2012 RISK & CAPITAL REPORT

Incorporating the requirements of APS 330

Third Quarter Update
as at 30 June 2012

National Australia Bank

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1. Introduction

The Group, as defined in *Section 2. Scope of Application*, applies the Basel II framework as a cornerstone of its risk management framework and capital strategy, and recognises it is critical for achieving the Group's strategic agenda.

This report provides quarterly information on the following:

- Capital Adequacy - Risk-Weighted Assets (RWA) and Capital Ratios
- Credit Risk Exposures
- Credit Risk Provisions, Impaired and Past Due Facilities
- Charges for Specific Provisions and Write-offs
- Securitisation

In Australia, the Australian Prudential Regulation Authority (APRA) has regulatory responsibility for the implementation of Basel II through the release of prudential standards.

This Risk and Capital Report addresses the requirements of APRA's Pillar 3 public disclosure standard, *Prudential Standard APS 330 Capital Adequacy: Public Disclosure of Prudential Information* (APS 330) for the quarter ended 30 June 2012.

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

Capital Ratio Summary

The Group's Tier 1 capital ratio of 10.15% at 30 June 2012 is consistent with the Group's objective of maintaining a strong capital position.

	As at	
	30 Jun 12	31 Mar 12
Capital ratios	%	%
Level 2 Tier 1 capital ratio	10.15%	10.17%
Level 2 total capital ratio	11.49%	11.52%

1.1 The Group's Basel II Methodologies

National Australia Bank Limited and its controlled entities (the National Australia Bank Group) operate in Australia, Asia, New Zealand, the United Kingdom and North America. The following table sets out the approach to Basel II, which is applied across the Group as at 30 June 2012.

Basel II Approach	Credit Risk	Operational Risk	Non-Traded Market Risk	Traded Market Risk
National Australia Bank Limited	Advanced IRB	AMA	IRRBB	Standardised and IMA
Bank of New Zealand	Advanced IRB	AMA	IRRBB	Standardised and IMA
Clydesdale Bank PLC	Standardised	Standardised	IRRBB	n/a
Great Western Bank	Standardised	Standardised	IRRBB	n/a

IRB: Internal Ratings Based approach
AMA: Advanced Measurement Approach
IRRBB: Interest Rate Risk in the Banking Book
IMA: Internal Models Approach

Bank of New Zealand (BNZ) is regulated by the Reserve Bank of New Zealand (RBNZ). Credit risk exposures consolidated in the Group position are calculated under RBNZ requirements.

The National Australia Bank Group's subsidiary in the United Kingdom, Clydesdale Bank PLC, is regulated by the Financial Services Authority (FSA). Clydesdale Bank PLC has been accredited to apply the standardised approach to operational and credit risk management in accordance with the regulatory requirements. Credit risk exposures consolidated in this Report are calculated under APRA requirements.

Great Western Bank (GWB) is regulated in the United States of America by the South Dakota Division of Banking, the Federal Deposit Insurance Corporation and the Federal Reserve System.

GWB Credit Risk and Operational Risk risk weighted assets (RWA) are subject to APRA Basel II Standardised methodology. From 31 December 2011, IRRBB for GWB was calculated using the IRRBB internal model.

1.2 Disclosure Governance

The National Australia Bank Group's External Disclosure Policy defines Board and management accountabilities for APS 330 disclosure, including processes and practices to ensure the integrity and timeliness of prudential disclosures and compliance with National Australia Bank Group policies.

The National Australia Bank Group's Chief Executive Officer attests to the reliability of the Group's APS 330 disclosure within the annual declaration provided to APRA under Prudential Standard APS 310 Audit and Related Matters.

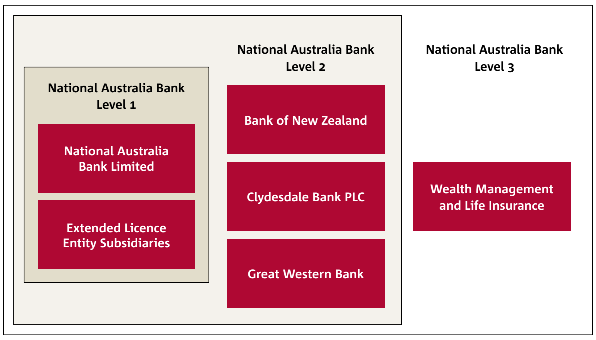
2. Scope of Application

APRA measures the National Australia Bank Group's capital adequacy by assessing financial strength at three levels:

- Level 1: comprises National Australia Bank Limited and its subsidiary entities approved by APRA as part of the Extended Licensed Entity (ELE);
- Level 2: comprises National Australia Bank Limited and the entities it controls, subject to certain exceptions set out below; and
- Level 3: comprises the Conglomerate Group.

