NATIONAL AUSTRALIA BANK LTD
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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON DC 20549

FORM 6-K

REPORT OF FOREIGN ISSUER

Pursuant to Rule 13a-16 or 15d-16 of

the Securities Exchange Act of 1934

For the month of December 2006

National Australia Bank Limited

ACN 004 044 937

(Registrant s Name)

Level 24

500 Bourke Street

MELBOURNE VICTORIA 3000

AUSTRALIA

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F x Form 40-F o

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes o No x

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82

National Australia Bank Limited

ABN 12 004 044 937

This annual financial report 2006 is lodged with the Australian Securities and Investments Commission and Australian Stock Exchange Limited.

National Australia Bank Limited is publicly listed in Australia and overseas and, as such, must meet regulatory requirements of all jurisdictions it operates in internationally. This report contains information prepared on the basis of the *Banking Act 1959 (Cth)*, *Corporations Act 2001 (Cth)*, Australian equivalents to International Financial Reporting Standards, United States generally accepted accounting principles and various disclosures rules of the Securities Exchange Commission.

To view a concise version of this report, visit www.nabgroup.com. Alternatively, to arrange for a copy to be sent to you free of charge, call Shareholder Services on 1300 367 647 from within Australia, or +61 3 9415 4299.

Nothing in this report is, or should be taken as, an offer of securities in National Australia Bank Limited for issue or sale, or an invitation to apply for the purchase of such securities. All figures in this document are in Australian dollars unless otherwise stated.

Cover: Commonwealth discus champion Scott Martin has serious talent. His determination to prove himself to push himself, to be the best that he could be in achieving gold in the Melbourne 2006 Commonwealth Games drew us to supporting him.

At NAB, we re inspired by people s potential to do amazing things. It s why we look to get behind people in all fields of endeavour on the sports ground, in business, and throughout their lives.

Your success, translates to our success and then to shareholder returns. Our involvement in the Melbourne 2006 Commonwealth Games, gave us the chance to unite key customers and stakeholders across all our businesses internationally whilst celebrating the spirit of achievement.

Table of contents

Chairman s message

I am pleased to report that your Company achieved good growth in profitability and steady progress in its business improvement program in the 2006 year.

Net profit attributable to members of the Company increased 10.0% to $4,392 million and cash earnings before significant items rose 21.9% to $3,967 million.

These results were achieved despite an increasingly competitive lending environment and a substantial amount of management time being devoted to improving the Bank s internal systems and complying with the requirements of new international regulatory frameworks and standards.

The Company s culture change program, initiated in 2005, is achieving early success, especially at senior levels. The program seeks to clarify individual accountability and empower employees at every level to take initiative in their day-to-day decisions and interactions.

The success of these efforts is evidenced by numerous positive developments across the Group from a recovery in the Australian bank s market share in business lending, to the growth of the Integrated Financial Solutions Centre (FSC) business in the UK, the rebuilding of nabCapital and the success of the Unbeatable home loan campaign in New Zealand.

In Australia, our efforts were recognised via Money Magazine s Bank of the Year Award, CFO Magazine s Business Bank of the Year Award and Australian Banking and Finance Magazine s Life Insurance Company of the Year Award for MLC.

Much, however, remains to be done. The principal message being conveyed by the Board to senior management, and through them to employees, is that the Company s goal of providing sustainable satisfactory shareholder returns will only be achieved through an unwavering focus on our customers needs, ethical behaviour at all levels and recognition in the community of our operating companies as good corporate citizens.

The investment of time and money by the Company in developing its systems to meet regulatory requirements is substantial. These investments will ultimately result in an even sharper appreciation of risk across the business.

In the meantime, such demands do result in a lesser focus on market-oriented initiatives than would otherwise be the case.

Increasingly in the markets in which we operate there is strong competition from non-traditional sources, which are not required to meet the same regulatory standards.

The tilting of the playing field in this way works to the detriment of banks, a development that is not in the interest of either our shareholders or our economy. At a time when governments are beginning to recognise the costly burden being placed on companies by regulation generally, this is a trend that needs to be monitored closely.

During the year, the directors declared dividends totalling 167 cents per share, a small increase on that paid in 2005. As a result of the increase in net profit attributable to members of the Company, the Company s dividend payout ratio fell from 79.6% to 67.4% which is closer to the board s target range of 60% to 65%.

In July 2006, Mr Robert Elstone resigned from the Board as a result of his appointment as Chief Executive of the Australian Stock Exchange. Rob s departure is a real loss to the Company, in particular given his keen appreciation of risk across all parts of the finance sector. Rob made a significant contribution during his two years on the Board and we are indebted to him for that.

Fortunately the Board is well placed in respect of finance industry expertise and Mr Paul Rizzo was able to assume the role of Chair of the Risk Committee seamlessly upon Rob s departure.

In closing, I would like to thank my fellow directors and the Company s employees for their dedication and effort over the past year.

/s/ Michael A Chaney AO
Michael A Chaney AO
Chairman

Group Chief Executive Officer s message

2006 at a glance

- Net profit attributable to members of the Company increased 10.0% to $4,392 million;
- Business portfolio aligned to core capabilities;
- Share buy back; and
- Improving customer satisfaction.

National Australia Bank is about to commence the next phase of its development focused on creating sustainable satisfactory shareholder value.

The progress made in all parts of the Group during the past year was very pleasing. All of our key businesses are gaining momentum. Our portfolio is now well suited to our core capabilities and has the ability to produce sustainable growth in shareholder value.

Net profit attributable to members of the Company was up 10.0% to $4,392 million. This was affected by significant items, largely in respect of the UK pension reforms in 2006 and profit on the sale of the Irish Banks and restructuring provisions in 2005. This was all a part of getting the National Australia Bank match fit .

In 2006, net profit attributable to members of the Company before significant items was up 25.3% to $4,154 million. This is a better reflection of the underlying performance of the Group, but was also affected by the introduction of the Australian equivalents to International Financial Reporting Standards.

In line with our commitment to active capital management we will undertake a $500 million on-market share buy back to commence in the first half of 2007. We intend to neutralise the capital impact of shares issued under the dividend reinvestment plan and various employee share plans by either buying back shares issued or purchasing shares on market to satisfy our obligations rather than issuing new shares.

We have carefully managed margins, asset quality remains sound overall and we continued to strive to improve customer satisfaction levels throughout the Group.

The Corporate Centre was reduced in size and is focused on creating value for shareholders, strategic development of our portfolio of businesses, financial and risk performance and governance, developing and retaining talent and capital and balance sheet management.

The establishment of a regional business model has created a more nimble, customer-focused organisation in the regions in which we operate.

In the Australian business, we developed and launched new products, built market share in target areas and managed expenses.

As the major business within our portfolio, Australia also faced the largest challenge in the turnaround and made progress on all fronts.

This was reflected in the increase of 27.0% in net profit attributable to members of the Company to $2,515 million and excluding significant items, was up 10.9%.

In New Zealand, despite challenging economic conditions and fierce competition, our Bank of New Zealand operation performed well. Using the Unbeatable home loan campaign to position itself in a crowded market, net profit attributable to members of the Company increased 26.7% to $389 million and excluding significant items, was up 22.7%.

The United Kingdom operation differentiates National Australia Bank from other Australian banks. The net profit attributable to members of the Company of $868 million, a decrease of 46.7% (largely related to the profit on sale of the Irish Banks in 2005), represents 19.8% of overall Group net profit. Net profit attributable to members of the Company, excluding significant items, was up 15.7% to $618 million.

We successfully worked to rejuvenate the existing branch network, and expand into the southeast of England with Financial Solutions Centres targeting small to medium enterprises, and the mass affluent personal sector.

nabCapital, formerly Institutional Markets and Services increased net profit attributable to members of the Company by 22.9% to $618 million and excluding significant items was up 8.0%, while reducing the amount of capital deployed in the business. nabCapital further evolved its originate warehouse and distribute business model to provide greater linkage between the various parts of its business, and both borrowers and investors.

During the year we continued to develop the Corporate Social Responsibility (CSR) program within our businesses. Paying attention to broader social and environmental issues helps manage risks and identify new opportunities that add value to our business for shareholders and the communities in which we operate. This year we will produce our third CSR Report to outline our progress in this area.

I would like to thank the Board for its support, especially in leading the culture change program. A great deal of practical work has been completed to support the new Corporate Principles and measure behaviours. Over time, I am confident this will result in a fundamental and lasting shift in the culture.

And finally, thank you to all of our staff who worked very hard to contribute towards the National Australia Bank s success in 2006.

/s/ John Stewart

John Stewart
Group Chief Executive Officer

Refer to non-GAAP measures on page 56 for an explanation of the Group s non-GAAP measures, including significant items, and reconciliations of non-GAAP financial measures , including significant items on page 7.

Presentation of information

Basis of presentation

This annual financial report is prepared in accordance with Australian equivalents to International Financial Reporting Standards (AIFRS) which differ in some respects from US GAAP ***(as set out in note 57 in the financial report)*****. Comparative amounts have been reclassified to accord with changes in presentation made in 2006, except where otherwise stated.**

This is the Group s first annual financial report prepared in accordance with AIFRS. The 2005 annual financial report was prepared in accordance with previous Australian Generally Accepted Accounting Principles (AGAAP), which differs from AIFRS in certain respects *(as set out in note 1 in the financial report*).

This annual financial report does not include all of the requirements of the United States Securities and Exchange Commission (SEC) for an annual report on Form 20-F and will not be filed with the SEC as an annual report on Form 20-F. A separate annual report will be prepared and filed with the SEC on Form 20-F.

Currency of presentation

All currency amounts are expressed in Australian dollars unless otherwise stated. Merely for the convenience of the reader, this annual financial report contains translations of certain Australian dollar amounts into US dollars at specified rates. These translations should not be construed as representations that the Australian dollar amounts actually represent such US dollar amounts or could be converted into US dollars at the rate indicated. Unless otherwise stated, the translations of Australian dollars into US dollars have been made at the rate of US$0.7461 = A$1.00, the noon buying rate in New York City for cable transfers in Australian dollars as certified for customs purposes by the Federal Reserve Bank of New York (noon buying rate) on September 30, 2006.

Certain definitions and glossary

The Company s fiscal year ends on September 30. The fiscal year ended September 30, 2006 is referred to as 2006 and other fiscal years are referred to in a corresponding manner. The abbreviations $m and $bn represent millions and thousands of millions (ie. billions) of Australian dollars respectively. Any discrepancies between total and sums of components in tables contained in this annual financial report are due to rounding.

