PILLAR 3 REPORT 2019

Incorporating the requirements of APS 330

31 December 2018

National Australia Bank Limited ABN 12 004 044 937

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Section 1

Introduction

National Australia Bank Limited (NAB) is an Authorised Deposit-taking Institution (ADI) subject to regulation by the Australian Prudential Regulation Authority (APRA) under the authority of the *Banking Act 1959* (Cth). This document has been prepared in accordance with the quarterly reporting requirements of APRA Prudential Standard APS 330 *Public Disclosure*.

APS 330 requires disclosure of information to the market relating to capital adequacy and risk management practices. APS 330 was established to implement the third pillar of the Basel Committee on Banking Supervision's framework for bank capital adequacy. In simple terms, the framework consists of three mutually reinforcing pillars.

Pillar 1 Minimum capital requirement	Pillar 2 Supervisory review process	Pillar 3 Market discipline
Minimum requirements for the level and quality of capital, and a non-risk based leverage ratio	Management's responsibility for capital adequacy to support risks beyond the minimum requirements, including an Internal Capital Adequacy Assessment Process (ICAAP)	Disclosure to the market of qualitative and quantitative aspects of risk management, capital adequacy and various risk metrics

This document provides information about risk exposures, capital adequacy and liquidity.

Amounts are presented in Australian dollars unless otherwise stated, and have been rounded to the nearest million dollars ($m) except where indicated.

1.1 Capital Adequacy Methodologies

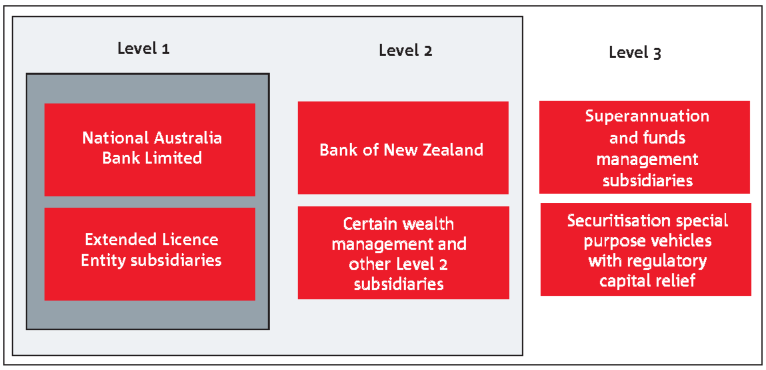
The following illustration sets out the Group's approach to measuring capital adequacy as at 31 December 2018.

Credit Risk	Operational Risk	Non-traded Market Risk	Traded Market Risk
Advanced Internal Ratings Based Approach (IRB)	Advanced Measurement Approach (AMA)	Internal Model Approach (IMA)	Standardised and Internal Model Approach (IMA)

Bank of New Zealand (BNZ), is a wholly owned subsidiary of the Group and is a registered bank under the *Reserve Bank of New Zealand Act 1989*. BNZ is subject to capital adequacy requirements mandated by the Reserve Bank of New Zealand (RBNZ), under which BNZ applies the Internal Models Based Approach. BNZ credit risk exposures consolidated in the Group exposures are calculated under RBNZ requirements.

1.2 Scope of Application

APRA measures capital adequacy by assessing financial strength at three levels as illustrated below.



Level 1 comprises NAB and its subsidiary entities approved by APRA as part of the Extended Licensed Entity.

Level 2 comprises NAB and the entities it controls, excluding superannuation and funds management entities and securitisation special purpose vehicles to which assets have been transferred in accordance with the requirements for regulatory capital relief in APS 120 *Securitisation*. Level 2 controlled entities include BNZ and other financial entities such as broking, wealth advisory and leasing companies.

Level 3 comprises the consolidation of NAB and all of its subsidiaries.

This report applies to the Level 2 Group, headed by NAB, unless otherwise stated.

Section 2

Capital

Capital Adequacy [APS 330 Attachment C, Table 3a - f]

The following tables provide the risk-weighted assets (RWA) for each risk type, capital ratios and leverage ratio for the Level 2 Group.

