Public version

Application by ANZ Banking Group New Zealand Limited
for clearance of a proposed business acquisition

13 August 2003

Public version

COMMERCE ACT 1986: BUSINESS ACQUISITION
SECTION 66: NOTICE SEEKING CLEARANCE

Date: 13 August 2003

The Registrar
Business Acquisitions and Authorisations
Commerce Commission
PO Box 2351
WELLINGTON

Pursuant to s66(1) of the Commerce Act 1986 notice is hereby given seeking clearance of a proposed business acquisition.

Contents

Executive Summary

Executive Summary

Introduction

ANZ Banking Group (New Zealand) Limited (**ANZ**) or a related company nominated by ANZ is seeking clearance for the acquisition of NBNZ Holdings Limited, the New Zealand holding company of The National Bank of New Zealand Limited and its controlled subsidiaries (**National**), from its parent, Lloyds TSB Bank plc.

ANZ is New Zealand's oldest bank (its presence in New Zealand dating back to 1840 when its predecessor, the Union Bank of Australia, became the first bank in New Zealand). In 1989 ANZ bought PostBank from the New Zealand government. Today, more than one million New Zealanders bank with ANZ and it has a Standard and Poor's long term rating of AA-.

In the last 16 years National has become a leading full service bank. During that time National merged with Southpac Investment Management Limited (1987), acquired The Rural Bank Limited from Fletcher Challenge (1992) and acquired Countrywide Banking Corporation from Bank of Scotland (1998). National has also continued to grow organically in recent years.

ANZ sees this acquisition as an opportunity for it to continue to enhance its ongoing drive to improve its performance and business in New Zealand.

A dynamic industry

The New Zealand banking and finance industry continues to achieve significant growth in lending assets and strong profit performance. At the same time, the industry is highly competitive and dynamic. This is illustrated by the large number of existing competitors (both banks and non banks), the entry of new competitors (most recently Kiwibank, Superbank and GE Capital), the emergence of new competitors utilising existing competitors' systems (such as Kiwibank's arrangements with Westpac), declining interest rate margins and the tight range of interest rates and charges as between the competitors.

As well as the change that has occurred in the number and identity of competitors, there have been a number of other significant changes. The introduction of new technology has seen a change in customers' behaviour and preferences. Over the last five years the use of ATMs, EFTPOS, internet and telephone banking has increased dramatically. Correspondingly, customers' use of over-the-counter transactions in branches has declined substantially. Banks have responded to the changing customer preferences by increasing the functionality of the electronic services available and reducing the number of branches. Data showing these trends is included in Appendix 1. In addition, customers have increasingly been prepared to purchase individual products from banks and other financial providers. Banks have responded by ensuring that individual products are competitive in their own right.

ANZ considers that its acquisition of National will not affect the highly competitive and dynamic nature of this industry. Post acquisition ANZ will continue to be constrained by existing competitors, near and new entrants and the countervailing power of purchasers.

A summary of the reasons for this conclusion is set out below. ANZ's application then follows.

No substantial lessening of competition

Existing competition

The banking markets relevant to this acquisition are highly competitive. There are five major banks operating in New Zealand (Westpac, National, BNZ, ANZ and ASB). In addition to these major providers, a number of other competitors (both banks and non banks) operate in each market. For example, international investment banks and financiers operate in the institutional and corporate markets, there are over 20 other providers (including finance companies, building societies and credit unions) in the mortgage market, there are over 10 other providers (e.g. Rabobank) operating in the rural market, and there are over 30 providers (including Kiwibank and SuperBank) in the savings account market.

While in some markets ANZ's market share post acquisition will fall outside the Commission's safe harbour guidelines, the proposed acquisition will not affect competition in any of the markets. Existing competitors alone will ensure prices and quality of service remain competitive. Barriers to expansion are low. Existing competitors have substitutable products and strong brands. The ability of competitors to increase supply is limited only by demand. Customers are driven by price and service. Switching costs (such as application fees and charges) in each of the relevant markets are low. The lack of material barriers to expansion in the various markets is evidenced by, amongst others, ASB's national expansion strategy, and Rabobank's expansion in the rural market.

In addition, the proposed acquisition will not increase the risk of coordinated behaviour in the relevant markets. As well as the above factors, there are differences between existing competitors (e.g. cost structures and strategies) and "fringe" competitors are active.

Potential competition

To enter the relevant markets a provider must meet certain capital and regulatory requirements, incur set up costs and establish a reputation and brand. New Zealand has relatively low regulatory barriers to entry. In addition, the need for a branch network has diminished by the existence and use of alternative distribution channels, the ability to use other major retail outlets, and the increasing use of electronic (non cash and non cheque) mediums. Evidence of the lack of barriers to entry in the various markets is evidenced by, amongst other things, the entry of the Commonwealth Bank of Australia (**CBA**) into the institutional market, the entry of Rabobank into the rural market, GE Capital's entry and expansion into the small to medium business market and the entry of Kiwibank and Superbank into the retail markets.

ANZ considers that existing competitors will respond if ANZ post acquisition were to increase price (charges or lending interest rates) above competitive levels or decrease quality of service. However, because barriers to entry are also low, potential new entrants will also provide a real constraint on ANZ post acquisition.

Acquirers

Acquirers of banking products in the high value transaction markets are sophisticated, well informed and highly price sensitive. This, combined with the opportunities presented by existing competitors, and the low switching costs, means that acquirers in these markets will continue to constrain ANZ post acquisition.

In the retail markets, acquirers have access to a formal complaint procedure and good, reliable information about banking products. They are price focused and well informed about alternative sources of supply and switching opportunities. They also have access to a high number of substitutable products. These factors will continue to act as a real constraint on ANZ post acquisition. If ANZ (post acquisition) were to increase its charges or lending interest rates above competitive levels, consumers would switch to an alternative supplier.

Conclusion

The proposed acquisition by ANZ will not result in a substantial lessening of competition in any of the relevant markets (or breach section 47 of the Commerce Act). Post acquisition, ANZ will continue to be constrained by existing competitors, near and new entrants and acquirers.

PART I: THE TRANSACTION DETAILS

The business acquisition

1. The business acquisition for which the clearance is sought

1. The business acquisition for which clearance is sought is the acquisition by ANZ or a related company nominated by ANZ of all the shares in and assets of National from its parent, Lloyds TSB Bank plc.

The person giving notice

2. Who is the person giving this notice?

2. The person giving notice is ANZ (or a related company nominated by ANZ).

Level 15
ANZ Tower
215-229 Lambton Quay
Wellington

Attention: Susan Peterson
General Counsel

Contact (in the first instance):

Bell Gully: Phil Taylor (09) 916 8940
Jill Mallon (04) 915 6831

Confidentiality

3. Do you wish to request a confidentiality order for:

3.1 The fact of the proposed acquisition?

3. No.

3.2 Specific information contained in or attached to the notice?

4. Yes. Confidentiality is sought in respect of all items included in square brackets (**confidential information**). Confidentiality is sought indefinitely or until ANZ advises the Commission that it can make disclosure of those details.

5. A confidentiality order is sought in respect of the confidential information under section 100 of the Commerce Act 1986 (the **Act**). Confidentiality is also claimed under section 9(2)(b)(ii) of the Official Information Act 1982 on the grounds that:

   (a) the information is commercially sensitive and valuable and is confidential to the participants; and

   (b) disclosure of it is likely to give unfair advantage to competitors of the participants and/or to unreasonably prejudice the commercial position of the persons involved.

6. ANZ also requests that it is notified of any request made to the Commission under the Official Information Act for the confidential information, and that the Commission seeks ANZ's views as to whether the information remains confidential and commercially sensitive at the time those requests are being considered.

Details of the participants

4. Who are the participants (i.e. the parties involved)?

7. The acquirer is ANZ (or a related company nominated by ANZ).

   Level 15
   ANZ Tower
   215-229 Lambton Quay
   Wellington

   Telephone: 04 496 8434
   Facsimile: 04 496 8872

   Attention: Susan Peterson
   General Counsel

   ANZ was incorporated under the Companies Act 1955 on 23 October 1979, by virtue of the ANZ Banking Group (New Zealand) Act 1979. It was re-registered under the Companies Act 1993 on 13 June 1997.

8. National's assets are being sold by Lloyd's TSB plc. All queries regarding the sale of National's assets and shares should be directed to:

   Chapman Tripp
   1-13 Grey Street
   Wellington

   Telephone: (04) 499 5999
   Facsimile: (04) 472 7111

   Attention: Grant David

   National was originally incorporated in England on 14 August 1872. National began trading in New Zealand in 1873 and was incorporated in New Zealand under The National Bank of New Zealand (Limited) Act 1873. Pursuant to the National Bank of New Zealand Act 1985, National was deemed to be incorporated under the Companies Act 1955 on 19 June 1985.

It ceased to be incorporated in the United Kingdom in 1985. National was re-registered under the Companies Act 1993 on 20 December 1995.

5. Who is interconnected or associated with each participant?

ANZ

9. The immediate parent company of ANZ is ANZ Holdings (New Zealand) Limited (incorporated in New Zealand). That company is wholly owned by ANZ Funds Pty Limited (incorporated in Australia). The ultimate parent company is Australia and New Zealand Banking Group Limited, which is incorporated in Australia. Its registered office is Level 6, 100 Queen St, Melbourne. A diagram showing the structure of the group in New Zealand is attached as Appendix 2.

10. ANZ has a number of subsidiaries in New Zealand. For example, UDC Finance Limited is a wholly owned subsidiary of ANZ that specialises in asset financing, and in particular, vehicle and equipment financing and leasing.

11. ANZ also has relevant interests in the following companies:

    (a) EFTPOS New Zealand Limited (**ENZ**) (ANZ's agent for its merchant acquiring business (supply of terminals and processing systems to merchants)) - 100%;

    (b) Interchange & Settlement Limited (**ISL**) (which operates the major retail payment processing system) – 13%; and

    (c) Visa New Zealand Limited (**VNZL**) (which grants access to the Visa network in New Zealand) – 16%.

12. A description of these companies is set out below in response to question 7.

The National Group

13. National is a wholly owned subsidiary of Lloyds TSB Bank plc. The ultimate parent company is Lloyds TSB Group plc. A diagram showing the structure of the group in New Zealand is attached as Appendix 3.

14. Appendix 3 shows National's 25% interest in Electronic Transaction Services Limited (**ETSL**). ETSL is the alternative system for the interchange and clearance of EFTPOS and credit card transactions. It is owned in equal shares by National, ASB, Westpac and BNZ. Further details on ETSL (and ANZ's alternative EFTPOS system) are set out below at paragraphs 25 to 27.

6. Does a participant, or any interconnected body corporate thereof, already have a beneficial interest in or is beneficially entitled to, any shares or other pecuniary interest in another participant?

15. To the best of ANZ's knowledge, neither ANZ, National nor any of their related companies currently have a beneficial interest in, or are beneficially entitled to, any shares or other pecuniary interest in each other.

7. Identify any links, formal or informal, between any participant/s including any interconnected bodies corporate and other persons identified above and its/ their existing competitors in each market

16. ANZ and National each hold shares in ISL and VNZL. Details of these shareholdings are set out below. The proposed acquisition will not increase ANZ's market power in respect of either of these facilities (see paragraphs 17-23 and 190-193 below).

ISL

17. ISL operates the major retail payment processing system in New Zealand. The system is used to interchange cheques, direct debits, direct credits, automatic payments, ATM transactions, telephone banking transactions, and off-site electronic banking transactions. ISL has been in operation since the mid-1960s.

18. ISL is owned collectively by 9 registered banks in New Zealand. Respective shareholdings are:

Company	***Shareholding***
ANZ	12.7%
BNZ	12.7%
National	12.7%
Westpac	12.7%
ASB	10.7%
Citibank	10.7%
HSBC	10.7%
TSB	10.0%
Deutsche	7.3%
TOTAL	**100%**

19. Participation in ISL's system is governed by, but not limited to, ISL's owners. The owners set the rules governing the operation of the clearing house including transaction pricing. At present, providers are required to be registered banks. However:

(a) non bank financial institutions have agency arrangements in place with participant banks. For example, the PSIS has an agency arrangement with Westpac through which PSIS transactions are settled via the ISL system; and

(b) some non bank financial institutions have a user licence agreement with ISL, which gives them the right to settle payments via the ISL system in return for the payment of a fee. NZ Post Financial Services Limited (on behalf of Kiwibank) is the only company at the present time with such an agreement.

VNZL

20. Both ANZ and National are members of Visa International. Members of Visa International are entitled to solicit prospective cardholders and issue Visa and Bankcard credit cards, extend credit to cardholders through the use of those credit cards, solicit and sign up merchants who agree to honour those credit cards, and interchange drafts, contracts and other instruments arising from the use of the cards.

21. Last year, Visa International reviewed the manner in which it granted access to the Visa network and payment system in New Zealand. Instead of granting membership to each card issuing agency, VNZL was incorporated as a joint venture vehicle to provide shareholders with access to the system.

22. VNZL's Board has a discretion to issue shares to any applicant that agrees to accept the obligations of being a shareholder and would otherwise be eligible for direct membership in Visa International. Shares may be issued in any of the following classes, which correspond to the categories of membership within Visa International:

    (a) ***Principal shares***: Principal shareholders have full rights to solicit prospective cardholders and issue Visa cards bearing the name of the shareholder, and to extend credit to cardholders through the use of Visa cards, solicit and sign up merchants who agree to honour Visa cards, and interchange drafts, contracts and other instruments arising from the use of the cards.

    (b) ***Associate shares***: Associate shareholders must be sponsored by a Principal shareholder. Associate shareholders have the same rights as a Principal shareholder, except Associate shareholders do not have the right to sponsor further Associate shareholders.

    (c) ***Card Issuing shares***: Card Issuing shareholders have the same rights as a Principal shareholder except they do not have the rights to solicit and sign up merchants and to sponsor Associate shareholders.

    (d) ***Participant shares***: Participant shareholders must be sponsored by a Principal shareholder, Associate shareholder or Card Holding shareholder. Participant shareholders may not enter into direct contractual relationships with persons for the issuance of cards or with prospective merchants, must not issue cards in their own name, and have no direct right to interchange drafts, contracts or other instruments arising through the use of cards.

    (e) ***Cheque Issuing shares***: Cheque Issuing shareholders are entitled to issue, sell, honour, cash and refund traveller's cheques bearing the Traveller's Cheque Plan marks and may appoint in writing shareholders and others to sell, refund and cash such traveller's cheques.

    (f) ***Plus shares***: Plus shareholders are entitled to issue debit cards bearing the Plus Plan marks, which can be used with their corresponding PINs at electronic cash dispensing devices displaying the Plus Plan mark.

23. Current shareholdings in VNZL are:

Company	***Shareholding***
ANZ	1 Principal share 1 Plus share
BNZ	1 Principal share 1 Plus share 1 Cheque Issuing share
National	1 Principal share 1 Plus share
Westpac	1 Principal share 1 Plus share
ASB	1 Principal share 1 Plus share
HSBC	1 Plus share
TSB	1 Associate share
TOTAL	**13 shares**

MasterCard International

24. Both ANZ and National are members of MasterCard International. Members of MasterCard International are entitled to solicit prospective cardholders and issue MasterCard credit cards, extend credit to cardholders through the use of MasterCard credit cards, solicit and sign up merchants who agree to honour MasterCard credit cards, and interchange drafts, contracts and other instruments arising from the use of the cards. In addition, members have access to the Maestro debit card, MasterCard Electronic and Cirrus ATM cash access programs.

EFTPOS and Credit Card Payment Services

25. As referred to above, there are two systems available in New Zealand for the interchange and clearance of EFTPOS and credit card transactions: the ETSL system and ANZ's system.

26. All EFTPOS and credit card transactions generated through a merchant are "switched" through either the ANZ switch or the ETSL switch in order to reach the cardholder's account. The system used is determined by the relationship that the merchant has established. For example, if a National customer makes a purchase from a merchant who uses ANZ's system, the transaction will be switched through the ANZ switch directly to National for authorisation (this is the primary authorisation route). In the event that ANZ cannot reach National due to systems or communications issues, ANZ can alternately route the transaction through the ETSL system (this is the secondary authorisation route).

27. ANZ has a number of agreements in place governing this debit card authorisation process:

    (a) ANZ has an agreement with ETSL whereby ANZ pays a debit interchange fee of 6.75 cents to ETSL for all ANZ issued debit card transactions switched through the ETSL system to ANZ for authorisation; and

    (b) ANZ has an agreement with each of the other New Zealand banks whereby each bank pays a debit interchange fee of 6.75 cents to ANZ for that bank's debit card transactions which are switched through the ANZ system for authorisation by that bank.

