PILLAR 3 REPORT 2018

National Australia Bank

Incorporating the requirements of APS 330

Third Quarter Update
as at 30 June 2018

"My patients weren't liking the shoes out there. That's when I decided to design my own range."

Caroline McCulloch
FRANKiE4 Footwear
Brisbane, QLD
NAB customer

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). This document is prepared in accordance with NAB Group Disclosure and External Communication Policy, and the quarterly reporting requirements of APRA Prudential Standard APS 330 *Public Disclosure*. It presents information on capital adequacy, credit risk and securitisation exposures and activity.

All figures in this report are in Australian dollars (AUD) unless otherwise noted.

1.1 Capital Adequacy Methodologies

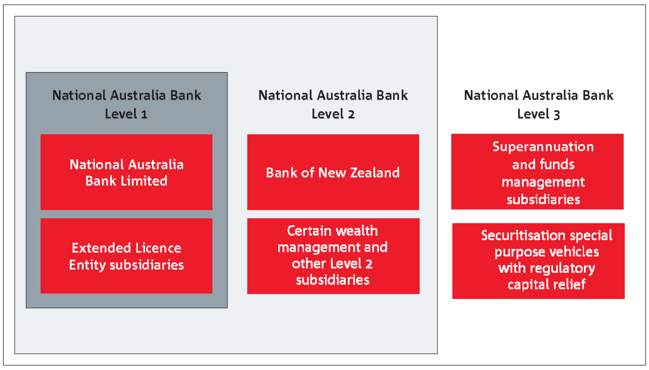
The following table sets out the NAB Group's approach to measuring capital adequacy as at 30 June 2018.

Methodology Approach	Credit Risk	Operational Risk	Non-Traded Market Risk	Traded Market Risk
National Australia Bank Limited and Bank of New Zealand	Advanced Internal Ratings Based (IRB) Approach	Advanced Measurement Approach (AMA)	Interest Rate Risk in the Banking Book (IRRBB)	Standardised and Internal Model Approach (IMA)

Bank of New Zealand (BNZ), the NAB Group's main operating subsidiary in New Zealand, is regulated by the Reserve Bank of New Zealand (RBNZ). Credit risk exposures consolidated in the NAB Group position 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.

This report applies to the Level 2 consolidated group (the Level 2 Group).

Section 2

Capital

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

The following tables provide the Risk-weighted Assets (RWA), capital ratios and leverage ratio for the Level 2 Group.

	As at 30 Jun 18 $m	31 Mar 18 $m
Credit risk [(1)]		
Subject to IRB approach		
Corporate (including Small and Medium Enterprises (SME))	117,792	115,478
Sovereign	1,394	1,291
Bank	11,414	10,751
Residential mortgage	103,796	102,448
Qualifying revolving retail	4,115	4,124
Retail SME	6,556	6,573
Other retail	3,482	3,517
Total IRB approach	**248,549**	**244,182**
Specialised lending (SL)	**61,922**	**59,899**
Subject to standardised approach		
Residential mortgage	1,583	1,623
Corporate	4,552	4,436
Other	511	513
Total standardised approach	**6,646**	**6,572**
Other		
Securitisation	4,427	4,313
Credit Value Adjustment	9,003	8,958
Central counterparty default fund contribution guarantee	1,132	1,029
Other [(2)]	4,965	4,929
Total other	**19,527**	**19,229**
Total credit risk	**336,644**	**329,882**
Market risk	9,070	8,656
Operational risk	37,726	39,027
Interest rate risk in the banking book	11,613	9,850
Total risk-weighted assets	**395,053**	**387,415**

(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 asset exposures and an RBNZ overlay adjustment to maintain a minimum risk profile for the New Zealand agriculture portfolio.*

Capital ratios (Level 2)	As at 30 Jun 18 %	31 Mar 18 %
Common Equity Tier 1 ratio	9.7	10.2
Tier 1 Capital ratio	11.9	12.4
Total Capital ratio	13.6	14.4

Leverage ratio	As at 30 Jun 18 $m	31 Mar 18 $m	31 Dec 17 $m	30 Sep 17 $m
Tier 1 Capital	46,967	48,048	47,396	47,417
Total exposures	887,837	864,625	870,574	856,241
Leverage ratio (%)	**5.3%**	**5.6%**	**5.4%**	**5.5%**

Section 3

Credit Risk Exposures

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

This table provides the credit risk exposure subject to the standardised and IRB approaches.