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

National Australia Bank Group Consolidation



The controlled entities in the Group include the Bank of New Zealand, Clydesdale Bank PLC, Great Western Bank and other financial entities (e.g. finance companies and leasing companies).

Wealth management and life insurance are excluded from the calculation of Basel II RWA and the related controlled entities are deconsolidated from the National Australia Bank Group for the purposes of calculating capital adequacy. Capital adequacy deductions are applied to the investments in, and profits of, these activities.

In addition, certain securitisation special purpose vehicles (SPVs) to which assets have been transferred in accordance with APRA's requirements as set out in *Prudential Standard APS 120 Securitisation* (APS 120) have been deconsolidated from the National Australia Bank Group for the purposes of this disclosure. For regulatory purposes credit risk is removed from the sold assets and there is no requirement to hold capital against them.

3. Capital

Capital Adequacy [APS 330 Tables 16a – e]

The following table provides the Basel II RWA and capital ratios for the Group.

	As at	
	30 Jun 12	31 Mar 12
	RWA	RWA
	$m	$m
Credit risk [(1)]		
IRB approach		
Corporate (including SME)	107,697	109,312
Sovereign	1,462	1,290
Bank	8,528	8,179
Residential mortgage	58,207	56,351
Qualifying revolving retail	4,228	4,055
Retail SME [(2)]	7,546	7,318
Other retail	3,602	3,652
Total IRB approach	**191,270**	**190,157**
Specialised lending (SL) [(3)]	**50,517**	**45,439**
Standardised approach		
Australian and foreign governments	76	81
Bank	141	205
Residential mortgage	19,023	18,823
Corporate	29,663	29,979
Other	3,148	3,165
Total standardised approach	**52,051**	**52,253**
Other		
Securitisation	4,213	4,314
Equity	1,917	2,006
Other [(4)]	7,268	6,016
Total other	**13,398**	**12,336**
Total credit risk	**307,236**	**300,185**
Market risk	4,359	5,277
Operational risk	23,242	23,810
Interest rate risk in the banking book	4,858	6,281
Total risk-weighted assets	**339,695**	**335,553**

Capital ratios	**%**	**%**
Level 2 Tier 1 capital ratio	10.15%	10.17%
Level 2 total capital ratio	11.49%	11.52%

(1) *RWA which are calculated in accordance with APRA's requirements under Basel II are required to incorporate a scaling factor of 1.06 to assets that are not subject to specific risk weights.*

(2) *As at 30 June 2012, all Retail SME assets collateralised by Residential Mortgage, were applied the Residential Mortgage risk-weight function. The net impact of this change was an increase in RWA of $1,426 million.*

(3) *Further changes to the classification of the commercial property portfolio meeting the slotting criteria were made in the June 2012 quarter. This resulted in a reclassification of additional Corporate & Retail SME assets to Specialised Lending (Income Producing Real Estate). The net impact of this reclassification was an increase in RWA of $1,876 million.*

(4) *'Other' includes non-lending asset exposures that are not covered in the above categories. Non-lending assets are specifically excluded from credit risk exposures shown on pages 4 to 7 of this report.*

4. Credit Risk Exposures

Total and Average Credit Risk Exposures [APS 330 Table 17a]

This table provides the amount of gross credit risk exposure subject to the Standardised and Advanced IRB approaches. The Group has no credit risk exposures subject to the Foundation IRB approach. Gross credit risk exposure refers to the potential exposure as a result of a counterparty default prior to the application of credit risk mitigation. It is defined as the outstanding amount on drawn commitments plus a credit conversion factor on undrawn commitments on a given facility. For derivatives, the exposure is defined as the mark-to-market value plus a potential value of future movements. The average credit risk exposure is the sum of the gross credit risk exposure at the beginning of the reporting period plus the gross credit risk exposure at the end of the reporting period divided by two.