28. In respect of credit card interchange, the agreements are between each bank and the card issuer with no direct arrangement between the banks. i.e. the card issuer (e.g. American Express, Diners Club) deducts interchange from each acquiring bank transaction and then separately pays an amount of interchange to the issuing bank for each transaction.

Other

29. ANZ and National are parties to syndicated loans and shared security arrangements as part of their normal business banking services. Each bank maintains a direct relationship with its customers and takes its own view on matters of credit, pricing and marketing.

8. Do any directors of the acquirer also hold directorships in any other companies which are involved in the markets in which the target company / business operates?

30. ANZ's directors hold the following offices in addition to their directorships in ANZ Banking Group (New Zealand) Limited:

Name of Director	*Company / entity*	*Position*
Dr R S Deane Independent chairman	Telecom Corporation of New Zealand Limited	Chairman and Director
	Australia and New Zealand Banking Group Limited (Australia)	Director
	Fletcher Building Limited	Chairman and Director
	Fletcher Building Finance Limited	Director
	Cordyline Limited	Director
	New Zealand Seed Management Fund Limited	Chairman and Director
	New Zealand Seed Fund Partnership Limited	Chairman and Director
	Totara Holdings Nominees Limited	Director

Name of Director	***Company / entity***	***Position***
	IHC Mortgages Limited	Director
	Woolworths Ltd	Director
	TransAlta Corporation (Canada)	Director
	IHC NZ Inc	Patron Member, Board of Governance
Mr J G Todd Independent director	Dynasty Hotel Group Limited	Director
	Southern Cross Benefits Limited	Director
	Southern Cross Healthcare Nominees Limited	Director
	Sanford Limited	Director
	GMV Associates Limited	Director
	Aetna Health (NZ) Limited	Director
	The New Zealand Guardian Trust Company	Director
Hon F H Wilde Independent director	The New Zealand Way Limited	Director
	Wellington Waterfront Limited	Chairman and Director
	Southern Cross Healthcare Nominees Limited	Director
	Fran Wilde & Associates Limited	Director
	Ceanic Limited	Director
Mr P J O Hawkins Executive director	ANZ Insage Pty Limited (Australia)	Director
	Esanda Finance Corporation Limited (Australia)	Director
	ANZ General Insurance Pty Limited (Australia)	Director
	ING Australia Limited (Australia)	Director
	ING Custodians Pty Limited (Australia)	Director

Name of Director	*Company / entity*	*Position*
	ING Life Limited (Australia)	Director
	ANZ Life Assurance Company Limited (Australia)	Director
	ANZ Managed Investments Limited (Australia)	Director
	Optimix Investment Management Limited (Australia)	Director
	ING Investment Services Limited	Director
	ING (NZ) Limited	Director
Mr D L Boyles Executive director	ANZ Information Technology Pvt Limited	Director
Mr P C McMahon Executive director	ANZ Insage Pty Limited (Australia)	Director
	Esanda Finance Corporation Limited (Australia)	Director
	ANZ General Insurance Pty Limited (Australia)	Director
	ING Australia Limited (Australia)	Director
	ING Custodians Pty Limited (Australia)	Director
	ING Life Limited (Australia)	Director
	ANZ Life Assurance Company Limited (Australia)	Director
	ANZ Managed Investments Limited (Australia)	Director
	Optimix Investment Management Limited (Australia)	Director
	ING Investment Services Limited	Director
	ING (NZ) Limited	Director
Mr G J Camm	UDC Finance Limited	Director

Name of Director	*Company / entity*	*Position*
Managing director	EFTPOS New Zealand Limited	Director
	ANZ Holdings (New Zealand) Limited	Director
	ANZ Investment Services (New Zealand) Limited	Director
	ANZ Lenders Mortgage Insurance Pty Limited (Australia)	Director
	NMRSB Pty Limited (Australia)	Director

9. What are the business activities of each participant?

31. Both ANZ and National provide financial products and services in New Zealand. As at 31 December 2002, National was New Zealand's second largest bank with total assets of \$38.9 billion and ANZ was New Zealand's fourth largest bank with total assets of NZ\$28 billion.

32. Key business areas are:

(a) ***Personal Banking***: providing banking products and services to personal (retail) customers through branch networks and direct sales and service channels (such as internet banking and telephone banking). Both ANZ and National have specialised personal banking divisions for high value personal customers. The core business of the personal banking sector is the provision of traditional banking products and related financial services, such as:

- current and savings accounts;
- term deposits;
- personal loans;
- home loans;
- general insurance;
- term life insurance; and
- managed funds.

(b) ***Consumer Finance***: providing Visa, MasterCard and other credit card services to personal customers and business card products to business customers.

(c) ***Business Banking***: providing business banking products and services to small sized enterprises and owner-managed businesses with turnover of up to \$5 million (National) and \$10 million (ANZ)[1]. Business banking products include transactional

[1] Internally, each bank may define its products and customers in slightly different ways. For example, ANZ segregates its business customers into Business Banking (comprising businesses with turnovers below NZ\$10 million), Corporate Banking (comprising businesses with turnover between NZ\$10 million and NZ\$100 million) and Institutional Banking (comprising businesses with turnover in excess of NZ\$100

banking, working capital funding (overdrafts and revolving credit lines), term debt funding, interest bearing deposit facilities, trade finance, international payment services, EFTPOS facilities, treasury services and asset financing. In addition, ANZ offers merchant payment services (EFTPOS hardware, merchant support and transaction processing services). Customers are serviced primarily by specialist business banking managers located in the branch network.

(d) ***Corporate Banking***: providing banking products and services to large corporate clients with turnover of up to $100 million. In addition to the usual suite of business banking products and services, this includes the provision of custody, international payments, cash management and clearing products and structured finance products.

(e) ***Institutional Banking***: providing banking products and services to large corporate clients with turnover of over $100 million.

10. What are the reasons for the proposal and the intentions in respect of the acquired or merged business?

33. It is ANZ’s intention to continue to strengthen its business in New Zealand.

34. National has an excellent reputation for maintaining strong customer relationships in the retail markets. This acquisition is an opportunity for ANZ to enhance its ongoing drive to improve its performance in the retail markets, to strengthen its overall management capability and to improve efficiency through economies of scale and scope.

35. The acquisition would also provide ANZ with a more balanced and diversified business. For example, National has been strong in the rural sector while ANZ has not.

PART II: IDENTIFICATION OF THE MARKETS AFFECTED

Markets

Product markets

36. In this application ANZ has considered the proposed acquisition on the basis that the relevant product markets are those that were identified by the Australian Competition and Consumer Commission (**ACCC**) when it considered the CBA[2] and Colonial Limited merger (the **CBA / Colonial case**) and Westpac’s acquisition of the Bank of Melbourne (the **Bank of Melbourne case**)[3]. This represents the most conservative view of the relevant product

million). In reality, ANZ does not impose these as bright line tests. Rather, they provide a useful guide that allows ANZ to focus on customer needs. ANZ understands that National segregates its business customers into Business Banking (comprising businesses with less than NZ$2 million turnover), Corporate & Commercial (comprising business with turnover in excess of NZ$5 million) and customers with turnovers between NZ$2 million and NZ$5 million are placed in one of these groups according to their needs.

[2] ACCC Media release 109/00: *ACCC Not to Oppose Commonwealth Bank/Colonial Merger*, ACCC website, 30 May 2000, www.accc.gov.au

[3] ACCC Media release 109/00: *ACCC Not to Oppose Westpac/Bank of Melbourne Merger*, ACCC website, 25 July 1997, www.accc.gov.au

markets. ANZ considers that the acquisition raises no competitive concerns in those markets (and accordingly there are also no competition concerns if broader markets were more appropriate). Based on the ACCC's approach, the relevant product markets are:

(a) The institutional corporate market

The institutional corporate market involves lending to institutional corporate providers. This market is national, but it has a significant international element in the form of overseas financiers and investment banks. The providers in this market include four of the five major banks (National Bank, Westpac, BNZ and ANZ), CBA as well as both New Zealand and international investment banks and financiers such as Citibank and Deutsche Bank.

(b) The middle corporate market

The middle corporate market involves lending to corporate providers with turnover of between NZ$10 million and NZ$100 million. The providers in this market include the five major banks as well as New Zealand and international financiers.

(c) The credit card issuing market

The credit card issuing market includes the provision of credit card finance to consumers. There are in excess of 18 providers in this market.

(d) The mortgage market

The mortgage market encompasses the provision of secured home loan products. There are in excess of 30 providers in this market.

(e) The personal loan market

The ACCC considered that this market included banks, building societies, credit unions and finance companies. The Commission took a similar approach in Decision 461. In that decision, the Commission defined a consumer finance market to cover the provision of finance to consumers and included personal loans, store HP cards and credit card facilities. However, ANZ considers that credit cards and personal loans are not always substitutable for each other. For the purposes of this application, ANZ has treated personal loans as a separate market from other finance products. In addition to the five major banks, there are approximately 15 other providers in the personal loan market.

(f) The small to medium enterprise (**SME**) market

The SME market provides facilities for frequent cash deposits and withdrawals, lines of credit and overdrafts, after hours cash deposit facilities and business loans. There are approximately 10 suppliers in this market.

ANZ has included in this market credit and debit card payment processing services acquired by SMEs that are retailers (merchants). It has done so on the basis that this is part of the range of products offered to an SME that is a retailer (merchant). Arguably, the credit card merchant acquiring market could be treated as a separate market, and in the discussion on competition in this market below, ANZ has discussed this aspect of this market separately.

(g) The term deposit / savings account market

The term deposit / savings account market involves the provision of term deposits and savings accounts. There are over 40 providers of term deposits and savings accounts in New Zealand.

(h) The transaction accounts market

The transaction account market involves the provision of cheque accounts. There are currently in excess of 20 providers in this market.

(i) The rural banking market

The rural banking market involves the provision of lending and other banking services to the rural sector. In Decision 264B, the Commission defined a regional market for farm finance services. The Commission stated that farm finance services were available from a wide range of providers ranging from trading banks to finance companies. There are presently in excess of 15 providers in this market.

37. Additionally, ANZ considers the following market is also relevant:

(j) the managed funds market. It was unnecessary for the ACCC in the CBA / Colonial and the Bank of Melbourne cases to consider whether there was a separate market for managed funds. However, in Decision 392 the Commission found that the managed funds market included managed funds and superannuation products. ANZ therefore adopts this product market. There are in excess of 30 providers in this market.

38. It may well be, however, that the relevant product markets are broader than the markets adopted by the ACCC in the CBA / Colonial and Bank of Melbourne cases. For example, it may be that personal loans, credit cards, mortgages, savings accounts / term deposits and transaction accounts are in the same market because they are part of a suite of products provided by all major banks to individuals, even though those individuals may choose to unbundle them. It may also be that the rural market is part of the SME market because the same kinds of products are provided in each market. For the purposes of this application therefore, ANZ adopts the product markets identified by the ACCC in above cases, but it does so without prejudice to relying on broader product markets.

Geographical scope

39. Based on the CBA / Colonial and Bank of Melbourne cases and Decision 392, ANZ considers that the product markets identified above are national markets. ANZ understands that the ACCC defined the product markets identified above in (a) to (e) as national or state to national because:

(a) in relation to product markets (a) and (b), a large number of national and international competitors existed;

(b) in relation to product market (c), the evidence showed that customers were unbundling their credit cards from their transaction accounts;

(c) in relation to product market (d), the evidence showed that mortgage originators and regional banks were supplying customers in locations where there was little or no branch presence; and

(d) in relation to product market (e), the evidence showed that state based players and finance companies traditionally had been strong in the provision of personal loans and the importance of branch networks for distributing personal lending products was declining.

The Commission defined product market (j) as national. It accepted that these services were provided throughout New Zealand.

40. In the CBA / Colonial case, ANZ understands that the ACCC adopted state markets for product markets (g) and (h) and state to local markets for product markets (f) and (i). In relation to product market (i), in Decision 264B the Commission adopted a regional market for farm finance services.

41. Given the size of each state market in Australia in comparison with the size of New Zealand as a whole, ANZ considers it is appropriate to equate state markets in Australia to a national market in New Zealand. In addition, from a supply side perspective, these markets are national. Providers operate nationally and do not differentiate between regions when determining prices (interest rates or charges). From a demand side perspective, while branch networks traditionally have been important, since the mid-1990s, the emergence of telecommunications and the internet as points of customer interface, the necessity for branch networks has been reduced (see Appendix 1). ANZ has, however, provided data in some places on a regional basis to assist the Commission in its analysis of the effects of the proposed acquisition.

Horizontal aggregation

11. Horizontal aggregation: are there any markets in which there would be an aggregation of business activities as a result of the proposed acquisition?

42. The proposed acquisition will result in some horizontal aggregation in all of the relevant markets. Details of the extent of horizontal aggregation in the relevant markets are set out below.

Differentiated product markets

12. Are the products identified above standardised or differentiated?

43. In general, the products supplied in each of the relevant markets are similar in nature across all providers in that market and are therefore able to be substituted for one another. These products may be differentiated by such things as:

(a) price;

(b) interest rates;

(c) the terms and conditions offered (for example, the ability to repay loans early and the penalties that apply);

(d) the existence of "added" benefits and features (for example, credit cards linked with loyalty schemes);

(e) the existence of "added" service propositions (for example, private banking offers individualised services to high level customers);

(f) the target audience (some products are tailor made for specific markets such as students, children etc);

(g) the risk / credit policies of each bank (for example, some banks may offer loans up to a maximum loan valuation ratio of 80% while others offer up to 90%);

(h) the security requirements;

(i) volume concessions (granted where the customer purchases more than one product or service from the bank); and

(j) access options (for example, whether a product can be accessed through branches, the internet, telephone banking, ATMs, EFTPOS or only some of these).

Vertical integration

14. Will the proposal result in vertical integration between firms involved at different functional levels?

44. No. National and ANZ do not operate at different functional levels from each other.

Previous acquisitions

15. Identification of all previous proposed acquisitions involving either participant.

Identify all proposed acquisitions of a business or shares involving either participant notified to the Commission in the last three years.

45. ANZ has not notified the Commission of any proposed acquisitions of the assets of or shares in a business in the last 3 years. As far as ANZ is aware, National has not notified the Commission of any proposed acquisitions of assets of or shares in a business in the last 3 years.

Identify any other acquisition of assets of a business or shares which either participant has undertaken in the last three years.

46. The only acquisition made by ANZ in New Zealand within the last three years was its purchase of 100% of the shares in ENZ in May 2000. ENZ has been referred to earlier in this submission in response to question 5.

47. Australia and New Zealand Banking Group Limited (**ANZ Australia**) also made the following acquisitions in Australia:

    (a) Bank of Hawaii: On 4 October 2001 ANZ Australia agreed to acquire the Bank of Hawaii's operations in Papua New Guinea, Vanuatu and Fiji. The acquired business operates from two branches in Papua New Guinea, two branches in Vanuatu and three branches in Fiji.

    (b) ING Joint Venture: On 30 April 2002 ANZ Australia formed a joint venture with ING Group. Each of the ANZ Group and the ING Group sold their Australian and New Zealand funds management businesses to a joint venture company, ING Australia Limited. ANZ Australia owns 49% and the ING Group owns 51% of the shares in that company. The joint venture operates in New Zealand via a wholly owned subsidiary, ING (NZ) Limited.

    (c) Etrade: ANZ has increased its shareholding in publicly listed company Etrade to 35%. Under the agreement, ANZ is required to, amongst other things, market Etrade services to its customers.

    (d) Other smaller acquisitions have taken place in Australia. These acquisitions are not relevant to this application.

PART III: CONSTRAINTS ON MARKET POWER BY EXISTING COMPETITION

Existing competition

16. In the market or market(s), who are the suppliers of competing products including imports?

Overview of existing competition

Core banking market

48. The banking market in New Zealand has five large players. In terms of assets:

    (a) Westpac had total assets of $38.9 billion at the end of 2002;

    (b) National had total assets of $38.9 billion (just $27 million less than Westpac) at the end of 2002;

    (c) BNZ had total assets of $37 billion at the end of 2002;

    (d) ANZ had total assets of $28 billion at the end of 2002; and

    (e) ASB had total assets of $26 billion at the end of 2002.[4]

[4] Allens Consulting Group *State of Play of the Banking Industry in New Zealand* June 2003 page 3.

49. Westpac, BNZ, National and ANZ have extensive nationwide branch networks. These four providers have competing branches in almost all areas (see Appendix 4). ASB's branch network is substantial in most areas and it is expanding that network to the point that ANZ expects it to have comparable coverage to the other major banks.

50. In addition to the above five major banks, the New Zealand banking market contains a number of comparatively smaller but well established providers.

