Disclosure Statement.

For the six months ended 31 December 2014.

Kiwibank.

Number 54

Contents.

General matters

Details of incorporation

Kiwibank Limited ("**Kiwibank**") is a company domiciled in New Zealand and was incorporated in New Zealand under the Companies Act 1993 on 4 May 2001. On 29 November 2001, Kiwibank was registered as a bank under the Reserve Bank of New Zealand Act 1989 (the "**RBNZ Act**") and was required to comply with the conditions of registration as laid down by the Reserve Bank of New Zealand ("**RBNZ**") from that date onwards.

This Disclosure Statement has been issued by Kiwibank for the six months ended 31 December 2014, in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (the "**Order**"). Words and phrases defined by the Order have the same meanings when used in this Disclosure Statement.

In this Disclosure Statement, "**Banking Group**" means Kiwibank's financial reporting group, which consists of Kiwibank, all of its wholly owned entities and all other entities consolidated for financial reporting purposes.

Address for service

The registered office and address for service is: Kiwibank Limited, New Zealand Post House, Level 12, 7 Waterloo Quay, Wellington 6011, New Zealand.

Other material matters

The Board of Directors of Kiwibank (the "**Board**") are of the opinion that, other than outlined below, there are no matters relating to the business or affairs of Kiwibank or the Banking Group, which would, if disclosed in this Disclosure Statement, materially affect the decision of a person to subscribe for debt securities of which Kiwibank or any member of the Banking Group is the issuer.

Kiwibank has determined that it is appropriate to modernise its core banking system over the next 3-5 years. Therefore, there will be a higher level of investment during this period which will be actively managed to minimise the risk of unplanned costs or operational risk from a significant change programme.

Pending proceedings or arbitration

The Board are of the opinion that, other than outlined below, there are no pending legal proceedings or arbitration concerning Kiwibank or any member of the Banking Group, whether in New Zealand or elsewhere, that may have a material adverse effect on Kiwibank or the Banking Group.

In June 2013, a group called Fair Play on Fees announced plans for a representative action against banks in New Zealand in relation to certain default fees charged to New Zealand customers. In November 2013, the group issued proceedings against Kiwibank. The potential outcome of the proceedings cannot be determined with any certainty at this stage.

Credit ratings

Kiwibank has the following credit ratings applicable to its long term unsecured obligations payable in New Zealand, in New Zealand dollars:

Rating agency	Credit rating and outlook
Standard & Poor's (Australia) Pty Limited ("**S&P**")	A+ (negative outlook)
Moody's Investors Service	Aa3 (stable outlook)
Fitch Ratings	AA+ (positive outlook)

Conditions of registration

Non-compliance with conditions of registration

Lindsay Wright was appointed to the boards of certain sister companies of Kiwibank on 18 August 2014. The Reserve Bank has confirmed that these appointments do not disqualify her from being considered an independent director of Kiwibank. However, this confirmation was not obtained until 15 October 2014 and the Reserve Bank considers that Kiwibank was in breach of condition 6(c) of its conditions of registration during the intervening period.

Changes in conditions of registration

With effect from 1 November 2014, the Bank's conditions of registration were amended to refer to revised versions of Connected Exposures Policy (BS8) and Framework for Restrictions on High-LVR Residential Mortgage Lending (BS19).

Directorate

On 12 December 2014 Mark Yeoman resigned as an alternate director.

There have been no other changes in the Board during the period ended 31 December 2014.

Responsible persons

Rob Morrison and Alison Gerry have been authorised in writing to sign this Disclosure Statement in accordance with Section 82 of the RBNZ Act, on behalf of the other directors, being:

Robert William Bentley Morrison	Hon. Sir Michael John Cullen
Alison Rosemary Gerry	Brian Joseph Roche
Catherine Maria Savage	David Stephen Willis
Carol Anne Campbell	Lindsay Wright

Auditors

The auditor whose review opinion is referred to in this disclosure statement is Chris Barber assisted by PricewaterhouseCoopers, acting as agent on behalf of the Office of the Auditor-General. His address for service is PricewaterhouseCoopers, 113-119 The Terrace, Wellington, New Zealand.

Guarantees

As at the date the Board approved this Disclosure Statement, the payment obligations of Kiwibank have the benefit of a deed poll guarantee by NZP (the "**NZP Guarantee**") and (in relation to certain debt securities issued by Kiwibank) a guarantee by Kiwi Covered Bond Trustee Limited (the "**Covered Bond Guarantee**"). A summary of the details of each guarantee are set out below.

Further details on the NZP Guarantee can be obtained by referring to Kiwibank's Disclosure Statement for the year ended 30 June 2014 which is available at www.kiwibank.co.nz.

NZP Guarantee

NZP supports Kiwibank as a registered bank. By way of example, NZP has contracted with Kiwibank to offer banking services through NZP's existing retail network for an unlimited period.

The following is a summary of the main features of the NZP Guarantee as at 31 December 2014:

i. The address for service of NZP is: New Zealand Post House, Level 12, 7 Waterloo Quay, Wellington 6011, New Zealand.

ii. NZP is not a member of the Banking Group (as that term is defined in the Order).

iii. The NZP Guarantee is an unsecured guarantee of all the payment obligations (excluding any payment obligations, the terms of which expressly provide in writing that they do not have the benefit of the NZP Guarantee) of Kiwibank. The NZP Guarantee can be terminated on not less than three months' notice being given to creditors (as that term is defined in the NZP Guarantee). Any such termination does not affect any existing payment obligations owed under the NZP Guarantee at the termination date. The NZP Guarantee has no expiry date.

NZP has a credit rating applicable to its long term unsecured obligations payable in New Zealand, in New Zealand dollars, from S&P of A+ (negative outlook).

Covered Bond Guarantee

Certain debt securities ("**Covered Bonds**") issued by Kiwibank are guaranteed by Kiwi Covered Bond Trustee Limited (the "**Covered Bond Guarantor**"), solely in its capacity as Trustee of Kiwibank Covered Bond Trust. The Covered Bond Guarantor has guaranteed the payment of interest and principal of Covered Bonds, pursuant to a guarantee which is secured over a pool of assets. The Covered Bond Guarantor's address for service is Level 35, Vero Centre, 48 Shortland Street, Auckland, New Zealand. The Covered Bond Guarantor is not a member of the Banking Group. The Covered Bonds have been assigned a long term rating of Aaa and AAA by Moody's Investors Service and Fitch Ratings respectively.

Directors' statement

The directors of Kiwibank state that each director believes, after due enquiry, that:

1. As at the date on which the Disclosure Statement is signed:
   i. the Disclosure Statement contains all the information that is required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014; and
   ii. the Disclosure Statement is not false or misleading.
2. During the period ended 31 December 2014:
   i. Kiwibank has complied with the conditions of registration applicable during the period, except as stated below;
   ii. credit exposures to connected persons were not contrary to the interests of the Banking Group;
   iii. Kiwibank had systems in place to monitor and control adequately the Banking Group's material risks, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk and other business risks, and that those systems were being properly applied.

Lindsay Wright was appointed to the boards of certain sister companies of Kiwibank on 18 August 2014. The Reserve Bank has confirmed that these appointments do not disqualify her from being considered an independent director of Kiwibank. However, this confirmation was not obtained until 15 October 2014 and the Reserve Bank considers that Kiwibank was in breach of condition 6(c) of its conditions of registration during the intervening period.

Signed by Rob Morrison and Alison Gerry as directors and responsible persons on behalf of all the directors listed in the Directorate of this Disclosure Statement:

17 February 2015

Interim financial statements

Consolidated income statement

For the six months ended 31 December 2014

		The Banking Group		
Dollars in millions	Note	**Unaudited 6 months ended 31/12/14**	Unaudited 6 months ended 31/12/13	Audited year ended 30/06/14
Interest income		**472**	387	798
Interest expense		**(293)**	(247)	(505)
Net interest income		**179**	140	293
Net gains/(losses) on financial instruments at fair value	2	**3**	2	3
Other income		**101**	89	183
Total operating income		**283**	231	479
Operating expenses		**(176)**	(160)	(344)
Impairment (losses)/reversals on loans and advances	9	**(9)**	1	4
Profit before taxation		**98**	72	139
Income tax expense		**(27)**	(20)	(39)
Profit after taxation		**71**	52	100
Attributable to:				
Owners of the parent		**71**	52	100
Non-controlling interest		**–**	–	–

Consolidated statement of comprehensive income

For the six months ended 31 December 2014

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/14**	Unaudited 6 months ended 31/12/13	Audited year ended 30/06/14
Profit after taxation	**71**	52	100
Other comprehensive income			
Net gain/(loss) from changes in reserves that may subsequently be reclassified to profit or loss			
Available-for-sale reserve (net of tax)	**4**	(4)	(4)
Cash flow hedge reserve (net of tax)	**(36)**	19	18
Other comprehensive income for the period/year	**(32)**	15	14
Total comprehensive income for the period/year	**39**	67	114
Attributable to:			
Owners of the parent	**39**	67	114
Non-controlling interest	**–**	–	–

The notes on pages 8 to 24 form part of these interim financial statements.

