36	12.86	12.85	14.46
Kiwibank	11.60	13.00	13.20	13.30	12.40	13.40	12.80	12.80
Southland Building Society	13.69	15.64	16.02	16.07	15.61	14.59	14.21	14.27
The Co-operative Bank Limited	16.80	16.80	16.80	16.50	16.50	16.30	16.20	15.80
TSB Bank Limited	14.21	14.77	14.98	13.48	13.85	13.71	15.77	14.86
Westpac[2, 3]	12.10	11.70	12.30	11.60	12.10	12.40	13.30	13.90
	Net Profit ($Million)							
ANZ[2]	460	390	468	425	452	427	467	347
BNZ	195	205	252	232	270	295	241	192
CBA + ASB[2]	214	191	227	214	218	212	234	243
Heartland Bank	9	10	10	10	11	10	10	15
Kiwibank	22	26	35	36	29	27	33	38
Southland Building Society	5	4	6	5	4	6	4	5
The Co-operative Bank Limited	2	2	2	3	2	2	3	3
TSB Bank Limited	13	16	12	-18	16	13	25	13
Westpac[2]	230	281	242	244	247	266	249	251
Total	**1,150**	**1,125**	**1,254**	**1,151**	**1,249**	**1,259**	**1,266**	**1,107**

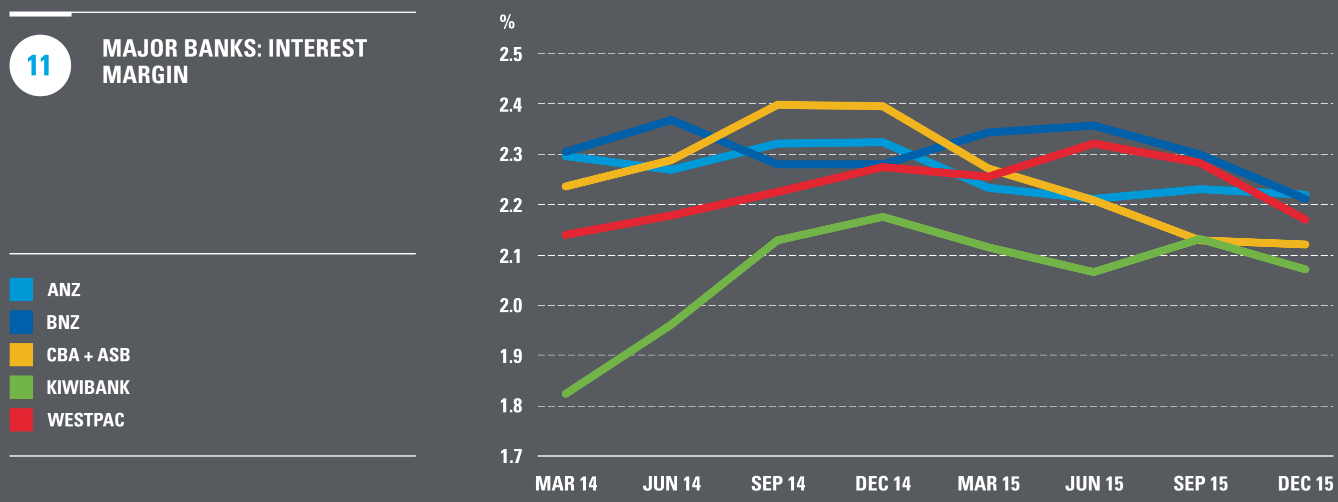
2. The results for Australia and New Zealand Banking Group, Commonwealth Bank of Australia and Westpac Banking Corporation relate to the total New Zealand operations of these entities.
3. The capital adequacy ratio's reported are for the overseas banking group.
4. Total Assets = Total Assets - Intangible Assets.
5. Operating income for Heartland includes net interest income, net operating lease income, other income and fee income.