(a) Rabobank New Zealand (**Rabobank**) is the rural banking arm of Rabobank Nederland New Zealand Banking Group. Rabobank currently has 27 offices nationwide and offers rural business, corporate banking products and other financial products. Rabobank's total assets at the end of December 2002 were $2.52 billion.[5]

(b) TSB Bank Limited (**TSB**) is a smaller provincial bank, based primarily in the Taranaki region. At the end of December 2002, TSB's total assets were $1.8 billion.[6]

51. There are a total of 18 registered banks in New Zealand. In addition to the banks referred to above (at paragraphs 48-50), registered banks include Kiwibank, Superbank, Citibank, Deutsche Bank, HSBC, ABN Amro New Zealand, Bank of Tokyo-Mitsubishi (Australia), CBA and Kookmin Bank. As registered banks, the above providers have the ability to deal in both higher value / wholesale transactions (approximately 4000 transactions of this nature take place per day involving $40 billion) and the low value / retail transactions (approximately 2.3 million transactions of this nature take place per day involving $4.5 billion dollars). More detail is provided on the New Zealand payments industry at paragraphs 188-197.

52. In addition to the 18 registered banks, there are a number of other providers operating in the core banking market (e.g. GE Capital and Allied Finance). Many of these have well known and established international parents. These banks and financial service providers deal in high value transactions or are involved in finance company activities. Although currently they do not raise deposits directly from the public potentially they could deal in low value / retail transactions via an agency agreement with a registered bank. For example, HSBC provides transactional services using Westpac's existing networks.

Other financial services

53. Apart from the activities undertaken in the core banking market, banks also compete with other providers in relation to managed fund and insurance based financial services.

A dynamic market

54. The banking market is dynamic and highly competitive. The costs to enter the market or to expand within the market are relatively low.

---

[5] Allens Consulting Group *State of Play of the Banking Industry in New Zealand* June 2003 pages 4-5.

[6] Allens Consulting Group *State of Play of the Banking Industry in New Zealand* June 2003 page 5.

55. Following deregulation of the banking industry in the 1980s, a number of providers entered the market. A timeline showing entry and exit over the period 1989 to 2003 is set out in KPMG's report.[7] Some examples include:

    (a) in about 1997, BNP Paribas wrote approximately $1 billion worth of business in a year;

    (b) CBA entered the institutional corporate market in June 2000 with total assets of $876 million.[8] It has relationships with 90 of the top 200 companies in New Zealand;

    (c) in the rural sector, Rabobank entered the market in 1996 after entering into a strategic alliance with Wrightson Limited in 1998 and purchasing Wrightson Farmers Finance Limited. It now has a national market share of approximately **[ ]**, with its highest regional market share of **[ ]** in Southland; and

    (d) in the mortgage market, AMP Bank Limited began operations in 1998 and grew its mortgage portfolio, commercial property portfolio and rural portfolio to $1,919 million, $509 million and $191 million respectively before selling them earlier this year.

56. In the retail market in the last two years there have been two new bank entrants in the form of Kiwibank and Superbank. Both of these operate via a considerably greater number of outlets than any of the other banks.

    (a) Kiwibank (through its agency relationship with NZ Post) has approximately 280 outlets nationwide. Kiwibank also offers ATM, EFTPOS, internet and telephone banking services. By December 2002 (having officially opened on 23 March 2002), Kiwibank had signed up 100,000 customers.[9]

    (b) Superbank is backed by St. George Bank Limited, which is the fifth largest bank in Australia. Superbank currently offers one savings product only. It operates via 474 Foodstuffs outlets as well as telephone and internet banking channels. Superbank plans to provide full-banking facilities including cheque accounts, credit cards, home loans, personal loans, insurance and term deposits for retail customers. Superbank has not stated any plans to enter the commercial banking market. However, the potential is there for it to expand into this market should it wish to do so.

57. In addition, non bank providers have entered the banking market. For example, the Warehouse formed a joint venture with Westpac in August 2001 and offers three credit cards and basic insurance cover to retail customers.

58. Competitive pressure in the New Zealand banking market has resulted in a decline in both interest rate margins and interest rate spreads since the mid 1990s. Evidence of the competitive nature of the banking markets can be seen in Appendix 5. Figure 1 in

---

[7] *Preliminary report for ANZ on New Zealand Banking Industry*, 6 May 2003, pages 23-24.

[8] KPMG Financial Institutions Performance Survey 2003 page 22.

[9] Allens Consulting Group *State of Play of the Banking Industry in New Zealand* June 2003 page 5.

Appendix 5 shows that interest margins have generally declined over the last five years.[10] Figure 1 also shows that in comparison with Australia, New Zealand's interest rate margins are considerably lower.[11] This reinforces the view that the New Zealand market for financial services is very competitive.

Comment on safe harbours

59. ANZ considers that, in each of the relevant markets, the proposed acquisition will not substantially lessen competition because:

(a) the banking market is and will remain highly competitive and dynamic;

(b) the market shares of ANZ (post acquisition) are likely to be overstated because **[ ]**; and

(c) Barriers to entry and expansion are low (see paragraphs 114-175 and 183-226).

Horizontal Aggregation

Institutional corporate market

60. The institutional corporate market is a highly competitive market. Competitors include four of the five major banks (National, Westpac, BNZ and ANZ), CBA and New Zealand based and international investment banks and financiers. The number of customers in New Zealand is estimated to be less than 500. No accurate market share information is available because:

(a) customers spread their business over a number of banks;

(b) all banks define institutional customers differently; and

(c) most customers also source funding overseas.

61. Due to the highly competitive and fluid nature of this market, ANZ considers it is unlikely that its market share post acquisition will fall outside the Commission's safe harbour guidelines. Even if it did, any increase in interest rates and fees can lead a customer to switch to a competing provider. Customers in this market have countervailing power. ANZ (post acquisition) would therefore continue to be significantly constrained by existing providers in the market.

---

[10] ANZ understands that the 2001 / 2002 increase was attributable to the lag caused by New Zealand banks holding a large proportion of fixed rate assets, still earning higher than current floating rates. While the banks moved quickly to reprice their deposit funding, their fixed rate assets were still earning rates fixed up to 3 years prior. In addition, margins were seen to increase in 2002 due to an upward movement in the interest rate cycle driven by the Reserve Bank's Official Cash Rate. ANZ expects the NZ margin to flatten or decline as those assets roll off their fixed rates.

[11] Allens Consulting Group *State of Play of the Banking Industry in New Zealand* June 2003 page 7.

Middle corporate market

62. The middle corporate market is highly competitive. Competitors comprise the five major banks and New Zealand based and international financiers. The number of customers in New Zealand is estimated to be approximately 2,500 of which ANZ has relationships with approximately 800. It is difficult to provide accurate and reliable market share data for corporate banking markets because customers are shared between the banks. However, Table 1 below shows each bank's percentage of primary relationships with corporate banking customers.[12]

Table 1 – Share of middle corporate market primary relationships

Company	*Share of primary relationships*	*Post acquisition market share*	*Three firm concentration ratio post acquisition*
ANZ	**[ ]**	**[ ]**	**[ ]**
National	**[ ]**		
BNZ	**[ ]**	**[ ]**	
Westpac	**[ ]**	**[ ]**	
ASB	**[ ]**	**[ ]**	**[ ]**
Other	**[ ]**	**[ ]**	**[ ]**
TOTAL	**100%**	**100%**	**100%**

Source: ANZ estimates

63. Based on the market shares above, ANZ's market share (post acquisition) will fall outside the safe harbour guidelines relating to aggregated market share.

64. However, this market is highly competitive. Any increase in interest rates and fees will lead a customer to switch to a competing provider. Post acquisition, ANZ would continue to be significantly constrained by existing providers in the market.

Credit card issuing market

65. In the credit card issuing market there are in excess of 18 credit card issuers. Table 2 sets out the respective market shares of the providers in the credit card issuing market. These shares are based on the funds under management (**FUM**).

---

[12] A bank is said to have a primary relationship with a customer if that bank is the primary supplier of banking services to that customer. A bank is said to have a secondary relationship with a customer if that bank is not the main provider, but is the second largest supplier of banking services to that customer.

Table 2 - Share of Credit Card FUM

Company	*Pre acquisition market share*	*Post acquisition market share*	*Three firm concentration ratio post acquisition*
ANZ	**[ ]**	**[ ]**	**[ ]**
National	**[ ]**		
BNZ	**[ ]**	**[ ]**	
Westpac	**[ ]**	**[ ]**	
ASB	**[ ]**	**[ ]**	**[ ]**
Farmers	**[ ]**	**[ ]**	**[ ]**
TSB	**[ ]**	**[ ]**	**[ ]**
Other	**[ ]**	**[ ]**	**[ ]**
TOTAL	**100%**	**100%**	**100%**

Source: ANZ based on AC Neilson Financial Monitor

66. Based on the market shares above, post acquisition ANZ‘s market share (post acquisition) will fall outside the safe harbour guidelines relating to aggregated market share, but only by **[ ]**.

67. Post acquisition, ANZ’s market share in this market will not be significantly higher than the market shares of BNZ **[ ]** and Westpac **[ ]**. In Decision 461, the Commission adopted a conservative approach and considered consumer finance companies in their own right. However the Commission concluded that banks and credit card issuers could be included in the consumer finance market to the extent that the products they offered were substitutable. The competition between ANZ and other banks in this market will remain post acquisition. Finance companies will also provide a further competitive constraint on ANZ (post acquisition) as will other payment options, such as EFTPOS. Post acquisition, ANZ would therefore continue to be constrained by existing providers in this market.

Mortgage market

68. There are in excess of 30 existing providers in the mortgage market. Table 3 sets out the market shares of the five major banks in the mortgage market and based on FUM. Table 3 includes all mortgages on consumer homes, holiday houses and investment properties.

<u>Table 3 – Share of Mortgage FUM</u>

<table>
<tr><th>Company</th><th>Pre acquisition market share</th><th>Post acquisition market share</th><th>Three firm concentration ratio post acquisition</th></tr>
<tr><td>ANZ</td><td>[ ]</td><td rowspan="2">[ ]</td><td rowspan="4">[ ]</td></tr>
<tr><td>National</td><td>[ ]</td></tr>
<tr><td>Westpac</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>ASB</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>BNZ</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Others</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>TOTAL</td><td>100%</td><td>100%</td><td>100%</td></tr>
</table>

Source: ANZ based on ACNielsen Consumer Finance Monitor 2002

69. Based on the market shares above, ANZ's market share (post acquisition) will fall outside the safe harbour guidelines relating to aggregated market share, but only by **[ ]**. If that were not the case, then ANZ (post acquisition) would fall within the safe harbours in this market.

70. Post acquisition, ANZ would face significant constraint in the mortgage market from the other major banks (Westpac, BNZ and ASB) and other mortgage providers and through the presence of mortgage brokers:

(a) Westpac, BNZ and ASB are well established, experienced and vigorous competitors. ASB has a stronger position in the Auckland market than it does nationally. Its market shares of **[ ]** in North Shore, **[ ]** in Waitakere, **[ ]** in Auckland City and **[ ]** in South Auckland are higher than the market share of ANZ and National together in these areas (**[ ]**, **[ ]**, **[ ]** and **[ ]** respectively).[13] ASB can leverage its strong position in Auckland to expand its market shares in other regions. There are no barriers to ASB expanding in the remainder of New Zealand.

(b) As set out in Table 3, **[ ]** of mortgages are provided by providers other than the major banks. ANZ understands that approximately **[ ]** of mortgages are arranged through a mortgage broker.[14] Mortgage brokers provide a comparative service that assists consumers to shop around for the best mortgage deal. Mortgage brokers have removed the traditional relationship that existed between a bank and its customers in this market and have, in so doing, encouraged customers to select a

[13] Merrill Lynch *New Zealand Banking: Structural Review of the New Zealand Banking Market*, April 2003, page 11.

[14] Good Returns article: *Few Think BNZ's Decision* Good 7 May 2003.

mortgage provider purely on price. This provides a further and major constraint on ANZ (post acquisition)pricing at uncompetitive levels.

Personal loans market

71. In addition to the five major banks, there are approximately 15 other providers in the personal loans market. Table 4 provides market shares of providers in the personal loan market on a national basis and based on FUM.

<u>Table 4 - Personal loan value of account balance</u>

<table>
<tr><th>Financial Institution</th><th>Pre acquisition market share</th><th>Post acquisition market share</th><th>Three firm concentration ratio post acquisition</th></tr>
<tr><td>ANZ / UDC</td><td>[ ]</td><td rowspan="2">[ ]</td><td rowspan="4">[ ]</td></tr>
<tr><td>National</td><td>[ ]</td></tr>
<tr><td>Westpac</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>BNZ</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>ASB</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Credit Union</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Sovereign</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Other</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Total</td><td>100%</td><td>100%</td><td>100%</td></tr>
</table>

Source: ACNielsen Financial Monitor

72. Table 5 sets out the post acquisition market shares in the personal loan market in the Upper North Island (Northland, Auckland, Upper Waikato), rest of the North Island and South Island based on FUM.

<u>Table 5 – Regional share of Total FUM</u>

<table>
<tr><th>Region</th><th>ANZ</th><th>National</th><th>Post acquisition market share</th><th>Post acquisition three firm concentration ratio</th><th colspan="2">Largest competitor (market share)</th></tr>
<tr><td>Upper North Island</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>Westpac</td><td>[ ]</td></tr>
<tr><td>Rest of North</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>BNZ</td><td>[ ]</td></tr>
</table>

Region	***ANZ***	***National***	***Post acquisition market share***	***Post acquisition three firm concentration ratio***	***Largest competitor (market share)***	
Island						
South Island	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac Trust	**[ ]**

Source: ANZ based on ACNielsen Finance Monitor 2002

73. Post acquisition, if calculated on a national basis, ANZ's market share will fall within the Commission's safe harbour guidelines. It is outside the safe harbour guidelines in the Upper North Island and South Island regional submarkets.

74. In relation to the branch network, in all local areas where there is aggregation as a result of the acquisition, there are at least two other branches in that area. ANZ considers that switching costs are low (see below).

75. Finance companies, building societies and credit unions also constrain providers in this market. In Decision 461, the Commission concluded that "existing competition from other finance companies, banks and credit card issuers in the consumer finance market is sufficiently robust to constrain the merged entity".[15]

76. For these reasons, ANZ (post acquisition) will continue to face significant constraint from existing competition.

Managed funds market

77. There are in excess of nine providers in the managed funds market. Table 6 sets out the respective market shares of the main providers and based on FUM.

<u>Table 6 – Share of Managed Fund / Unit Trust FUM</u>

Company	***Pre-acquisition market share***	***Post acquisition market share***
ANZ Australia / ING[16]	**[ ]**	**[ ]**
National	**[ ]**	**[ ]**
AMP	**[ ]**	**[ ]**
Westpac	**[ ]**	**[ ]**

[15] Decision 461, paragraph 132.

[16] ANZ does not have any direct interest in the ANZ/ING joint venture. ANZ Australia owns 49% of ING Australia, the joint venture vehicle in Australia. ING Australia owns 100% of the shares in ING New Zealand.

Company	*Pre-acquisition market share*	*Post acquisition market share*
ASB	**[ ]**	**[ ]**
BNZ	**[ ]**	**[ ]**
Sovereign	**[ ]**	**[ ]**
Money Managers	**[ ]**	**[ ]**
Tower	**[ ]**	**[ ]**
AXA	**[ ]**	**[ ]**
Other	**[ ]**	**[ ]**
TOTAL	**100%**	**100%**

Source: ANZ based on ACNielsen Consumer Finance Monitor 2002

78. ANZ considers the proposed acquisition would have no effect on this market. ANZ Australia does not have a controlling interest in that joint venture. In any event, if the market shares of National and the joint venture were combined, the largest three providers in the managed funds market would be **[ ]**, while ANZ's market share would be **[ ]**. Accordingly, ANZ (post acquisition) would fall within the Commission's safe harbour guidelines.

79. As illustrated, there are a significant number of providers in this market. It is highly competitive and barriers to expansion are low. That this is the case is reinforced by the Commission's Decision 392 where the Commission concluded that:

> "… the existing major competitors of CBA and Colonial are large and experienced operators. They include AMP, AXA, Tower and Royal Sun Alliance. In addition, there are several small competitors. There is little doubt that these competitors would have the ability effectively to constrain a merged CBA/Colonial. All of the industry participants spoken to by Commission staff considered that the market would remain strongly competitive".[17]

80. For these reasons, the managed funds market is not discussed further in this application.

Rural banking market

81. There are in excess of 15 providers in this market. Table 7 provides market shares of providers in the rural banking market on a national level (on the basis of share of customers, total funds under management, total loan funds under management and total deposits funds under management).

[17] Decision 392, paragraph 62.

