Impact of AIFRS on 31 December 2005 Profit Announcement Disclosure on Average Balances and Related Interest

Background

Due to the 1 July 2005 effective transition date for those AIFRS standards dealing with recognition, classification and measurement of financial instruments, many line items within the average balance sheet and related interest disclosure, as set out on page 77 to the Bank's 31 December 2005 Profit Announcement, are not comparable to the prior periods.

The purpose of this note is to outline and explain the major impacts AIFRS transition has had on the average balance and related interest disclosure. The quantifications below have been approximated.

Major AIFRS Impacts

The major AIFRS impacts affecting the half year ended 31 December 2005 are:

(1) Hedging - reclassification of accrued interest on hedge derivatives;
(2) Fair Valuation - reclassification of balances and related interest between interest earning asset and liability line items;
(3) Non-Hedged Derivatives -reclassification of interest expense on non-hedged derivatives to other banking income; and
(4) Hybrids - reclassification of hybrid instruments from Shareholders' Equity to Loan Capital.

Further explanation and quantification of the impact on each is set out below.

(1) Hedging - reclassification of accrued interest on hedge derivatives

Under previous Australian GAAP, the accrued interest on hedge derivatives was allocated to the underlying asset or liability being hedged. On transition to AIFRS, derivatives were designated within hedge relationships with different underlying assets or liabilities. This resulted in a reclassification of the related hedge interest to the new underlying item, principally being liabilities.

These reclassifications had the following impacts on interest income and expense:

Average Balance Sheet Line Item	Interest income	Interest expense
Business and corporate	Increase $80 million	n/a
Certificates of deposit	n/a	Increase $150 million
Debt issues	n/a	Reduce $130 million
Loan capital	n/a	Increase $60 million

The total impact on Net Interest Income of the above reclassifications was nil.

(2) Fair valuation - reclassification of balances and related interest between interest earning asset and liability line items

On application of those AIFRS standards relating to the fair valuation of financial instruments (AASB 132 and 139), some balances and their related interest were reclassified to new asset and liability categories. The principal reclassifications had the following effects on the average balances and related interest for the half year ended 31 December 2005:

Assets

- Business and corporate loans reduced by approximately $1.8 billion ($50 million related interest);
- Cash and other liquid assets reduced by approximately $1.1 billion (minimal related interest);
- Assets at fair value through profit and loss increased by approximately $2.3 billion ($50 million related interest); and
- Available-for-sale securities increased by approximately $600 million (minimal related interest).

Liabilities

- Certificates of deposit and other reduced by approximately $5 billion ($100 million related interest);
- Liabilities at fair value through profit and loss increased by approximately $15 billion ($260 million related interest); and
- Debt issues reduced by approximately $10 billion ($160 million related interest).

The total impact on Assets, Liabilities and Net Interest Income of the above reclassifications was nil.

(3) Non-hedged derivatives - reclassification of interest expense on non-hedged derivatives to other banking income

Under previous Australian GAAP, all interest accrued on derivatives used for hedging purposes was classified within net interest income.

On transition to AIFRS, only the interest related to derivatives that qualify for hedge accounting are included within net interest income. Interest accrued on non-hedged derivatives included within other banking income, similar to the treatment of trading derivatives.

In the half year ended 31 December 2005, this had the impact of reducing the interest expense on debt issues by $55 million, which was reclassified to Other Banking Income.

(4) Hybrids - reclassification of hybrid instruments from Shareholders' Equity to Loan Capital

On reclassification of certain hybrid financial instruments of the Bank (being PERLS, PERLS II and Trust Preferred Securities) from Shareholders' Equity to Loan Capital on 1 July 2005, the Loan capital average balance increased by approximately $2.2 billion, with related interest expense increasing by $57 million.