A glossary of some of the key terms used in this annual financial report is contained at page 285. In addition, non-GAAP financial measures have been defined at page 56.

Forward-looking statements

This annual financial report contains certain forward-looking statements within the meaning of section 21E of the United States *Securities Exchange Act of 1934*. The United States *Private Securities Litigation Reform Act of 1995* provides a safe harbour for forward-looking information to encourage companies to provide prospective information about themselves without fear of litigation, so long as the information is identified as forward-looking and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those projected in the information.

Accordingly, the words anticipate, believe, expect, project, estimate, intend, should, could, may, target, goal, objective, plan, outlook and other similar expressions are used in connection with forward-looking statements.

In this annual financial report, forward-looking statements may, without limitation, relate to statements regarding:

economic and financial forecasts, including but not limited to statements in the financial review and the report of the directors;

anticipated implementation of certain control systems and programs, including, but not limited to those described in risk management; and

certain plans, strategies and objectives of management.

Such forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors, many of which are beyond the control of the Group, that may cause actual results to differ materially from those expressed in the statements contained in this annual financial report. For example:

the economic and financial forecasts contained in this annual financial report will be affected by movements in interest and foreign currency exchange rates, which may vary significantly from current levels, as well as by general economic conditions in each of the Group s major markets. Such variations may materially impact the Group s financial condition and results of operations;

the implementation of control systems and programs will be dependent on such factors as the Group s ability to acquire or develop necessary technology or systems, its ability to attract and retain qualified personnel and the response of customers and third parties such as vendors; and

the plans, strategies and objectives of management will be subject to, among other things, government regulation, which may change at any time and over which the Group has no control. In addition, the Group will continue to be affected by general economic conditions in Australia and worldwide, movements and conditions in capital markets, the competitive environment in each of its markets and political and regulatory policies.

There can be no assurance that actual outcomes will not differ materially from the forward-looking statements contained in this annual financial report.

Selected financial data

The information hereunder has been derived from the audited financial report of the Group, or where certain items are not shown in the Group s financial report, it has been prepared for the purpose of this annual financial report. Accordingly, this information should be read in conjunction with and is qualified in its entirety by reference to the financial report.

		Group	
	2006 $m	2006 (1) US$m	2005 $m
Income statement summary			
Net interest income	**8,686**	**6,481**	6,944
Net life insurance income	**1,417**	**1,057**	1,505
Gains less losses on financial instruments at fair value	**471**	**351**	639
Other income *(2)*	**4,615**	**3,443**	5,251
Significant revenue	**334**	**249**	1,354
Operating expenses *(3)*	**(7,642)**	**(5,702)**	(7,995)
Charge to provide for doubtful debts	**(606)**	**(452)**	(534)
Significant expenses			(748)
Profit before income tax expense	**7,275**	**5,428**	6,416
Income tax expense	**(2,134)**	**(1,592)**	(1,814)
Net profit	**5,141**	**3,836**	4,602
Net profit attributable to minority interest	**(749)**	**(559)**	(610)
Net profit attributable to members of the Company	**4,392**	**3,277**	3,992
Dividends paid/payable *(4)*	**2,554**	**1,905**	2,454

		Group	
	2006 $m	2006 (1) US$m	2005 $m
Balance sheet summary			
Investments relating to life insurance business	**54,784**	**40,874**	49,783
Loans and advances	**283,777**	**211,726**	264,674
Total assets	**484,785**	**361,698**	422,598
Total risk-weighted assets *(5)*	**318,323**	**237,501**	289,833
Deposits and other borrowings	**222,277**	**165,841**	212,557
Life policy liabilities	**46,475**	**34,675**	42,123
Bonds, notes and subordinated debt	**65,006**	**48,501**	41,490
Other debt issues	**2,274**	**1,697**	1,559
Net assets	**27,972**	**20,870**	31,547
Contributed equity	**12,279**	**9,161**	10,828
Ordinary shares	**7,948**	**5,930**	6,894
Other equity instruments *(6)*	**4,331**	**3,231**	3,934
Total equity (excludes minority interest)	**27,804**	**20,745**	25,323

	Group 2006 $	2006 (1) US$	2005 $
Shareholder information			
Earnings per share *(7)*			
Basic	**2.63**	**1.96**	2.46
Diluted	**2.62**	**1.95**	2.42
Dividends per share *(4)*	**1.67**	**1.25**	1.66
Dividends per American depositary share (ADS) *(4)*	**8.35**	**6.23**	8.30
Dividend payout ratio (%) *(4)*	**67.35**	**67.35**	79.56
Net assets per share	**17.38**	**12.97**	20.13
Share price at year end	**36.70**	**27.38**	33.05
Number of ordinary shares at year end (No. 000)	**1,610,288**	**n/a**	1,567,654

	Group 2006 %	2005 %
Selected financial ratios		
Average equity (ordinary shareholder funds) to average total assets (excluding statutory funds) *(8) (9)*	**5.4**	5.5
Return on average assets *(10)*	**0.9**	0.9
Return on average equity (ordinary shareholder funds) *(9) (10)*	**18.8**	18.0
Average net interest spread	**1.88**	1.69
Average net interest margin	**2.31**	2.13
Gross impaired assets to gross loans and acceptances *(11)*	**0.30**	0.35
Net impaired assets to equity (parent entity interest)	**3.1**	2.8
Total provisions for doubtful debts to gross impaired assets	**191.3**	235.8
Capital risk asset ratios *(12)*		
Tier 1	**7.3**	7.9
Tier 2	**3.9**	3.6
Deductions	**(0.4)**	(1.0)
Total	**10.8**	10.5

US GAAP measures

	Group 2006 $m	2006 (1) US$m	2005 $m	2004 $m	2003 $m	2002 $m
Selected financial data in accordance with US GAAP						
Net income	**4,232**	**3,157**	3,891	2,781	3,667	3,455
Total assets	**485,728**	**362,402**	424,628	417,758	398,448	380,280
Total equity	**25,911**	**19,332**	23,385	23,311	22,297	24,005

	2006 $	2006 (1) US$	2005 $	2004 $	2003 $	2002 $
Selected shareholder information in accordance with US GAAP						
Net income per share *(7)*						
Basic	**2.60**	**1.94**	2.44	1.71	2.30	2.11
Diluted	**2.57**	**1.92**	2.40	1.71	2.22	2.06
Dividends per ADS (US$) *(4) (13)*	**n/a**	**n/a**	6.09	6.13	6.03	4.12
Dividends as percentage of net income (%)	**63.48**	**63.48**	67.45	89.78	64.14	65.59

	2006 %	2005 %	2004 %	2003 %	2002 %
Selected financial ratios in accordance with US GAAP					
Net income as a percentage of					
Average total assets (excluding statutory funds) *(8)*	**1.1**	1.0	0.8	1.0	1.0
Average equity	**17.2**	16.7	12.2	15.8	14.5
Total equity as percentage of total assets (excluding statutory funds) *(8)*	**6.0**	6.3	6.2	6.2	6.9

	Group 2006 $m	2005 $m
Reconciliations of non-GAAP measures *(14)*		
Net profit attributable to members of the Company	**4,392**	3,992
Adjusted for		
Significant revenue	**(334)**	(1,354)
Significant expenses		748
Income tax expense/(benefit) on significant items	**96**	(72)
Net profit attributable to members of the Company before significant items	**4,154**	3,314
Net profit to cash earnings before significant items reconciliation		
Net profit attributable to members of the Company	**4,392**	3,992
Adjusted for		
Net profit/(loss) attributable to minority interest	**749**	610
Net profit	**5,141**	4,602
Adjusted for		
Net (profit)/loss attributable to minority interest	**(749)**	(610)
Distributions on other equity instruments	**(254)**	(204)
Treasury shares (after-tax)	**126**	143
Investment earnings on shareholders retained profits and capital from life businesses discount rate variation	**6**	
Revaluation gains/(losses) on exchangeable capital units (after-tax)	**112**	
Net (profit)/loss on sale of controlled entities (after-tax)	**(108)**	
Economic hedge (gain) on proceeds from sale of controlled entities (after-tax)	**(22)**	
Cash earnings	**4,252**	3,931
Adjusted for		
Significant revenue	**(402)**	(1,354)
Significant expenses		748
Income tax expense/(benefit) on significant items	**117**	(72)
Cash earnings before significant items	**3,967**	3,253
Average ordinary shareholder funds reconciliation		
Total average equity *(refer to note 42 in the financial report)*	**26,016**	28,806
Adjusted for		
National Income Securities (average)	**(1,945)**	(1,945)
Trust Preferred Securities (average)	**(975)**	(975)
Trust Preferred Securities II (average)	**(1,014)**	(531)
National Capital Instruments (average)	**(13)**	
Minority interest (average)	**(50)**	(4,281)
Average ordinary shareholder funds	**22,019**	21,074

	Group 2006	2005	2004	2003	2002
Employees					
Full-time equivalent *(15)*	**38,433**	38,933	43,517	42,540	43,202

			Group		
	2006	**2005**	**2004**	**2003**	**2002**
Exchange rates (average and closing per A$1.00)					
Average					
British pound	**0.4150**	0.4141	0.4055	0.3824	0.3622
United States dollar	**0.7467**	0.7654	0.7265	0.6125	0.5324
New Zealand dollar	**1.1432**	1.0847	1.1254	1.1142	1.1992
Closing					
British pound	**0.3991**	0.4326	0.3973	0.4072	0.3474
United States dollar	**0.7478**	0.7617	0.7149	0.6804	0.5440
New Zealand dollar	**1.1439**	1.0991	1.0682	1.1446	1.1565

			Group		
	2006	**2005**	**2004**	**2003**	**2002**
United States dollar (per A$1.00)					
Average *(16)*	**0.7468**	0.7655	0.7263	0.6167	0.5329
September 30	**0.7461**	0.7643	0.7244	0.6797	0.5628

On November 10, 2006 the noon buying rate was US$0.7673 per A$1.00.