Table 7 – National market share

<table>
<tr><th>Company</th><th>Pre acquisition share of customers</th><th>Pre acquisition loan FUM</th><th>Pre acquisition deposit FUM</th><th>Pre acquisition total FUM</th><th>Post acquisition market share based on total FUM</th><th>Three firm concentration ratio post acquisition based on total FUM</th></tr>
<tr><td>ANZ</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td rowspan="2">[ ]</td><td rowspan="4">[ ]</td></tr>
<tr><td>National</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>BNZ</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Westpac</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>ASB</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Rabobank</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Other</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
</table>

Source: ANZ based on ACNielsen Rural Finance Monitor 2002

82. Table 8 sets out the concentration ratios in this market post acquisition on a regional basis and based on FUM.

Table 8 - Regional share of Rural FUM

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*
Northland	[ ]	[ ]	[ ]	[ ]
Auckland	[ ]	[ ]	[ ]	[ ]
Waikato	[ ]	[ ]	[ ]	[ ]
Bay of Plenty	[ ]	[ ]	[ ]	[ ]
East Coast	[ ]	[ ]	[ ]	[ ]
Hawkes Bay	[ ]	[ ]	[ ]	[ ]
Wellington	[ ]	[ ]	[ ]	[ ]
Taranaki	[ ]	[ ]	[ ]	[ ]
Manawatu /	[ ]	[ ]	[ ]	[ ]

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*
Wanganui				
Nelson / Marlborough	[ ]	[ ]	[ ]	[ ]
West Coast	[ ]	[ ]	[ ]	[ ]
Canterbury	[ ]	[ ]	[ ]	[ ]
Otago	[ ]	[ ]	[ ]	[ ]
Southland	[ ]	[ ]	[ ]	[ ]

Source: ANZ based on ACNielsen Rural Finance Monitor 2002

83. Based on the market shares set out above, if calculated on a national basis, ANZ's market share post acquisition would fall outside the Commission's safe harbour guidelines relating to aggregated market share. It is also outside these guidelines in some regional submarkets.

84. As is apparent from the national market data, ANZ's market share post acquisition derives primarily from National's market share. National's strong position in the rural market arose primarily from its acquisition of Rural Bank, which had a historically high market share. ANZ's market share (post acquisition) is therefore not evidence of artificial constraint on the ability of others to enter or grow their share of the market. ANZ (post acquisition) will continue to be constrained by BNZ, Westpac, ASB, Rabobank and others.

85. If the Commission considers branch networks are important in the rural market then it is important to note that in all local areas where there is aggregation as a result of ANZ's acquisition, there are at least two other branches in that area (Appendix 4). Additionally there are finance companies and stock and station agents who operate on a mobile basis without branches. Rabobank is a major rural player that does not have physical local branches. These competitors provide customers with a number of choices in a market where the cost in switching providers is low (see below). Accordingly, post acquisition ANZ would continue to be significantly constrained by existing competitors.

SME market

86. There are five major providers in the SME market. Table 9 provides market shares of providers in the SME market (on a national level on the basis of share of customers, total funds under management, total loan funds under management and total deposit funds under management).

Table 9 – National market share

Company	*Pre acquisition share of customers*	*Pre acquisition loan FUM*	*Pre acquisition deposit FUM*	*Pre acquisition total FUM*	*Post acquisition market share based on total FUM*	*Three firm concentration ratio post acquisition based on total FUM*
ANZ	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
National	[ ]	[ ]	[ ]	[ ]		
BNZ	[ ]	[ ]	[ ]	[ ]	[ ]	
Westpac	[ ]	[ ]	[ ]	[ ]	[ ]	
ASB	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Other	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]

Source: ANZ based on ACNielsen Small Business Finance Monitor 2001-2002

87. Table 9 illustrates that National and BNZ are the largest providers in the SME market on a national level, closely followed by Westpac (when measured as a share of customers).

88. Table 10 sets out the post acquisition market shares in the SME market on a regional basis and based on FUM.

Table 10 – Regional share of SME FUM

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
Northland	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Auckland	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Waikato	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Bay of Plenty	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Hawkes Bay	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Taranaki	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Manawatu / Wanganui	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
Wellington	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
Nelson / Marlborough	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**
Canterbury	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
Otago	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Southland	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**

Source: ANZ based on ACNielsen Small Business Finance Monitor 2001-2002

89. Based on the market shares set out above, if calculated on a national basis, ANZ's market share post acquisition would fall outside the Commission's safe harbour guidelines relating to aggregated market share (but only by **[ ]**). It would also fall outside these guidelines in some regional submarkets.

90. In relation to the branch network, post ANZ's acquisition there would continue to be at least two other bank branches in every town where there is aggregation of branches as a result of the acquisition. The cost for an SME to switch providers, in the event that a bank branch imposed an increase in price, is very low.

91. In relation to the Australian market, Allens Consulting reported that the SME market for SME products is "dynamically evolving and becoming broader … as a result of increased unbundling of financial products and the increasing acceptance and use of online banking by small businesses".[18] The same can be said of the New Zealand SME market.

92. Through existing competition and the low cost of switching, ANZ (post acquisition) would continue to be significantly constrained.

Credit / debit card merchant acquiring services

93. Merchant acquiring services involve the provision to merchants of credit and debit card payment processing services.

94. All five major banks currently provide merchant acquiring services to merchants in relation to debit card and Visa and MasterCard credit card transactions. Transactions put through merchants who contract with Westpac, ASB, BNZ or National are processed via the ETSL switch. Transactions put through merchants who contract with ANZ are processed through the ANZ switch. ANZ also provides EFTPOS equipment and support services to merchants. However, merchants who acquire services from any of the other four of the major banks must contract with a third party for the provision of such equipment.

[18] Allens Consulting Group: *Trends in the Financial Services Sector 2003* page 16.

95. Merchant acquiring services are also provided by card issuing agencies such as American Express, Diners' Club and Farmers' Card. Any merchant who accepts these cards, must contract with the card issuing agency for merchant acquiring services. These services are limited solely to the processing of transactions on the relevant credit card. Each card issuing agency has an agreement with ANZ and ETSL that allows the card transactions to be switched through the ANZ and ETSL systems.

96. No accurate market share information is available, as the banks do not publish the number of transactions going through the two switches. ANZ has provided an estimate of market share based on its analysis of the transactions going through ANZ's system and the ANZ card transactions going through ETSL's system. This is set out in Table 11.

Table 11

Bank	***Share of credit card $ spend (as at 31 March 2003)***	***Share of debit card transactions (as at 31 March 2003)***
ASB	**[ ]**	**[ ]**
ANZ	**[ ]**	**[ ]**
BNZ	**[ ]**	**[ ]**
National	**[ ]**	**[ ]**
Westpac	**[ ]**	**[ ]**
Other	**[ ]**	**[ ]**
Total	**100%**	**100%**

Source: ANZ estimates

97. Based on the market shares set out above, post acquisition ANZ's market share would fall outside the Commission's safe harbour guidelines relating to aggregated market share. However, ANZ's acquisition of National's 25% interest in ETSL does not have any effect on the competition in the merchant acquiring services market. This is because ANZ will not possess a controlling interest in ETSL.[19]

98. Competition in relation to the provision of merchant acquiring services occurs principally over the level of charges and the quality of service provided to customers. These factors will continue to constrain ANZ post acquisition.

99. There is a market associated with the supply of equipment. It is however irrelevant for the purposes of this application. That is because ANZ is the only bank that owns the equipment supplied to merchants. All other banks introduce the merchant to a third party equipment supplier. There is therefore no real competition for equipment supply between relevant providers in this market.

---

[19] ETSL's constitution provides that decisions are made either by ordinary resolution, or in some cases, by special resolution (requiring a majority of at least 75%).

Term deposit / savings account market

100. This market involves the provision of term deposits and savings accounts. There are over 40 providers of term deposits and savings accounts in New Zealand. Table 12 sets out the market shares of providers in the term deposit market on a national basis.

Table 12 - Share of term deposit balance

Company	*Pre acquisition market share*	*Post acquisition market share*	*Three firm concentration ratio post acquisition*
ANZ / UDC	[ ]	[ ]	[ ]
National	[ ]		
Westpac	[ ]	[ ]	
BNZ	[ ]	[ ]	
ASB	[ ]	[ ]	[ ]
PSIS	[ ]	[ ]	[ ]
Southland Building Society	[ ]	[ ]	[ ]
Other	[ ]	[ ]	[ ]
Total	**100%**	**100%**	**100%**

Source: ACNielsen Financial Monitor

101. Table 13 sets out the post acquisition market shares of term deposit / savings account market on a regional basis and based on FUM.

Table 13 – Regional share of Term Deposit FUM

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
Northland	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
North West Auckland	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Auckland City	[ ]	[ ]	[ ]	[ ]	ASB	[ ]

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
South Auckland	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Waikato / King Country	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Bay of Plenty	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
East Coast	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Western Central North Island	[ ]	[ ]	[ ]	[ ]	TSB	[ ]
Wellington	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Upper West South Island	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Christchurch	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Lower South Island	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]

Source: ANZ based on ACNielsen Finance Monitor 2002

102. Based on the market shares above, if calculated on a national basis, ANZ' s market share post acquisition will fall outside the Commission's safe harbour guidelines relating to aggregated market share (but only by **[ ]**). It will also fall outside these guidelines in some regional submarkets.

103. Table 14 sets out the post acquisition shares of savings account providers on a national basis

Table 14 - Share of savings call account balance

Company	*Market share*	*Post acquisition market share*	*Three firm concentration ratio post acquisition*
ANZ / UDC	[ ]	[ ]	[ ]
National	[ ]		
Westpac	[ ]	[ ]	
ASB	[ ]	[ ]	

Company	*Market share*	*Post acquisition market share*	*Three firm concentration ratio post acquisition*
BNZ	**[ ]**	**[ ]**	**[ ]**
TSB	**[ ]**	**[ ]**	**[ ]**
Other	**[ ]**	**[ ]**	**[ ]**
Total	**100%**	**100%**	**100%**

Source: ACNielsen Financial Monitor

104. Table 15 sets out the post acquisition market shares of savings account providers on a regional basis and based on FUM.

Table 15 - Regional share of Savings Account FUM

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
Northland	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
Rodney	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
North Shore	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**
Waitakere	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**
Auckland City	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**
Manukau City	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**
Papakura / Franklin	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**
Coromandel / North Waikato	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Hamilton	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
South Waikato / King Country	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Tauranga	**[ ]**	**[ ]**	**[ ]**	**[ ]**	ASB	**[ ]**

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
Bay of Plenty	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
East Coast	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
Hastings / Napier	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Southern HB / Wairarapa	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Taranaki	**[ ]**	**[ ]**	**[ ]**	**[ ]**	TSB	**[ ]**
Central West North Island	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Palmerston North	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Upper Hutt / Porirua	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Lower Hutt	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
Wellington City	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Northern South Island	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
West Coast	**[ ]**	**[ ]**	**[ ]**	**[ ]**	BNZ	**[ ]**
Canterbury (not Christchurch)	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Christchurch	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Dunedin	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Otago	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**
Southland	**[ ]**	**[ ]**	**[ ]**	**[ ]**	Westpac	**[ ]**

Source: ANZ based on AC Neilson Financial Monitor

105. Based on the market shares above, if calculated on a national basis, ANZ's market share (post acquisition) will fall outside the Commission's safe harbour guidelines relating to aggregated market share (but only by **[ ]**). It will also fall outside these guidelines in

some regional submarkets. However, ANZ (post acquisition) will continue to be constrained by existing competition because of:

(a) the large number of existing providers;

(b) the low cost of expansion; and

(c) the low switching costs for customers.

Paragraphs (b) and (c) are discussed further below.

106. In relation to the branch network, in all local areas where there is aggregation as a result of the acquisition by ANZ, there are at least two other branches in that area. The costs of switching providers are low (see below).

107. For these reasons, ANZ would continue to be constrained post acquisition.

Transaction accounts market

108. Transaction accounts are essentially cheque accounts. There are currently in excess of 20 providers in this market. Table 16 sets out the post acquisition shares of bank transaction account providers on a national basis.

Table 16 - Share of transaction account balance

<table>
<tr><th>Company</th><th>Pre acquisition market share</th><th>Post acquisition market share</th><th>Three firm concentration ratio post acquisition</th></tr>
<tr><td>ANZ / UDC</td><td>[ ]</td><td rowspan="2">[ ]</td><td rowspan="4">[ ]</td></tr>
<tr><td>National</td><td>[ ]</td></tr>
<tr><td>Westpac</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>BNZ</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>ASB</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>TSB</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Other</td><td>[ ]</td><td>[ ]</td><td>[ ]</td></tr>
<tr><td>Total</td><td>100%</td><td>100%</td><td>100%</td></tr>
</table>

Source: ACNielsen Financial Monitor

109. Table 17 sets out the post acquisition market shares in the transaction accounts market on a regional basis and based on FUM.

Table 17 – Regional share of Total FUM

Region	ANZ	National	Post acquisition market share	Post acquisition three firm concentration ratio	Largest competitor (market share)	
Northland	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Rodney	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
North Shore	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Waitakere	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Auckland City	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Manukau City	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Papakura / Franklin	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Coromandel / North Waikato	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Hamilton	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
South Waikato / King Country	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Tauranga	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Bay of Plenty	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Gisborne / Wairoa	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Hastings / Napier	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Southern HB / Wairarapa	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Taranaki	[ ]	[ ]	[ ]	[ ]	TSB	[ ]
Central West North Island	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Palmerston North	[ ]	[ ]	[ ]	[ ]	PSIS	[ ]
Upper Hutt / Porirua	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]

Region	*ANZ*	*National*	*Post acquisition market share*	*Post acquisition three firm concentration ratio*	*Largest competitor (market share)*	
Lower Hutt	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Wellington City	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Northern South Island	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
West Coast	[ ]	[ ]	[ ]	[ ]	ASB	[ ]
Canterbury (not Christchurch)	[ ]	[ ]	[ ]	[ ]	BNZ	[ ]
Christchurch	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Dunedin	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Otago	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]
Southland	[ ]	[ ]	[ ]	[ ]	Westpac	[ ]

Source: ANZ based on ACNielsen Finance Monitor

110. Based on the market shares set out above, if calculated on a national basis, ANZ's market share post acquisition will fall outside the Commission's safe harbour guidelines relating to aggregated market share (but only by **[ ]**). It will also fall outside these guidelines in some of the regional submarkets.

111. ANZ has considered the importance of the branch network in these markets. Where there is aggregation in local areas as a result of the acquisition by ANZ, there are at least two other branches in that area. The costs of switching providers are low**.**

112. In addition:

(a) in many areas, the market shares of the other providers are high relative to ANZ's market share post acquisition (for example, Auckland City, Manukau City, Papakura/Franklin, Lower Hutt and Christchurch);

(b) Allens Consulting suggests that the Australian transaction market is likely to become more competitive in the next few years as direct transaction account institutions (such as internet and phone-based organisations) are established.[20] In New Zealand in 2002, 87% of all payments were made by an electronic medium.[21]

(c) In addition to bank providers, there are also other providers such as building societies and credit unions providing competition in this market. (For example, Southland Building Society has branches in Christchurch, Invercargill, Gore, Dunedin, Hamilton, Nelson and Queenstown. In addition, member credit unions of the New Zealand Association of Credit Unions and Manchester Unity offer transaction account services locally as well as nationally in some cases (e.g. Clerical and Industrial Credit Union).)

113. For these reasons ANZ would continue to face significant constraint from other competitors post acquisition.

Other considerations

16.5 Please identify any firms that are not currently producing the product in the market, but could enter the market quickly (using essentially their existing productive capacity) in response to an attempt by suppliers to raise prices or reduce output or quality (near entrants).

Introduction

114. If existing providers raised their prices or reduced their quality then any number of providers could enter each of these markets. For example, those operating in the institutional and corporate markets could enter the retail markets and vice versa. Also, communication networks are now so good that it is possible for overseas providers to establish a business in New Zealand based on their existing overseas banking systems. The establishment of Superbank, relying on the existing systems of St George Bank in Australia, is an example of this.

Institutional corporate market

115. If the profit potential existed, then other overseas providers such as Bank of America, Royal Bank of Scotland, Standard Chartered, UBS and Bank of Tokyo could enter this market quickly in response to an attempt by existing providers to raise prices outside usual market fluctuations.

Middle corporate market

116. A number of other providers, including for example ABN Amro, Deutsche Bank, Rabobank, and Superbank, could enter this market quickly in response to an attempt by existing providers to raise prices outside usual market fluctuations.

---

[20] Allens Consulting Group: *Trends in the Financial Services Sector 2003* page 18.

[21] 35% are EFTPOS transactions, 13% electronic credits, 5% direct debits, 17% credit cards and 12% ATMs, leaving 13% being cheques and paper deposits. KPMG *Financial Institutions Performance Survey* 2003, page 35.