Interim financial statements continued

Consolidated statement of changes in equity

For the six months ended 31 December 2014

	The Banking Group						
Dollars in millions	Fully Paid Ordinary Shares	Retained earnings	Available-For-Sale Reserve	Cash Flow Hedge Reserve	Total Equity Attributable to Owners of the Parent	Non-Controlling Interest	Total
Balance at 1 July 2013	360	345	2	2	709	149	858
Unaudited 6 months ended 31 December 2013							
Unaudited profit for the period	–	52	–	–	52	–	52
Other comprehensive income							
Available-for-sale financial assets (net of tax)	–	–	(4)	–	(4)	–	(4)
Cash flow hedges (net of tax)	–	–	–	19	19	–	19
Total other comprehensive income	–	–	(4)	19	15	–	15
Total comprehensive income	–	52	(4)	19	67	–	67
Transactions with owners							
Dividends paid to non-controlling interest	–	(4)	–	–	(4)	–	(4)
Unaudited balance at 31 December 2013	360	393	(2)	21	772	149	921
Audited year ended 30 June 2014							
Audited profit for the year	–	100	–	–	100	–	100
Other comprehensive income							
Available-for-sale financial assets (net of tax)	–	–	(4)	–	(4)	–	(4)
Cash flow hedges (net of tax)	–	–	–	18	18	–	18
Total other comprehensive income	–	–	(4)	18	14	–	14
Total comprehensive income	–	100	(4)	18	114	–	114
Transactions with owners							
Issue of share capital	40	–	–	–	40	–	40
Dividends paid to non-controlling interest	–	(9)	–	–	(9)	–	(9)
Audited balance at 30 June 2014	400	436	(2)	20	854	149	1,003
Unaudited 6 months ended 31 December 2014							
Unaudited profit for the period	**–**	**71**	**–**	**–**	**71**	**–**	**71**
Other comprehensive income							
Available-for-sale financial assets (net of tax)	**–**	**–**	**4**	**–**	**4**	**–**	**4**
Cash flow hedges (net of tax)	**–**	**–**	**–**	**(36)**	**(36)**	**–**	**(36)**
Total other comprehensive income	**–**	**–**	**4**	**(36)**	**(32)**	**–**	**(32)**
Total comprehensive income	**–**	**71**	**4**	**(36)**	**39**	**–**	**39**
Transactions with owners							
Transaction with non-controlling interest	**–**	**–**	**–**	**–**	**–**	**1**	**1**
Dividends paid on ordinary shares	**–**	**(1)**	**–**	**–**	**(1)**	**–**	**(1)**
Dividends paid to non-controlling interest	**–**	**(4)**	**–**	**–**	**(4)**	**–**	**(4)**
Unaudited balance at 31 December 2014	**400**	**502**	**2**	**(16)**	**888**	**150**	**1,038**

The notes on pages 8 to 24 form part of these interim financial statements.

Interim financial statements continued

Consolidated balance sheet

As at 31 December 2014

Dollars in millions	Note	**Unaudited 31/12/14**	Unaudited 31/12/13	Audited 30/06/14
		The Banking Group		
Assets				
Cash and cash equivalents		**448**	561	461
Due from NZP related parties	3	**77**	76	77
Due from other financial institutions	4	**119**	164	121
Financial assets held for trading		**48**	44	44
Available-for-sale assets		**1,083**	1,051	1,093
Loans and advances	5	**15,054**	13,952	14,630
Derivative financial instruments		**184**	150	130
Property, plant and equipment		**15**	14	13
Intangible assets		**97**	80	86
Deferred taxation		**17**	7	5
Other assets		**19**	13	16
Total assets		**17,161**	16,112	16,676
Liabilities				
Due to other financial institutions		**118**	171	185
Due to NZP related parties	3	**8**	14	27
Deposits and other borrowings	6	**13,283**	12,412	12,751
Derivative financial instruments		**302**	208	236
Debt securities issued	7	**2,067**	2,152	2,143
Current tax liability		**17**	10	8
Other liabilities		**76**	75	76
Subordinated debt	8	**252**	149	247
Total liabilities		**16,123**	15,191	15,673
Equity attributable to owners of the parent				
Share capital		**400**	360	400
Reserves		**488**	412	454
Total equity attributable to owners of the parent		**888**	772	854
Non-controlling interest		**150**	149	149
Total equity		**1,038**	921	1,003
Total liabilities and shareholders equity		**17,161**	16,112	16,676

The notes on pages 8 to 24 form part of these interim financial statements.

Interim financial statements continued

Consolidated cash flow statement

For the six months ended 31 December 2014

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/14**	Unaudited 6 months ended 31/12/13	Audited year ended 30/06/14
Cash flows from operating activities			
Interest received	**477**	391	805
Interest paid	**(277)**	(247)	(502)
Fees and other income	**101**	89	183
Operating expenses paid	**(166)**	(151)	(311)
Taxes paid	**(17)**	(19)	(38)
Net cash flows from operating activities before changes in operating assets and liabilities	**118**	63	137
Net changes in operating assets and liabilities			
Decrease in financial assets held for trading	**–**	109	111
Decrease/(increase) in available-for-sale assets	**16**	(92)	(132)
Increase in loans and advances	**(418)**	(685)	(1,406)
(Increase)/decrease in net amounts due from related parties	**(20)**	–	12
Decrease/(increase) in balances due from other financial institutions	**3**	(5)	37
Increase in deposits and other borrowing	**517**	297	632
(Decrease) in balances due to other financial institutions	**(67)**	(99)	(85)
Net cash flows provided by operating activities	**149**	(412)	(694)
Cash flows from investing activities			
Purchase of property, plant and equipment	**(5)**	(1)	(3)
Purchase of intangible assets	**(21)**	(17)	(40)
Net cash flows from investing activities	**(26)**	(18)	(43)
Cash flows from financing activities			
Issue of share capital	**–**	–	40
Net (decrease)/increase in debt securities issued	**(135)**	643	719
Net (redemption)/issue of subordinated debt	**–**	(60)	40
Dividends paid on ordinary shares	**(1)**	–	–
Dividends paid to non-controlling interest	**(4)**	(4)	(9)
Net cash flows from financing activities	**(140)**	579	790
(Decrease)/increase in cash and cash equivalents	**(17)**	149	53
Cash and cash equivalents at beginning of the period/year	**461**	415	415
Effect of exchange translation adjustments	**4**	(3)	(7)
Cash and cash equivalents at end of the period/year	**448**	561	461

The notes on pages 8 to 24 form part of these interim financial statements.

Notes to the interim financial statements

1. Summary of significant accounting policies

1.1 Reporting entity

In these interim financial statements, the reporting entity is Kiwibank Limited ("**Kiwibank**" or the "**Bank**"). The "**Banking Group**" consists of Kiwibank and its subsidiaries. Kiwibank is a profit oriented entity incorporated and domiciled in New Zealand under the Companies Act 1993 and is registered as a bank under the Reserve Bank of New Zealand Act 1989.

The principal activity of the Banking Group is the provision of retail and banking products and services to individuals and small to medium-sized businesses.

Kiwibank's immediate parent company is Kiwi Group Holdings Limited ("**KGHL**"), its ultimate parent company is New Zealand Post Limited ("**NZP**") and the ultimate shareholder of Kiwibank is the New Zealand Crown (the "**Crown**").

1.2 Basis of preparation

These interim financial statements are for the Banking Group for the six months ended 31 December 2014 and have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand, as appropriate for profit oriented entities. They comply with NZ IAS 34 *Interim Financial Reporting*, IAS 34 *Interim Financial Reporting* and the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (the "**Order**"). These interim financial statements should be read in conjunction with the Banking Group's financial statements for the year ended 30 June 2014, which comply with International Financial Reporting Standards ("**IFRS**") as issued by the International Accounting Standards Board.

Measurement base

These interim financial statements are based on the general principles of historic cost accounting, modified by the application of fair value measurements for available-for-sale financial assets, financial instruments held at fair value through profit or loss and all derivative contracts. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges, and otherwise carried at amortised cost, are adjusted to record changes in fair value attributable to the risks that are being hedged.

1.3 Accounting policies

The accounting policies adopted in the preparation of the interim financial statements are consistent with those followed in the preparation of the Banking Group's annual financial statements for the year ended 30 June 2014, except for the adoption of new standards and interpretations effective as of 1 July 2014.

The Banking Group has applied, for the first time, the following new standards and amendments:

NZ IAS 32 (Amendment) – *Financial Instruments: Presentation* – Offsetting Financial Assets and Financial Liabilities.

The application of the above standard does not have a material effect on the financial results of the Banking Group.