	As at	
	31 Dec 18	**30 Sep 18**
	$m	**$m**
Credit risk [1]		
Subject to internal ratings based (IRB) approach		
Corporate (including Small and Medium Enterprises (SME))	120,249	116,709
Sovereign	1,425	1,293
Bank	9,865	10,042
Residential mortgage	105,237	103,868
Qualifying revolving retail	3,931	3,993
Retail SME	6,618	6,531
Other retail	3,445	3,419
Total IRB approach	**250,770**	**245,855**
Specialised lending	**59,897**	**60,444**
Subject to standardised approach		
Residential mortgage	1,656	1,558
Corporate	4,728	4,670
Other	491	493
Total standardised approach	**6,875**	**6,721**
Other		
Securitisation exposures	4,540	4,598
Credit Value Adjustment	8,510	7,670
Central counterparty default fund contribution guarantee	1,177	1,138
Other [2]	11,016	4,955
Total other	**25,243**	**18,361**
Total credit risk	**342,785**	**331,381**
Market risk	9,563	9,460
Operational risk	39,367	37,500
Interest rate risk in the banking book	10,638	11,343
Total RWA	**402,353**	**389,684**

(1) *Assets that are not subject to specific risk weights incorporate a scaling factor of 1.06 in accordance with APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk.*

(2) *Other includes non-lending assets and RWA overlay adjustments for regulatory prescribed methodology requirements. The increase over the period is largely driven by higher RWA overlay adjustments reflecting a change in the recognition and exposure measurement of certain off-balance sheet facilities.*

	As at	
	31 Dec 18	**30 Sep 18**
Capital ratios	**%**	**%**
Common Equity Tier 1	10.0	10.2
Tier 1	12.0	12.4
Total	13.6	14.1

Leverage ratio	As at			
	31 Dec 18	**30 Sep 18**	**30 Jun 18**	**31 Mar 18**
	$m	**$m**	**$m**	**$m**
Tier 1 capital	48,408	48,254	46,967	48,048
Total exposures [1]	930,879	896,120	900,904	877,544
Leverage ratio (%) [1]	**5.2%**	**5.4%**	**5.2%**	**5.5%**

(1) *The 30 June 2018 and 31 March 2018 total exposures have been restated from those previously disclosed ($887,837 million and $864,625 million respectively), resulting in a restatement to the leverage ratio at those dates (previously disclosed as 5.3% and 5.6% respectively).*

Section 3

Credit Risk

Information presented in this section excludes credit risk information in respect of certain securitisation exposures and non-lending assets. In particular, it excludes information on third party securitisation exposures and own asset securitisations with capital relief which have separate disclosures in section 4: *Securitisation*.

Credit Risk Exposures [APS 330 Attachment C, Table 4a]

The following table provides a breakdown of credit risk exposures. Credit risk exposure is shown net of eligible financial collateral. The average credit risk exposure is the simple average of the credit risk exposure at the beginning and end of the reporting period.

	As at 31 Dec 18				3 months ended 31 Dec 18
	On-balance sheet exposure	Non-market related off-balance sheet	Market related off-balance sheet	Total exposure	Average total exposure
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach					
Corporate (including SME)	154,740	70,224	16,959	**241,923**	238,324
Sovereign	62,636	475	3,841	**66,952**	65,058
Bank	24,141	3,280	9,125	**36,546**	36,475
Residential mortgage	339,157	49,389	-	**388,546**	386,639
Qualifying revolving retail	5,811	5,542	-	**11,353**	11,346
Retail SME	13,521	4,412	-	**17,933**	17,934
Other retail	3,225	1,191	-	**4,416**	4,376
Total IRB approach	**603,231**	**134,513**	**29,925**	**767,669**	**760,152**
Specialised lending	**57,516**	**9,563**	**640**	**67,719**	**67,880**
Subject to standardised approach					
Residential mortgage	2,079	137	-	**2,216**	2,178
Corporate	7,498	594	5,290	**13,382**	13,321
Other	1,118	1	-	**1,119**	1,126
Total standardised approach	**10,695**	**732**	**5,290**	**16,717**	**16,625**
Total exposure (EaD)	**671,442**	**144,808**	**35,855**	**852,105**	**844,657**