Credit card issuing market

117. Any number of providers could enter this market quickly in response to an attempt by existing providers to raise prices outside usual market fluctuations. Examples include Kiwibank and Superbank. Kiwibank has recently announced the launch of a new low interest credit card. Any large merchant (e.g. Farmers Mutual), building societies (e.g. Southland Building Society) or credit unions could follow the examples of Farmers or The Warehouse and offer credit cards. Global Cards 'monoline' providers such as MBNA could also enter the New Zealand market.

118. There is also the potential for other transaction processing options to evolve. For example, telecommunications companies in New Zealand have existing transaction processing infrastructures that would allow them to enter this market very quickly. They can effectively allow customers to charge goods and services to their telephone bills.

Mortgage market

119. Any number of providers could enter this market quickly in response to existing providers raising prices outside usual market fluctuations. Examples include Superbank, other Australian and European banks and non bank mortgage lenders such as Aurora Home Loans and Wizard.

Rural market

120. Any number of providers could enter this market quickly in response to existing providers raising prices outside usual market fluctuations. Examples include finance companies, Kiwibank, Superbank and other providers such as ABN Amro, Citibank, building societies and credit unions.

SME banking market

121. Kiwibank, Superbank and other providers such as Rabobank, ABN Amro, Citibank, building societies, credit unions and Farmers Mutual could enter this market quickly in response to an attempt by existing providers to raises prices outside usual market fluctuations. Any of these providers would be able to supply merchant acquiring services through an arrangement with ETSL or ANZ.

Personal loans market

122. Superbank and other providers such as Rabobank, and finance companies such as Allied Finance and GE Capital, could enter this market quickly in response to an attempt by existing providers to raise prices outside usual market fluctuations.

Term deposit / savings account market

123. Any number of providers (such as Superbank or Rabobank) could enter this market quickly in response to an attempt by existing providers to raise prices outside usual market fluctuations. However, all providers in this market must comply with the Securities Act regulations, which concern disclosure rather than entry criteria.

Transaction accounts market

124. Any number of providers (such as Superbank or Rabobank) could enter this market quickly in response to an attempt by existing providers to raise prices outside usual market fluctuations.

16.6 Estimate the productive capacity that such near entrants potentially could bring to the market.

125. In each of the above markets, near entrants have the potential for almost unlimited capacity. There is a global funding market that near entrants can access for the purpose of financing asset growth. It is demand, not productive capacity, that would limit a provider's scope to enter these markets.

16.7 Please indicate the extent to which imports provide a constraint on domestic suppliers. What costs are incurred by importers that are not incurred by domestic suppliers? How sensitive is the domestic price of imports to changes in the New Zealand dollar exchange rate?

Institutional corporate market

126. Existing domestic providers in the institutional market face strong competition from foreign competitors. A large corporate can, for example, raise funds from within New Zealand or from international lenders with negligible cost.

127. The exchange rate does not affect the competitiveness of foreign suppliers of funds as it is not difficult or expensive to hedge loans back into their currency of origin. While foreign providers may not travel to New Zealand to write one small loan or mortgage, if a market offers sufficient margins they will come in to establish an on-the-ground business.

Middle corporate market

128. As for institutional market.

Other markets

129. Imports do not provide a constraint in any of the other markets

16.8 To what extent is the product exported?

130. Banking products and services tend not to be exported in the ordinary sense of being marketed to international entities with no other link to New Zealand. Banks usually only provide products and services (such as loans, transaction accounts and foreign currency) to overseas entities where the entity has a presence and/or assets in New Zealand or an overseas bank provides comfort in relation to the entity's performance of its obligations. For example, ANZ will provide New Zealand dollar lending facilities to ANZ Group customers that are based overseas, but only in reliance on a bank guarantee from the overseas ANZ Group branch.

131. As a result, banks in New Zealand tend to develop their products and services for the domestic market and not specifically for the purpose of any international market.

16.9 Please indicate whether the target company could be described as a vigorous and effective competitor, taking into account its pricing behaviour, its record of innovation, its growth rate relative to the market, and its history of independent behaviour

132. National has been a vigorous and effective competitor in all the relevant markets. However, National does not fit the criteria of a “maverick” competitor. It cannot, for example, be distinguished from the other four major providers by a history of aggressive behaviour, a record of superior innovation, a growth rate exceeding that of the market or a history of independent behaviour. In addition, in ANZ’s view, it is not significant in a competition sense that National is not an Australian bank.

133. In Decision 495 (Brambles’ Application to acquire the business and assets of GE Capital Returnable Packaging Systems) the Commission concluded that the proposed acquisition would have eliminated a maverick competitor whose activities provided a useful constraint on the two remaining providers, both of whom were vertically integrated. In contrast, after the proposed acquisition, four major providers (who are not vertically integrated) will remain, in addition to the other providers who supply each of the relevant markets.

Conditions of expansion

17. Which conditions do you consider would be likely to act as a barrier to the expansion of existing competitors, where they have the incentive do to so in response to a sustained effort by the merged entity to raise price or to lower service quality or product quality?

Please provide evidence, where available of expansion by existing competitors in the relevant markets during the past five years

Introduction

134. There are no material barriers to expansion in the relevant markets. Faced with an increase in price by ANZ (post acquisition) or a decrease in quality of service in any of the relevant markets, an existing participant could expand its market share so as to constrain ANZ.

135. Evidence of the lack of material barriers to expansion in the various markets is evidenced by:

(a) ASB’s national expansion strategy, in place since 1991, which has included the establishment of 30 new branches and business line diversification into commercial and rural banking, managed funds, life insurance and stock broking[22];

[22] ASB’s growth is based around its very strong position in Auckland, a strong Australian parent in the Commonwealth Bank of Australia, a strong and recognisable brand, a recognised position as the leader in the use of technology in the banking industry and strong performance in terms of customer satisfaction (KPMG *Financial Institutions Performance Survey* 2003 page 20).

(b) Rabobank's expansion in the rural market to the point where it has market share of up to **[ ]**. KPMG, in its 2002 Financial Institutions Performance Survey, stated:

> "Rabobank has consolidated its position in the rural sector and continues to grow its share of the rural product market. Rabobank achieved significant growth in its rural and equipment finance business through its customer focused, and knowledge driven strategies"[23];

(c) in the mortgage market, AMP Bank Limited began operations in 1998 and grew its mortgage portfolio, commercial property portfolio and rural portfolio to $1,919 million, $509 million and $191 million respectively before selling them earlier this year;

(d) CBA's expansion following its entry into the institutional markets in June 2000 to the point where it has relationships with 90 of the top 200 companies in New Zealand and total assets of $876 million;

(e) Kiwibank's entry into the retail banking market in 2002, growing its customer base to 135,000 by the end of May 2003[24]; and

(f) Superbank's entry into the retail banking market earlier this year.

136. Details of the potential for expansion in each of the relevant markets are set out below.

Institutional corporate market

137. There are no material barriers to expansion in the institutional corporate market. An institutional customer is unlikely to retain only one provider as its bank. From a prudential management perspective, institutional customers are likely to use a panel of banks and therefore, have a number of existing bank relationships both in New Zealand and overseas. All providers offer similar products and customers can easily determine the interest rates being charged in the market. As a result, the cost of switching banks is low and the interest rates between the providers fall within a narrow range.

138. The lack of material barriers in the institutional corporate market is evidenced by the growth of CBA in the last three years outlined at paragraph 135(d) above.

139. Accordingly, faced with a sustained effort by ANZ (post acquisition) to raise prices (in the form of interest rate rises and/or fees) or to lower service quality or product quality, customers will quickly switch providers and existing providers will expand their market share in this market.

[23] KPMG *Financial Institutions Performance Survey* 2002 page 18.

[24] Kiwibank press release entitled "Kiwibank launches low interest MasterCard" dated 23/5/03

Middle corporate market

140. There no material barriers to expansion in the middle corporate market. Relationships are important in this market and the provider and customer are likely to meet several times a year and talk on the telephone at least once a month. The relationship between the provider and the customer provides:

(a) the provider with detailed knowledge of the customer's business, its history and its likely future, which allows the provider to make a more accurate assessment of the risk profile of that customer; and

(b) the customer with the certainty and knowledge that the provider understands its business.

141. Despite the importance of a relationship, from a customer's perspective, price is paramount. While a customer would face some cost and inconvenience in switching providers, customers readily incur this to obtain a better price. In any event, all banks are aware that anti-competitive behaviour may result in switching when customers' existing arrangements come up for renewal.

142. Customers are most likely to reassess their banking relationship when a "relationship event" (e.g. a change in relationship manager) occurs. When a relationship event occurs, a customer is likely to put its banking contract out to tender. The major switching "cost" faced by a middle corporate customer is the disruption associated with re-educating a new relationship manager should that customer change banks. However, in ANZ's view, this switching cost is low. Evidence of the low switching cost is provided by the approximately **[ ]** of customers in this market who tender their banking contracts each year.

143. From a provider's perspective, the cost associated with expansion principally involves the time spent in researching and understanding a new customer's risk profile. These costs do not provide a barrier to expansion. The entry and expansion of ASB and AMP Bank Limited (until it sold its book earlier this year) illustrate the ability for existing providers to expand in the middle corporate market.

144. Accordingly, faced with a sustained effort by ANZ (post acquisition) to raise price or to lower service quality or product quality, customers are likely to switch providers and existing providers are likely to attempt to expand their market share in this market.

Credit card issuing market

145. There are no significant barriers to expansion in this market. All existing providers supply products that are well branded and internationally or locally recognised. A customer wishing to switch credit card providers would incur no switching costs. Many credit card applications can be completed without a customer needing to access a physical location and without any application fee. Therefore, faced with a sustained effort by ANZ (post acquisition) to raise prices or to lower service quality or product quality, existing providers are likely to expand their market share in this market.

Mortgage market

146. There are no material barriers to expansion in the mortgage market. ASB's successful expansion of its services beyond its traditional core Auckland market is evidence that barriers to entry in this market are low. 15.2% of all mortgages are provided by providers

other than major banks, which illustrates that consumers are willing to use non major bank providers to source mortgage products. The growth of mortgage brokers has also reduced the barriers to expansion in this market. Given the increasing use of the internet by consumers, there is considerable effort by non bank providers (such as brokers) to expand their operations if the bank providers increased their prices.

147. A customer wishing to switch finance providers may face all or a combination of the following costs:

(a) the legal costs associated with discharging an existing security and registering a new security;

(b) the legal costs of preparing new loan documentation;

(c) application fees for a new loan; and

(d) if a loan is a fixed rate loan, break costs associated with early termination.

148. However, in ANZ's view, none of these costs in isolation or collectively amount to a significant switching cost. Accordingly, faced with a sustained effort by ANZ (post acquisition) to raise prices or to lower service quality or product quality, existing providers are likely to expand their market share in this market.

Rural market

149. There are no material barriers to expansion in this market. As noted above, Rabobank has expanded in this market to the point where it has up to **[ ]** market share in the Southland region and an overall market share of **[ ]**. Also AMP Bank Limited grew its rural property finance banking portfolio from zero to $191 million in four years before selling it earlier this year. Faced with a sustained effort by ANZ (post acquisition) to raise prices or to lower service quality or product quality, existing providers such as Westpac, BNZ, ASB and Rabobank are likely to expand their market shares in this market.

SME market

150. There are no significant barriers to expansion in the SME market. The SME market is driven primarily by relationship. Although the ACCC has previously bundled deposits, transactions and debt financing into one SME market, ANZ has considered the barriers to expansion for each product in the SME market.

Deposits

151. There are no barriers to expansion in the deposit segment. Customers can and do switch providers easily and at little or no cost. Information on deposit rates is readily available. For example, call rates are published every day in major newspapers, in bank branches and on bank websites. Further, it does not cost a customer to switch deposits once the deposit has matured. While there maybe a switching cost during the term of a deposit, the rate offered on that term deposit is fixed. That is, the rate was locked in at the time the deposit was entered into. Accordingly, competition between banks is for new or renewing customers. Given that there is competition for new term deposit customers, post acquisition, ANZ will not have the ability to decrease returns for existing deposit customers.

152. Increasingly, SME customers are becoming more sophisticated and are shopping around for attractive term deposit rates. Indeed, there is an increasing trend for SME customers to tender for deposit products. These tender markets are very competitive.

153. On the supply side, there are no capacity constraints on a provider taking deposits. Further, a provider will become quickly aware if its deposit price is out of line with the market. In fact, a provider's deposit book can be substantially affected by pricing decisions in as little as a week[25]. In addition, technological advances made in relation to e-commerce and online banking will enable direct response and internet banks such as Bankdirect to expand. These companies have successfully expanded their operations in both Australia and Canada.[26]

Debt / financing

154. There are no material barriers to expansion in the debt / financing segment of the SME market. On the customer side, the only costs faced by a customer to switching provider during the course of a debt / financing relationship are the costs identified in paragraph 151 above. However, it is not uncommon for a provider attempting to attract a SME customer to pay that customer's early termination fees and, in any event, ANZ does not believe these costs are significant.

155. On the supply side, there are no material barriers facing an existing provider wishing to expand its debt / financing share. The only limitation faced by an existing provider would be that provider's own internal prudential limits. While a provider would have to make an assessment as to the risk associated with a certain lending transaction, there is no barrier to that provider taking that risk.

156. The lack of barriers to expansion is evidenced by AMP Bank Limited growing its property finance assets portfolio to $1,919 million before it sold its portfolio earlier this year.

Transactions

157. There are low costs to expansion in the transactions segment of the SME market. Due to the nature of transactional banking, from a customer's perspective, there is an inconvenience cost associated with switching providers. However, this inconvenience is not so large as to allow ANZ (post acquisition) to impose a small but significant non-transitory increase in price without invoking a reaction from both its customers and other providers.

---

[25] For example, a promotional five month strategy launched by ANZ on 27 June 2003 generated **[ ]** inflows in one week compared with the average inflow of **[ ]**over the previous four weeks.

[26] Allens Consulting Group: *Trends in the Financial Services Sector 2003* page 10.

158. On the supply side, post acquisition ANZ would face branch competition from at least two other banks in every local area where an aggregation of branches would occur post acquisition. As a result, these existing providers would face no material barrier to expanding their transactional business. In addition, providers who do not have existing branch networks can provide transactional services by either:

(a) engaging another provider to 'white label' transactional services. For example, HSBC provides transactional services using Westpac's existing network; and

(b) using other agencies as a collection point. For example, Kiwibank's use of New Zealand Post outlets (though not in the SME context at this stage).

Merchant acquiring services

159. Any other party may provide merchant acquiring services, provided that:

(a) in relation to the processing of credit card transactions, they are licensed to do so by the relevant card issuing agency;

(b) in relation to the processing of debit card transactions, they are a participant in the ISL payment system (see paragraphs 17-19); and

(c) they have an agreement with a switch provider (currently either ETSL or ANZ) for the switching of the transactions.

160. Although there are currently only two switches, any provider could operate its own switch. For example, ANZ elected to operate its own switch rather than be part of the ETSL system. A provider could set up its own switch. Alternatively, a provider could have an arrangement with a provider operating a switch in another country (e.g. First Data Resources Limited, which is a United States company with a subsidiary company based in Australia), in which case the cost would be less. Switch providers may also need to meet certain minimal technical standards set by the credit card issuing agencies before being permitted to switch those agencies' credit card transactions.

161. Therefore, faced with a sustained effort by ANZ (post acquisition) to increase prices, existing providers are likely to expand their market share in this market.

Personal loans market

162. There are no material barriers to expansion in this market. Providers compete for new customers and that competition sets the charges (interest and fees). However, once a customer has entered into a personal loan arrangement, the provider does not then differentially price against a potential new customer. Accordingly, the need to continue to attract new customers would constrain ANZ's ability post acquisition to increase prices or reduce service.

163. A customer wishing to switch finance providers may have to pay an application fee. These fees are low, being around $150 or 1% of the average loan balance. Therefore, faced with a sustained effort by ANZ (post acquisition) to increase prices, existing providers are likely to expand their market share in this market.

Term deposit / savings account market

164. As stated above at paragraph 151 in respect of the SME market, there are no material barriers to expansion in this market. Customers increasing use of electronic methods of transacting, the highly transparent nature of deposits rates and low customer switching costs mean that there are no material barriers to expansion. A customer wishing to switch a term deposit product mid term would incur break fees. The only cost a customer would face when switching a non term or a matured term deposit would be any application fees charged by the new provider. Further, in many cases it is not necessary for a depositor to visit a provider to establish a deposit. Deposits can be established remotely via the telephone or the internet.

165. Therefore, faced with a sustained effort by ANZ (post acquisition) to increase prices, existing providers are likely to expand their market share in this market.