1.4 Basis of consolidation

The consolidated interim financial statements of the Banking Group comprise the interim financial statements of Kiwibank and its subsidiaries for the period ended 31 December 2014, using the acquisition method. Subsidiaries are entities that are controlled by Kiwibank.

1.5 Functional and presentation currency

The functional and presentation currency of Kiwibank and the Banking Group is New Zealand dollars. All amounts are expressed in millions of New Zealand dollars, unless otherwise stated.

Notes to the interim financial statements continued

2. Net gains/(losses) on financial instruments at fair value

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/14**	Unaudited 6 months ended 31/12/13	Audited year ended 30/06/14
Derivative financial instruments held for trading	**(2)**	(1)	(2)
Financial assets held for trading	**3**	1	2
Cumulative gain transferred from available-for-sale reserve	**–**	1	1
Cumulative loss transferred from cash flow hedge reserve	**1**	–	1
Net foreign exchange gains	**1**	1	1
Total gains on financial instruments	**3**	2	3

Net ineffectiveness on qualifying cash flow hedges is $nil (31 December 2013: $0.1m; 30 June 2014: $0.1m). Net ineffectiveness on qualifying fair value hedges is ($0.1m) (31 December 2013: $0.2m; 30 June 2014: $0.4m).

3. Related parties

	The Banking Group
Dollars in millions	**Unaudited as at 31/12/14**
Outstanding balances	
Due to NZP related parties	**8**
Included in deposits	**27**
Included in non-controlling interest	**1**
Total balances due to related parties	**36**
Receivables	
Due from NZP related parties	**77**
Included in loans and advances	**2**
Total balances due from related parties	**79**

NZP has a credit facility with the Banking Group, allowing NZP to draw down to the extent that the Banking Group does not exceed credit exposure to connected persons of 15% of Tier 1 capital, as required in its banking conditions of registration. When loans are drawn down the transaction is undertaken at market interest rates. As at 31 December 2014 the amount owed by NZP to the Banking Group was $76m (31 December 2013: $76m; 30 June 2014: $76m). This does not exceed the 15% of Tier 1 capital requirement.

The Crown has entered into a $300m uncalled capital facility with NZP where NZP can drawdown capital for contingent events around Kiwibank's conditions of registration. The annualised cost of this facility on charged to Kiwibank by NZP is $3.6m.

During the period ended 31 December 2014, the Banking Group transferred the members and assets of the Kiwibank KiwiSaver Scheme to the Kiwi Wealth KiwiSaver Scheme, operated by Kiwi Wealth Limited ("**KWL**"), a fellow member of the KGHL Group. In compensation for the transfer, the Banking Group received $2.1m from KWL, which has been recognised in other income.

Notes to the interim financial statements continued

4. Due from other financial institutions

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/14**	Unaudited as at 31/12/13	Audited as at 30/06/14
Unsettled receivables	**–**	98	5
Short term advances due from other financial institutions	**11**	1	20
Collateralised loans	**108**	65	96
Total – current	**119**	164	121

As at 31 December 2014, included within the balance above, is $108.4m of collateral pledged by Kiwibank in respect of its credit support annex obligations to derivative counterparties (31 December 2013: $64.9m; 30 June 2014: $95.9m).

5. Loans and advances

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/14**	Unaudited as at 31/12/13	Audited as at 30/06/14
Loans and advances at amortised cost	**15,111**	14,019	14,689
Allowance for impairment losses (note 9)	**(57)**	(67)	(59)
Total net loans and advances	**15,054**	13,952	14,630
Current	**1,038**	1,088	1,102
Non-current	**14,016**	12,864	13,528

6. Deposits and other borrowing

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/14**	Unaudited as at 31/12/13	Audited as at 30/06/14
Demand deposits non-interest bearing	**1,213**	1,101	1,078
Demand deposits bearing interest	**2,608**	2,491	2,553
Term deposits	**9,462**	8,820	9,120
Total deposits from customers	**13,283**	12,412	12,751
Current	**12,924**	12,075	12,398
Non-current	**359**	337	353

In the event of the liquidation of Kiwibank, deposit holders will rank equally with all other creditors but ahead of subordinated debt holders and shareholders. In addition, all payment obligations of Kiwibank, excluding any payment obligations, the terms of which expressly provide that they do not have the benefit of the guarantee, are guaranteed under the NZP Guarantee.

The Kiwibank PIE Unit Trust (the "**Trust**"), established under the Unit Trusts Act 1960 in May 2008, operates three funds; the PIE Term Deposit Fund, the Notice Saver and PIE Online Call Fund. Kiwibank Investment Management Limited is the Issuer and Manager (the "**Manager**"), Trustees Executors Limited is the Trustee and Kiwibank is the Promoter of the Trust. Units in the Trust do not directly represent deposits or liabilities of Kiwibank, however the Trust is invested exclusively in term and call deposits with Kiwibank. At 31 December 2014, $3,664m of the Trust's funds were invested in Kiwibank products or securities (31 December 2013: $3,632m; 30 June 2014: $3,679m).

Kiwibank guarantees the payment obligations of the Manager and any amounts owing to Unitholders under the Trust Deed in respect of their Units and agrees to pay to Unitholders any shortfall between the amount they may receive on redeeming their Units or in the winding up of the Trust and the balance of their Unit Accounts.

Notes to the interim financial statements continued

7. Debt securities issued

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/14**	Unaudited as at 31/12/13	Audited as at 30/06/14
Short term debt			
Commercial paper at fair value through profit or loss	**531**	903	731
Certificates of deposit – amortised cost	**339**	340	206
Long term debt			
Medium term notes	**989**	705	1,005
Covered bonds	**192**	204	191
Fair value hedge adjustment	**16**	–	10
Total debt securities issued	**2,067**	2,152	2,143
Current	**870**	1,600	1,212
Non-current	**1,197**	552	931

In the event of the liquidation of Kiwibank, holders of these debt securities, with the exception of covered bonds, will rank equally with all other creditors but ahead of subordinated debt holders and shareholders. In addition, all payment obligations of Kiwibank, excluding any payment obligations, the terms of which expressly provide that they do not have the benefit of a deed poll guarantee (the "**NZP Guarantee**") provided by NZP, are guaranteed under the NZP Guarantee.

The guarantee arrangements and other details relating to covered bonds are disclosed in note 17.

Kiwibank has not had any defaults of principal, interest or other breaches with respect to debt securities issued during the period (six months ended 31 December 2013: none; year ended 30 June 2014: none).

8. Subordinated debt

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/14**	Unaudited as at 31/12/13	Audited as at 30/06/14
Face value	**250**	150	250
Interest accrued	**3**	1	1
Transaction costs	**(3)**	(2)	(4)
Fair value hedge adjustment	**2**	–	–
Total subordinated debt	**252**	149	247
Current	**3**	1	1
Non-current	**249**	148	246

During the period $nil of subordinated debt was issued and $nil of subordinated debt was called by the Banking Group (period ended 31 December 2013: $nil was issued and $60m was called; year ended 30 June 2014: $100m was issued and $60m was called).

As at 31 December 2014, $208m (31 December 2013: $108m; 30 June 2014: $208m) of the subordinated debt qualified as Tier 2 capital for Capital Adequacy calculation purposes.

The contractual terms of subordinated debt instruments on issue expressly provide that they do not have the benefit of the NZP Guarantee.

The Banking Group has not had any defaults of principal, interest or other breaches with respect to these liabilities during the period (period ended 31 December 2013: none; year ended 30 June 2014: none).

Notes to the interim financial statements continued

8. Subordinated debt continued

The subordinated debt instruments on issue are subordinate to all other general liabilities of the Banking Group and are denominated in New Zealand dollars.

The terms and conditions of the subordinated debt instruments on issue are as follows.

Instrument	Issue date	Amount $m's	Coupon rate	Call date	Maturity date	Credit rating
Subordinated bonds	10 December 2012	150	5.80% p.a.	15 December 2017	15 December 2022	BB
Capital notes	6 June 2014	100	6.61% p.a.	15 July 2019	15 July 2024	BB+

Capital Notes

The Capital Notes have been issued by Kiwi Capital Funding Limited ("**KCFL**"), an entity controlled by Kiwibank and which is part of the consolidated Banking Group. The entire proceeds from the issue of Capital Notes was used to purchase convertible subordinate bonds issued by Kiwibank (the "**Kiwibank Bonds**"). Interest on the Capital Notes is payable semi-annually at an initial rate of 6.61% p.a. subject to the condition that KCFL receives a corresponding payment of interest from Kiwibank on its investment in the Kiwibank Bonds. KCFL's obligation to pay interest changes or will terminate should any of the Kiwibank Bonds be converted into ordinary shares or written off. The Capital Notes have a maturity date of 15 July 2024, however, KCFL will make early repayment of the Capital Notes should Kiwibank elect to make early repayment of the Kiwibank Bonds as outlined above. KCFL's obligation to repay the capital notes changes or will terminate should any of the Kiwibank Bonds be converted into ordinary shares or written off.