Gross credit risk exposure refers to the potential exposure as a result of a counterparty default prior to the application of credit risk mitigation. It represents the outstanding amount on drawn commitments plus a credit conversion factor on undrawn commitments on a given facility. For derivatives, exposure is defined as the mark-to-market plus a potential value of future movements. This table includes total Exposure at Default (EaD) net of Eligible Financial Collateral (EFC). The average credit risk exposure is the simple average of the gross credit risk exposure at the beginning and end of the reporting period.

For the IRB approach, EaD is reported gross of any specific provision and partial write-offs. For the standardised approach, EaD is reported net of any specific provision. Exposures exclude non-lending assets and third party securitisation exposures.

	As at 30 Jun 18					3 months ended 30 Jun 18
	On-balance sheet exposure	Non-market related off-balance sheet	Market related off-balance sheet	Total exposure gross of EFC	Total exposure net of EFC	Average total exposure gross of EFC
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach						
Corporate (including SME)	147,321	68,153	90,614	306,088	231,112	300,743
Sovereign	61,949	506	21,430	83,885	67,814	82,949
Bank	27,508	3,256	37,927	68,691	40,297	64,834
Residential mortgage	332,394	48,888	-	381,282	381,282	379,600
Qualifying revolving retail	5,775	5,774	-	11,549	11,548	11,583
Retail SME	13,492	4,182	-	17,674	17,671	17,682
Other retail	3,237	1,177	-	4,414	4,411	4,446
Total IRB approach	**591,676**	**131,936**	**149,971**	**873,583**	**754,135**	**861,837**
Specialised lending (SL)	**57,688**	**11,253**	**686**	**69,627**	**69,003**	**69,258**
Subject to standardised approach						
Residential mortgage	2,064	125	-	2,189	2,187	2,224
Corporate	7,314	567	72,364	80,245	12,861	69,800
Other	1,177	2	-	1,179	1,150	1,162
Total standardised approach	**10,555**	**694**	**72,364**	**83,613**	**16,198**	**73,186**
Total exposure (EaD)	**659,919**	**143,883**	**223,021**	**1,026,823**	**839,336**	**1,004,281**

	As at 31 Mar 18					3 months ended 31 Mar 18
	On-balance sheet exposure	Non-market related off-balance sheet	Market related off-balance sheet	Total exposure gross of EFC	Total exposure net of EFC	Average total exposure gross of EFC
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach						
Corporate (including SME)	144,188	66,634	84,576	295,398	225,040	291,944
Sovereign	64,998	508	16,507	82,013	69,248	84,451
Bank	24,458	3,443	33,077	60,978	37,650	61,840
Residential mortgage	328,796	49,122	-	377,918	377,918	377,418
Qualifying revolving retail	5,883	5,734	-	11,617	11,617	11,668
Retail SME	13,357	4,332	-	17,689	17,685	17,027
Other retail	3,273	1,206	-	4,479	4,477	4,465
Total IRB approach	**584,953**	**130,979**	**134,160**	**850,092**	**743,635**	**848,813**
Specialised lending (SL)	**57,172**	**10,997**	**718**	**68,887**	**68,282**	**68,505**
Subject to standardised approach						
Residential mortgage	2,137	123	-	2,260	2,258	2,250
Corporate	7,102	529	51,723	59,354	11,986	61,105
Other	1,144	1	-	1,145	1,116	1,140
Total standardised approach	**10,383**	**653**	**51,723**	**62,759**	**15,360**	**64,495**
Total exposure (EaD)	**652,508**	**142,629**	**186,601**	**981,738**	**827,277**	**981,814**

Section 4

Credit Provision and Losses

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

This table sets out information on credit risk by asset class, excluding non-lending assets and third party securitisation exposures. Specific provision for credit impairment represents the provision assessed on an individual basis in accordance with Australian Accounting Standard AASB 9 *Financial Instruments*.