	As at 30 Sep 18				3 months ended 30 Sep 18
	On-balance sheet exposure	Non-market related off-balance sheet	Market related off-balance sheet	Total exposure	Average total exposure
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach					
Corporate (including SME)	150,239	68,358	16,128	**234,725**	232,918
Sovereign	58,584	485	4,096	**63,165**	65,489
Bank	24,936	3,055	8,412	**36,403**	38,350
Residential mortgage	334,880	49,852	-	**384,732**	383,007
Qualifying revolving retail	5,623	5,716	-	**11,339**	11,444
Retail SME	13,611	4,323	-	**17,934**	17,803
Other retail	3,160	1,176	-	**4,336**	4,374
Total IRB approach	**591,033**	**132,965**	**28,636**	**752,634**	**753,385**
Specialised lending	**57,145**	**10,295**	**600**	**68,040**	**68,522**
Subject to standardised approach					
Residential mortgage	2,012	127	-	**2,139**	2,163
Corporate	7,441	560	5,259	**13,260**	13,060
Other	1,133	1	-	**1,134**	1,142
Total standardised approach	**10,586**	**688**	**5,259**	**16,533**	**16,365**
Total exposures (EaD)	**658,764**	**143,948**	**34,495**	**837,207**	**838,272**

Credit Provisions and Losses [APS 330 Attachment C, Table 4b - c]

The following table provides provisioning information by asset class.

	As at 31 Dec 18			3 months ended 31 Dec 18	
	Impaired facilities	**Past due facilities ≥90 days**	**Specific provision for credit impairment**	**Specific credit impairment charge**	**Net write-offs**
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach					
Corporate (including SME)	872	143	437	(13)	15
Residential mortgage	299	2,362	93	27	28
Qualifying revolving retail	-	65	-	49	40
Retail SME	75	144	44	10	13
Other retail	5	56	4	28	30
Total IRB approach	**1,251**	**2,770**	**578**	**101**	**126**
Specialised lending	**164**	**69**	**63**	**5**	**4**
Subject to standardised approach					
Residential mortgage	8	27	4	-	-
Corporate	1	1	6	-	2
Total standardised approach	**9**	**28**	**10**	**-**	**2**
Total	**1,424**	**2,867**	**651**	**106**	**132**
General reserve for credit losses			2,808		

	As at 30 Sep 18			3 months ended 30 Sep 18	
	Impaired facilities	**Past due facilities ≥90 days**	**Specific provision for credit impairment**	**Specific credit impairment charge**	**Net write-offs**
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach					
Corporate (including SME)	970	143	467	21	29
Residential mortgage	289	2,166	87	17	13
Qualifying revolving retail	-	65	-	49	54
Retail SME	77	123	45	14	12
Other retail	4	56	3	27	29
Total IRB approach	**1,340**	**2,553**	**602**	**128**	**137**
Specialised lending	**172**	**69**	**61**	**-**	**-**
Subject to standardised approach					
Residential mortgage	8	22	4	1	-
Corporate	1	4	8	3	1
Total standardised approach	**9**	**26**	**12**	**4**	**1**
Total	**1,521**	**2,648**	**675**	**132**	**138**
General reserve for credit losses			2,691		

Section 4

Securitisation

The Group engages in securitisation activities in relation to third parties, as well as its own assets.

Recent Securitisation Activity [APS 330 Attachment C, Table 5a]

The following table provides the amount of assets sold by the Group to securitisation special purpose vehicles (SPVs) and any gain or loss on sale.

Own asset securitisation activities may be used for funding, capital and liquidity purposes and can be broken down as follows:
- capital relief - significant risk transfer of the underlying exposure is achieved for regulatory purposes
- funding only - significant risk transfer is not achieved
- internal residential mortgage-backed securities (RMBS) - securities are issued and held internally for contingent liquidity purposes (also known as self-securitisation).

	3 months ended 31 Dec 18			
	Group originated capital relief	Group originated funding only	Group originated internal RMBS	Recognised gain or loss on sale
Underlying asset	**$m**	**$m**	**$m**	**$m**
Residential mortgage	1,630	-	7,550	-

There was no such activity in the three months ended 30 September 2018.