Transaction accounts market

166. As stated above at paragraph 157 in respect of the SME market, there are no material barriers to expansion in this market because existing competitors are able to increase their market shares with no material increase in their costs that is not readily recovered by that increase in market share.

167. There are two distinct cost associated with switching transaction accounts. First, there are visible costs such as the need for a customer to pay an establishment fee for the account and to pay fees to set up new automatic payments and direct debit authorities. ANZ considers that these costs are low. For example, the cost to set up an automatic payment is around 30 to 35 cents but there is often no charge. Secondly, and perhaps more importantly, in addition to the direct tangible fees set out above there is an inconvenience cost associated with switching providers. However, in ANZ's view, these costs are not so large as to allow ANZ (post acquisition) to impose a small but significant non-transitory increase in price without invoking a reaction from both its customers and other providers.

18. Please name any business which already supplies the market- including overseas firms- which you consider could increase supply of the product concerned in the geographic market by diverting production into the market (e.g. from exports), increasing utilisation of existing capacity or expansion of existing capacity

Introduction

168. All existing providers could increase their supply to (and market share of) each of the relevant markets. In addition to the four major banks, specific examples of existing providers that could increase their supply of products to the credit card issuing market and the rural market are set out below.

Specific examples

Credit card issuing market

169. Barriers to expansion are low with all providers supplying products that are well branded, and internationally or locally recognised. American Express and Diners Club account for only a small percentage of the total credit card issuing market (**[ ]** and **[ ]** respectively).

However, their respective positions as international credit card suppliers provides a strong base from which to expand in the event that any New Zealand credit card issuer engaged in anti-competitive conduct. Accordingly, the potential for American Express and Diners to expand in this market would provide a constraint on ANZ (post acquisition). Also, other existing banks with small cards businesses (for example, Citibank, ABN Amro, Deutsche Bank, HSBC) could quickly expand their card issuing should excess profits appear.

Rural market

170. Any of the existing providers in this market could expand capacity in this market.

19. Of the conditions of expansion listed above, which do you consider would influence the business decision in each case to increase supply?

171. All the relevant banking markets are highly competitive. Any increase in price or a decrease in the quality offered by one provider in any one market would encourage an existing provider to immediately expand its supply in that market.

20. How long would you expect it to take for supply to increase in each case?

172. The banking industry is mature. From the supply side there is no time delay to meet demand.

21. In your opinion, to what extent would the competitive response of existing suppliers constrain the merged entity?

173. Despite ANZ's post acquisition market share in the relevant markets, ANZ would be significantly constrained by competitive response from existing suppliers. To this end, ANZ notes the Court of Appeal's statement in *Commerce Commission v Southern Cross Medical Care Society* [27] that:

> "[w]hatever the size of the merged entity's market share, it is elementary that its market power will not be insufficiently [*sic:* sufficiently] constrained unless there are barriers to entry or expansion which protect it from effective rivalrous reaction to the exercise of its market power."

and:

> "What level of market power a firm has, as a result of its market share, will depend substantially on the level of barriers to entry and expansion which apply to the market. If the barriers are low, a high market share is unlikely to result in an insufficiently constrained level of market power."

174. As outlined above, existing providers in the relevant banking markets face no significant barriers to expansion. Accordingly, in ANZ's view, post acquisition it will face significant constraint in all relevant banking markets.

---

[27] Court of Appeal 21 December 2001 CA 89/91 at page 39.

22. Looked at overall, and bearing in mind the increase in market concentration that would be brought about by the acquisition, to what extent do you consider the merged entity would be constrained in its actions by the conduct of existing competitors in the markets affected?

175. As stated above, due to low barriers to expansion, the existing highly competitive market and the recognition by competitors that the transaction represents a major market opportunity for them, the competitive response of existing competitors would be a significant constraint on ANZ (post acquisition) .

Coordinated market power

23. Identify the various characteristics of the market that, post acquisition, you consider would either facilitate or impede coordination effects

176. In its Practice Note on section 47, the Commission identifies a number of factors which are likely to be conducive to collusion. Of those factors, only two are relevant to the current application: high seller concentration and industry associations. The high seller concentration in these markets has been discussed previously under the heading existing competition. Industry associations are discussed below.

177. The major banks meet periodically. These meetings involve discussions on collective issues that face the New Zealand payments industry as a whole such as increasing processing efficiencies, reducing systematic, operational and settlement risks, system changes, rule changes and Reserve Bank and global central bank initiatives.

178. These issues impact (either directly or indirectly) across the industry payment switches. All the major providers have a vested interest in ensuring that the New Zealand financial systems are systematically safe and operationally efficient. Discussions at a cooperative level with other banks and regulators ensure this.

24. Identify the various characteristics of the market that, post acquisition, you consider would either facilitate or impede the monitoring and enforcement of coordinated behaviour by market participants

179. As above. Coordinated market power cannot survive in markets that are characterised by lively competition and low barriers to expansion and entry.

25. Indicate whether the markets identified in paragraphs 36 and 37 above show any evidence of price coordination, price matching or price following by market participants

180. There is no tacit collusion by providers (through price coordination, price matching or price following). Existing providers must monitor changes in the market to remain competitive. The prices charged by all providers are therefore within a tight range. This is because of strong competition, the highly public nature of these charges, and the similarity of product offerings from different banks.

26. Please state the reasons why, in your opinion, the transaction will not increase the risk of coordinated behaviour in the relevant market(s).

181. Banks are free to compete on price and service and have done so vigorously since de-regulation in the mid 1980s. The acquisition will not increase the likelihood of coordinated behaviour. That is because:

(a) major providers pursue different strategies;

(b) major providers also have different cost structures. These structures change from time to time in line with providers' changing product strategies (see Appendix 6);

(c) some providers have different governance structures (e.g. incorporation versus non-incorporation);

(d) fringe competitors (offering specialised products or targeting niche sectors) are active in all of the relevant markets;

(e) there are no barriers to, and low costs of, expansion for existing providers (who have no real capacity limitations);

(f) there are no barriers to entry, and there are low costs of entry, through for example, utilisation of alternative distribution channels; and

(g) there is elastic demand in respect of a particular provider's products which is aided by the presence of brokers.

182. The Commission has previously considered whether a reduction of competitors from three to two will increase the potential for coordination (Decisions 438, 439, 441 and 495). In two of these decisions (Decision 438 and 495), the Commission considered that a reduction from three to two existing providers would substantially lessen competition and declined to clear the applications. In the other two decisions (Decision 439 and 441), the Commission granted clearance on the basis that the reduction in competitors was outweighed by other competition factors. Post acquisition, in all relevant markets, four of the major providers will remain as well as a range of other providers (from, depending on the market, large to comparatively smaller providers). This, coupled with the factors identified above, suggest that collusion is unlikely to occur as a result of the acquisition.

PART IV: CONSTRAINTS ON MARKET POWER BY POTENTIAL COMPETITION

Conditions of entry

27. Which if any of the conditions identified above do you consider would be likely to act as a barrier to entry of new competitors, where they would otherwise have the incentive to do so in response to a sustained effort by the combined entity to raise price, or to lower service or product quality?

Introduction

183. Potential barriers to, or costs of, entry in markets relevant to this transaction include capital requirements, regulatory requirements, sunk costs and the influence of branding and sales promotion. ANZ outlines the impact of these costs on the relevant markets below. However, ANZ considers that the low barriers to expansion that exist are more important and alone will ensure that it remains constrained post acquisition.

Regulatory barriers

184. New Zealand has relatively low regulatory barriers to entry in the relevant markets. Finance companies, savings institutions and fund managers operate in substantially unregulated markets (unlicensed and subject only to the Securities Act and the Credit Contracts Act and any legislation and Codes of Practice specific to the industry and institution concerned).

185. Registered banks are more regulated. Registration is currently a requirement of ISL membership (see paragraph 191 below). The Reserve Bank prescribes conditions for registration for each registered bank. Those currently applying to ANZ and its financial reporting group ("banking group") are:

(a) Minimum capital requirements

- Minimum capital of $15 million.
- Minimum capital of 8% of risk weighted assets.
- Minimum tier 1 capital of 4% of risk weighted assets.

(b) Other

- The banking group does not conduct any non-financial activities, that in aggregate are material relative to its total activities.
- The banking group's insurance business is not greater than 1% of its total consolidated assets.
- The banking group's aggregate credit exposures (of a non-capital nature and net of specific provisions) to connected persons do not exceed the applicable rating contingent limit set out below:

Credit Rating	Connected Exposure Limit (% of the banking group's tier 1 capital)
AA/Aa2 and above	75

AA-/Aa3	70
A+/A1	60
A/A2	40
A-/A3	30
BBB+/Baa1 and below	15

The credit rating is the rating applicable to the ANZ's long-term senior unsecured NZ dollar obligations (currently AA-). Within this rating contingent limit, credit exposures to non-bank connected persons must not exceed 15% of the banking group's tier 1 capital.

- Exposures to connected persons are not on more favourable terms (e.g. as relates to such matters as credit assessment, tenor, interest rates, amortisation schedules and requirements for collateral) than corresponding exposures to non-connected persons.
- The board of ANZ contains at least two independent directors (i.e. not employees of ANZ, and not directors, trustees or employees of any holding company of ANZ or any other entity capable of controlling or significantly influencing ANZ).
- The chairperson of the board is not an employee of ANZ.
- The constitution of ANZ does not permit directors to act in the interests of any holding company of ANZ where to do so would conflict with the interests of ANZ or its creditors.
- A substantial portion of ANZ's business is conducted in and from New Zealand.

186. KPMG considers that these regulatory requirements are not material barriers to entry.[28] This is evident from the recent entry of Kiwibank and Superbank.

The New Zealand payment system

187. Certain conditions must be met to enter the New Zealand payment system. The barriers to entry into the lower value payment system have been reduced by agency relationships and licence agreements with existing providers. ANZ considers that there are no material barriers to entry into the higher value payment system.

Lower value payments

188. The New Zealand payment system comprises a series of different entities. Lower value payments (such as retail transactions, cheques, direct debits, direct credits, automatic payments and ATM transactions) are processed through the ISL or through the ANZ or ETSL systems.

ISL

189. The lower value bank transactions taking place on any day are processed by ISL between 12.15 am and 8.30 am the following day. ISL produces a bilateral settlement report that balances these transactions.

190. As stated previously, ISL is owned collectively by 9 registered banks. To become a member of ISL, a provider must be a registered bank (registered banks have exchange

[28] *Preliminary report for ANZ on New Zealand Banking Industry*, 6 May 2003, pages 23-24.

settlement accounts with the Reserve Bank and are members of the New Zealand Bankers Association). ISL is a cost recovery company.

191. It is not necessary to join ISL (i.e. become a registered bank) to participate in the lower value payment system. Agency relationships and license agreements enable non bank financial institutions to gain access to this system. For example:

(a) PSIS and Superbank have agency relationships in place with participating banks (Westpac for both) that enable them to take advantage of these systems through the registered member bank (and their bank number); and

(b) Kiwibank has a user licence agreement with ISL. As a licensee, Kiwibank must pay an annual licence fee and a fee that varies depending on the volume of transactions it generates. Kiwibank was also required to meet the costs of adding an additional banking number to the ISL system.

192. ISL's constitution provides that if one bank becomes a shareholder or a subsidiary of another bank, then the shares of each are treated as combined. The effect of this is that the combined shareholders only have one vote and also the right to appoint only one director.

ANZ/ETSL Systems

193. As stated above, there are two systems available in New Zealand for the interchange and clearance of EFTPOS and credit card transactions: the ETSL system and ANZ's system. If an ANZ customer purchases a product from a Westpac retailer with a Westpac account, that transaction must be processed through both the ANZ and ETSL switches. If the situation was reversed and the retailer was an ANZ customer and the buyer a Westpac customer, again, the transaction would have to be processed through both switches. Accordingly, in any transaction that involves ANZ and another bank as payer or payee bank, both ETSL and ANZ systems will be utilised. Because each system must interrelate with the other, both ETSL and ANZ charge 6.75 cents per transaction processed on behalf of the other through their respective systems.

194. Although there are currently only two switches, any provider could operate its own switch. For example, ANZ elected to operate its own switch rather than be part of the ETSL system. A provider could set up its own switch or have an arrangement with a provider operating a switch in another country (e.g. First Data Resources Limited, which is a United States company with a subsidiary company based in Australia).

Higher value payments

195. High value transactions (or wholesale transactions) are processed in a real time gross settlement environment. There are two key systems.

(a) **Austraclear** is a settlement system for the transfer of securities and their proceeds between Austraclear members in New Zealand and overseas. Membership is available to any institution (domestic or foreign) that, in the RBNZ's opinion, is of good standing and has the necessary resources to meet its obligations as a member. There are currently 232 members in New Zealand and Australia. These include banks, financial institutions, investment managers (such as TOWER, AMP and AXA), share brokers and custodians.

(b) The **Same Day Cleared Payment (SCP)** system is a payment service facilitated by the RBNZ using the Exchange Settlement Account System (**ESAS**)/SWIFT (Society for Worldwide International Financial Telecommunications) interface.

SCP permits providers to transfer irrevocable New Zealand dollar transactions within New Zealand. Details of the transfer are communicated by way of the SWIFT network. The transfer is then settled from the participant's ESAS account. As a result, all providers in the system must have an ESAS account and be a member of SWIFT.

Currently all ESAS account holders are registered banks. However, access rules permit other organisations meeting certain criteria to have accounts as well. These criteria include that the applicant falls within the definition of "financial institution" for the purposes of the Reserve Bank Act 1989, that providing access to the applicant would not detract from the soundness or efficiency of the financial system, that there is a legitimate business interest to be served by granting access to an ESAS account and that the provision of an account would not adversely affect the reputation of the Reserve Bank.

Any organisation will be considered for membership of SWIFT provided that it is involved in the same type of business as the other members and is involved in international financial message transmission. There are different categories of membership, each of which may have additional eligibility criteria attached to them. There are currently over 7000 members in 199 countries around the world. These include banks, broker/dealers and investment managers.

Financial institutions that do not hold an ESAS account or are not members of SWIFT are able to access the SCP system by way of agency relationships with registered banks.

196. ANZ believes that there are no material restrictions on access to this high value payment arena.

Institutional corporate market

197. For the reasons stated above (paragraphs 195-196), besides the regulatory conditions described above, there are no material barriers to entry in this market.

Middle corporate market

198. There are no material barriers to entry in the middle corporate market. As stated above, the middle corporate market is dependent on relationships. Accordingly, a new entrant would need to establish a team of relationship managers to develop a presence within this market. However, as stated above, from a customer's perspective price is paramount, which means that no significant part of the market is foreclosed to a potential entrant.

199. From a provider's perspective, the cost associated with entry into this business involves time spent on researching and understanding a new customer's risk profile. However, this does not amount to a barrier to entry. It merely increases the potential cost associated with attracting a customer. The entry of BNP into this market shows that knowledge of New Zealand's risk profiles does not amount to a barrier to entry.

Credit card issuing market

200. There are few barriers to entering this market. New entrants may either negotiate with a credit card agency (such as Visa or MasterCard) to issue their own credit cards, or may do so in association with an existing card issuer. For example, the Warehouse and Kiwibank each offer a credit card in conjunction with Westpac. The fact that credit card applications can now be done remotely via the telephone or the internet also makes entry into this market more simple. A local network is not a pre-requisite to entering this business.

Mortgage market

201. New entrants face low barriers to entry in offering home loans to customers. Barriers to entry are low because:

(a) A relatively efficient capital market (via securitisation) exists. This means that if a product provider sought to increase prices or reduce quality, new entrants could provide mortgages funded via the capital market serviced by an existing participant. This would be relatively easy to achieve given that most banks have excess capacity in relation to core processing and there are options for servicing out of Australia. Aussie Home Loans pursued this strategy in the mid 1990s, and independent originators are also present in New Zealand.

(b) Alternative distribution channels exist such as via mortgage brokers or through the use of the internet. BankDirect is an example of a financial institution that has utilised the internet.

202. There are processing costs involved in administering mortgages. In addition, it is beneficial to have economic mass in terms of the volume of portfolio and sales to positively fund the infrastructure needed to administer the mortgages. However, a third party administrator (such as Baycorp) could be used to provide these services, allowing a new entrant to avoid the cost of establishing its own administration systems.

Rural market

203. There are low barriers to offering debt/deposit products, although some customers may find it more difficult to transfer their business if their assets are secured because legal fees will be incurred in changing the securities. Other issues may arise in relation to transactional banking if alternative physical outlets are not present in the local market. However, in recent times there has been a rapid increase in the use of mobile sales forces, who will visit anyone regardless of location. Access issues can also be overcome through other banking channels such as ATMs and telephone and internet banking, meaning that customers are no longer as reliant on physical locations.