			Group 2006			
	November	**October**	**September**	**August**	**July**	**June**
United States dollar (per A$1.00)						
High	0.7837	0.7738	0.7713	0.7677	0.7675	0.7522
Low	0.7619	0.7421	0.7459	0.7573	0.7419	0.7293

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(1) *Translated at the noon buying rate on September 30, 2006 of US$0.7461 = A$1.00.*

(2) *In 2006, other income includes the net profit (before-tax) from the sale of the Custom Fleet business.*

(3) *In 2006, operating expenses includes the net loss (before-tax) from the sale of the MLC Asia businesses.*

(4) *Dividend amounts for a year represent the final and interim dividend in respect of that year, irrespective of when they are declared, determined and publicly recommended and includes issues under the bonus share plan in lieu of cash and the dividend reinvestment plan. Dividends and book value per ordinary share and per American depositary share (ADS) calculations are based on year-end fully paid equivalent ordinary shares, adjusted for loans and rights issues as appropriate. Dividend payout ratio is the dividend amounts for a year divided by cash earnings before significant items. Refer to page 7 for a reconciliation of cash earnings before significant items and page 56 for an explanation of non-GAAP financial measures.*

(5) *The calculation to determine the market risk capital component of risk-weighted assets at September 30, 2006 and September 30, 2005 was carried out under the Standard Method as directed by APRA. The Standard Method as prescribed by the APRA Prudential Standard (APS 113), limits recognition of portfolio effects on outstanding positions and is substantially more restrictive on the rules regarding the matching of positions.*

(6) *Equity instruments comprise preference shares, National Income Securities, Trust Preferred Securities, Trust Preferred Securities II and National Capital Instruments.*

(7) *Refer to notes 8 and 57 in the financial report for an explanation of earnings per share.*

(8) *Statutory funds are excluded given the significant restrictions imposed on these assets by life insurance legislation, regulations and the regulators thereunder. However, current Australian accounting requirements do not allow for these assets and liabilities to be separated and disclosed separately on the balance sheet.*

(9) *Refer to page 7 for a reconciliation of average ordinary shareholder funds.*

(10) *Return represents net profit attributable to members of the Company after deducting distributions on other equity instruments.*

(11) *In 2006, this includes loans accounted for at fair value.*

(12) *As defined by APRA (refer to liquidity, funding and capital resources on page 27).*

(13) *Dividend amounts are translated into US dollars per ADS (representing five fully paid ordinary shares) at the exchange rate on each of the respective payment dates for interim and final dividends. The 2006 final dividend of $0.84 per ordinary share is not payable until December 12, 2006. Accordingly, the total US dollar dividend per ADS for 2006 cannot be determined until that date.*

(14) *Refer to page 56 for explanations of non-GAAP financial measures .*

(15) *Full-time equivalent employees (FTEs) includes part-time staff (pro-rated) and non-payroll FTEs (ie. contractors).*

(16) *The daily average of the noon buying rates.*

Business overview

Introduction

The Group is an international financial services group that provides a comprehensive and integrated range of financial products and services.

The Company traces its history back to the establishment of The National Bank of Australasia in 1858. National Australia Bank Limited is a public limited company, incorporated on June 23, 1893 in Australia, which is the Company s main domicile. Its registered office is 35th floor, 500 Bourke Street, Melbourne Victoria 3000, Australia. The Company operates under the requirements of the *Banking Act* 1959 (Cth) and the *Corporations Act* 2001 (Cth).

In 1981 the National Bank of Australasia merged with the Commercial Banking Corporation of Sydney which was established in 1834.

Globally, as at September 30, 2006, the Group had:

- total assets of $485 billion;
- $97 billion in assets under management and administration;
- $474 billion in funds under custody and investment administration; and
- 8.0 million banking and 2.3 million wealth management customers.

Strategy and corporate principles

The Group s corporate purpose is to generate sustainable satisfactory returns to shareholders.

The Group s strategies are focused on the turnaround of the Group and building new avenues for growth. There has been, and continues to be a focus on:

- re-invigorating the Group s franchise and brand;
- improving the Group s core infrastructure;
- accelerating cultural change around the Group s corporate principles;
- enhancing the Group s disciplined approach to performance improvement;
- improved regulatory and key stakeholder engagement;
- strengthening risk and capital management; and
- leveraging our distinctive capabilities to create new and differentiated growth opportunities.

The Group s corporate principles will continue to be embedded in the Group s culture to ensure that thinking and actions are aligned with the Group s strategic direction.

The five principles are:

- we will be open and honest;
- we take ownership and hold ourselves accountable (for all our actions);
- we expect teamwork and collaboration across our organisation for the benefit of all stakeholders;
- we treat everyone with fairness and respect; and
- we value speed, simplicity and efficient execution of our promises.

Organisational structure and operating model

National Australia Bank Limited is the holding company for the Group, as well as the main operating company. During 2006, the Company had four wholly-owned main operating subsidiaries: Bank of New Zealand, Clydesdale Bank PLC, MLC Limited and National Australia Financial Management Limited.

The Company continues to consider a range of options to optimise its domestic and international operations, including a non-operating holding company. The Company is participating in industry-wide consultation with regulators in the relation to the matter. Consideration of various structural options which involves a range of complex issues, the analysis and subsequent decision on a particular path are expected to take some time to complete.

During the 2006 year, two divestments occurred, the Custom Fleet and MLC Asia businesses. *For further information on these divestments refer to page 45 and page 46 respectively).*

In 2005, one significant divestment occurred. In February 2005, the Group sold the shares of National Europe Holdings (Ireland) Limited, the immediate parent entity of Northern Bank Limited and National Irish Bank Limited. *For further information on this divestment, refer to page 45.*

The business operating model is run along regional lines of business as follows:

- Australia Region comprises Australian Banking and Wealth Management Australia;
- United Kingdom Region comprises United Kingdom Banking and Wealth Management United Kingdom;
- New Zealand Region comprises New Zealand Banking and Wealth Management New Zealand; and
- nabCapital (global).

This is supported by the Group s Other business segment, which includes streamlined functions that support all the regional businesses and comprises Group Funding and Corporate Centre activities.

The Group operates around 1,715 outlets and offices worldwide, of which 58% are in Australia, with the largest proportion of the remainder being in the UK. Approximately 12% of the 1,715 outlets and offices are owned directly by the Group, with the remainder being held under commercial leases.

Refer to note 45 in the financial report for details of the principal controlled entities of the Group and note 21 for details of the Group s property, plant and equipment.

Australia Region

The Australia Region of the Group provides a broad range of banking and wealth management products and services. As well as lending and deposit taking, Australia Region includes the Australian cards, custody and other transactional banking operations, as well as its wealth management activities including insurance, investments and superannuation, in both Australia and Asia. It does not include nabCapital s operations in Australia and Asia.

The Australia Region incorporates an extensive distribution network to service customers. At September 30, 2006, there were 85 integrated financial service centres (catering for customers financial advice needs), 186 business banking centres, 110 agribusiness locations, 27 private banking suites, 787 branches and agencies, and over 3,200 Australia Post GiroPost outlets.

Electronic distribution also provides customers with the choice to meet their financial needs via the internet, over the telephone, through more than 1,290 automatic teller machines (ATM) as at September 30, 2006, or through an extensive network of electronic funds transfer point of sale (EFTPOS) terminals. There were over 1.1 million registered internet banking customers at September 30, 2006.

At September 30, 2006, Australia Region had 22,411 full-time equivalent employees.

In 2005, four key strategies were focused upon:

- customer and employee satisfaction;
- simplifying our business through productivity, efficiency and quality gains;
- re-investing in our critical infrastructure; and
- managing our business units for performance.

Key achievements and actions taken during the 2006 year include:

- awarded Bank of the Year in Money Magazine s 2006 Consumer Finance Awards;
- MLC Insurance Limited awarded Insurance Company of the Year 2006 at the Australian and New Zealand Industry Awards;
- updated its brand in February 2006, supported by significant internal and external communications and sponsorship of the 2006 Commonwealth Games, the Socceroos and the Australian Football League;
- Customer First program a reconfiguration of the business and retail network - with rollout in Queensland completed;
- new and enhanced product offerings, which have delivered substantial revenue growth;
- stable net interest margin and overall risk quality;
- cross-selling of Wealth Management products in bank channels up 31% (investments), up 35% (insurance) and up 22% (debt products) in Wealth Management channels on the 2005 year;

sale of MLC Asia businesses and Custom Fleet business; and

the final review by an independent expert, PricewaterhouseCoopers, was conducted, following which APRA and ASIC jointly considered that all actions under the MLC enforceable undertakings and directions issued to the relevant MLC group companies are now complete.

Management also continues to drive significant cultural and behavioural change within Australia Region. Recent internal surveys have highlighted improvement in employees sharing a common vision and having clarity about what they need to do to help the region meet its goals and objectives. Importantly customer satisfaction improved significantly this year due to the region s commitment to improving the customer experience in the front line through branch refurbishment, service improvement and product innovation.

Five key themes will guide effort over the next few years:

improving process quality to increase customer satisfaction and lower costs;

reducing enterprise costs;

extending customer relationships, to grow revenue, especially cross-selling;

renewing infrastructure; and

creating a distinctive NAB way of working and leading.

Commentary on each of the divisions of the Australia Region is provided below.

Business and Private Banking

The Business and Private Banking operation provides lending, deposit, transaction and specialist services to over 1 million customers, including businesses and high net worth individuals in Australia.

During the 2006 year Business and Private Banking implemented a new operating model bringing together both the product management and distribution management aspects of the business. This change has been instrumental in ensuring a consolidation of the turnaround performance of last year and has enabled a continuation of focused sales campaigns, improved product offerings (eg, Business Options, Business Cash Maximiser and the Portfolio Facility) and increased capacity for our people.

The Company continues to be Australia s largest business lender with a market share of 19.0% (source: RBA financial system, company data, September 2006), and largest business deposit-taker with a market share of over 24.9% (source: APRA banking system, company data, September 2006). The business is underpinned by an extensive distribution network and excellent business bankers. Improvement in processes has led to improved client service and the capacity release for future growth. Emphasis has been on training to ensure the business has strong credit skills and are able to provide value to clients. Growth has also been underpinned by an embedded performance management framework aligned to the Group s corporate principles.

Management are continuing to improve the service and support offered to business customers with the ongoing development of a new business internet banking platform - the foundation release is currently in use with upcoming releases in the first quarter of 2007.

Other key focus areas include the ongoing refinement of the relationship management model, reinforcing sales capability, customer retention, growing deposits, cross-sales and industry specialisation.