Securitisation Exposures Retained or Purchased [APS 330 Attachment C, Table 5b]

The following table provides the amount of securitisation exposures held in the banking book, broken down between on and off-balance sheet exposures.

Securitisation exposures include the following exposure types:
- liquidity facilities - facilities provided to securitisation vehicles for the primary purpose of funding any timing mismatches between receipts of funds on underlying exposures and payments on securities issued by the SPV or to cover the inability of the SPV to roll-over securities due to market disruption
- warehouse facilities - lending facilities provided to securitisation vehicles for the financing of exposures in a pool. These may be on a temporary basis pending the issue of securities or on an on-going basis
- credit enhancements - protection provided against credit losses to parties holding a securitisation exposure
- securities - holding of debt securities issued by securitisation vehicles
- derivatives - derivatives provided to securitisation vehicles, other than credit derivatives.

	As at 31 Dec 18			As at 30 Sep 18		
	On-balance sheet	Off-balance sheet	Total	On-balance sheet	Off-balance sheet	Total
Securitisation exposure type	**$m**	**$m**	**$m**	**$m**	**$m**	**$m**
Liquidity facilities	60	2,409	**2,469**	43	2,210	**2,253**
Warehouse facilities	7,924	2,171	**10,095**	8,036	3,627	**11,663**
Credit enhancements	-	-	**-**	-	-	**-**
Securities	9,960	-	**9,960**	9,433	-	**9,433**
Derivatives	22	48	**70**	26	25	**51**
Total	**17,966**	**4,628**	**22,594**	**17,538**	**5,862**	**23,400**

The Group has $215 million of derivatives exposures held in the trading book subject to IMA (default risk) under APS 116 *Capital Adequacy: Market Risk* as at 31 December 2018 (30 September 2018: $265 million).

Section 5

Liquidity Coverage Ratio

The Liquidity Coverage Ratio (LCR) for the Level 2 Group for the three months ended 31 December 2018 and 30 September 2018 is presented in the LCR disclosure template below and is based on a simple average of daily LCR outcomes excluding weekends.

There have been no material movements in the LCR from the September 2018 quarter to the December 2018 quarter. From 1 October 2018, caps on New Zealand dollar (NZD) liquid asset holdings included in the calculation of the LCR have been applied against RBNZ eligible securities rather than High-quality Liquid Assets (HQLA). This has resulted in RBNZ securities decreasing on average by $3 billion in the December 2018 quarter with an equivalent offset in HQLA.

Liquidity Coverage Ratio Disclosure Template [APS 330 Attachment F, Table 20]

		3 months ended			
		31 Dec 18 64 data points		30 Sep 18 65 data points	
		Total unweighted value (average) $m[1]	Total weighted value (average) $m	Total unweighted value (average) $m[1]	Total weighted value (average) $m
Liquid assets, of which:			**143,665**		**141,869**
1	High-quality liquid assets (HQLA) [2]	n/a	85,675	n/a	81,121
2	Alternative liquid assets (ALA)	n/a	55,342	n/a	55,317
3	Reserve Bank of New Zealand (RBNZ) securities [2]	n/a	2,648	n/a	5,431
Cash outflows					
4	Retail deposits and deposits from small business customers	187,522	21,784	185,462	21,558
5	of which: stable deposits	57,940	2,897	57,073	2,854
6	of which: less stable deposits	129,582	18,887	128,389	18,704
7	Unsecured wholesale funding	128,002	62,172	130,581	64,611
8	of which: operational deposits (all counterparties) and deposits in networks for cooperative banks	55,664	15,053	56,148	15,270
9	of which: non-operational deposits (all counterparties)	60,185	34,966	59,766	34,674
10	of which: unsecured debt	12,153	12,153	14,667	14,667
11	Secured wholesale funding	n/a	1,014	n/a	467
12	Additional requirements	173,269	33,905	171,512	32,296
13	of which: outflows related to derivatives exposures and other collateral requirements	17,558	17,558	16,817	16,817
14	of which: outflows related to loss of funding on debt products	-	-	-	-
15	of which: credit and liquidity facilities	155,711	16,347	154,695	15,479
16	Other contractual funding obligations	2,555	426	1,201	97
17	Other contingent funding obligations	74,122	5,313	73,588	5,336
18	**Total cash outflows**	**n/a**	**124,614**	**n/a**	**124,365**
Cash inflows					
19	Secured lending (e.g. reverse repos)	61,531	1,653	53,143	1,508
20	Inflows from fully performing exposures	21,177	12,057	21,882	12,818
21	Other cash inflows	263	263	465	465
22	**Total cash inflows**	**82,971**	**13,973**	**75,490**	**14,791**
23	**Total liquid assets**		**143,665**		**141,869**
24	**Total net cash outflows**		**110,641**		**109,574**
25	**Liquidity Coverage Ratio (%)**		**130%**		**129%**