Entity	Profitability Measures							
	31 Mar 14	30 Jun 14	30 Sep 14	31 Dec 14	31 Mar 15	30 Jun 15	30 Sep 15	31 Dec 15
	Interest Margin (%)							
ANZ[2]	2.30	2.27	2.32	2.33	2.23	2.21	2.23	2.22
BNZ	2.30	2.37	2.28	2.28	2.34	2.36	2.30	2.21
CBA + ASB[2]	2.24	2.29	2.40	2.40	2.27	2.21	2.13	2.12
Heartland Bank	4.45	4.94	4.99	5.06	4.91	4.83	4.81	5.18
Kiwibank	1.82	1.96	2.13	2.17	2.12	2.07	2.13	2.07
Southland Building Society	2.58	2.81	2.97	2.97	2.93	2.86	2.67	2.63
The Co-operative Bank Limited	2.78	2.85	2.95	2.90	2.80	2.81	2.77	2.71
TSB Bank Limited	1.99	2.17	2.30	2.15	2.20	2.12	2.14	2.08
Westpac[2]	2.14	2.18	2.23	2.28	2.26	2.32	2.28	2.17
Average	**2.25**	**2.28**	**2.32**	**2.34**	**2.29**	**2.28**	**2.25**	**2.21**
	Non-interest Income/Total Tangible Assets (%)							
ANZ[2]	0.59	0.73	1.00	0.79	0.90	0.76	0.80	0.33
BNZ	0.47	0.53	1.06	0.63	0.94	0.97	0.83	0.42
CBA + ASB[2]	0.59	0.64	0.58	0.63	0.56	0.52	0.66	0.77
Heartland Bank	0.63	0.45	0.33	0.41	0.41	0.36	0.39	0.47
Kiwibank	0.77	0.58	0.72	0.73	0.57	0.57	0.59	0.62
Southland Building Society	0.71	0.77	0.93	0.96	1.03	0.98	0.95	1.03
The Co-operative Bank Limited	0.90	1.17	1.14	1.13	0.24	1.00	0.99	1.02
TSB Bank Limited	0.33	0.33	0.38	0.35	0.40	0.24	0.38	0.20
Westpac[2]	0.69	0.73	0.78	0.73	0.66	0.73	0.69	0.63
Average	**0.59**	**0.66**	**0.86**	**0.71**	**0.77**	**0.74**	**0.74**	**0.51**
	Impaired Asset Expense/Average Gross Loans and Advances (%)							
ANZ[2]	-0.08	0.07	0.04	0.05	0.07	0.10	0.06	0.09
BNZ	0.13	0.11	0.12	0.02	0.26	0.10	0.38	0.22
CBA + ASB[2]	0.09	0.16	0.10	0.29	0.14	0.08	0.09	0.14
Heartland Bank	0.31	0.46	0.36	0.52	0.44	0.74	0.56	0.34
Kiwibank	0.03	-0.11	0.08	0.16	0.08	0.03	0.08	0.07
Southland Building Society	0.43	0.51	0.35	0.43	0.79	0.31	0.62	0.33
The Co-operative Bank Limited	0.07	0.07	0.08	0.07	0.05	0.16	0.04	0.08
TSB Bank Limited	0.05	0.11	0.85	6.06	0.04	0.07	-1.47	0.08
Westpac[2]	-0.06	0.01	0.13	0.12	0.07	0.08	0.01	-0.01
Average	**0.01**	**0.08**	**0.10**	**0.17**	**0.13**	**0.09**	**0.11**	**0.11**
	Operating Expenses/Operating Income (%)							
ANZ[2]	40.66	39.85	37.81	39.02	36.61	38.03	36.34	43.30
BNZ	40.85	41.67	43.07	39.67	32.91	34.47	35.81	42.26
CBA + ASB[2]	37.52	38.15	37.66	37.04	37.60	41.19	37.73	36.76
Heartland Bank[5]	51.35	47.98	49.15	48.13	47.14	48.45	49.94	45.69
Kiwibank	68.27	70.19	56.78	54.10	62.07	67.52	59.84	59.35
Southland Building Society	61.20	63.33	62.83	66.27	62.82	60.39	67.73	70.22
The Co-operative Bank Limited	83.96	81.97	82.85	77.95	78.63	80.40	77.65	73.38
TSB Bank Limited	42.26	36.91	38.20	37.95	42.72	44.68	42.50	47.83
Westpac[2]	40.54	39.64	37.70	38.97	37.89	38.95	43.11	40.48
Average	**41.74**	**41.51**	**40.20**	**39.98**	**37.89**	**39.80**	**39.52**	**42.45**