SME market

204. In ANZ's view, a "greenfield" entrant that wished to replicate the incumbent banks' branch networks nationwide would face significant costs to enter. These costs could be prohibitive due to the competitive nature of the market. However, a physical branch network is not a necessary condition for entry. Entry by establishing agencies is a cost effective and internationally recognised method of entry.

205. As outlined above, the entry of Kiwibank (through NZ Post) and Superbank (through Foodstuffs outlets) is evidence of this method of entry. This method of entry considerably

lowers network costs. However, a new entrant would still need to find an agency that would have branches in a sufficient number of towns across New Zealand. For example, an agency such as Public Trust has branches in most local centres in New Zealand. Alternatively, petrol stations and other large national merchants may provide a viable solution.

206. In any event, a niche participant could enter one section of the market and leverage off an existing participant's branch network. For example, HSBC competes in the SME market by providing transactional services through Westpac Trust. There is no barrier to stop another niche entrant from establishing a similar relationship with another major bank.

207. Any provider can supply merchant acquiring services via arrangements with ANZ or ETSL provided that they are licensed by the relevant credit card issuing agencies and are participants in the ISL payment system. It is also possible for any provider to set up its own switch (see paragraphs 193-194).

Personal loan market

208. In Decision 461, the Commission concluded that:

> "… existing competition from other finance companies, banks and credit card issuers in the consumer finance market is sufficiently robust to constrain the merged entity."[29]

209. Further, the Commission concluded that:

> "… there are no significant barriers to entry likely to deter expansion or new entry. Potential competition, in addition to the strength of existing competition…is likely to provide constraint on the merged entity, and the industry as a whole."[30]

210. Post acquisition, ANZ will still be constrained by existing providers in this market because barriers to expansion are low.

Term deposit / savings account market

211. The importance of the branch network in this market is declining. The fact that new entrants such as Kiwibank and Superbank can establish a business without investing in a branch network are evidence of this. Both of these banks are able to provide services via a third party's retail outlets. Also, they rely on the fact that more and more customers are using the internet or telephone to invest money in term deposits and savings accounts.

212. The increasing use of the internet and telephone banking to conduct term deposit and savings account transactions would reduce the costs of entry and potentially extend the geographic scope of the market.[31]

---

[29] Decision 461, paragraph 132.

[30] Decision 461, paragraph 191.

[31] KPMG *Financial Institutions Performance Survey 2003*, page 36

Transaction accounts market

213. The same factors discussed above in paragraphs 204-207 in relation to the SME market apply to the market for transaction accounts.

28. Please name any businesses (including overseas businesses) which do not currently supply the market but which you consider could supply the relevant market(s) by investing in new production facilities to produce the product, overseas companies diverting production to New Zealand or domestic companies expanding, or changing the utilisation of, existing capacity to produce the relevant products (where this would involve substantial new investment).

214. Existing overseas banks such as Bank of America, Standard Chartered, Hang Seng, Halifax Bank of Scotland, Royal Bank of Scotland and Bank of Tokyo, could offer the full suite of services across all these markets. In addition, there are any number of potential entrants that could enter individual markets or individual segments of markets. The entry of CBA into the institutional market, Rabobank into the rural market and St. George Bank into retail banking markets is evidence of this.

29. What conditions of entry do you consider would most influence the business decisions to enter in each case?

215. As discussed above, barriers to entry in the relevant markets are low. Further, all the relevant banking markets are highly competitive. Accordingly, the key factor that would influence a decision to enter the relevant markets is price and quality of service. Any market opportunity presented by existing providers either increasing price or a decreasing the quality of their products would encourage other providers to enter that market.

Likelihood, sufficiency and timeliness of entry

How long would you expect it to take for supply to increase in each case?

216. As stated in its *Practice Note 4*, the Commission:

> "…considers that, for most markets, entry which cannot be achieved and have a significant effect within two years from initial planning is unlikely to be sufficiently timely to alleviate concerns about market power".

217. As stated above, in ANZ's view barriers to expansion are low in all the relevant markets. This is evidenced by the entry and subsequent expansion of various providers in the relevant markets. For example:

(a) Kiwibank was registered as a bank in November 2001 and opened its first pilot branches in February 2002. In the 18 months since registration, Kiwibank has expanded to the point where it has approximately 280 branches nationwide.

(b) Superbank has entered personal banking markets after being registered as a bank on 3 February 2003.

(c) In SME banking, AMP Bank Limited entered the market in October 1998 and expanded its banking activities until it sold off its residential property and rural and commercial property books earlier this year. By purchasing AMP Bank's commercial property book, GE Finance has entered the SME business product market.

(d) In the institutional corporate market, CBA entered the market in June 2000 and expanded in its first year to the point where it had total assets of NZ$881 million.

218. The examples listed above demonstrate that the relevant markets are fluid and dynamic. Entry and expansion decisions can be made and acted on quickly and certainly within the Commission's two-year time frame.

Given the assessed entry conditions, and the costs that these might impose upon an entrant, is it likely that a potential entrant would consider entry profitable at pre-acquisition prices?

219. The history of entry and expansion in the relevant markets illustrates that a potential entrant into any of these markets is likely to conclude that entry at pre-acquisition prices is profitable. Further, given the low barriers to entry, in the unlikely event that ANZ (post acquisition) attempted to raise prices in any of the relevant markets, it is almost certain that potential entrants would view market entry as profitable. As a result, this threat of entry provides a constraint on ANZ post acquisition.

Would the threat of entry be at a level and spread of sales that is likely to cause market participants to react in a significant manner?

220. The banking industry is already highly competitive. Existing players are unlikely to be able to change their behaviour in response to entry by a new competitor.

What conditions of entry would influence the business decision to enter the market by setting up from scratch?

221. A de novo entrant in personal, rural and SME markets would consider the need to establish a physical distribution system as a key influence. However, as discussed above, the costs associated with establishing such a physical distribution network have declined and did not amount to barriers to entry for Superbank or Kiwibank.

How long would you expect it to take for de novo entry to occur?

222. As evidenced by Kiwibank and Superbank in personal banking markets, AMP Bank Limited and GE Finance in SME markets and CBA in Institutional banking markets, de novo entry can occur quickly and certainly within two years.

To what extent would the possibility of de novo entry constrain the merged entity?

223. As discussed at paragraphs 131-136 above, current market conditions dictate that, post acquisition, ANZ would be significantly constrained by existing competition from other major bank providers and smaller niche operators in various segments of the relevant markets. Further, ANZ (post acquisition) would be constrained by corporate customers' countervailing power. In the mortgage market ANZ would also be constrained by the existence of mortgage brokers. As a result, ANZ is likely to consider de novo entry as a constraint post acquisition although to a lesser extent in this case because of the already high levels of constraint which will be imposed by existing competitors and their ability to expand.

PART V: OTHER POTENTIAL CONSTRAINTS

The conduct of suppliers

36. Who would be the suppliers of goods to the merged entity in each market?

224. No suppliers exercise any material constraint on ANZ.

37. Who owns them?

225. Not applicable.

38. To what extent would the conduct of suppliers of goods to the merged entity constrain it in each affected market?

226. Not applicable.

The conduct of acquirers

39. Who would be the acquirers of goods to the merged entity in each market?

Introduction

227. ANZ is constrained by acquirers in both the high value and low value / retail markets in which it operates. Of particular significance in the low value / retail markets is the Code of Banking Practice (the **Code**), the provisions of which ANZ has agreed to observe. This Code sets out a formal process which consumers can invoke if they are dissatisfied with the handling of a complaint. Details of this process and the effect of acquirers on ANZ in each the relevant markets are set out below.

Code of Banking Practice and the Banking Ombudsman

228. The Code sets out the minimum standards of good banking practice to be observed by member banks of the New Zealand Bankers' Association.

229. ANZ's product terms and conditions are drafted to be consistent with provisions of the Code. Therefore, a breach of the Code will usually result in a breach of these terms and conditions, and vice versa. The Code is monitored by the Banking Ombudsman through complaint investigations. The Banking Ombudsman has the ability to award costs and compensation for breaches of the Code that fall within her jurisdiction. It is also possible (although currently untested) that the courts would treat the Code as evidence of good banking practice.

230. By subscribing to the Code, ANZ offers a free, three-stage complaints review procedure for handling complaints under $100,000 about its product or services. This process is as follows:

    (a) ANZ will undertake an initial review according to its own internal complaints review procedure.

(b) If the customer remains dissatisfied after being advised of ANZ's decision about the complaint, ANZ must inform the customer that he or she may refer the complaint to the Banking Ombudsman for further consideration, and inform the customer how to do so.

(c) The Banking Ombudsman may then independently review the complaint and may, where appropriate, facilitate the satisfaction, settlement or withdrawal of the complaint, whether by agreement, making recommendations or awards or by any other means that seem expedient.

231. The Code and the Banking Ombudsman increase the transparency of member banks' operations and reduce the power imbalance between large banks and small customers.

Institutional corporate market

232. Post acquisition, ANZ is likely to face strong countervailing power from institutional corporates. Institutional corporates are by their nature large and well informed about alternative sources of supply. An institutional corporate could readily switch providers and also, with little difficulty, access a provider outside New Zealand.

Middle corporate market

233. Post acquisition, ANZ is also likely to face strong countervailing power from customers (albeit to a lesser extent than extent than in the institutional corporate market). Corporate customers with turnovers between NZ$10 million and NZ$100 million are likely to be well informed about alternative sources of supply. Further, because switching costs are low, these corporate customers could switch providers easily.

234. In both the institutional corporate market and middle corporate market, customers are generally sophisticated enough to realise that a high level of competition is in their interests, and would probably act deliberately to ensure this by moving some business away from ANZ (post acquisition) (if encouraged to do so by signs of uncompetitive behaviour).

Credit card market

235. Post acquisition, ANZ is likely to face strong countervailing power from customers. Once customers have paid off the balance on their credit card, they can readily switch providers without incurring significant costs.

Mortgage market

236. The strong countervailing power of purchasers was recognised in the Bank of Melbourne case. The market evidence indicated that the cost of unbundling was relatively low in this market compared with the potential benefits. In particular, the evidence indicated that refinancing was popular (with more than 20% of new home loans taken out for refinancing purposes) and financial institutions offered loans in geographic markets where they had no branch network.

237. This view is supported by a report prepared by Allens Consulting Group which stated:

> "Another factor driving competition in the home loan submarket is increased consumer awareness of switching opportunities and the best available deals (i.e. looking beyond

> simple headline rates). Consumer awareness of the home loans submarket has also been encouraged by technological advances such as the internet and scrutiny by the media and Government … Price transparency and comparability between home loan providers has changed significantly with independent institutions providing this information freely to consumers.
>
> As these products also allow consumers to choose between the many different banks and the competitive fringe of home loan operators, consumers are easily able to choose the cheapest home loan alternative with fairly insignificant transaction costs. The competitiveness of the home loans sub market is further illustrated by the willingness of households to switch their borrowing to take advantage of the most attractive rates on offer."[32]

Rural market

238. The power of purchasers in this market has increased as a result of the ready availability of information and improved access to products (via alternative distribution channels).

SME market

239. The power of purchasers in this market is increasing as a result of the increased unbundling of financial products and the increasing acceptance and use of online banking by small businesses. In Australia, Allens Consulting has reported that more small businesses have been enticed to change banks because of better performance, rates or overall package.[33] This suggests that there has been a shift away from purchasing services as a cluster, as was the case in the Westpac / Bank of Melbourne and CBA / Colonial decisions.

Personal loans markets

240. In the Westpac / Bank of Melbourne decision, the ACCC found that many consumers unbundled their banking loans from the institution where they acquired most of their other banking services. Many consumers had personal loans and transaction accounts with different institutions. This suggests that consumers have the ability to switch providers relatively easily.

Term deposit / savings account market

241. As for paragraph 239 above.

Transaction accounts market

242. As for paragraph 239 above.

40. Who owns them?

243. Not applicable.

---

[32] Allens Consulting Group: *Trends in the Financial Services Sector 2003* page 13.

[33] Allens Consulting Group: *Trends in the Financial Services Sector 2003* page 13.

41. To what extent would the conduct of acquirers of goods to the merged entity constrain it in each affected market?

244. The banking market is highly competitive. Institutional customers are highly sophisticated. Smaller consumers have access to good, reliable information about banking products. Therefore, ANZ will be constrained by the countervailing power of purchasers post acquisition.

THIS NOTICE is given by ANZ Banking Group (New Zealand) Limited (**ANZ**)

I, Susan Ruth Peterson, General Counsel / Company Secretary of ANZ am authorised to make this application on ANZ's behalf.

I hereby confirm that to the best of my knowledge:

(a) All information specified by the Commission has been supplied;

(b) All information known to the applicant which is relevant to the consideration of this application has been supplied;

(c) All information supplied is correct as at the date of this application.

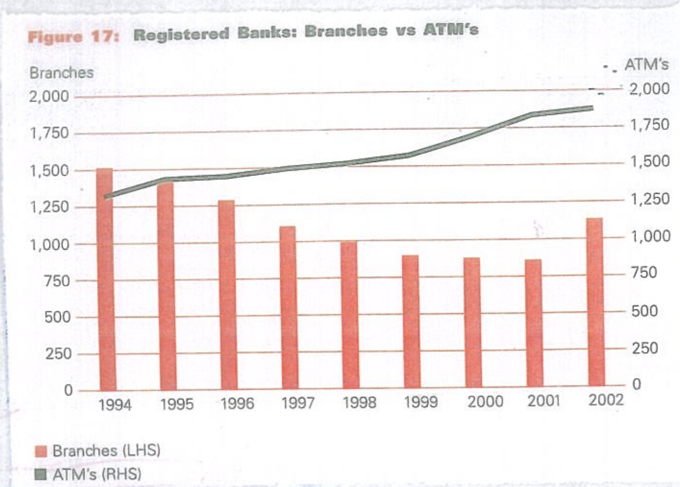
I undertake to advise the Commission immediately of any material change in circumstances to the application.

Dated this day of 2003.

APPENDIX 1 – MARKET TRENDS

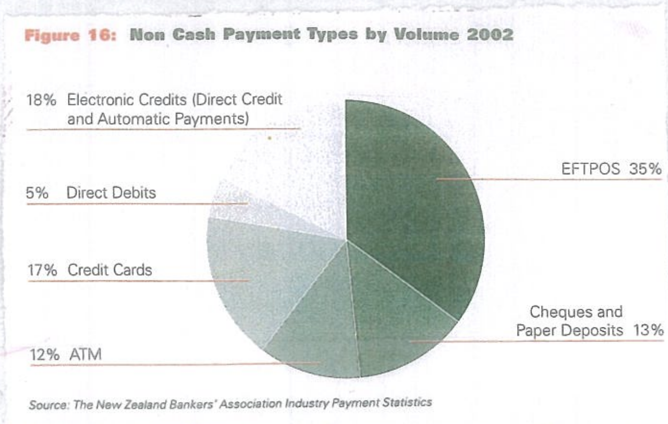
APPENDIX - RECENT TRENDS IN BANKING INDUSTRY

Figure 1 - Registered Banks: Branches versus ATMs



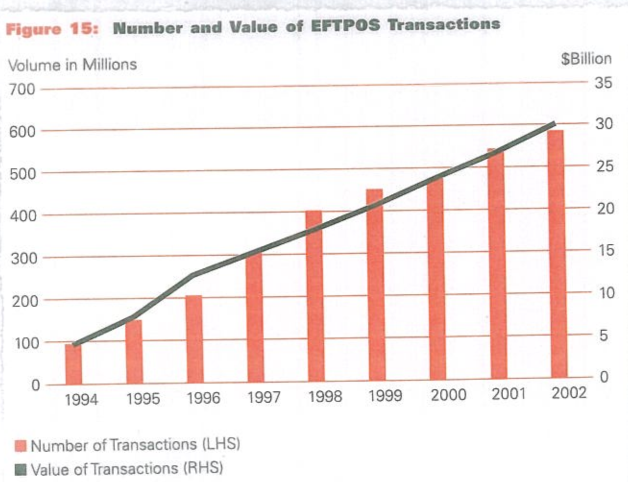
Source: KPMG Financial Institutions Performance survey 2003 page 36