9. Asset quality

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/14**	Unaudited as at 31/12/13	Audited as at 30/06/14
Allowance for impairment losses in balance sheet			
Collective allowance for impairment losses	**40**	42	37
Allowance for individually impaired assets	**17**	25	22
Total allowance for impairment losses	**57**	67	59

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/14**	Unaudited 6 months ended 31/12/13	Audited year ended 30/06/14
Impairment losses per income statement			
Collective impairment/(reversals) on loans and advances	**3**	(2)	(3)
Individual impairment/(reversals) on loans and advances	**6**	1	(1)
Total impairment losses/(reversals) per income statement	**9**	(1)	(4)

Notes to the interim financial statements continued

9. Asset quality continued

Summary of lending

Allocations in the following summary are those used by the Bank and reflect the commercial nature of the loan.

Unaudited as at 31 December 2014 Dollars in millions	The Banking Group Loans and advances to retail customers	Loans and advances to corporate and institutional customers	Total
Neither past due nor impaired	13,466	1,476	14,942
Past due but not impaired (a)	136	3	139
Impaired (b)	9	21	30
Gross	13,611	1,500	15,111
Collective allowance for impairment (c)	(19)	(21)	(40)
Individual allowance for impairment (d)	(3)	(14)	(17)
Net loans and advances	13,589	1,465	15,054

a: Loans and advances past due but not impaired

Unaudited as at 31 December 2014 Dollars in millions	The Banking Group Residential unsecured lending	Residential mortgage loans	Corporate exposures	Total
Past due less than 30 days	28	68	1	97
Past due 30 – 59 days	8	14	1	23
Past due 60 – 89 days	4	3	–	7
Past due 90 days or greater	4	7	1	12
Total past due but not impaired	44	92	3	139

b: Impaired assets

The breakdown of the gross amount of individually impaired loans and advances by class, as defined by the Order, is as follows:

Unaudited 6 months ended 31 December 2014 Dollars in millions	The Banking Group Residential unsecured lending	Residential mortgage loans	Corporate exposures	Total
Gross impaired				
Balance at beginning of the period	1	14	29	44
Transfers from performing	2	3	7	12
Transfers to performing	–	(2)	–	(2)
Asset realisations and loans repaid	–	(1)	(12)	(13)
Amounts written off	(2)	(2)	(7)	(11)
Balance at end of the period	1	12	17	30
Individual allowance for impairment	(1)	(7)	(9)	(17)
Total net impaired assets	–	5	8	13

Notes to the interim financial statements continued

9. Asset quality continued

c: The reconciliation of the collective allowance account for losses on loans and advances by class is as follows:

	The Banking Group			
Unaudited 6 months ended 31 December 2014 Dollars in millions	Residential unsecured lending	Residential mortgage loans	Corporate exposures	Total
Balance at beginning of the period	8	15	14	37
Impairment losses on loans not at fair value through profit or loss	–	1	2	3
Total collective allowance for impairment losses	**8**	**16**	**16**	**40**

d: Reconciliation of the individual allowance for impairment

	The Banking Group			
Unaudited 6 months ended 31 December 2014 Dollars in millions	Residential unsecured lending	Residential mortgage loans	Corporate exposures	Total
Balance at beginning of the period	1	9	12	22
Impairment losses on loans and advances	2	1	5	8
Amounts written off	(2)	(2)	(7)	(11)
Reversals of previously recognised impaired assets	–	(1)	(1)	(2)
Total individual allowance for impairment losses	**1**	**7**	**9**	**17**

e: Asset quality of loans and advances:

Interest revenue foregone on impaired assets is calculated using actual interest written off and interest suspended during the period. There are no real estate or other assets acquired through the enforcement of security/collateral held at 31 December 2014 (31 December 2013: nil; 30 June 2014: nil). There are no assets under administration as at 31 December 2014 (31 December 2013: nil; 30 June 2014: nil).

There are no unrecognised impaired assets as at 31 December 2014 (31 December 2013: nil; 30 June 2014: nil). The aggregate amount of undrawn balances on lending commitments to counterparties for whom drawn balances are classified as individually impaired is $2.5m at 31 December 2014 (31 December 2013: $0.3m; 30 June 2014: $0.6m).

f: Credit quality of financial assets neither past due nor impaired

A large portion of the credit exposures, such as residential mortgages, are secured. That is, the fair value of associated security is sufficient to ensure that the Banking Group will recover the entire amount owing over the life of the facility and there is reasonable assurance that collection efforts will result in payment of the amounts due in a timely manner.

The credit quality of loans and advances to customers that were neither past due nor impaired can be assessed by reference to the Bank's credit scoring systems. At the origination of loans and advances to Customers, retail advances are credit scored based on a combination of debt servicing ability, behavioural loan characteristics and loan-to-valuation ("LVR") ratios. Non-retail advances are individually risk graded against similar characteristics. These credit scoring characteristics are reviewed periodically for adverse changes during the loan's life. Interest continues to be accrued on all loans. No interest has been foregone.

Notes to the interim financial statements continued

10. Segment analysis

During the period ended 31 December 2014 Kiwibank underwent an internal restructuring which resulted in changes to reportable operating segments. As such the comparative segmental information presented on page 15 has been restated to align to the current reportable operating segments.

For the purposes of determining reportable operating segments, the chief operating decision-maker has been identified as the Kiwibank Leadership Team (“**KBLT**”), which consists of the Chief Executive and his direct reports. The KBLT reviews the Banking Group’s internal reporting pack on a regular basis to assess performance and to allocate resources. A reportable operating segment is a distinguishable part of the Banking Group, engaged in providing products and services which are subject to risks and returns that are different from those of other segments. The business segments are defined by the customers that they service and the services they provide.

The KBLT assesses the performance of the operating segments based on a measure of profit before tax. This measurement basis includes a reallocation of internal overhead expenses from non-income generating cost centres of the business. Net interest income at a segmental level includes an allocation for internal transfer pricing which eliminates to zero at a Banking Group level. Transfer pricing is allocated on a basis which reflects intersegment funding arrangements.

A summarised description of each business unit is shown below:

- Personal– Provides banking products and services to the personal banking segment via the Banking Group and NZP distribution channels and the bank’s funding reserves.
- Business– Provides banking products and services to the business sector, via the Banking Group and NZP distribution channels. Included within the segment are Business and Treasury services.

Under the current structure, the previously reported Payment Services segment has been split between Personal and Business segments.

	The Banking Group		
Dollars in millions	Personal markets	Business markets	Total
Unaudited 6 months ended 31 December 2014			
External revenues	**280**	**3**	**283**
Intersegment revenues	**(91)**	**91**	**–**
Total revenues	**189**	**94**	**283**
Profit before taxation	**58**	**40**	**98**
Restated 6 months ended 31 December 2013			
External revenues	227	4	231
Intersegment revenues	(73)	73	–
Total revenues	154	77	231
Profit before taxation	36	36	72
Restated year ended 30 June 2014			
External revenues	480	(1)	479
Intersegment revenues	(158)	158	–
Total revenues	322	157	479
Profit before taxation	69	70	139

Notes to the interim financial statements continued

11. Concentration of credit risk

The table below represents a worst case scenario of the credit risk exposure of the Banking Group. The exposures set out are based on net carrying amounts as reported in the balance sheet.

Australian and New Zealand Standard Industrial Classification ("**ANZIC**") codes have been used as the basis for disclosing customer industry sectors.

	The Banking Group
Dollars in millions	Unaudited as at 31/12/14
New Zealand	
Government, local authorities and services	1,112
Finance, investment and insurance	879
Households	13,607
Transport and storage	55
Electricity, gas and water	3
Construction	123
Property and business services	890
Agriculture	24
Health and community services	60
Personal and other services	36
Retail and wholesale trade	72
Food & other manufacturing	156
Overseas	
Finance, investment and insurance	53
	17,070
Less allowance for impairment losses	(57)
Other financial assets	11
Total	17,024

Notes to the interim financial statements continued

11. Concentration of credit risk continued

	The Banking Group		
Unaudited as at 31 December 2014 Dollars in millions	Maximum exposure	Collateral	Net exposure
Credit risk relating to balance sheet assets			
Fixed rate lending at amortised cost	10,690	(10,677)	13
Variable rate lending	4,050	(4,046)	4
Unsecured lending	371	–	371
Due from other financial institutions	119	–	119
Balances with related parties	77	–	77
Derivative financial instruments	184	–	184
Financial assets held for trading	48	–	48
Available-for-sale assets	1,083	–	1,083
Cash and cash equivalents	448	–	448
Other financial assets	11	–	11
	17,081	(14,723)	2,358
Less allowance for impairment	(57)	–	(57)
Total	17,024	(14,723)	2,301

The exposure of the Banking Group derived from loans and advances to retail and corporate customers is 88% of the total maximum exposure.