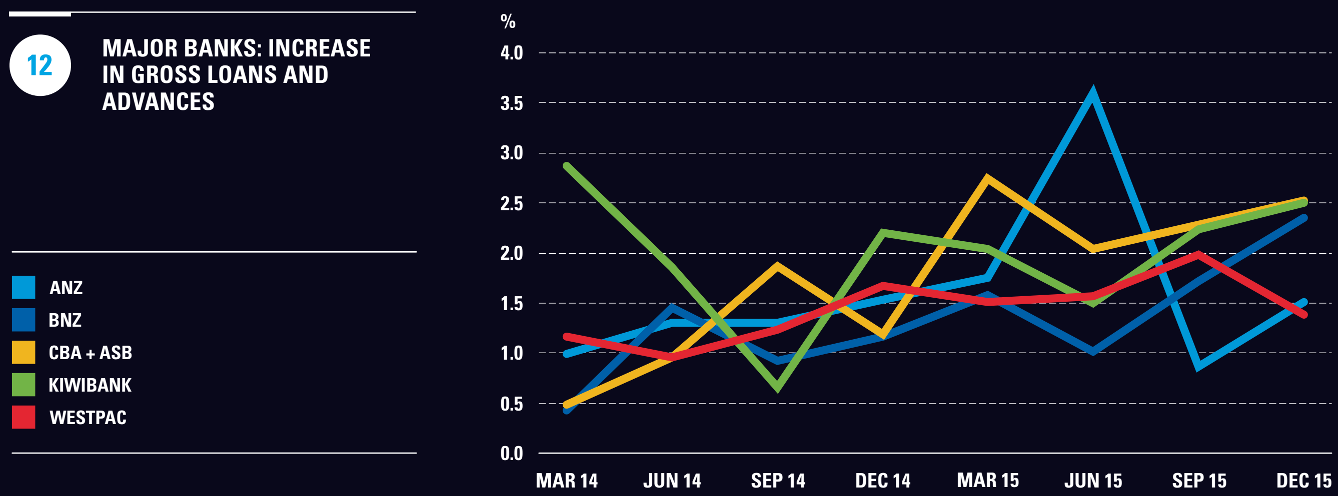
10 MAJOR BANKS: NET PROFIT



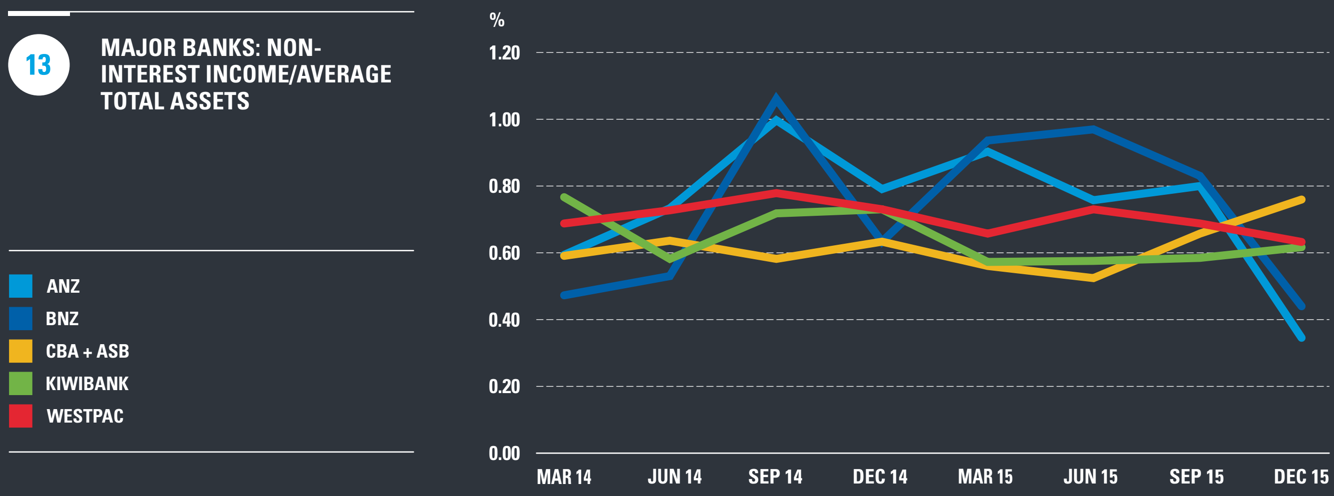
11 MAJOR BANKS: INTEREST MARGIN



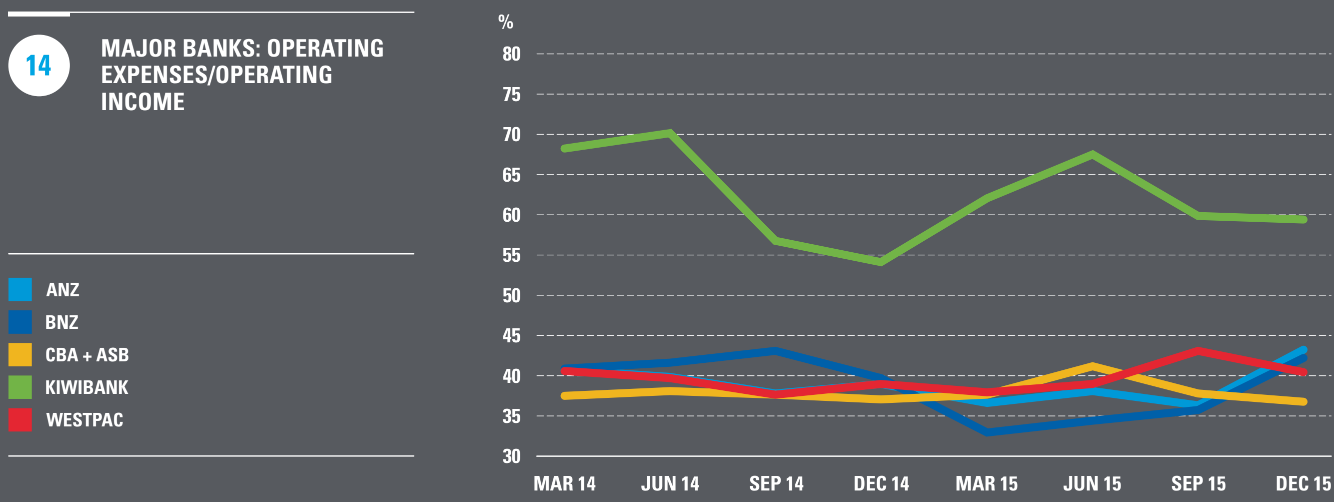
12 MAJOR BANKS: INCREASE IN GROSS LOANS AND ADVANCES