For the IRB approach, Exposure at Default (EaD) is reported gross of specific provisions and partial write-offs and prior to the application of on-balance sheet netting and credit risk mitigation. For the Standardised approach, EaD is reported net of any specific provision and prior to the application of on-balance sheet netting and credit risk mitigation. Exposures exclude non-lending assets, equities and securitisation.

	As at 30 Jun 12				3 months ended 30 Jun 12
	On-balance sheet exposure	Non-market related off-balance sheet	Market related off-balance sheet	Total exposure	Average total exposure
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
IRB approach					
Corporate (including SME)	115,522	47,609	36,242	**199,373**	**196,548**
Sovereign	34,582	607	9,968	**45,157**	**44,519**
Bank	33,567	776	43,481	**77,824**	**78,216**
Residential mortgage	238,506	36,775	-	**275,281**	**272,903**
Qualifying revolving retail	5,743	5,514	-	**11,257**	**11,179**
Retail SME	13,988	3,646	-	**17,634**	**18,423**
Other retail	3,345	1,232	-	**4,577**	**4,584**
Total IRB approach	**445,253**	**96,159**	**89,691**	**631,103**	**626,372**
Specialised lending (SL)	**51,015**	**7,651**	**2,050**	**60,716**	**57,523**
Standardised approach					
Australian and foreign governments	3,893	160	-	**4,053**	**4,151**
Bank	10,810	38	267	**11,115**	**10,388**
Residential mortgage	33,335	2,321	-	**35,656**	**35,309**
Corporate	26,144	3,523	453	**30,120**	**30,272**
Other	3,449	164	-	**3,613**	**3,630**
Total standardised approach	**77,631**	**6,206**	**720**	**84,557**	**83,750**
Total	**573,899**	**110,016**	**92,461**	**776,376**	**767,645**

	As at 31 Mar 12				6 months ended 31 Mar 12
	On-balance sheet exposure	Non-market related off-balance sheet	Market related off-balance sheet	Total exposure	Average total exposure
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
IRB approach					
Corporate (including SME)	117,718	45,742	30,263	**193,723**	**191,803**
Sovereign	28,033	693	15,156	**43,882**	**39,881**
Bank	31,549	935	46,123	**78,607**	**75,023**
Residential mortgage	233,896	36,629	-	**270,525**	**260,742**
Qualifying revolving retail	5,682	5,418	-	**11,100**	**11,039**
Retail SME	15,267	3,945	-	**19,212**	**19,434**
Other retail	3,376	1,215	-	**4,591**	**4,591**
Total IRB approach	**435,521**	**94,577**	**91,542**	**621,640**	**602,513**
Specialised lending (SL)	**45,865**	**6,959**	**1,506**	**54,330**	**51,868**
Standardised approach					
Australian and foreign governments	4,077	171	-	**4,248**	**4,330**
Bank	9,160	26	475	**9,661**	**10,084**
Residential mortgage	32,648	2,315	-	**34,963**	**40,248**
Corporate	26,269	3,732	423	**30,424**	**31,813**
Other	3,479	169	-	**3,648**	**3,872**
Total standardised approach	**75,633**	**6,413**	**898**	**82,944**	**90,347**
Total	**557,019**	**107,949**	**93,946**	**758,914**	**744,728**

5. Credit Provisions and Losses

Credit Risk Provisions [APS 330 Table 17b – c]

The following tables set out information on credit risk provision by Basel II asset class, excluding non-lending assets, equities and securitisation exposures. Definitions of impairment and past due facilities are based on APS 220 Credit Quality and related guidance notes or return instructions. The determination of specific provisions is in accordance with APRA Guidance Note AGN 220.2: Impairment, Provisioning and the General Reserve for Credit Losses.