The table above provides a quantification of the value of the financial charges the Banking Group holds over a borrower's specific asset (or assets) where the Banking Group is able to enforce the collateral in satisfying the debt in the event of the borrower failing to meet its contractual obligations. For the purposes of this disclosure, where collateral held is valued at more than the corresponding credit exposure, coverage is capped at the value of the credit exposure less amounts for which an individual impairment allowance has been recognised. The most common type of collateral is over real estate including residential, commercial, industrial and rural property.

The Banking Group is potentially exposed to credit risk for undrawn loan commitments (note 14) for an amount equal to the undrawn balance.

Notes to the interim financial statements continued

12. Concentration of funding

Concentrations of funding arise where the Banking Group is funded by industries of a similar nature or in particular geographies. ANZIC codes have been used as the basis for disclosing industry sectors. An analysis of financial liabilities by industry sector and geography at the reporting date is as follows:

	The Banking Group
Dollars in millions	Unaudited as at 31/12/14
Analysis by industry sector	
New Zealand	
Transport and storage	**145**
Finance, investment and insurance	**3,244**
Electricity, gas and water	**25**
Food & other manufacturing	**56**
Construction	**62**
Communications	**22**
Government, local authorities and services	**463**
Agriculture	**31**
Health and community services	**220**
Personal and other services	**232**
Property and business services	**371**
Education	**124**
Retail and wholesale trade	**51**
Households	**9,609**
Overseas	
Finance, investment and insurance – Australia	**60**
Finance, investment and insurance – rest of world	**1,083**
Households – Australia	**33**
Households – rest of world	**191**
	16,022
Other financial liabilities	**61**
Total	**16,083**

Notes to the interim financial statements continued

13. Interest repricing

The table below summarises the Banking Group's exposure to interest rate risk. It includes financial instruments at their carrying amounts, categorised by the earlier of contractual repricing or maturity dates. The fair value adjustment on the revaluation of financial instruments is categorised in the appropriate repricing category.

	The Banking Group						
	Unaudited as at 31/12/14						
Dollars in millions	Total	Non-interest bearing	Up to 3 months	3 to 6 months	6 months to 1 year	Between 1 & 2 years	Over 2 years
Financial assets							
Cash and cash equivalents	448	43	405	–	–	–	–
Due from other financial institutions	119	–	119	–	–	–	–
Financial assets held for trading	48	–	7	2	–	9	30
Available-for-sale assets	1,083	–	242	393	–	11	437
Loans and advances	15,054	(33)	4,993	1,305	2,008	4,641	2,140
Derivative financial instruments	184	184	–	–	–	–	–
Due from NZP related parties	77	2	45	–	–	–	30
Other financial assets	11	11	–	–	–	–	–
Total financial assets	17,024	207	5,811	1,700	2,008	4,661	2,637
Financial liabilities							
Due to other financial institutions	(118)	(5)	(113)	–	–	–	–
Deposits and other borrowings	(13,283)	(1,212)	(8,430)	(1,834)	(1,456)	(183)	(168)
Derivative financial instruments	(302)	(302)	–	–	–	–	–
Debt securities issued	(2,067)	–	(1,307)	(42)	(7)	(10)	(701)
Term subordinated debt	(252)	–	–	–	–	–	(252)
Due to NZP related parties	(8)	(8)	–	–	–	–	–
Other financial liabilities	(53)	(53)	–	–	–	–	–
Total financial liabilities	(16,083)	(1,580)	(9,850)	(1,876)	(1,463)	(193)	(1,121)
On-balance sheet gap	941	(1,373)	(4,039)	(176)	545	4,468	1,516
Net derivative notional principals	(56)	–	6,749	(994)	(699)	(4,213)	(899)
Net effective interest rate gap	885	(1,373)	2,710	(1,170)	(154)	255	617

14. Liquidity

The table on page 20 summarises the cash flows of the Banking Group by remaining contractual maturities as at the reporting date. The amounts disclosed are the contractual undiscounted cash flows and include principal and future interest cash flows and therefore may not agree to the carrying values on the balance sheet. Actual cash flows may differ significantly from the contractual cash flows disclosed below as a result of future actions of the Banking Group and/or its counterparties, such as early repayments or refinancing of term loans.

The majority of the longer term Loans and advances are housing loans which are likely to be repaid earlier than their contractual terms. Deposits and other borrowings include substantial customer savings deposits and cheque accounts, which are at call. History demonstrates that such accounts provide a stable source of long term funding for the Bank.

The Banking Group does not manage its liquidity risk on the basis of the information provided on page 20.

Notes to the interim financial statements continued

14. Liquidity continued

	The Banking Group						
	Unaudited as at 31/12/14						
Dollars in millions	On demand	Up to 3 months	3 to 12 months	Between 1 & 5 years	More than 5 years	Gross nominal inflow/ outflow	Carrying amount
Non-derivative cash flows							
Liabilities							
Due to other financial institutions	(118)	–	–	–	–	(118)	(118)
Deposits and other borrowings	(7,332)	(2,128)	(3,454)	(418)	–	(13,332)	(13,283)
Debt securities issued	(362)	(479)	(67)	(1,021)	(232)	(2,161)	(2,067)
Subordinated debt	(3)	–	(12)	(294)	–	(309)	(252)
Due to NZP related parties	(8)	–	–	–	–	(8)	(8)
Other financial liabilities	(53)	–	–	–	–	(53)	(53)
Total financial liabilities	(7,876)	(2,607)	(3,533)	(1,733)	(232)	(15,981)	(15,781)
Assets							
Cash and cash equivalents	448	–	–	–	–	448	448
Due from other financial institutions	119	–	–	–	–	119	119
Financial assets held for trading	–	1	5	26	25	57	48
Available-for-sale assets	12	110	444	564	25	1,155	1,083
Loans and advances	264	549	1,248	3,663	27,688	33,412	15,054
Due from NZP related parties	–	29	18	33	–	80	77
Other financial assets	11	–	–	–	–	11	11
Total financial assets	854	689	1,715	4,286	27,738	35,282	16,840
Net non-derivative cash flows	(7,022)	(1,918)	(1,818)	2,553	27,506	19,301	1,059
Derivative cash flows - net							
Interest rate derivatives	(1)	(16)	(4)	(48)	(4)	(73)	
Total	(1)	(16)	(4)	(48)	(4)	(73)	
Derivative cash flows – gross							
Foreign exchange derivatives							
Inflow	305	277	160	453	232	1,427	
Outflow	(315)	(285)	(178)	(577)	(246)	(1,601)	
Total	(10)	(8)	(18)	(124)	(14)	(174)	
Off balance sheet cash flows							
Capital commitments	–	(4)	(1)	(3)	–	(8)	
Undrawn loan commitments	(2,330)	–	–	–	–	(2,330)	
Lease commitments	–	(1)	(4)	(18)	(2)	(25)	
Total	(2,330)	(5)	(5)	(21)	(2)	(2,363)	
Net cash flows	(9,363)	(1,947)	(1,845)	2,360	27,486	16,691	
Cumulative net cash flows	(9,363)	(11,310)	(13,155)	(10,795)	16,691	16,691	

Notes to the interim financial statements continued

14. Liquidity continued

The Banking Group holds a diversified portfolio of high quality liquid securities to support its liquidity risk management. The size of the Banking Group's liquidity portfolio is based on the amount required to meet its liquidity policy and includes items both classified as cash and cash equivalents and those classified as operating assets in the consolidated cash flow statement.

	The Banking Group
Dollars in millions	**Unaudited as at 31/12/14**
The Banking Group's liquidity portfolio is based on the amount required to meet its liquidity policy.	
Cash on hand and with central banks	**396**
Certificates of deposit	**18**
Government bonds and treasury bills	**537**
Local body stock and bonds	**20**
Other bonds	**861**
Total	**1,832**

15. Financial instruments

Fair value measurement

Assets and liabilities carried at fair value or for which fair values are disclosed have been classified into three levels according to the quality and reliability of information used to determine the fair values. The three levels of the fair value hierarchy are defined as follows:

Level 1 – Fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 – Fair value measurements are those where quoted market prices are not available, for example where the instrument is traded in a market that is not considered to be active or valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3 – Fair value measurements where at least one input which could have a significant effect on the instrument's valuation is not based on observable market data.

Valuation methodology

The fair values of assets and liabilities carried at fair value were determined by application of the following methods and assumptions.

Held for trading and available-for-sale securities

Estimates of fair value for both held for trading and available-for-sale securities are based on quoted market prices or determined using market accepted valuation models as appropriate (including discounted cash flow models) with inputs including an interest rate yield curve developed from quoted rates and market observable credit spreads.

Debt securities issued

Debt securities issued that are classified at fair value through profit or loss are short term in nature. For these liabilities fair value has been determined using a discounted cash flow model with inputs including an interest rate yield curve developed from quoted rates and market observable credit spreads.