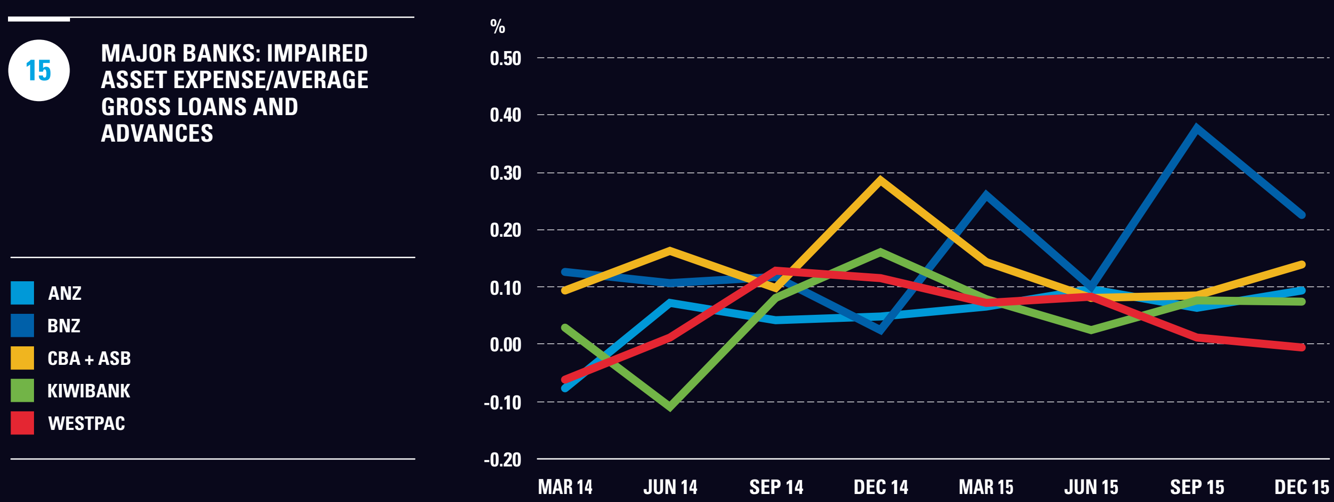
13 MAJOR BANKS: NON-INTEREST INCOME/AVERAGE TOTAL ASSETS



14 MAJOR BANKS: OPERATING EXPENSES/OPERATING INCOME



15 MAJOR BANKS: IMPAIRED ASSET EXPENSE/AVERAGE GROSS LOANS AND ADVANCES



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