Retail Banking

Retail Banking provides lending, deposit and transaction services to approximately 3.2 million retail customers through extensive physical and virtual distribution networks.

The key areas of focus for Retail Banking during the year have been the re-invigoration of the sales channel and product innovation.

The re-invigoration of the retail distribution sales channel has resulted in significant change at the front line. These efforts have concentrated on improving branch sales capability, empowering front line staff and enhancing the customer experience.

A local market operating model was established during the year, with newly appointed regional executives having financial accountability for their local area. Other key initiatives included a realignment of the mobile banker channel, rollout of a new customer segmentation model and branch refurbishment program. This has increased branch home loan sales capability. The refurbishment of 198 branches was completed by September 30, 2006.

As competitive pressure has continued to characterise the external operating environment, product innovation has been another important area of focus. New products launched during the year have included the Velocity Card, Low Rate Visa Card, Custom Home Loan and the NAB Investment Cash Manager. Coupled with new products launched toward the end of the 2005 year (high-yield internet savings account and the Personal Project Loan), these product developments continue to enhance the Group s product offerings and improve sales through targeted campaigns.

Wealth Management

Under the MLC brand, Wealth Management provides investment, superannuation and insurance solutions to 1.9 million retail and corporate customers. As at September 30, 2006, Wealth Management managed approximately $94 billion on behalf of its customers.

Wealth Management s Financial Planning and Third Party division manages relationships with its network of salaried, self-employed aligned and external financial planners, as well as mortgage brokers. The division provides a range of tools and support services to financial planners and mortgage brokers including practice management support, financial planning software, and business growth and efficiency support.

Wealth Management has more than 1,300 aligned and salaried advisers and relationships with more than 1,200 external advisers at September 30, 2006. At the same time, it has relationships with approximately 12,200 brokers.

In its core Australian market, as at June 30, 2006, MLC held the largest share of total individual risk business with a 15.0% share of inforce annual premiums (source: DEXX&R Life Analysis Report, date: June 30, 2006). At the same time, it was ranked number one in market share of master trusts, with a 15.5% market share of funds under management (source: Plan for Life Australian Retail & Wholesale Investments Market Share & Dynamics Report, date: June 30, 2006).

Focus on the utilisation of the regional model to promote business strategies and deliver improved outcomes for customers continued throughout 2006. Product initiatives in 2006 included:

Masterkey Fundamentals, a no commission version of our MasterKey platform, supporting a growing number of advisers operating under a fee for service model;

MLC Long Term Absolute Return (LTAR) Fund, which is an unconventional investment strategy explicitly designed to maximise the long term net real return to investors over rolling 20-year time frames;

two JANA retail investment trusts; and

MLC EasyCover, a debt insurance solution purpose-built for mortgage brokers.

Wealth Management completed its regulatory undertakings to the Australian Securities and Investments Commission (ASIC) and Australian Prudential Regulation Authority (APRA) and also completed the compensation program for investors in a number of products that were adversely affected by October 2001 unit pricing reductions, as well as two associated historical unit pricing errors.

Asia

The Australia Region is also responsible for the Group s banking and wealth management activities in Asia. In May 2006, the Wealth businesses in Hong Kong and Indonesia were sold to AXA Asia Pacific. The remaining businesses have been consolidated with Hong Kong as the primary base supporting both the Tokyo and Singapore branches. The business commenced a strategic alliance with China Union Pay which claims to have up to 99% of the credit and debit card market in China. Chinese visitors to Australia will have access at NAB ATMs and EFTPOS terminals.

Refer to page 35 for detailed information of the financial performance of the Australia Region.

United Kingdom Region

United Kingdom Region (UK), consists of banking and wealth management activities in the UK that provide financial solutions to approximately 3.1 million customers in the UK. It includes nabCapital s operations in the UK. At September 30, 2006, UK had 8,822 full-time equivalent employees.

The Group s activities in the UK operate under two brands, Clydesdale Bank and Yorkshire Bank, within one legal entity, Clydesdale Bank PLC.

Clydesdale Bank was established in 1838 in Glasgow, has a long history of support for Scottish industries and communities, and has been part of the Group since 1987. Clydesdale Bank is one of Scotland s largest retail banks, as well as one of the country s leading business banks. In the 2006 year, Clydesdale Bank has continued to expand its network of Financial Solutions Centres in the south of England.

Yorkshire Bank was founded in 1859 in Halifax, West Yorkshire, and today maintains a strong regional focus in the north of England and the Midlands. Yorkshire Bank has a strong personal customer base and business capability, and has been part of the Group since 1990.

Each bank offers a broad range of financial products and services to both retail and business customers. Products and services provided by Wealth Management and nabCapital offer customers a further range of financial solutions.

Following the sale of Northern Bank Limited and National Irish Bank Limited to Danske Bank A/S in February 2005, the Group provided transitional services to Danske Bank A/S in respect of the Northern Bank Limited and National Irish Bank Limited operations to assist in the transition of ownership of those businesses. These transitional services were provided at cost and ended in April 2006. Subsequently, any ongoing services provided to Danske Bank A/S have been on commercial business terms.

In the 2005 year, the Group recorded a provision of $266 million to cover costs of restructuring initiatives including the streamlining of operations, reductions in staffing levels and the reconfiguration of its distribution networks. It was anticipated that the restructuring would lead to a total reduction of approximately 1,700 positions across the UK over a 12-to-18 month period, together with the closure of approximately 60 Clydesdale Bank branches and 40 Yorkshire Bank branches. This decision reflected the changing needs of customers and the different ways in which they are banking. The branch closure programme was completed in March 2006, six months ahead of schedule, with a total of 105 branches closed and 99% of the reduced staffing positions being achieved by September 30, 2006.

At September 30, 2006, the Group s UK distribution network comprised 153 Clydesdale Bank branches, 190 Yorkshire Bank branches and 74 Financial Solutions Centres, supported by 2 customer contact centres, internet banking, telephone banking and 921 ATMs.

During the 2006 year, a further 6 Financial Solutions Centres were opened in the south and, as at September 30, 2006, there were 38 centres operating in Scotland and the north of England and 36 centres operating in the south of England. Financial Solutions Centres offer integrated business and private banking services to small-medium sized business customers.

In the retail distribution network, the branch network rationalisation has been completed and other locations with potential have been reinforced with investment in flagship branches, which handle micro businesses as well as retail customers.

Further expansion into the mortgage intermediary market continued with the marketing of Clydesdale Bank branded mortgage products through third party distributors. As at September 30, 2006, more than 450 broker relationships have been established.

In July 2006, Clydesdale Bank established an offshore branch banking operation in Guernsey, initially taking deposits with plans to expand the range of services offered.

Further progress has been made toward centralising, streamlining and simplifying technology and operations. Customer Connect , which is the Bank s sales and service illustration tool, has been rolled out to all Yorkshire branches and a new teller system is now successfully operating in over half of those branches. The programme of process simplification and workload removal has continued with greater process and transaction centralisation. In addition, the processing of third party originated mortgages and procurement was outsourced during the year.

Rationalisation of products continues with a planned reduction in product numbers over the next 12-18 months. New base rate tracker mortgage and savings products and offshore deposit products have been launched to enhance our product offerings.

Major pension reforms were implemented during the 2006 year following consultations with staff, unions and pension fund trustees, including a ballot of employees to seek their agreement to the revised benefits. This has resulted in the three defined benefit schemes moving from final salary to a career average structure for benefits accrued from April 1, 2006. As part of the reforms, the Group made a one-off contribution across the defined benefit schemes during the 2006 year and improvements were made to the defined contribution scheme.

Attention has also been directed to further develop talent and the quality of leadership. A branch development programme has been undertaken with more than 200 senior retail staff to enhance leadership skills in areas such as coaching, mentoring and performance management.

Refer to page 36 for detailed information of the financial performance of United Kingdom Region.

New Zealand Region

New Zealand (NZ) Region consists of NZ Banking and Wealth Management activities, and at September 30, 2006 had 4,505 full-time equivalent employees. It does not include nabCapital s operations in New Zealand.

NZ Banking represents the retail and business banking arm of the Group in NZ, which together with nabCapital operates under the Bank of New Zealand (BNZ) brand. Custom Fleet s operations in NZ were also part of NZ Banking until they were sold on July 31, 2006. NZ Banking provides financial solutions for 1.1 million customers at September 30, 2006 and is the primary contributor of the NZ financial result. The Investment Management arm of the Wealth Management operations was sold during January 2006.

BNZ, acquired by the Group in 1992, is one of the largest financial service providers in NZ and has a strong brand position with comprehensive coverage in a very competitive market.

BNZ has strong market share positions in business, corporate, agribusiness and cards. A major component of BNZ s longer-term strategy is also to drive growth in key personal market segments of housing, small-medium enterprises and youth.

BNZ continued its strong programme of re-investing in its people, products and infrastructure which is reflected in gains in customer satisfaction and brand awareness, and BNZ winning domestic and international awards for its Customer Contact Centres.

Focus on people development, performance and customers, and the ongoing enhancement of the physical distribution network, coupled with improved technology, automation and functionality through electronic and remote channels, continue to be core to the strategy. This, together with the strategic decision to discontinue the mortgage broker distribution channel, reflects BNZ s vision to empower its customers with a range of convenient and cost-effective channels.

The distribution network at September 30, 2006 comprised of 180 outlets, 402 ATMs, and shared access to an extensive nationwide EFTPOS network. BNZ also has well-established telephone banking capabilities, in addition to its internet banking service catering for more than 310,000 registered users as at September 30, 2006.

Refer to page 37 for detailed information of the financial performance of New Zealand Region.

nabCapital (formerly Institutional Markets & Services)

nabCapital is a global business with operations in Australia, the United Kingdom, New Zealand, United States and Asia. At September 30, 2006, it had 2,075 full-time equivalent employees. nabCapital provides debt financing, financial risk management and investor services and products to the Group s customers, and trades financial risk management products. It is also responsible for the management of relationships with top tier corporate clients and financial institutions.

In July 2006, the business was reorganised to establish two global business lines Global Markets and Structuring & Investments - and three regionally focused businesses, Australia (including Asia and the US), the United Kingdom and New Zealand.

Global Markets is focused on traded products and financial risk management solutions. It provides foreign exchange, money market, commodities and derivatives products globally through a dedicated 24-hour dealing capability. Structuring & Investments is responsible for manufacturing investment products and managing nabCapital s assets. The three regions are responsible for managing the franchise and customer relationships, including the provision of corporate finance products and services such as project finance and leveraged finance.