Derivative financial instruments

Where the Banking Group's derivative financial assets and liabilities are not traded on an exchange, they are valued using valuation techniques, including discounted cash flow and option pricing models, as appropriate. The types of derivatives classified as level 2 and the valuation techniques used include:

- Interest rate swaps which are valued using discounted cash flow models; the most significant inputs into those models are interest rate yield curves which are developed from quoted rates.
- Foreign exchange derivatives that do not contain options which are priced using rates available from publicly quoted sources.

Notes to the interim financial statements continued

15. Financial instruments continued

	The Banking Group			
Dollars in millions	Level 1	Level 2	Level 3	Total
Unaudited as at 31 December 2014				
Financial assets				
Derivative financial assets	**–**	**184**	**–**	**184**
Financial assets held for trading	**3**	**45**	**–**	**48**
Available-for-sale financial assets	**650**	**433**	**–**	**1,083**
Total financial assets at fair value	**653**	**662**	**–**	**1,315**
Financial liabilities				
Derivative financial liabilities	**–**	**302**	**–**	**302**
Debt securities issued	**–**	**531**	**–**	**531**
Total financial liabilities at fair value	**–**	**833**	**–**	**833**

	The Banking Group			
Dollars in millions	Level 1	Level 2	Level 3	Total
Unaudited as at 31 December 2013				
Financial assets				
Derivative financial assets	–	150	–	150
Financial assets held for trading	–	44	–	44
Available-for-sale financial assets	590	461	–	1,051
Total financial assets at fair value	590	655	–	1,245
Financial liabilities				
Derivative financial liabilities	–	208	–	208
Debt securities issued	–	903	–	903
Total financial liabilities at fair value	–	1,111	–	1,111

	The Banking Group			
Dollars in millions	Level 1	Level 2	Level 3	Total
Audited as at 30 June 2014				
Financial assets				
Derivative financial assets	–	130	–	130
Financial assets held for trading	44	–	–	44
Available-for-sale financial assets	534	559	–	1,093
Total financial assets at fair value	578	689	–	1,267
Financial liabilities				
Derivative financial liabilities	–	236	–	236
Debt securities issued	–	731	–	731
Total financial liabilities at fair value	–	967	–	967

There have been no transfers between levels 1 and 2 during the period ended 31 December 2014 (period ended 31 December 2013: no transfers; year ended 30 June 2014: no transfers). There were also no transfers into/out of level 3 during the period ended 31 December 2014 (period ended 31 December 2013: no transfers; year ended 30 June 2014: no transfers).

Notes to the interim financial statements continued

15. Financial instruments continued

	The Banking Group					
	Unaudited as at 31/12/14		Unaudited as at 31/12/13		Audited as at 30/06/14	
Dollars in millions	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Assets						
Financial assets held for trading	**48**	**48**	44	44	44	44
Available-for-sale assets	**1,083**	**1,083**	1,051	1,051	1,093	1,093
Loans and advances	**15,054**	**15,100**	13,952	13,920	14,630	14,613
Derivative financial instruments	**184**	**184**	150	150	130	130
Due from NZP related parties	**77**	**77**	76	76	77	77
Liabilities						
Deposits and other borrowings	**(13,283)**	**(13,285)**	(12,412)	(12,420)	(12,751)	(12,753)
Derivative financial instruments	**(302)**	**(302)**	(208)	(208)	(236)	(236)
Debt securities issued	**(2,067)**	**(2,076)**	(2,152)	(2,158)	(2,143)	(2,154)
Subordinated debt	**(252)**	**(258)**	(149)	(148)	(247)	(249)
Due to NZP related parties	**(8)**	**(8)**	(14)	(14)	(27)	(27)

The carrying values of the following financial instruments are a reasonable approximation of fair value because, for example, they are short-term in nature or reprice to current market rates frequently: cash and cash equivalents, due from other financial institutions, other financial assets, due to other financial institutions and other financial liabilities.

16. Credit exposure concentrations

Credit exposures to individual counterparties

Credit exposure concentrations are disclosed on the basis of actual credit exposures and gross of set-offs. Peak end-of-day aggregate credit exposures have been calculated using the Banking Group's Tier 1 capital at the end of the period.

There are no individual counterparties (excluding connected parties, governments and banks with long term credit ratings of A-, A3 or its equivalent or above), where the period end and peak end-of-day aggregate actual credit exposures, net of individual credit impairment allowances (which were nil), equalled or exceeded 10% of the Banking Group's shareholder equity as at the reporting date.

17. Fiduciary activities and securitisation

Provision of financial services

Financial services provided by Kiwibank to entities which are involved in trust, custodial, funds management and other fiduciary activities, are provided at fair value, except that Kiwibank does not charge Kiwibank Investment Management Limited, the Manager of the Kiwibank PIE Unit Trust, any bank fees. Further, the Kiwibank PIE Unit Trust bank account used for tax payments does not earn interest.

Insurance business

The Banking Group does not market or distribute its own insurance products.

Kiwi Covered Bond Trust

On 23 January 2013, the Kiwi Covered Bond Trust (the "**Covered Bond Trust**") was established to hold Kiwibank housing loans and to provide guarantees to certain debt securities issued by the Bank. Guarantees provided by Kiwi Covered Bond Trustee Limited, as Trustee of the Covered Bond Trust, have a priority claim over the assets of the Covered Bond Trust. Since 19 February 2013, selected Kiwibank housing loans have been transferred to the Covered Bond Trust in order to facilitate the Bank's covered bond programme. These assets do not qualify for derecognition as the Banking Group retains a continuing involvement and retains substantially all the risks and rewards of ownership of the transferred assets. The Covered Bond Trust is consolidated within the Banking Group.

Substantially all of the assets of the Covered Bond Trust comprise housing loans originated by the Bank, which are security for the guarantee of issuances of covered bonds by the Bank. The assets of the Covered Bond Trust are not available to creditors of the Bank, although the Bank (or its liquidator or statutory manager) may have a claim against the residual assets of the Covered Bond Trust (if any) after all prior ranking creditors of the Covered Bond Trust have been satisfied.

The carrying value of the Covered Bond Trust pool at 31 December 2014 is $316m (31 December 2013: $316m; 30 June 2014: $316m). These securities are ring fenced to ensure they are not used as collateral outside of agreements established in relation to the Covered Bond Trust.

Notes to the interim financial statements continued

17. Fiduciary activities and securitisation continued

Kiwibank RMBS Trust Series 2009-1

The purpose of the Kiwibank RMBS Trust Series 2009-1 (the "**RMBS Trust**") is to provide an in-house residential mortgage-backed securities facility to issue securities as collateral for borrowing from the Reserve Bank of New Zealand. As at 31 December 2014, included within Loans and advances to customers on the Banking Group's consolidated balance sheet were housing loans with a carrying value of $600m held by the RMBS Trust (31 December 2013: $600m; 30 June 2014: $600m). These housing loans do not qualify for derecognition as the Bank retains substantially all of the risks and rewards of ownership. The RMBS Trust is consolidated within the Banking Group.

18. Risk management

There have been no material changes to the Banking Group's policies for managing risk, or material exposures to new categories of risk since 30 June 2014.

19. Interest earning and discount bearing assets and liabilities

	The Banking Group
Dollars in millions	**Unaudited as at 31/12/14**
Interest earning and discount bearing assets	**16,817**
Interest and discount bearing liabilities	**14,503**

20. Capital expenditure commitments

Capital expenditure commitments contracted for as at 31 December 2014, but not provided for in these interim financial statements, total $7.9m (31 December 2013: $6.1m; 30 June 2014: $8.0m) of which $2.5m (31 December 2013: $3.5m; 30 June 2014: $2.8m) are due between one and five years from the reporting date.

21. Contingent liabilities and loan commitments

In June 2013, a group called Fair Play on Fees announced plans for a representative action against banks in New Zealand in relation to certain default fees charged to New Zealand customers. In November 2013, the group issued proceedings against Kiwibank. The potential outcome of the proceedings cannot be determined with any certainty at this stage.

Other than the above, there are no material contingent liabilities as at 31 December 2014 (31 December 2013: nil; 30 June 2014: nil).

Undrawn loan commitments as at the reporting date are disclosed in note 14.

22. Events subsequent to the reporting date

There were no material events which occurred subsequent to the reporting date, that require recognition, or additional disclosure in these interim financial statements.

Capital adequacy

The "**Banking Group**" consists of Kiwibank Limited and its subsidiaries. The Banking Group is subject to the capital adequacy requirements for registered banks as specified by the Reserve Bank of New Zealand ("**RBNZ**"). The RBNZ has set minimum acceptable regulatory capital requirements that are consistent with the internationally agreed framework developed by the Basel Committee on Banking Supervision.