	As at 30 Jun 12			3 months ended 30 Jun 12	
	Impaired facilities (1)	Past due facilities ≥90 days	Specific provisions (2)	Charges for specific provisions (3)	Net Write-offs
Exposure type	**$m**	**$m**	**$m**	**$m**	**$m**
IRB approach					
Corporate (including SME)	2,044	297	698	133	90
Sovereign	-	-	-	-	-
Bank	11	-	11	(20)	-
Residential mortgage	718	1,261	171	44	31
Qualifying revolving retail	-	64	-	44	52
Retail SME	174	120	92	23	26
Other retail	14	47	5	31	24
Total IRB approach	**2,961**	**1,789**	**977**	**255**	**223**
Specialised lending (SL)	**1,381**	**188**	**334**	**115**	**42**
Standardised approach					
Australian and foreign governments (4)	-	21	-	-	-
Bank	-	-	-	-	-
Residential mortgage	111	121	24	7	5
Corporate	1,683	293	441	183	125
Other	9	27	4	1	2
Total standardised approach	**1,803**	**462**	**469**	**191**	**132**
Total	**6,145**	**2,439**	**1,780**	**561**	**397**
Additional regulatory specific provisions (2)			545		
General reserve for credit losses (5)			2,661		

(1) *Impaired facilities includes $226 million of restructured loans (March 2012: $235 million), which includes $1 million of restructured fair value assets (March 2012: $nil million).*

Impaired facilities includes $245 million of gross impaired fair value assets (March 2012: $174 million).

(2) *Specific provisions for prudential purposes include all provisions for impairment assessed on an individual basis in accordance with IFRS excluding securitisation. All collective provisions on defaulted or otherwise non-performing assets, regardless of expected loss, such as those for 90+ days past due retail and in default with no loss non-retail exposures, have been reported as additional regulatory specific provisions and shown in this report as a separate item.*

Specific provisions includes $104 million (March 2012: $82 million) of specific provisions on gross impaired fair value assets.

(3) *Charges for specific provisions include loans accounted for at fair value. In the March 2012 half year results, $29 million of charges relating to fair value loans were excluded.*

The year to date total of charges for specific provisions is $1,839 million.

(4) *Past due facilities ≥ 90 days includes amounts relating to the acquisition of certain assets of TierOne Bank in June 2010. These amounts are reported gross of the FDIC loss sharing agreement, where the FDIC absorbs 80% of the credit losses arising on the majority of the acquired loan portfolio.*

(5) *The General Reserve for Credit Losses (GRCL) at 30 June 2012 is calculated as follows:*

	$m
Collective provision for doubtful debts	*3,080*
Less collective provisions reported as additional regulatory specific provisions	*(545)*
Collective provision for doubtful debts eligible for inclusion in a general reserve for credit losses (pre-tax basis)	*2,535*
Less tax effect	*(562)*
Collective provision for doubtful debts eligible for inclusion in a general reserve for credit losses (after-tax basis)	*1,973*
Plus reserve created through a deduction from retained earnings	*688*
General reserve for credit losses (after-tax basis)	*2,661*

Exposure type	As at 31 Mar 12 Impaired facilities $m	Past due facilities ≥90 days $m	Specific provisions $m	6 months ended 31 Mar 12 Charges for specific provisions $m	Net Write-offs $m
IRB approach					
Corporate (including SME)	2,163	332	667	484	490
Sovereign	-	-	-	-	-
Bank	35	-	34	-	-
Residential mortgage	669	1,226	161	60	53
Qualifying revolving retail	-	68	-	93	96
Retail SME	179	129	92	37	35
Other retail	12	47	3	45	47
Total IRB approach	**3,058**	**1,802**	**957**	**719**	**721**
Specialised lending (SL)	**1,352**	**118**	**249**	**95**	**133**
Standardised approach					
Australian and foreign governments	-	23	-	-	-
Bank	-	-	-	-	-
Residential mortgage	100	134	22	7	14
Corporate	1,565	269	398	381	240
Other	9	27	4	47	47
Total standardised approach	**1,674**	**453**	**424**	**435**	**301**
Total	**6,084**	**2,373**	**1,630**	**1,249**	**1,155**

Additional regulatory specific provisions	513
General reserve for credit losses (1)	2,694

(1) *The General Reserve for Credit Losses (GRCL) at 31 March 2012 is calculated as follows:*

	$m
Collective provision for doubtful debts	*3,058*
Less collective provisions reported as additional regulatory specific provisions	*(513)*
Collective provision for doubtful debts eligible for inclusion in a general reserve for credit losses (pre-tax basis)	*2,545*
Less tax effect	*(561)*
Collective provision for doubtful debts eligible for inclusion in a general reserve for credit losses (after-tax basis)	*1,984*
Plus reserve created through a deduction from retained earnings	*710*
General reserve for credit losses (after-tax basis)	*2,694*

6. Securitisation

Securitisation Exposures [APS 330 Table 18b]

The following two tables provide information about assets that the Group manages as securitisations (predominantly for third party clients) where the exposures are risk weighted under APS 120. These tables do not provide information on Group assets that have been sold to securitisations whether or not the assets are risk weighted under APS 120. The table below breaks down the securitisation exposures by type of facility as defined in the Glossary.