The reorganisation of the business ensures nabCapital s structure aligns to its operating model of originating a more diverse mix of funding and risk management products, repackaging or warehousing the risk around those products, and distributing them to a larger pool of investors. This has helped nabCapital maintain its strong position in Australian bonds, loan syndications and project finance league tables (source: Thomson Financial and Dealogic), and saw positive movement in client satisfaction measures.

A strong emphasis on remediation work remains as the business continues towards obtaining internal model re-accreditation for its Market Risk systems from APRA. The cultural change agenda continues with two-thirds of nabCapital employees participating in a cultural diagnostic which is helping to shape the next steps in the cultural development of nabCapital. In addition, nabCapital has initiated a three year Strategic Investment Program aimed at delivering a simplified, flexible, and cost effective business and technology platform to support its growth initiatives.

The move during the year to a new name and a distinct brand identity reflects more accurately the nature of the business. The new branding applies to nabCapital s global operations except in New Zealand, where it continues to operate under the Bank of New Zealand brand.

Refer to page 38 for detailed information of the financial performance of nabCapital.

Other

The Group s Other business segment includes streamlined functions that support all the regional businesses and comprises Group Funding and Corporate Centre activities. Group Funding acts as the central vehicle for movements of capital and structural funding to support the Group s operations. Corporate Centre activities include strategic development of the portfolio of businesses, financial and risk governance, developing and retaining talent, capital and balance sheet management.

Employees

The following tables summarise the Group s staffing position as at September 30:

	2006 Number	2005 Number	2004 Number
By geographic region			
Australia	**24,263**	23,554	24,567
Europe	**9,197**	9,868	13,324
New Zealand	**4,686**	4,814	4,766
United States	**93**	114	141
Asia	**194**	583	719
Total full-time equivalents *(1)*	**38,433**	38,933	43,517

	2006 Number	2005 Number	2004 Number
By line of business			
Australia Region	**22,411**	22,136	23,128
United Kingdom Region	**8,822**	9,480	12,865
New Zealand Region	**4,505**	4,645	4,596
nabCapital	**2,075**	1,993	2,073
Other	**620**	679	855
Total full-time equivalents *(1)*	**38,433**	38,933	43,517

(1) *Full-time equivalent employees (FTEs) includes part-time (pro-rated) and non-payroll FTEs (ie. contractors).*

The Group s full-time equivalent (FTE) employee numbers decreased by 500 or 1.3% to 38,433 during the 2006 year. This decrease primarily reflects the following:

the sale of the Group s Custom Fleet and MLC Asia businesses which reduced FTE by 923;

restructuring activities, particularly in Australia and the United Kingdom, which decreased FTE by 1,654; partly offset by

the uplift associated with projects and business initiatives, which increased FTE by 1,815.

The Group s FTE employee numbers decreased by 4,584 or 10.5% to 38,933 during the 2005 year. This decrease primarily reflected the following:

the sale of Northern Bank Limited and National Irish Bank Limited, which had 2,712 FTE at September 30, 2004; and

the significant restructure, reorganisation and integration of all of the Group s businesses, particularly in the Australia, United Kingdom and nabCapital segments, amounting to a reduction of 1,964 FTE.

Refer to page 47 for further information on the Group s restructuring expenses and provisions recorded by the Company during the 2005 year.

The Group continues to work professionally and constructively with the unions in Australia, United Kingdom, New Zealand and in other countries where the Group operates, recognising their members as key stakeholders in the organisation. The Group utilises a number of industrial instruments including individually negotiated contracts and collective agreements.

In Australia, there is a single enterprise agreement, which comprises the terms and conditions for all employees. This agreement was developed and negotiated with the Finance Sector Union and was certified in

February 2006. The agreement replaced all previous agreements and some site agreements to provide a single consolidated version for Australian employees. The agreement runs from 2006 to 2009 and provides for a total of 4% pay increase each year for all employees, excluding those on management levels.

Bank of New Zealand has a collective agreement covering the branch network, contact centres and back-office locations. This collective agreement was renegotiated with FinSec late in calender 2005 and runs from November 2005 to October 2007. A pay increase of 4.35% was paid to these employees in November 2005, with a further 4% to be paid in November 2006.

Pay negotiations commenced with the UK union, Amicus, during November 2005. A single negotiation process replaced the three separate pay negotiations previously conducted annually. A pool of 3.3% was paid to these employees with a further 0.1% available for lower paid employees.

For further information on the remuneration and reward policies offered by the Group, refer to the remuneration report on pages 78 to 93 of this annual financial report and note 41 shares, performance options and performance rights and note 52 equity instrument holdings of key management personnel in the financial report.

Economic outlook

This section contains forward-looking statements. *Refer to forward-looking statements on page 4.*

Global economic conditions remained strong in 2006. While the US expansion has begun to moderate, China and more generally developing economies performed very strongly. In addition Japanese activity picked up significantly and the Euro area has improved.

Business conditions in the countries that contain the bulk of the Group s assets remained solid but varied by regions and sectors. In New Zealand, slow growth emerged as households adjusted to higher interest rates and cooling property markets. Australian activity remained strong and unemployment levels continue to fall. Resource and related sectors and regions were boosted by high commodity prices, while conditions moderated in retail and manufacturing sectors. UK activity picked up with contributions from both household spending and business investment.

The global growth outlook is for a moderation in activity in 2007. The normalising of interest rates and continued high oil prices are expected to continue to slow the pace of the current global expansion. Growth is also expected to be sustained in the Group s main operating regions. In Australia, some moderation in domestic spending is expected. The drought and slower domestic demand is expected to impact growth. Faced with capacity and inflationary pressures, New Zealand looks set to sustain slow growth in domestic spending. In the UK, growth is expected to remain reasonable with a strong services sector but a weak manufacturing sector.

The Group s main areas of operation continue to face similar economic risks and vulnerabilities. External imbalances and already stretched fiscal positions especially in the US and Europe might limit any response to any increased geopolitical tensions. Any disruption to the current strong growth in China and other emerging economies would also be expected to lead to a marked revaluation of global income growth and asset prices. On the other hand, overly aggressive action by central banks in response to inflation pressures could also trigger negative wealth effects and a marked slowdown in household spending.

Competition

The Australian financial system is characterised by intense competition from a large number of traditional and new players, and well-developed equity and corporate bond markets. There are four major national banks and many other financial conglomerates with national operations offering a complete range of financial services, as well as a number of smaller regional institutions and niche players. Non-bank financial institutions are a force in the Australian financial system, although many have demutualised over the past decade to capture capital-related and other competitive advantages. Non-bank financial institutions offer a wide portfolio of products and services including insurance, investments and superannuation (pensions).

Competition also comes from numerous Australian and, in many cases, international non-bank financial intermediaries including investment and merchant banks, specialist retail and wholesale fund managers, building societies, credit unions and finance companies. Product and functional specialists operate and are important players in the household and business mortgage, credit card deposit and other payment services markets. The rapid development and acceptance of the internet and other technologies have increased competition in the financial services market and improved choice and convenience for customers.

These forces are evident across all of the Group s businesses in each of its geographic markets. Within the broader financial services industry, increased competition has led to a reduction in operating margin, partly offset by fees and other non-interest income and increased efficiencies. The latter has been largely achieved through greater investment in new technologies for processing, manufacturing and retailing products and services. These trends towards increasingly contestable markets offering improved access, wider choice and lower prices for customers are expected to continue in the future.

Risk management

Introduction

Effective management of risk is a key capability for a successful financial services provider, and is fundamental to the Group s strategy. A key component of the Group s risk management strategy is the establishment by the Board of a formal risk appetite statement for the Group.

This places an overall limit on the total amount of risk that the Group is prepared to take. That position is set with respect to the returns that the Group is seeking to provide to shareholders, the credit rating that the Group is seeking to maintain, and the Group s capital position and desired capital ratios.

This position informs the Group s risk, capital and business management limits and policies. It is periodically reviewed by the Board as a part of the strategic planning process, or as the commercial circumstances of the Group change.

The Group manages risk within an established three lines of defence framework. The first line of defence comprises the business units managing the risks associated with their activities. The second line encompasses dedicated risk functions at both a Group and regional level, which are accountable for independent monitoring and oversight. The third line of defence relates to Internal Audit independently reviewing, monitoring, and testing business unit compliance with risk policies and procedures, and regularly assessing the overall effectiveness of the risk management framework. Control is exercised through clearly defined delegation of authority, with clear communication and escalation channels throughout the organisation.

The Group Risk Management Committee, chaired by the Group Chief Executive Officer, serves as the principal risk strategy and risk policy decision making management body within the Group, and provides the Board with assurance in the performance of the overall risk management framework. This committee is supported by five sub-committees Group Credit Risk Committee, Group Market Risk Committee, Group Operational Risk and Compliance Committee, Group Asset and Liability Committee, and Group Economic Capital Committee each with a specialised focus.

Each of the four major regions also has a regional Risk Management Committee comprised of senior regional executives, which serves to provide a leadership focus on key risk issues within the region.

Refer to page 61 for Risk Committee members, responsibilities and charter.

In response to the March 2004 APRA report on the foreign currency options trading losses, significant progress has been made to improve market risk systems, governance processes, and organisational culture although the organisation continues to invest in further development of systems and culture. Key outcomes include the reopening in May 2005 of the foreign currency options trading desk, and closure of all governance and culture related remedial actions in April 2006. The Group is also at an advanced stage with its internal market risk model re-accreditation.

Risk factors

The following are certain risk factors that may impact the Group s future results. The factors discussed below should not be considered to be the complete list of all potential risks.

For a discussion of the Group s risk mitigation procedures, refer to risk mitigation on pages 16 to 20.

Credit risk

As a financial institution, the Group is exposed to the risks arising from changes in credit quality and the ability of the borrowers or counterparties to fulfil their contractual obligations under loan agreements or other credit facilities. The Group s provision for doubtful debts provides for loan losses incurred in loans and advances. Estimating losses incurred in the loan portfolio is of its very nature uncertain and the accuracy of those estimates depends on many factors, including general economic conditions, rating changes, structural changes within industries that alter competitive positions, and other external factors such as legal and regulatory requirements.