The Bank must comply with RBNZ minimum capital adequacy ratios, as calculated under the Basel III framework in accordance with the RBNZ document *Capital Adequacy Framework (Standardised Approach)* (BS2A), as determined in its conditions of registration.

During the reporting period the Banking Group complied with all of the RBNZ capital requirements to which it is subject.

Regulatory capital ratios

	The Banking Group	
Dollars in millions	**31/12/14**	31/12/13
Capital adequacy ratios		
Common Equity Tier 1 capital ratio	**9.4%**	8.3%
Tier 1 capital ratio	**10.8%**	10.2%
Total capital ratio	**13.3%**	11.5%
RBNZ minimum ratios		
Common Equity Tier 1 capital ratio	**4.5%**	4.5%
Tier 1 capital ratio	**6.0%**	6.0%
Total capital ratio	**8.0%**	8.0%
Buffer ratios		
Buffer ratio	**4.8%**	3.5%
Buffer ratio requirement	**2.5%**	2.5%

	Kiwibank Limited	
Dollars in millions	**31/12/14**	31/12/13
Capital adequacy ratios		
Common Equity Tier 1 capital ratio	**9.1%**	8.2%
Tier 1 capital ratio	**10.5%**	10.1%
Total capital ratio	**12.9%**	11.4%

Ordinary shares

The ordinary shares issued by the Bank, which are fully paid, are included within Common Equity Tier 1 capital. The material terms and conditions of the ordinary shares are:

a) each share contains a single right to vote;

b) there are no redemption, conversion or capital repayment options/facilities;

c) there is no predetermined dividend rate;

d) there is no maturity date; and

e) there are no options to be granted pursuant to any agreement.

Perpetual preference shares

The perpetual preference shares, issued by Kiwi Capital Securities Limited on 4 May 2010, are fully paid and are included within Additional Tier 1 capital. Their material terms and conditions are:

a) each share has no voting rights;

b) there are no redemption, conversion or capital repayment options/facilities;

c) dividends are paid quarterly in arrears at the discretion of the directors;

d) there is a predetermined dividend rate of 8.15% pa (which resets every 5 years);

e) there is no maturity date;

f) no provision has been made for a variation or suspension of dividend payments;

g) there are no options to be granted pursuant to any agreement; and

h) there are no dividends in arrears.

The $150m perpetual preference shares are subject to grandfathering under the RBNZ's Basel III transitional arrangements.

Capital adequacy continued

Subordinated bonds

The subordinated debt issue, issued by the Bank and which is fully paid, is included within Tier 2 capital. The issue is subordinate to all other general liabilities of the Banking Group and is denominated in New Zealand dollars. The material terms and conditions are:

Subordinated debt issued 10 December 2012:

a) the Subordinated Bonds constitute direct, unsecured, subordinated debt obligations of Kiwibank;

b) the Subordinated Bonds pay interest at the Coupon Rate of 5.8% pa;

c) interest will be paid in arrears in equal semi-annual instalments. Payments of interest are subject to Kiwibank and the Banking Group being able to satisfy the Solvency Test immediately following payment;

d) the maturity date of the Subordinated Bonds is 15 December 2022. Kiwibank may redeem the Subordinated Bonds on the First Call Date (15 December 2017) and on any Interest Payment Date thereafter subject to Kiwibank and the Banking Group being able to satisfy the Solvency Test immediately following the payment; Kiwibank may also redeem the Subordinated Bonds at any time (including before the First Call Date) if a Regulatory Event or a Tax Event occurs; and

e) the Subordinated Bonds are not guaranteed by any member of the Banking Group, Kiwibank's parent companies (including New Zealand Post), the Crown or by any other person.

Under the RBNZ's Basel III rules the $150m subordinated debt is subject to a loss absorbency haircut.

Convertible subordinated bonds

The convertible subordinated bond issue, issued by the Bank and which is fully paid, is included within Tier 2 capital. The issue is subordinate to all other general liabilities of the Banking Group and is denominated in New Zealand dollars. The material terms and conditions are:

a) the convertible subordinated bonds constitute direct, unsecured, subordinated debt obligations of Kiwibank;

b) interest on the convertible subordinated bonds is payable semi-annually at an initial rate of 6.61% p.a. subject to the condition that Kiwibank and the Banking Group is solvent after each payment;

c) the convertible subordinated bonds may be required to be converted into ordinary shares of Kiwibank Limited (or written off if conversion into ordinary shares is not possible) if certain events occur;

d) the convertible subordinated bonds have a maturity date of 15 July 2024, however, Kiwibank may elect to make early repayment on 15 July 2019 or any semi-annual interest payment date thereafter; and

e) the convertible subordinated bonds are not guaranteed by any member of the Banking Group, Kiwibank's parent companies (including New Zealand Post), the Crown or by any other person.

Risk exposures

Risk weighted exposures are derived by assigning risk weight percentages to certain material risk categories of exposures. These exposures are measured or estimated from: i) selected balance sheet assets; ii) off balance-sheet exposures and market contracts; and iii) business unit net income.

The Bank's current prudential capital requirements based on assessments of its material risk classes (commonly referred to as "Pillar I" risk classes under Basel III) can be summarised as follows:

- Credit risk - The vulnerability of the Banking Group's lending and investment portfolios to systemic counterparty default. The risk based capital allocation is computed based on RBNZ Standardised Approach Credit Risk methodology (BS2A).
- Market risk - The vulnerability of earnings to movements in interest rates and currency volatility. The risk based capital allocation is computed based on RBNZ Standardised Approach to Interest Rate Risk (BS2A).
- Operational risk - The risk of loss, resulting from inadequate or failed internal processes (including legal risks), people and systems and from external events. The risk based capital allocation is computed based on RBNZ Standardised Approach to Operational Risk methodology (BS2A).

Kiwibank's Board is ultimately responsible for capital adequacy and approves capital plans and establishes minimum internal capital levels and limits. These are typically higher than the regulatory minimum.

The capital adequacy tables set out on pages 25 to 31 summarise the composition of regulatory capital and capital adequacy ratios for the period ended 31 December 2014. Throughout the period Kiwibank and the Banking Group complied with both regulatory and internal capital adequacy requirements.

Capital adequacy continued

Regulatory capital

The following table shows the qualifying capital for the Banking Group.

	The Banking Group
Dollars in millions	31/12/14
Common Equity Tier 1 capital	
Issued and fully paid up share capital	400
Retained earnings	507
Dividends paid	(5)
Accumulated other comprehensive income and other disclosed reserves [1, 2]	(14)
Less deductions from Common Equity Tier 1 capital	
Intangible assets	(97)
Cash flow hedge reserve	16
Deferred tax assets	(11)
Total Common Equity Tier 1 capital	**796**
Additional Tier 1 capital	
Perpetual fully paid up non-cumulative preference shares [3]	117
Total Additional Tier 1 capital	**117**
Total Tier 1 capital	**913**
Tier 2 capital	
Subordinated debt	208
Total Tier 2 capital	**208**
Total capital	**1,121**

1 Includes Available for Sale Reserve of $2m. The available-for-sale reserve includes the cumulative net change in the fair value of available-for-sale securities until the investment is derecognised or impaired.

2 Includes cash flow hedge reserve of ($16m). The cash flow hedging reserve comprises the effective portion of the cumulative net change in the fair value of foreign exchange and interest rate derivative contracts related to hedged forecasted transactions that have not yet occurred. The cash flow hedge reserve is not eligible for inclusion in capital under BS2A 7 (3)(c).

3 Represents the face value of perpetual preference shares, which are classified as equity for financial reporting purposes, less the amount ineligible under Basel III transitional arrangements and issue costs.