	As at 30 Jun 18			3 months ended 30 Jun 18	
	Impaired facilities	Past due facilities ≥90 days	Specific provision for credit impairment[1]	Specific credit impairment charge	Net write-offs
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
Subject to IRB approach					
Corporate (including SME)	1,026	175	470	19	38
Residential mortgage	292	2,015	91	22	20
Qualifying revolving retail	-	72	-	47	50
Retail SME	82	106	46	11	8
Other retail	4	51	3	23	26
Total IRB approach	**1,404**	**2,419**	**610**	**122**	**142**
Specialised lending (SL)	**171**	**75**	**60**	**6**	**9**
Subject to standardised approach					
Residential mortgage	8	19	4	(1)	-
Corporate	2	1	8	1	-
Other	-	1	-	-	-
Total standardised approach	**10**	**21**	**12**	**-**	**-**
Total	**1,585**	**2,515**	**682**	**128**	**151**
General reserve for credit losses			**2,628**		

(1) *For regulatory reporting, collective provisions on defaulted or otherwise non-performing assets, regardless of expected loss, such as those for 90+ days past due retail and in default with no loss non-retail exposures, are treated as a regulatory specific provision. Such amounts have been excluded from the table and total $370 million (March 2018: $367 million).*

	As at 31 Mar 18			3 months ended 31 Mar 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)	1,051	154	496	31	11
Residential mortgage	286	1,956	93	17	10
Qualifying revolving retail	-	70	-	39	39
Retail SME	81	107	42	8	9
Other retail	4	52	3	26	26
Total IRB approach	**1,422**	**2,339**	**634**	**121**	**95**
Specialised lending (SL)	**177**	**70**	**64**	**(3)**	**5**
Subject to standardised approach					
Residential mortgage	9	18	5	-	1
Corporate	1	-	7	1	2
Total standardised approach	**10**	**18**	**12**	**1**	**3**
Total	**1,609**	**2,427**	**710**	**119**	**103**
General reserve for credit losses			**2,571**		

Section 5

Securitisation

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

This table shows exposures by type of facility provided to third party and own securitisation vehicles with capital relief where the exposures are risk weighted under APS 120 *Securitisation*.

	As at 30 Jun 18			As at 31 Mar 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	53	1,837	1,890	58	1,745	1,803
Warehouse facilities	6,860	3,050	9,910	6,382	2,907	9,289
Credit enhancements	-	-	-	141	230	371
Derivative transactions	20	27	47	34	-	34
Securities	10,039	-	10,039	9,362	-	9,362
Total securitisation exposures	**16,972**	**4,914**	**21,886**	**15,977**	**4,882**	**20,859**

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

This table shows activity with third party and own securitisation vehicles with capital relief in the three months to the end of the reporting period, including the notional amount of facilities provided and the value of debt securities issued by securitisation vehicles purchased.

	3 months ended 30 Jun 18	3 months ended 31 Mar 18
Securitisation exposure type	**$m**	**$m**
Liquidity facilities	159	343
Warehouse facilities	70	116
Credit enhancements	-	193
Derivative transactions [(1)]	-	34
Securities	1,442	390
Total securitisation activity	**1,671**	**1,076**

(1) *The amount of derivative transactions is measured as the credit equivalent amount as defined in APS 112 Capital Adequacy: Standardised Approach to Credit Risk.*

This table shows the value of assets which have been transferred to securitisation special purpose vehicles in the three months to the end of the reporting period, including to own securitisation vehicles with capital relief.