Market risk

The Group s earnings are also subject to a range of market risks, principally changes in market interest and foreign exchange rates, equity and commodity prices, and associated financial derivatives.

Liquidity and funding risk

The Group is exposed to liquidity and funding risk and its banking entities must comply with the relevant regulatory liquidity requirements of the banking and other regulators in the countries they operate in.

Operational risk

As a financial services group, the Group is exposed to operational risks, being the risk of loss resulting from inadequate or failed processes, people or systems or from external events.

Pension risk

Pension risk is the risk that, at any point in time, there are insufficient funds available to meet the pension obligations due now and in the future. There are a number of factors that underpin pension risk, each with differing characteristics. Broadly, pensions risk can be described as being the aggregation of asset risk, liability risk and accounting risk. The Pension Group s principal exposure to pension risk is in the UK business.

Regulatory risk

The Group is subject to substantial regulation in the countries where it operates. The Group s businesses and earnings maybe affected by fiscal or other policies that are adopted by various regulatory authorities, or the failure to meet the requirements of those regulators.

Changes or developments in regulations, including accounting standards, could impact the earnings performance of the Group. The nature and impact of future changes in such policies are not predictable and are beyond the Group s control.

Regulatory agencies have broad administrative power over many aspects of the Group s business, including liquidity, capital adequacy and permitted investments, money laundering, privacy and record keeping. Financial services laws and regulations currently governing the Group, the Group s branches and subsidiaries may change in ways that could have an adverse impact on the Group s business. Also, bank regulators and other supervisory authorities in Australia, the United Kingdom, the US and elsewhere continue to examine payment processing and transactions under regulations governing such matters as money laundering, prohibited transactions with countries subject to sanctions and other anti-corruption matters. If the Group fails to respond appropriately to regulatory developments, actions or measures, the Group s reputation could be harmed and could be subject to additional legal risk, such as fines or penalties.

Strategic risk

Strategic risk is the current or prospective risk to earnings and capital arising from poor business decisions, improper implementation of decisions or lack of responsiveness to changes in the business environment. These include the quality of the strategic planning process, the achievability of the strategy, the implications of the strategy on risk appetite and the nature of products, services and customers targeted.

Business conditions and general economy risk

As an international financial services group, the Group s businesses are affected by conditions in the markets in which it operates. The profitability of the Group s businesses could be adversely affected by a worsening of general economic conditions in Australia, New Zealand, the UK, the US, or elsewhere, as well as by foreign and domestic trading market conditions.

Legal risk

The Group may be and is subject to legal proceedings, including tax disputes with the taxation authorities in Australia and New Zealand. The outcome of these proceedings could affect earnings.

Refer to note 46 in the financial report for further information on the Group s contingent liabilities, including the tax disputes.

Fluctuations in currency exchange rates

As the Group prepares its annual financial report in Australian dollars, changes in currency exchange rates, particularly between the Australian dollar and the British pound, NZ dollar or US dollar, may have an adverse effect on the earnings that it reports.

Other

Many other types of risks such as those pertaining to payment systems, computer systems fraud, legislative compliance, business continuity, disaster recovery and e-commerce risks exist and are managed throughout the Group.

Risk mitigation

For the major areas of risk, the processes for managing these risks is discussed below:

Credit risk

The Group s credit risk management infrastructure is designed to provide sound management principles and practices to maintain appropriate asset quality across the Group.

The Group has dedicated divisions within Group Risk Management, responsible for the development and maintenance of credit policies, large counterparties credit approvals, and the development and maintenance of key credit risk systems.

Establishing an appropriate credit risk environment

Significant credit risk strategies and policies are reviewed and approved annually by the Risk Committee of the Board, and ultimately the Board. Through such policies, the Board establishes the Group s tolerance for risk. These policies are delegated to management and administered under their guidance and control.

Single large exposure policies and industry concentration limits are in place across the Group. Overall composition and quality of credit portfolio exposures are monitored and periodically reported to the regional boards and the Board, and, where required, to the relevant supervisory authorities.

Operating under a sound credit granting process

The Group has established processes for the origination of credit. Key considerations include:

- establishment of overall credit limits at the level of both individual counterparties and groups of connected counterparties for on- and off-balance sheet exposures;
- satisfaction with repayment capacity and integrity of the counterparty;
- use of financial covenants;
- use of collateral;
- consideration of economic and industry conditions; and
- an objective customer risk rating assessment system.

Supporting these considerations are defined and documented policies and processes for the origination of credit. The key elements of the process include:

- clearly defined authorities for the approving of credit; and
- a system of overview of credit approvals by a higher level of authority to ensure adherence to policies and good credit practice.

The delegated authorities are aligned to the counterparty risk by the inclusion of customer risk ratings in the authority matrix. The Group s credit rating system is based on probability of default of a counterparty and provides differentiation of credit risk and focus in pricing for risk.

For consumer credit, scoring systems are in place and are supported by appropriate monitoring tools. These tools provide the essential continual review of data integrity, scorecard performance and decision strategies.

Software to validate and verify input data is used globally to support data integrity and counteract fraudulent activity.

Maintaining adequate controls over credit risk

Monitoring the condition of individual credit exposures in the business units principally rests with the customer-facing relationship managers, with overview by Risk Management credit executives.

There is a formal process, undertaken by specialist units, of independent oversight of credit in each region across the Group. Periodic reporting is submitted to management and the Risk Committee of the Board.

Credit processes and policy compliance are subject to internal auditing. In addition, targeted credit reviews of specific business units or regions are undertaken by Risk Asset Review teams. Credit exposures identified by this team to be outside agreed parameters are reported to the appropriate levels of authority for attention.

Credit exposures showing adverse trends are passed to specialist units that undertake the collections and recovery processes. The Group utilises skilled internal resources supported by external resources. Through the use of due diligence techniques, the Group regularly targets areas of interest or concern within its credit portfolio to review and maintain the quality of the credit portfolio.

The Group also provides quarterly information to APRA, detailing large exposures to individual customers or groups of related customers in excess of 10% of total Tier 1 and Tier 2 capital. APRA applies restrictions on the Group s ability to accept large credit exposures.

Market risk

The management of market risk is segregated between risk derived in the Group s trading activities and risk resulting from mainstream banking activities.

Traded market risk

Traded market risk is mainly due to the trading activity undertaken by the Group through its dealing desks, which focus on traded products and risk management solutions for customers. The Group currently provides foreign exchange, money markets, commodities, credit products and associated derivatives products globally through a dedicated 24 hour dealing capability.

Traded market risk is managed and controlled in accordance with policy approved by the Risk Committee of the Board. Trading is conducted on the basis of specific purpose profit centres authorised to deal in certain instruments approved by a management committee.

Traded market risk is primarily managed and controlled using Value at Risk (VaR) which is a standard measure used in the industry. The global VaR limit is approved by the Board and delegated at the discretion of the Group Chief Executive Officer.

VaR methodology

VaR is an estimate of potential losses resulting from shifts in interest rates, currency exchange rates, traded credit spreads, option volatility, equity prices and commodity prices. The estimate is calculated on an entire trading portfolio basis, including both physical and derivative positions. The Group s VaR is predominantly calculated using historical simulation. This method involves multiple revaluations of the trading books using two years of historical pricing shifts. The pricing data is rolled monthly so as to have the most recent two year history of prices. The results are ranked and the loss at the 99th percentile confidence interval identified. The calculation and rate shifts used assume a one-day holding period for all positions.

In the case of small number of products such as commodities and equities, an alternate contingent loss matrix approach is used. While risk positions in these asset classes are small, efforts are continuing to bring them within the scope of the VaR methodology described above.

The use of a VaR methodology has limitations, which include:

the historical data used to calculate VaR is not always an appropriate proxy for current market conditions. If market volatility or correlation conditions change significantly, losses may occur more frequently and to a greater magnitude than in the VaR measure;

VaR methodology assumes that positions are held for one day and may underestimate losses on positions that cannot be hedged or reversed inside that timeframe;

VaR is calculated on positions at the close of each trading day, and does not measure risk on positions taken and closed before the end of each trading session; and

VaR measure does not describe the directional bias or size of the positions generating the risk.

VaR estimates are checked via backtesting for reasonableness and continued relevance of the model assumptions.

The Group employs other risk measures to supplement VaR, with appropriate limits to manage and control risks, and communicate the specific nature of market exposures to executive management, the Risk Committee of the Board and ultimately the Board. These supplementary measures include stress testing, stop loss, position and sensitivity limits.

Relationship between risk measures

Given the variance in the levels of detail and differing valuation shifts used to calculate these measures, the Group harmonises the specific desk controls with VaR. Market Risk conducts a calibration program supported by ongoing portfolio analysis, to maintain consistency across different risk controls. With the introduction of an Economic Capital framework, the various measures will be linked and derived from the economic capital allocated and used by each of the profit centres within traded market risk.

During the year, the Group s VaR exposure has been maintained within the Board approved limit. The following table shows the Group s VaR for all controlled banking entities trading portfolios, including both physical and derivative positions:

Value at risk at 99% confidence interval	**2006 $m**	**2005 $m**
Average value for year		
Foreign exchange risk	**1**	3
Interest rate risk	**9**	13
Volatility risk	**1**	1
Commodities risk	**1**	
Credit risk *(1)*	**1**	
Diversification benefit	**(3)**	(3)
Total	**10**	14
Minimum value for year *(2)*		
Foreign exchange risk	**1**	1
Interest rate risk	**5**	9
Volatility risk	**1**	1
Commodities risk		
Credit risk *(1)*	**1**	
Diversification benefit	**(1)**	
Total	**7**	11
Maximum value for year *(2)*		
Foreign exchange risk	**4**	7
Interest rate risk	**14**	18
Volatility risk	**1**	3
Commodities risk	**2**	1
Credit risk *(1)*	**4**	1
Diversification benefit	**(10)**	(10)
Total	**15**	20

(1) As of June 1, 2005, market risk included credit VaR as part of the internal model calculation.

(2) VaR is measured individually according to foreign exchange risk, interest rate risk, volatility risk, commodities risk and credit risk. The individual risk categories do not sum up to the total risk number due to diversification benefit.

Non-traded market risk

Non-traded market risk includes structural interest rate risk, structured foreign exchange risk, liquidity and funding risk.

The primary objective for the management and oversight of the risk is to maintain the risk profile within approved risk appetite and limits, while implementing strategies that optimise stable current and future earnings from the impact of market volatility.