	As at 30 Jun 12			As at 31 Mar 12		
	On-balance sheet $m	Off-balance sheet $m	Total $m	On-balance sheet $m	Off-balance sheet $m	Total $m
Securitisation exposure type						
Liquidity facilities	11	2,607	**2,618**	23	1,944	**1,967**
Warehouse facilities	9,079	1,519	**10,598**	9,952	1,002	**10,954**
Credit enhancements	7	34	**41**	12	56	**68**
Derivative transactions	180	-	**180**	236	-	**236**
Securities	310	-	**310**	32	-	**32**
Credit derivatives transactions	-	-	**-**	-	-	**-**
Other	3,959	-	**3,959**	3,764	-	**3,764**
Total securitisation exposures	**13,546**	**4,160**	**17,706**	**14,019**	**3,002**	**17,021**

Recent 3rd Party Securitisation Activity [APS 330 Table 18a]

This table provides information about new securitisation facilities provided in the six months to reporting date.

	Notional amount of facilities provided	
	6 months ended 30 Jun 12 $m	6 months ended 31 Mar 12 $m
Securitisation exposure type		
Liquidity facilities	729	23
Warehouse facilities	-	815
Credit enhancements	-	66
Derivative transactions	48	104
Securities	244	-
Credit derivatives transactions	-	-
Other	355	932
Total new facilities provided	**1,376**	**1,940**

Recent Group Own Securitisation Activity [APS 330 Table 18a]

This table may include assets which are sold to SPVs (1) which issue securities which meet the Reserve Bank of Australia's repurchase eligibility criteria; (2) which otherwise do not result in significant risk transfer and are considered on-balance sheet for regulatory purposes; or (3) in which significant risk transfer has taken place and which are considered off-balance sheet for regulatory purposes. The Group may retain an exposure to securitisation SPVs which are considered off-balance sheet for regulatory purposes.

	6 months ended 30 Jun 12			6 months ended 31 Mar 12		
	Amount securitised during period directly originated $m	Amount securitised during period indirectly originated $m	Recognised gain or loss on sale $m	Amount securitised during period directly originated $m	Amount securitised during period indirectly originated $m	Recognised gain or loss on sale $m
Underlying asset						
Residential mortgage	2,856	-	-	2,857	-	-
Credit cards	-	-	-	-	-	-
Auto and equipment finance	-	-	-	-	-	-
Commercial loans	-	-	-	-	-	-
Other	-	-	-	-	-	-
Total underlying asset	**2,856**	**-**	**-**	**2,857**	**-**	**-**