	3 months ended 30 Jun 18			3 months ended 31 Mar 18		
	Amount securitised during period directly originated	Amount securitised during period indirectly originated	Recognised gain or loss on sale	Amount securitised during period directly originated	Amount securitised during period indirectly originated	Recognised gain or loss on sale
Underlying asset	**$m**	**$m**	**$m**	**$m**	**$m**	**$m**
Residential mortgage	-	-	-	5,800	-	-
Total securitisation activity	**-**	**-**	**-**	**5,800**	**-**	**-**

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 (IRB) approach	The process used to estimate credit risk through the use of internally developed models to assess potential credit losses using the outputs from the probability of default, loss given default and exposure at default 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.
APS	Prudential Standards issued by APRA applicable to ADIs.
APRA	Australian Prudential Regulation Authority.
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.
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 common shares; retained profits; undistributed current period earnings; as well as other elements as defined in APS 111 *Capital Adequacy: Measurement of Capital.*
CET1 Capital ratio	CET1 Capital divided by RWA.
Corporate (including SME)	Corporate (including SME) consists of corporations, partnerships or proprietorships not elsewhere classified and includes non-banking entities held by banks.
Credit enhancements	In relation to securitisation exposures, credit enhancements are arrangements in which the Level 2 Group holds a securitisation exposure that is able to absorb losses in the pool, providing credit protection to investors or other parties to the securitisation.
Credit Value Adjustment (CVA)	A capital charge to reflect potential mark-to-market losses due to counterparty migration risk on 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.
Derivative transactions	In relation to securitisation exposures, derivative transactions include interest rate and currency derivatives provided to securitisation vehicles, but do not include credit derivative transactions.
Exposure at Default (EaD)	An estimate of the credit exposure amount a bank may be exposed consequent to default of an obligor.
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 eligible financial collateral is subject to the minimum conditions detailed in APS112.
Extended Licensed Entity	The ADI itself 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 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.
Internal Model Approach (IMA)	The approach used in the assessment of traded market risk. The NAB 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.
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 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).
Level 2 Group	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.*
Leverage ratio	A simple, non-risk based supplementary measure that uses exposures to supplement the risk-weighted assets based capital requirements and is prepared in accordance with APS 110 *Capital Adequacy.*
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.
Liquidity facilities	In relation to securitisation exposures, liquidity facilities are facilities provided to a special purpose vehicle (SPV) for the primary purpose of funding any timing mismatches between receipts of funds on underlying exposures and payments on securities issued by the SPV (asset liquidity facilities), or to cover the inability of the SPV to roll over asset-backed commercial paper (standby liquidity facilities).
NAB Group	NAB and its controlled entities.
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.
Qualifying revolving retail exposures	Revolving exposures to individuals less than $0.1m, unsecured and unconditionally cancellable by the NAB Group, including Australian retail credit cards.
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.
Securities	In relation to securitisation exposures, debt securities issued by a securitisation vehicle.

Term	Description
Securitisation	Structured finance technique which involves pooling, packaging cash-flows and converting financial assets into securities that can be sold to investors.
SME	Small and medium enterprises.
Specific provision	Specific provision for credit impairment represents the provision assessed on an individual basis in accordance with Australian Accounting Standard AASB 9 *Financial Instruments*.
Standardised approach	An alternative approach to the assessment of credit, operational and traded market risk whereby the 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 Common Equity Tier 1 (CET1) Capital and instruments issued by the NAB Group 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.
Tier 2 Capital ratio	Tier 2 Capital divided by RWA.
Total Capital	The sum of Tier 1 Capital and Tier 2 Capital.
Total Capital ratio	The sum of Tier 1 Capital and Tier 2 Capital divided by RWA.
Warehouse facilities	In relation to securitisation exposures, warehouse facilities are lending facilities provided to a special purpose vehicle 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.
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.