Policies, inclusive of risk appetite and limits, are approved by the Board, with Group authority delegated to the Group Asset and Liability Management Committee (Group ALCO) and Regional Asset and Liability Management Committees (Regional ALCOs) for their subsequent implementation and monitoring.

Interest rate risk management across the Group is directed by Group Treasury, with execution on a regional basis.

Risk oversight is the responsibility of the Group Non-Traded Market Risk team which reports directly to the Deputy Group Chief Risk Officer. This team maintains standards of independence and control resilience consistent with traded market risk, with teams in place across the regional businesses.

Structural interest rate risk

Structural interest rate risk is the risk to the Group s earnings and capital that arises out of customers demands for interest rate-related products with various re-pricing profiles. As interest rates and yield curves change over time the Group may be exposed to a loss in earnings and capital due to the re-pricing structure of the balance sheet. It includes:

re-pricing risk the risk of loss of earnings or economic value caused by the differential timing of the re-pricing of assets and liabilities in the banking book;

basis risk the risk of loss of earnings or economic value due to the repricing of assets and liabilities in the banking book relative to different wholesale market rates;

yield curve risk the risk of loss of earnings or economic value due to a change in the slope or shape of the yield curve; and

optionality the risk of loss of earnings or economic value owing to unanticipated changes to balance sheet volumes or rates as a result of embedded options in the banking book.

The objective of the Group is to secure stable and optimal net interest income over both a 12-month period and over the long term, as exemplified via the investment term of equity and non-interest-bearing deposits.

Interest rate risk is principally managed through the use of interest rate swaps, forward rate agreements, overnight index swaps and futures. All products are used within approved mandates, with strategies subject to monthly reporting to Group ALCO and Regional ALCOs.

Basis risk is more difficult to manage, given limited market liquidity in basis risk products. To mitigate this risk, Group Treasury and the Group Non-Traded Market Risk team closely monitor pricing strategies, product innovation and marketing, since these play an important role in reducing the mismatch attributable to repricing characteristics of assets and liabilities provided to customers.

The Group employs VaR as one of its principal measures for interest rate risk, along with an Earnings at Risk (EaR) measure that calculates the impact on future net interest income over the next 12 months. These limit measures are calibrated to calculate structural interest rate risk, incorporating different confidence intervals, holding periods and reporting timeframes than those for traded market risk, and are complemented by sensitivity and scenario analyses.

The table below presents a summary of the aggregated structural interest rate risk relating to non-trading assets and liabilities. The table contains forward-looking statements *(refer to forward-looking statements on page 4)*. Based on the structural interest rate risk position at balance date, the table shows the potential impact on net interest income, for the year ending September 30, 2007 of an immediate 1% parallel movement in interest rates across the whole yield curve.

The non-Australian exposure (expressed in Australian dollars) is the net exposure of offshore controlled branches and controlled entities, excluding life insurance and fund management entities. Structural interest rate exposure in some countries may be biased towards rising interest rates, whilst in others may be biased towards declining interest rates, depending on different economic conditions or cycles.

18

	Forecast effect on net interest income 2006(1)		Forecast effect on net interest income 2005(2)	
	Rates up 1% $m	Rates down 1% $m	Rates up 1% $m	Rates down 1% $m
Australian Operations	(11)	11	42	(42)
Non-Australian Operations	46	(46)	10	(10)

(1) Represents the forecast effect on net interest income for the year ending September 30, 2007 as calculated by the EaR measure.

(2) Represents the forecast effect on net interest income (as at September 30, 2005) for the year ended September 30, 2006.

Hedging strategies

Regional Treasuries execute hedging strategies to mitigate risk and manage exposures within limits and metrics set by Group and Regional ALCOs, in line with the risk appetite approved by the Board. The Regional Treasuries have a set of approved products to execute hedging strategies, primarily interest rate swaps, forward rate agreements and interest rate futures contracts. These strategies reduce risk via offsetting the exposures to achieve a lower level of VaR/EaR, consistent with the hedge strategy intent. The strategies are targeted to minimise the exposure to a loss of earnings and capital, and are subject to validation by Group Non-Traded Market Risk. In addition to the objective of reducing repricing risk across the balance sheet, the strategies are evaluated with regard to AIFRS reporting requirements. In the majority of cases, hedging relationships that are effective under AIFRS are established. Where the requirements of AIFRS are not met, such derivative financial instruments are classified as non-hedging for accounting purposes.

Hedge relationships are formally documented at inception. The documentation includes identification of the hedged item and the hedging instrument, details the risk that is being hedged and the way in which effectiveness will be assessed at inception and during the period of the hedge. If the hedge is not highly effective in offsetting changes in fair values or cash flows attributable to the hedged risk, consistent with the documented risk management strategy, hedge accounting is discontinued.

Structural foreign exchange risk

Structural foreign exchange risk arises from investments in the Group s foreign branches and controlled entities. Both earnings and capital are exposed to movements in foreign exchange rates as a result of these investments.

Reported earnings and capital are exposed to movements in exchange rates as a result of the need to translate earnings and net assets of the foreign operations into the Australian dollar consolidated financial statements. This exposure is referred to as an accounting or translation exposure which, in the absence of any long-term realignment in exchange rates, has no lasting impact on underlying economic exposures. As a consequence, the Group does not hedge these exposures as a matter of course.

Transaction foreign exchange exposures arise from the risk that future cash flows will be converted to Australian dollars at less favourable rates than at present. Such cash flows could result from the repatriation of profits or capital back to the Company. The policy of the Group is to fully hedge these exposures at the time of commitment, if they are of a material nature. Hedging of transaction exposures relating to offshore acquisitions and divestments is assessed on a case-by-case basis.

Liquidity and funding risk

Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due at acceptable cost, and includes:

intra-day ability of the Group to meet intra-day collateral requirements in relation to clearing and settlement obligations;

operational ability of the Group to meet refinancing requirement for a predefined period i.e. up to 30 days; and

structural liquidity risk profile of the Group balance sheet to accommodate the Group strategic plan and Board risk appetite.

Funding Risk is the appetite and capacity of the market to provide adequate diversified term and short term funds to meet the Group s strategic plan objectives, and includes:

concentration risk - ability of the Group to diversify its funding sources to prevent undue reliance on a single or related counterparties;

tenor risk - ability of the Group to raise adequate longer term funds (maturity at issue in excess of 12 months); and

market access risk - the risk that the Group cannot access the market either domestically or via other banking subsidiaries within the Group at the time funding is needed.

The Group manages liquidity and funding risk through a combination of positive cash flow management, the maintenance of portfolios containing high quality liquid assets, maintenance of a prudent funding strategy and diversification of its funding base. The Group undertakes a conservative approach by imposing internal prudential limits that are in addition to regulatory requirements.

Regulatory supervision of banking liquidity in Australia is undertaken by APRA through its Prudential Standard APS 210 Liquidity (APS 210). In accordance with the requirements of APS 210, risk is measured and managed in the Group s banking entities on a cash flow basis. Each regional bank is required to monitor under both going concern and name crisis scenarios, and cash flow mismatch limits have been established to limit the Group s exposure. An additional prudential requirement of the regional banks is to maintain liquid asset portfolios to meet unexpected cash flow requirements.

Regulatory authorities in some countries in which the Group operates impose their own requirements to ensure that liquidity is managed prudently. These requirements may involve the bank maintaining a reserve deposit account with the central bank, holding a portfolio of highly liquid securities and overseeing the internal prudential supervision of liquidity.

Short term funding (under one year) is managed by nabCapital and Regional Treasuries on a Regional basis, consistent with the Group s Liquidity objectives. Funding over one year is managed by Group Treasury.

A three-level contingency plan has been established for the management of an escalated liquidity requirement where the Group experiences either restricted access to wholesale funding, or a large increase in the withdrawal of funds. The plan identifies triggers on each level, details the action required, allocates the key tasks to individuals, provides a timeframe and defines a management committee to manage the action plan.

Refer also to liquidity, funding and capital resources on page 24.

Life insurance and funds management market risk

The life insurance business is exposed to market risk arising from adverse movements in market prices affecting fee income on investment-linked policies and the returns obtained from investing shareholder funds held in each life company. Market risk is also affected by mismatches between assets and the guaranteed returns offered on some classes of policy, which may not have been effectively hedged through the matching of assets.

The Group attempts, wherever possible, to segregate policyholder funds from shareholder funds. Appropriate investment mandates are then developed for each. The Group attempts to match asset characteristics with the nature of policy obligations. The shareholder funds are invested so as to meet the likely obligations of those funds in the event adverse risks transpire. However, certain clauses included in policy and sales documents, regulatory constraints or the lack of suitable investments may affect this.

The majority of the policyholder assets are held for investment-linked policies where the policyholder bears the risk of movements in the market value and determines the allocation of the assets. Should markets fall, fee income of the Group will decrease as it is based on the amount of assets invested.

Operational risk

Various reports are produced at management, Board committee and Board level to assist with their oversight and monitoring obligations. This incorporates regional reporting of risk profiles, key operational risk events, as well as consideration of external events and their relevance to the Group. This process generates visibility and understanding of the Group s overall operational risk profile.

The Operational Risk Framework is based on a set of core principles and defines the Group s standards for operational risk management. Its design recognises the importance of embedding operational risk into business-as-usual activities. It has particular focus on defining and implementing the right behaviours and incorporating risk considerations into the Group s systems and processes.

The Operational Risk Framework includes:

- a structured risk management process to facilitate the identification, assessment, quantification, monitoring and management of operational risks within the Group s operational risk appetite;
- systematic management and oversight of the Group s operational risk; and
- reference to the Group Risk Charter which contains an established governance structure that is used to ensure consistent application, management and reporting of the operational risk management process.

Regulatory risk

Regulatory risk arises from the risk of regulatory change or from failure to meet the requirements of law or regulation. Material impacts can include reputation impact, incurring restrictive conditions on how the Group does business or loss or suspension of licence to engage in certain activities. To mitigate this risk, the Group actively participates in regulatory developments with the regulatory authorities of the Australian Government, foreign governments and international agencies. The Group also places significant emphasis on maintaining appropriate internal compliance arrangements to ensure we meet these requirements.

Regulation of the financial services system

Australia

APRA is the prudential regulator of the Australian financial services industry, including authorised deposit-taking institutions (ADIs), life and general insurance companies, reinsurance companies, friendly societies and most members of the superannuation industry. ADIs are bodies corporate such as banks, credit unions and building societies that are authorised by APRA to conduct banking business in Australia.