7. Glossary

Term	Description
ADI	Authorised Deposit-taking Institution
Advanced IRB approach	The Advanced Internal Ratings Based (IRB) approach refers to the processes employed by the Group to estimate credit risk. This is achieved through the use of internally developed models to assess potential credit losses using the outputs from the PD, LGD and EaD models.
APRA	The Australian Prudential Regulation Authority
AMA	Advanced Measurement Approach (AMA) is the risk estimation process used for the Group's operational risk. It combines internally developed risk estimation processes with an integrated risk management process, embedded within the business with loss event management.
Company	National Australia Bank Limited ABN 12 004 044 937.
Capital adequacy	Capital adequacy is the outcome of identifying and quantifying the major risks the Group is exposed to, and the capital that the Group determines as an appropriate level to hold for these risks, as well as its strategic and operational objectives, including its target credit rating.
Credit derivative transactions	In relation to securitisation exposures, credit derivative transactions are those in which the credit risk of a pool of assets is transferred to the Group, usually through the use of credit default swaps.
Credit enhancements	Credit enhancements are arrangements in which the Group holds a securitisation exposure that is able to absorb losses in the pool, providing credit protection to investors or other parties to the securitisation. A first loss credit enhancement is available to absorb losses in the first instance. A second loss credit enhancement is available to absorb losses after first loss credit enhancements have been exhausted.
Derivative transactions	In relation to securitisation exposures, derivative transactions include interest rate and currency derivatives provided to securitisation SPVs, but do not include credit derivative transactions.
EaD	Exposure at Default (EaD) is an estimate of the total committed credit exposure expected to be drawn at the time of default for a customer or facility that the Group would incur in the event of a default. It is used in the calculation of RWA
ELE	The Extended License Entity (ELE) comprises the ADI itself and any APRA approved subsidiary entities assessed as effectively part of a single 'stand-alone' entity, as defined in *APS 110.*
Foundation IRB	Foundation Internal Ratings Based (FIRB) approach refers to an alternative approach to Advanced IRB for non-retail credit risk defined under Basel II where a Group develops its own PD models and seeks approval from its regulator to use these in the calculation of regulatory capital, and the regulator provides a supervisory estimate for LGD and EaD.
Group	The Level 2 Group, being the Company and the entities it controls subject to certain exceptions set out in *Section 2 Scope of Application*.
IAA	Internal Assessment Approach.
IFRS	International Financial Reporting Standards
Impaired facilities	Impaired facilities consist of Retail loans (excluding unsecured portfolio-managed facilities) which are contractually 90 days or more past due with security insufficient to cover principal and arrears of interest revenue. Unsecured portfolio managed facilities are classified as impaired assets when they become 180 days past due (if not written off) as per ARF 220 instructions; Non-retail loans that are contractually 90 days or more past due and/or sufficient doubt exists about the ultimate ability to collect principal and interest; and Impaired off-balance sheet credit exposures, where current circumstances indicate that losses may be incurred.
IPRE	Income Producing Real Estate
IRB	Internal Ratings Based (IRB) describes the approach used in the assessment of credit risk. Within this document it is used interchangeably with the term advanced Internal Ratings Based approach. This reflects the Group's development of internal credit risk estimation models covering both retail and non-retail credit.
IRRBB	Interest rate risk in the banking book
LGD	Loss Given Default (LGD) is an estimate of the expected severity of loss for a credit exposure following a default event. Regulatory LGDs reflect a stressed economic condition at the time of default. It is used in the calculation of RWA.
Liquidity facilities	Liquidity facilities are provided by the Group to an SPV for the primary purpose of funding any timing mismatches between receipts of funds on underlying exposures and payments on securities issued by the SPV (asset liquidity facilities), or to cover the inability of the SPV to roll over ABCP (standby liquidity facilities).
National Australia Bank Group	National Australia Bank Limited and its consolidated entities.
Net write-offs	Write-offs on loans at amortised cost net of recoveries.
Past due facilities ≥ 90 days	Past due facilities ≥ 90 days consist of well-secured assets that are more than 90 days past due and portfolio-managed facilities that are not well secured and between 90 and 180 days past due.
PD	Probability of Default (PD) is an estimate of the likelihood of a customer defaulting or not repaying their borrowings and other obligations to the Group within the next 12 months.
RWA	Risk-Weighted Assets
Securities	Securities include the purchase of securitisation debt securities for either trading or banking book purposes.
SME	Small and medium-sized entities
Specific provisions	Specific provisions for prudential purposes include all provisions for impairment assessed on an individual basis in accordance with IFRS excluding securitisation; all collective provisions on defaulted or otherwise non-performing assets, regardless of expected loss, are reported as additional regulatory specific provisions.
Standardised approach	Standardised refers to an alternative approach to the assessment of risk (notably credit and operational) whereby the institution uses external rating agencies to assist in assessing credit risk and/or the application of specific values provided by regulators to determine RWA.
Tier 1 capital ratio	Tier 1 regulatory capital, as defined by APRA, divided by RWA.
Tier 2 capital	Tier 2 capital includes other components of capital that, to varying degrees, fall short of the quality of Tier 1 capital but nonetheless contribute to the overall strength of an entity as a going concern. It is divided into: Upper Tier 2 capital comprising components of capital that are essentially permanent in nature, including some forms of hybrid capital instrument; and Lower Tier 2 capital comprising components of capital that are not permanent.
Warehouse facilities	Warehouse facilities are lending facilities provided by the Group to an SPV for the financing of exposures in a pool. These may be on a temporary basis pending the issue of securities or on an on-going basis.
Write-offs	Write-offs represent credit losses in accordance with accounting rules.

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