Capital adequacy continued

On-balance sheet exposures

	The Banking Group			
	31/12/14			
Dollars in millions	Total exposure	Risk weighting	Risk weighted exposure	Minimum Pillar I capital requirement
On-balance sheet exposures				
Cash and gold bullion	43	0%	–	–
Sovereigns and central banks	1,004	0%	–	–
Multilateral development banks and other international organisations	184	0%	–	–
Public sector entities	22	20%	4	–
Banks	322	20%	64	5
	125	50%	63	5
Corporate	77	50%	39	3
Residential mortgages not passed due	12,091	35%	4,232	339
	1,702	50%	851	68
	220	75%	165	13
	98	100%	98	8
Impaired assets	30	100%	30	2
Past due residential mortgages > 90 days	7	100%	7	1
Other past due assets	5	150%	8	1
Non risk weighted assets	241	0%	–	–
Other assets	990	100%	990	79
Total on-balance sheet exposures	**17,161**		**6,551**	**524**

Capital adequacy continued

Off-balance sheet exposures and market related contracts

	The Banking Group					
	31/12/14					
Dollars in millions	Total exposure	Credit conversion factor	Credit equivalent amount	Average risk weighting	Risk weighted exposure	Minimum Pillar I capital requirement
Direct credit substitute	**3**	**100%**	**3**	**100%**	**3**	**–**
Asset sale with recourse	**–**	**100%**	**–**	**–**	**–**	**–**
Forward asset purchase	**–**	**100%**	**–**	**–**	**–**	**–**
Commitment with certain drawdown	**53**	**100%**	**53**	**100%**	**53**	**4**
Note issuance facility	**–**	**50%**	**–**	**–**	**–**	**–**
Revolving underwriting facility	**265**	**50%**	**133**	**39%**	**52**	**4**
Revolving underwriting facility	**929**	**20%**	**186**	**39%**	**73**	**6**
Revolving underwriting facility	**113**	**0%**	**–**	**39%**	**–**	**–**
Performance-related contingency	**6**	**50%**	**3**	**100%**	**3**	**–**
Other commitments where original maturity is greater than one year	**270**	**50%**	**135**	**39%**	**53**	**4**
Other commitments where original maturity is less than or equal to one year	**85**	**20%**	**17**	**100%**	**17**	**1**
Other commitments where original maturity is less than or equal to one year	**2**	**20%**	**–**	**20%**	**–**	**–**
Other commitments that cancel automatically when the creditworthiness of the counterparty deteriorates or that can be cancelled unconditionally at any time without prior notice	**607**	**0%**	**–**	**0%**	**–**	**–**
Market related contracts: [1]						
(a) Foreign exchange contracts	**1,558**	**n/a**	**64**	**91%**	**58**	**5**
(b) Interest rate contracts	**37,650**	**n/a**	**311**	**56%**	**174**	**14**
Total off-balance sheet exposures	**41,541**		**905**		**486**	**38**

[1] The credit equivalent amount for market related contracts was calculated using the current exposure method.

Residential mortgages by loan-to-value ratio

	The Banking Group		
	31/12/14		
Dollars in millions	On-balance sheet	Off-balance sheet	Total
LVR 0% – 80%	**12,104**	**289**	**12,393**
LVR > 80% – 90%	**1,705**	**16**	**1,721**
LVR 90% +	**322**	**11**	**333**
Total	**14,131**	**316**	**14,447**

The LVR classification above is calculated in line with the Bank's Pillar I capital requirement, which includes capital relief for "Welcome Home" loans that are guaranteed by the New Zealand Crown. Loans with an LVR greater than 80% are presented after the mitigation of credit risk from third party lenders' mortgage insurance, where applicable.

At 31 December 2014, of the loans with an LVR greater than 80%, $478m relates to "Welcome Home" loans, whose credit risk is mitigated by the New Zealand Crown. Of the remaining loans with an LVR greater than 80%, Kiwibank uses lenders' mortgage insurance on selected loans.

Capital adequacy continued

Reconciliation of residential mortgage-related amounts

	The Banking Group
Dollars in millions	31/12/14
Residential mortgages total on-balance sheet exposures	14,131
Corporate lending residentially secured	(963)
Unsecured loans	372
Deferred arrangement fees	71
Collective allowance for impairment	(19)
Individual allowance for impairment	(3)
Net loans and advances to retail customers	**13,589**

Credit risk mitigation

No credit risk mitigation, as defined under Part 5 of BS2A, has been recognised as at 31 December 2014.

Operational risk

	The Banking Group	
	31/12/14	
Dollars in millions	Implied risk weighted exposure	Total operational risk capital requirement
Operational risk	1,048	84

Market risk

	The Banking Group			
	31/12/14			
	Implied risk weighted exposure		Aggregate capital charge	
Dollars in millions	End of period	Peak end-of-day	End of period	Peak end-of-day
Interest rate risk	349	432	28	35
Foreign currency risk	–	4	–	–
Equity risk	–	–	–	–

The aggregate market risk exposure above is derived in accordance with BS2A.

The peak end-of-day aggregate capital charge is the maximum over the half year accounting period at the close of each business day.

Capital adequacy continued

Total capital requirements

	The Banking Group		
	31/12/14		
Dollars in millions	Total exposure after credit risk mitigation	Risk weighted exposure or implied risk weighted exposure	Total capital requirement
Credit risk	**58,702**	**7,037**	**562**
Operational risk	**n/a**	**1,048**	**84**
Market risk	**n/a**	**349**	**28**
Total Pillar I risk	**n/a**	**8,434**	**674**

Other material risk (Pillar II)

The Bank has made an internal capital allocation of $46m (31 December 2013: $46m). The other material risks identified by the Bank include regulatory environment risk, reputational risk, systems risk and liquidity risk.

Independent Review Report

To the readers of Kiwibank Limited and Banking Group's Disclosure Statement for the six months ended 31 December 2014

The Auditor-General is the auditor of Kiwibank Limited (the "Bank") and the entities it controlled as at 31 December 2014 or from time-to-time during the period (the "Banking Group"). The Auditor-General has appointed me, Chris Barber, using the staff and resources of PwC, to carry out the annual audit of the Bank and the Banking Group, on her behalf.

In our capacity as auditor, we have carried out a review of the:

- interim financial statements on pages 4 to 24 of the Disclosure Statement of the Banking Group for the six months ended 31 December 2014 which comprise the balance sheet as at 31 December 2014, the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the six month period ended 31 December 2014 and selected explanatory notes; and
- supplementary information as required by Schedules 5, 7, 9, 13, 16 and 18 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 ("the Order") for the six months ended 31 December 2014.

Review Opinion
Based on our review, nothing has come to our attention that causes us to believe that:

- the interim financial statements on pages 4 to 24 (excluding supplementary information included in notes 3, 9, 11, 12, 13, 14, 16, 17, 18 and 19), are not prepared, in all material respects in accordance with New Zealand Equivalents to International Accounting Standard 34: *Interim Financial Reporting* and do not present fairly the financial position of the Banking Group as at 31 December 2014 and its performance and cash flows for the six months ended on that date;
- the supplementary information disclosed in notes 3, 9, 11, 12, 13, 14, 16, 17, 18 and 19 prescribed by Schedules 5, 7, 13, 16 and 18 of the Order does not fairly state the matters to which it relates in accordance with those Schedules; and
- the supplementary information relating to Capital Adequacy disclosed on pages 25 to 31 is not in all material respects prepared in accordance with the Bank's Conditions of Registration and disclosed in accordance with Schedule 9 of the Order.

The review was completed on 17 February 2015, and is the date at which our review opinion is expressed.

Responsibilities of the Board of Directors
The Board of Directors of Kiwibank Limited (the "Directors") are responsible for preparing the half-year Disclosure Statement which includes interim financial statements in accordance with Clause 25 of the Order and that present fairly the financial position of the Banking Group as at 31 December 2014 and its financial performance and cash flows for the period ended on that date. The Directors are also responsible for such internal controls as the Directors determine are necessary to enable the preparation of the Disclosure Statement that is free from material misstatement whether due to fraud or error.

In addition, the Directors are also responsible for including supplementary information in the half-year Disclosure Statement that complies with schedules 3, 5, 7, 9, 13, 16 and 18 of the Order.

These responsibilities are specified in the Order issued pursuant to the Reserve Bank of New Zealand Act 1989.

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Responsibilities of the Reviewer

We are responsible for reviewing the interim financial statements and supplementary information disclosed in accordance with Clause 25 and Schedules 5, 7, 9, 13, 16 and 18 of the Order, presented by the Directors.

We are responsible for reviewing the interim financial statements (excluding the supplementary information) in order to report to you whether, in our opinion on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the interim financial statements have not been prepared, in all material respects, in accordance with New Zealand Equivalents to International Accounting Standard 34: *Interim Financial Reporting*.

We are responsible for reviewing the supplementary information (excluding the supplementary information relating to Capital Adequacy) in order to report to you whether, in our opinion on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the supplementary information does not fairly state the matters to which it relates in accordance with Schedules 5, 7, 13, 16 and 18 of the Order.

We are responsible for reviewing the supplementary information relating to Capital Adequacy in order to report to you whether, in our opinion on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the supplementary information is not in all material respects prepared in accordance with the Bank's Conditions of Registration and disclosed in accordance with Schedule 9 of the Order.

We conducted our review in accordance with New Zealand Standards on Review Engagements 2410: *Review of Financial Statements Performed by Independent Auditor of the Entity* ("NZ SRE 2410"). As the auditor of the Bank, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

A review of interim financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with the Auditor-General's Auditing Standards and the International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on these interim financial statements.

Independence

In completing our review we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.

In addition to the review we have carried out assignments in the areas of accounting advice, other assurance and advisory services, which are compatible with those independence requirements. In addition, certain partners and employees of our firm may deal with the Banking Group on normal terms within the ordinary course of trading activities of the Banking Group. Other than in our capacity as auditor acting on behalf of the Auditor-General and these assignments we have no relationship with or interests in the Banking Group.

Chris Barber
On behalf of the Auditor-General
Wellington, New Zealand

PricewaterhouseCoopers