(1) *Unweighted inflow and outflow values are outstanding balances maturing or callable within 30 days.*

(2) *Weighted values are calculated after applying caps to the amount of NZD liquid asset holdings.*

Section 6

Glossary

Term	Description
Additional regulatory specific provisions	That portion of collective provisions covering facilities where any assessment of probability of default or loss would give rise to a reasonable expectation that the facilities in question will need in the short term to be subject to a write-down or write-off, or assessment for impairment on an individual facility basis.
ADI	Authorised Deposit-taking Institution.
Advanced Internal Ratings Based approach (IRB)	The process used to estimate credit risk through the use of internally developed models to assess potential credit losses using the outputs from the PD, LGD and EaD models.
Advanced Measurement Approach (AMA)	The risk estimation process used for operational risk, combining internally developed risk estimation processes with an integrated risk management process, embedded within the business with loss event management.
Alternative Liquid Assets (ALA)	Assets that qualify for inclusion in the numerator of the LCR in jurisdictions where there is insufficient supply of HQLA in the domestic currency to meet the aggregate demand of banks with significant exposure in the domestic currency in the LCR framework. The CLF provided by the RBA to ADIs is treated as an ALA in the LCR.
APRA	Australian Prudential Regulation Authority.
APS	Prudential Standards issued by APRA applicable to ADIs.
BNZ	Bank of New Zealand.
Central Counterparty (CCP)	A clearing house which interposes itself, directly or indirectly, between counterparties to contracts traded in one or more financial markets, thereby insuring the future performance of open contracts.
CET1 capital ratio	CET1 capital divided by RWA.
Committed Liquidity Facility (CLF)	A facility provided by the RBA to certain ADIs to assist them in meeting the Basel III liquidity requirements.
Common Equity Tier 1 (CET1) capital	The highest quality component of capital. It is subordinated to all other elements of funding, absorbs losses as and when they occur, has full flexibility of dividend payments and has no maturity date. It is predominately comprised of paid-up ordinary share capital, retained profits plus certain other items as defined in APS 111 *Capital Adequacy: Measurement of Capital*.
Corporate (including SME)	Corporate (including SME) consists of corporations, partnerships or proprietorships not elsewhere classified and includes non-banking entities held by banks.
Credit Value Adjustment (CVA)	A capital charge to reflect potential mark-to-market losses due to counterparty migration risk for bilateral over-the-counter derivative contracts.
Default fund	Clearing members' funded or unfunded contributions towards, or underwriting of, a CCP's mutualised loss sharing arrangements.
Eligible Financial Collateral (EFC)	Under the standardised approach, EFC is the amount of cash collateral, netting and eligible bonds and equities. Under the IRB approach, EFC is limited to the collateral items detailed in APS 112 *Capital Adequacy*: *Standardised Approach to Credit Risk*. Recognition of EFC is subject to the minimum conditions detailed in APS 112.
Exposure at Default (EaD)	An estimate of the credit exposure amount an ADI may be exposed consequent to default of an obligor. EaD is presented net of EFC.
Extended Licensed Entity	The ADI and any APRA approved subsidiary entities assessed as effectively part of a single 'stand-alone' entity, as defined in APS 222 *Associations with Related Entities*.
General Reserve for Credit Losses (GRCL)	An estimate of the reasonable and prudent expected credit losses over the remaining life of the portfolio and on non-defaulted assets as set out under APS 220 *Credit Quality*. The GRCL is calculated as a collective provision for credit impairment, excluding securitisation exposures and provision on default no loss assets. The difference between the GRCL and accounting collective provision is covered with an additional top-up, created through an appropriation of retained profits to a non-distributable reserve when the regulatory reserve is greater than the accounting provision. All collective provisions on defaulted or otherwise non-performing assets, regardless of expected loss, are reported as additional regulatory specific provisions.
Group	NAB and its controlled entities.
High-quality Liquid Assets (HQLA)	Consists primarily of cash, deposits with central banks, Australian semi-government and Commonwealth government securities and securities issued by foreign sovereigns as defined in APS 210 *Liquidity.*
Impaired facilities	Impaired facilities consist of: - Retail loans (excluding unsecured portfolio managed facilities) which are contractually past due 90 days with security insufficient to cover principal and interest - Non-retail loans which are contractually past due and / or there is sufficient doubt about the ultimate collectability of principal and interest - Impaired off-balance sheet credit exposures where current circumstances indicate that losses may be incurred - Unsecured portfolio managed facilities that are 180 days past due (if not written off).
Internal Model Approach (IMA)	The approach used in the assessment of traded market risk. The Group uses, under approval from APRA, the IMA to calculate general market risk for all transactions in the trading book other than those covered by the standardised approach.
Level 2 Group	NAB and the entities it controls excluding superannuation and funds management entities and securitisation SPVs to which assets have been transferred in accordance with the requirements for regulatory capital relief in APS 120 *Securitisation*.
Leverage ratio	Tier 1 capital divided by exposures as defined by APS 110 *Capital Adequacy.* It is a simple, non-risk based supplementary measure to supplement the RWA based capital requirements. Exposures include on-balance sheet exposures, derivative exposures, securities financing transaction exposures and other off-balance sheet exposures.
Liquidity Coverage Ratio (LCR)	A metric that measures the adequacy of HQLA available to meet net cash outflows over a 30-day period during a severe liquidity stress scenario.
Loss Given Default (LGD)	An estimate of the expected severity of loss for a credit exposure following a default event. Regulatory LGDs reflect a stressed economic condition at the time of default.
NAB	National Australia Bank Limited ABN 12 004 044 937.
Net write-offs	Write-offs of loans and advances measured at amortised cost and fair value, net of recoveries.
Past due facilities ≥ 90 days	Well-secured assets that are more than 90 days past due and portfolio-managed facilities that are not well secured and between 90 and 180 days past due.
Probability of Default (PD)	An estimate of the likelihood of a customer defaulting or not repaying their borrowings and other obligations in the next 12 months.