The Reserve Bank of Australia (RBA) has overall responsibility for monetary policy, financial system stability and, through a Payments System Board, payment system regulation including the operations of Australia s real-time gross settlement system.

ASIC enforces and regulates company and financial services laws to protect consumers, investors and creditors. ASIC is an independent government body that regulates financial markets, corporations, securities, futures and consumer protection in superannuation, insurance and deposit taking.

ASIC has granted the Group its Australian Financial Services Licences issued pursuant to the *Corporations Act* 2001 (Cth). The Group s Australian operations are operating under 19 licences representing the wide variety of financial services that it offers.

The Australian Competition and Consumers Commission (ACCC) administers the *Trade Practices Act* 1974 (Cth). The ACCC promotes competition and fair trade in the market place to benefit consumers, business and the general community.

Consumer affairs offices in each Australian State and Territory are responsible for specific credit and fair trading legislation.

The Australian Transaction Reports and Analysis Centre (AUSTRAC) oversees compliance with the requirements of the *Financial Transactions Reports Act* 1988 (Cth), which obliges the Group to identify its customers and collect and report information about certain transactions. AUSTRAC has dual roles as Australia s anti-money laundering regulator and specialist financial intelligence unit.

The *Banking Act* 1959 (Cth) allows APRA to issue prudential standards that, if breached by ADIs or groups containing ADIs, can trigger legally enforceable directions. Under the *Banking Act* 1959 (Cth), APRA has strong and defined powers to direct the activities of an ADI in the interests of depositors or when an ADI or a group containing an ADI has contravened its prudential framework. These direction powers enable APRA to impose corrective action without taking the step of assuming control. The *Banking Act* 1959 (Cth) also requires an ADI to inform APRA of breaches of prudential requirements and of any materially adverse events (whether in respect of an ADI in a group or the overall group containing that ADI).

APRA has maintained prudential standards covering capital adequacy, market risk, funds management and securitisation, liquidity, credit quality, large exposures, associations with related entities and group risk management, outsourcing, business continuity management, risk management of credit card activities and audit and related arrangements for prudential reporting.

With effect from July 1, 2006, revisions to the prudential standards covering capital adequacy, credit quality, large exposures and funds management and securitisation were issued by APRA to address its response to AIFRS. APRA has also issued two new prudential standards with effect from October 1, 2006, covering fitness and propriety of key responsible persons and corporate governance.

Further, APRA is in the process of fully updating its suite of capital adequacy standards to reflect the introduction of the Basel II Capital Accord framework (*refer to further discussion under changing regulatory environment*).

APRA requires ADIs to provide regular reports covering a broad range of information, including financial and statistical data relating to their financial position and prudential matters. APRA gives special attention to capital adequacy, sustainability of earnings, loan loss experience, liquidity, concentration of risks, potential exposures through equity investments, funds management and securitisation activities, and international banking operations.

In carrying out its supervisory role, APRA supplements its analysis of statistical data collected from ADIs with selective on-site visits by specialist teams to overview discrete areas of banks operations.

APRA also formalises a consultative relationship with each ADI s external auditor with the agreement of the ADI. The external auditors provide additional assurance to APRA that prudential standards applying to ADIs are being observed, and that statutory and other banking requirements are being met. External auditors also undertake targeted reviews of specific risk management areas selected at the annual meeting between the ADI, its external auditor and APRA. In addition, each ADI s chief executive officer attests to the adequacy and operating effectiveness of the risk management systems established to monitor and manage the key risks facing the ADI group.

Under APRA s prudential framework, the Company is required to obtain APRA s prior approval for the establishment or acquisition of a regulated presence domestically or overseas. There are also prior consultation requirements whereby the Company must consult with APRA before establishing or acquiring a subsidiary (other than certain special purpose financing entities), committing to acquire more than a 10% equity interest in an entity that operates in the field of finance, or in certain circumstances taking up an equity interest in an entity in a workout situation. Further, under section 63 of the *Banking Act* 1959 (Cth), without the consent of the Treasurer of the Commonwealth of Australia, no ADI may enter into any agreement or arrangement for the sale or disposal of its business (by amalgamation or otherwise), or for the carrying on of business in partnership with an ADI, or effect a reconstruction.

The Group s wealth management business is regulated by both ASIC and APRA. ASIC administers legislation relating to Wealth Management s key financial services, including managed investments, superannuation, retirement income streams and insurance. Its role is to ensure industry participants comply with legislation, while promoting fair, confident and informed participation in the Australian market by investors and consumers. APRA provides prudential regulation through the oversight of Wealth Management s life insurance companies and approved trustees of superannuation funds and responsible entities of managed investment schemes. As with ADIs, APRA undertakes both off-site and on-site assessment of this activity at both a Wealth Management group and individual entity/business line level. APRA s industry focus over the past year has been on the re-licensing of approved trustees.

Non-Australian jurisdictions

APRA, under the international Basel framework, assumes the role of home banking supervisor and maintains an active interest in overseeing the operations of the Group, including its offshore branches and subsidiaries.

The Group s branch and banking subsidiaries in the UK are subject to supervision by the Financial Services Authority (FSA). The Group s banking subsidiary in New Zealand is subject to supervision by the Reserve Bank of New Zealand (RBNZ). In other offshore areas of banking and wealth management activity, the Group is subject to the operating requirements of relevant local regulatory authorities.

The local UK regulatory frameworks are broadly similar to those in force in Australia, which incorporate risk-based capital adequacy guidelines in accordance with the framework developed by the Basel Committee on Banking Supervision. The FSA also regulates the Group s UK wealth management operations, and is responsible for maintaining market confidence, promoting public awareness, protecting customers and reducing financial crime. The FSA has also introduced since October 2004, comprehensive frameworks addressing the provision of mortgage and general insurance.

In New Zealand, the emphasis of the RBNZ s regulatory approach is primarily on enhanced disclosure and directors attestations to key matters. Under conditions of registration, banks are required to comply with minimum prudential and capital adequacy requirements. The RBNZ monitors banks financial condition and conditions of registration, principally on the basis of published disclosure statements.

The Group s largest branch in the Asian region is in Hong Kong. The primary regulator in Hong Kong is the Hong Kong Monetary Authority, which is responsible for maintaining monetary and banking stability by regulating banking business and deposits and the supervision of authorised institutions.

In the US, branch operations are subject to supervision by the Office of the Comptroller of the Currency. The other key regulators of financial services are the Securities and Exchange Commission (SEC), the Board of Governors of the Federal Reserve System and the Office of Foreign Assets Control.

Changing regulatory environment

Both within the financial services industry and more generally, businesses are working within a changing regulatory environment. An outline of the more significant current or pending regulatory changes impacting the Group is set out in the following sections.

Anti-money laundering

Each of the major countries in which the bank operates are undertaking revisions to their Anti-Money Laundering and Counter Terrorist Financing law and regulation.

Australia has issued a draft bill which is going through the legislative process, which is due for completion in late 2006 or early 2007. The Australian Government has also published a new bill which has just entered the legislative process. The bill implements the revised Financial Action Task Force 40 recommendations. The Group has been actively working with peer banks and external stakeholders in the development of the draft bill and the attendant rules. The implementation of the requirements within the bill will update and revise the anti-money laundering activity undertaken by the bank s Australian business operations. The bank has initiated a change program and project to implement the requirements of the bill and rules within the business operations.

Revised requirements are being developed in New Zealand and are anticipated to proceed through the legislative process from late 2007.

The FSA in the UK have revised their approach to anti-money laundering and have updated the anti-money laundering Sourcebook, replacing it with high level provisions in the Senior Management Systems and Controls sourcebook and placing more onus on the Joint Money Laundering Steering Group (JMLSG) guidance. Her Majesty s Treasury approved the revised JMLSG guidance in February 2006. The revised guidance changes the way that the processes designed to detect money laundering and terrorist financing regulation are managed, enabling the UK financial services industry to take a sharper risk-based approach to anti-money laundering activity. The UK is also revising the Money Laundering Regulations in order to implement the requirements contained in the 3rd European Union (EU) Directive.

Basel II Capital Accord

In 1988, the Bank for International Settlements (BIS) developed the Basel Capital Accord that set out international benchmarks for assessing banks capital adequacy requirements. In response to changes in banking practices, BIS reviewed the Basel Capital Accord and released a revised regulatory framework known as the Revised Framework or Basel II. Amongst various objectives the Revised Framework seeks to encourage the development and use of more risk-sensitive capital calculations and to do so through greater use of risk assessments provided by banks own internal systems.

The new framework incorporates changes to the measurement of banks minimum regulatory capital requirements and additional identification of risk types. The framework is structured on:

- minimum capital requirements;
- key principles of supervisory review processes and banks internal capital assessment processes; and
- market discipline (public disclosure).

APRA has commenced releasing draft prudential standards in conformity with the Revised Framework which is expected to commence in Australia at the start of calendar year 2008.

Consistent with APRA requirements, the Group has submitted its first parallel run report for Basel II accreditation. This forms part of an accreditation process that will continue throughout calendar year 2007.

The Group continues to work with its key regulators in Australia and overseas to ensure that the Group s Basel II program aligns with regulatory requirements.

Payment system reforms in Australia

The RBA s reforms which significantly reduce interchange fees for EFTPOS Debit purchases and Visa Debit came into force on November 1, 2006.

Members of the Australian Payments Clearing Association and the RBA have finalised their access regime to allow new entrants to more easily connect to the EFTPOS bilateral network. These reforms have taken effect in September 2006.

UK *Consumer Credit Acts* 1974 and 2006

The provision of credit to personal consumers in the UK is currently regulated by the *Consumer Credit Act* 1974 (CCA). The CCA regulates all aspects of lending to consumers from advertising and documentation through to settlement and default procedures. Major revisions were made to the advertising and documentation regulations in 2004 and 2005. A new *Consumer Credit Act* 2006 (CCA) was passed earlier this year which supplements the 1974 Act.

The provisions of the new Act include:

- new requirements for account maintenance and dealing with default;
- additional scope for borrowers to challenge unfair lending; and
- the removal of the current GBP25,000 financial limit to bring most consumer lending with the scope of the Act.

Implementation is phased, with the majority of the changes taking place in 2008. A project is underway to assess the impact and implement the changes.