Term	Description
Qualifying revolving retail exposures	Revolving exposures to individuals less than $100,000, unsecured and unconditionally cancellable by the Group. Only Australian retail credit cards qualify for this asset class.
RBA	Reserve Bank of Australia.
RBNZ	Reserve Bank of New Zealand.
Risk-weighted Assets (RWA)	A quantitative measure of risk required by the APRA risk-based capital adequacy framework, covering credit risk for on and off-balance sheet exposures, market risk, operational risk and interest rate risk in the banking book.
RMBS	Residential mortgage-backed securities.
SME	Small and medium sized enterprises.
Specific provision for credit impairment	The provision assessed on an individual basis in accordance with Australian Accounting Standard AASB 9 *Financial Instruments*.
SPV	Special purpose vehicle.
Standardised approach	An alternative approach to the assessment of credit, operational and traded market risk whereby an ADI uses external rating agencies to assist in assessing credit risk and/or the application of specific values provided by regulators to determine RWA.
Tier 1 capital	Tier 1 capital comprises CET1 capital and instruments that meet the criteria for inclusion as Additional Tier 1 capital set out in APS 111 *Capital Adequacy: Measurement of Capital*.
Tier 1 capital ratio	Tier 1 capital divided by RWA.
Tier 2 capital	Tier 2 capital includes other components of capital that, to varying degrees, fall short of the quality of Tier 1 capital but nonetheless contribute to the overall strength of an ADI and its capacity to absorb losses.
Total capital	The sum of Tier 1 capital and Tier 2 capital.
Total capital ratio	Total capital divided by RWA.
Write-offs	A reduction in the carrying amount of loans and advances where there is no reasonable expectation of recovery of a portion or the entire exposure.