Figure 2 - Cash Payment Types by Volume 2002



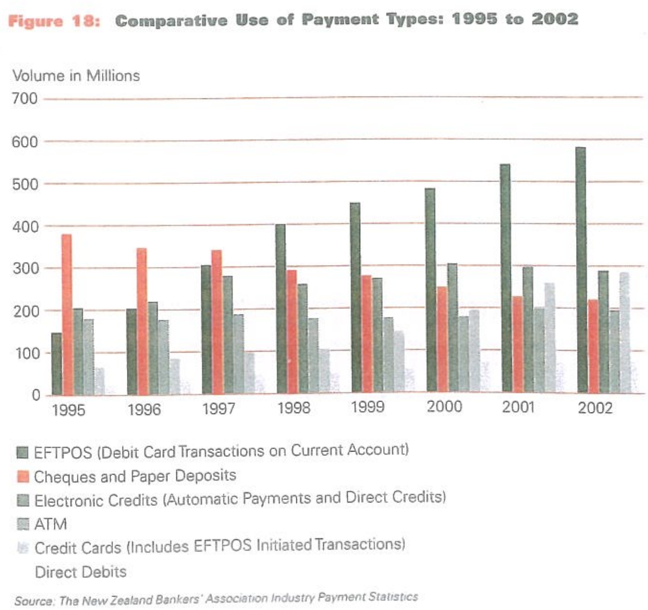
Source: KPMG Financial Institutions Performance survey 2003 page 36

Figure 3 - Growth in EFTPOS Transactions



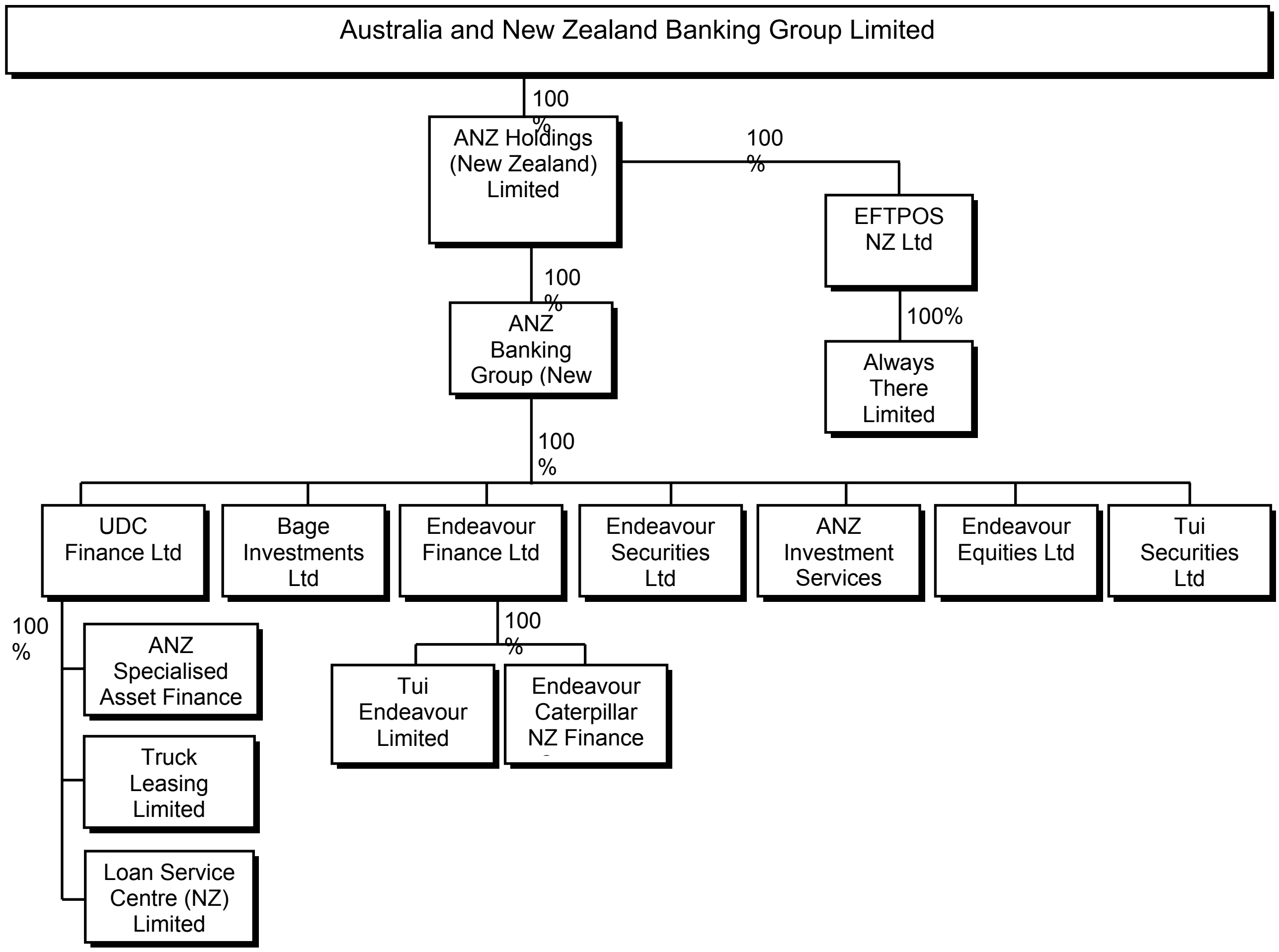
Source: KPMG Financial Institutions Performance survey 2003 page 35

Figure 4 - Trend comparative use of payment types 1995 – 2002

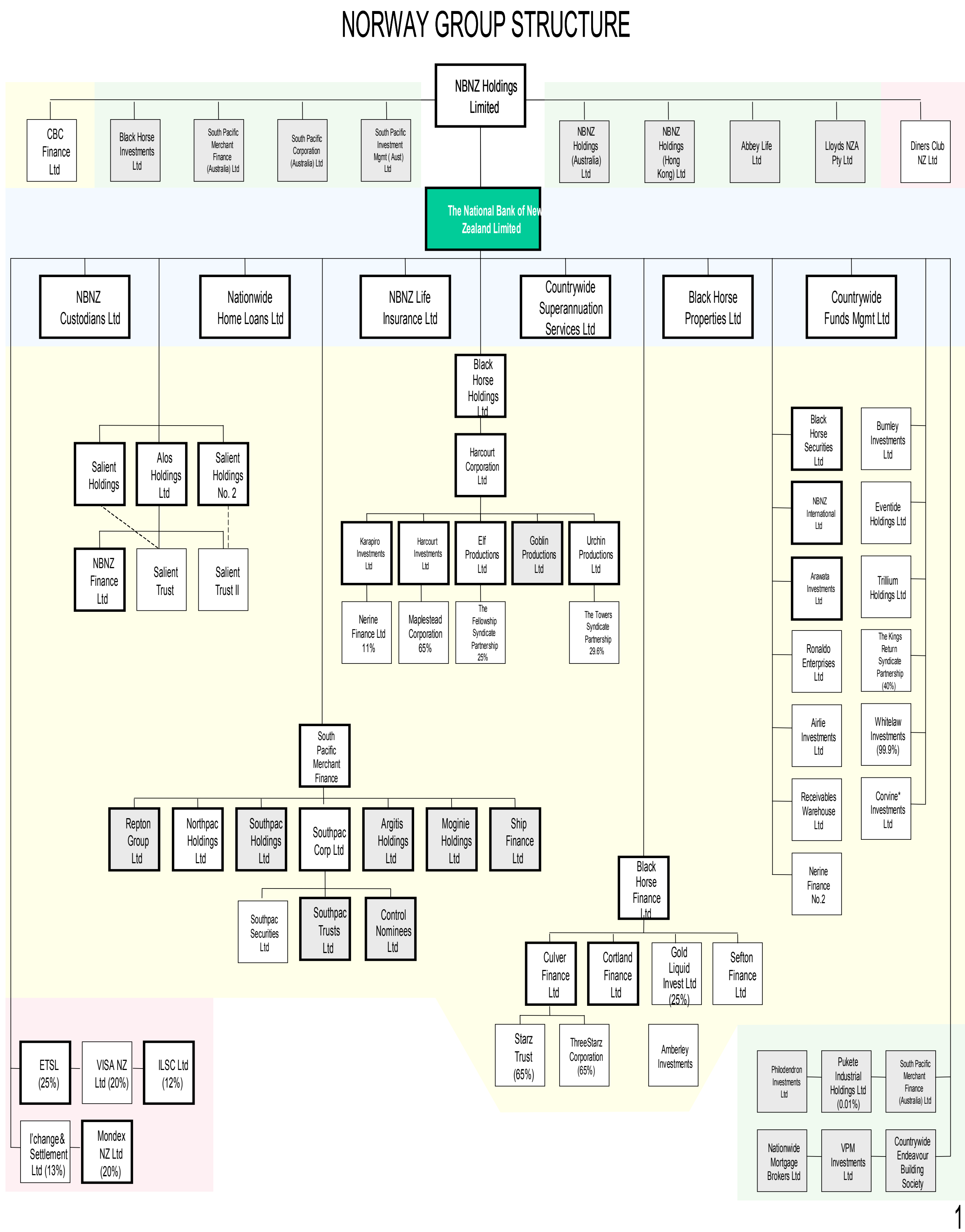


Source: KPMG Financial Institutions Performance survey 2003 page 36

APPENDIX 2 – ANZ GROUP STRUCTURE



APPENDIX 3 – NATIONAL GROUP STRUCTURE



APPENDIX 4 – ANALYSIS OF BRANCH COMPETITION IN LOCAL TOWNS WHERE THERE IS AGGREGATION OF BRANCHES

Market	*Competitors (post acquisition)*	*Number of Foodstuffs outlets*	*Locations*
Alexandra	BNZ, Westpac, Kiwibank	1	Tarbett Street
Ashburton	BNZ, Westpac, Kiwibank	1	Tancred Street (ANZ/BNZ), East Street (National, Westpac, Kiwibank)
Balclutha	BNZ, Westpac, Kiwibank	1	Clyde Street (BNZ, Westpac), John Street
Blenheim	BNZ, Westpac, ASB, Kiwibank	1	Queen Street (Westpac, ANZ), Market Street (ASB, BNZ, National), Main Street (Kiwibank)
Cambridge	BNZ, Westpac, Kiwibank	1	Victoria Street
Dannevirke	BNZ, Westpac, Kiwibank	1	High Street
Dargarville	BNZ, ASB, Kiwibank	0	Victoria Street
Feilding	BNZ, Westpac	1	Either Ferguson Street or Manchester Street
Gisborne	BNZ, Westpac, ASB, Kiwibank	1	Gladstone Road
Gore	BNZ, Westpac	1	Either Mersey Street or Main Street
Greymouth	BNZ, Westpac, ASB (two branches), Kiwibank	1	Tainui Street (BNZ, National, ANZ, Kiwibank), MacKay Street (Westpac, ASB), High Street (ASB)
Hastings (two National branches)	BNZ, Westpac, ASB, Kiwibank	1	Heretaunga Street (ANZ, Westpac, National, Westpac), Queen Street (National, ASB), Russell Street
Havelock North	BNZ, Westpac, Kiwibank	1	Middle Road (National , ANZ), Te Mata Road (BNZ, Westpac), Napier Road (Kiwibank)
Hawera	BNZ, Westpac, TSB	1	High Street (ANZ, Westpac, National), Princes Street (BNZ), Victoria Street (TSB)
Hokitika	BNZ, Westpac,	1	Revell Street (Westpac, ASB, Kiwibank),

Market	*Competitors (post acquisition)*	*Number of Foodstuffs outlets*	*Locations*
	ASB, Kiwibank		Weld Street (BNZ, National)
Huntly	BNZ, Westpac, Kiwibank	0	Main Street
Invercargill	BNZ, Westpac (five branches), ASB, Kiwibank	2	Kelvin Street (ANZ, BNZ, Westpac, National), Esk Street (ASB), Don Street (Westpac, Kiwibank), Elles Road (Westpac), North Road (Westpac), Windsor Street (Westpac)
Kaitaia	BNZ, Westpac, ASB, Kiwibank	1	Commerce Street
Katikati	BNZ, Westpac, Kiwibank	0	Main Street
Kerikeri	BNZ, Westpac, ASB	1	Main Road (ASB, Westpac), Kerikeri Road (ANZ, National, BNZ)
Levin	BNZ, Westpac, Kiwibank	1	Oxford Street
Masterton	BNZ, Westpac, Kiwibank	1	Queen Street (ANZ, BNZ, Westpac), Lincoln Road (National)
Matamata	BNZ, Westpac, Kiwibank	1	Arawa Street (ANZ, BNZ, Westpac, Kiwibank), Broadway (National)
Morrinsville	BNZ, Westpac, Kiwibank	1	Thames Street (ANZ, BNZ, National, Westpac), Sydholme Street (Kiwibank)
Mosgiel	BNZ, Westpac, Kiwibank	1	Gordon Road
Mount Maunganui (two ANZ branches and two National branches)	BNZ, Westpac (two branches) ASB, Kiwibank (two branches)	1	Bayfair Shopping Centre (ANZ, ASB, National, Westpac, Kiwibank), Maunganui Road (ANZ, BNZ, National, Westpac, Kiwibank)
Napier	BNZ, Westpac, ASB, Kiwibank	0	Hastings Street (ANZ, National, BNZ, ASB, Kiwibank), Dickens Street (Westpac)
Nelson	BNZ, Westpac, ASB, Kiwibank (three branches)	1	Trafalgar Street (ANZ, ASB, BNZ, National, Westpac, Kiwibank), Milton Street (Kiwibank), Toi Toi Street (Kiwibank)
New Plymouth	BNZ, Westpac (two branches), ASB, TSB (six	2	Currie Street (ANZ, Kiwibank), Devon Street (Westpac (two branches), ASB, BNZ, National, TSB (two branches)),

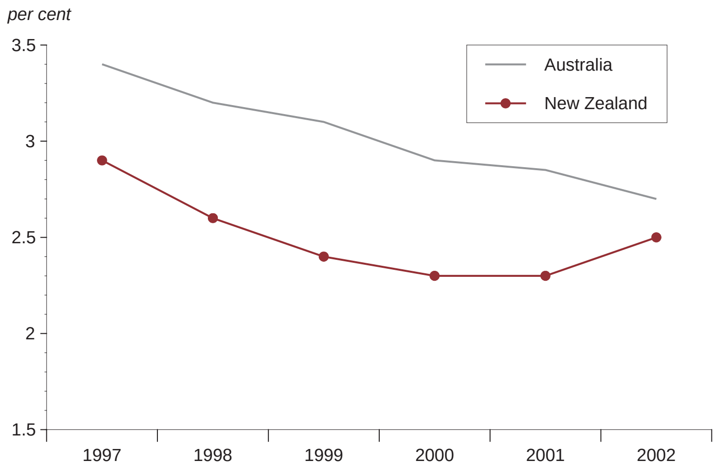
Market	***Competitors (post acquisition)***	***Number of Foodstuffs outlets***	***Locations***
	branches), Kiwibank		Govett Avenue (TSB), St Aubyn Street (TSB), Carrington Street (TSB), Tukapa Street (TSB)
Oamaru	BNZ, Westpac (two branches), Kiwibank (two branches)	2	Thames Street (All), Severn Street (Kiwibank)
Orewa	BNZ, Westpac, ASB	1	Hillary Square (ANZ), Hibiscus Coast Highway (ASB), Main Road (BNZ), Florence Avenue (National), Tamariki Avenue (Westpac)
Otorohanga	BNZ, Westpac, Kiwibank	0	Maniapoto Street
Paeroa	BNZ, Westpac, Kiwibank	0	Princes Street (ANZ, BNZ) Normandy Road (National, Westpac, Kiwibank)
Palmerston North (two ANZ branches, three National branches)	BNZ (two branches), Westpac (five branches), ASB, Kiwibank (4 branches)	3	The Square (ANZ, ASB, BNZ, Kiwibank), K-Mart Plaza (Westpac), Broadway Avenue (BNZ, National, Westpac), Rangitekei Street (BNZ, National, Westpac) Ruahine Street (ANZ, Kiwibank), Broadtop Shopping Centre (Westpac), Church Street (Kiwibank), Matthews Avenue (Kiwibank) Massey University (BNZ, National, Westpac)
Paraparaumu	BNZ, Westpac, ASB, Kiwibank	1	Coastlands
Queenstown	BNZ, Westpac, ASB, Kiwibank	1	Beach Street (ANZ, Westpac), Camp Street (ASB, Kiwibank), Rees Street (BNZ), Ballarat Street (National)
Richmond	BNZ, Westpac, ASB	1	Queen Street
Rotorua	BNZ (two branches), Westpac (four branches), ASB, Kiwibank (two branches)	1	Hinemoa Street (ANZ, BNZ, National, Westpac (two branches), Kiwibank), Tutanekai Street (ASB, BNZ), Haupapa Street (Westpac), Te Ngae Road (Westpac), Malfroy Road (Kiwibank)
Stratford	BNZ, Westpac, TSB, Kiwibank	1	Broadway (ANZ, BNZ, National, Westpac), Miranda Road (Kiwibank)

Market	***Competitors (post acquisition)***	***Number of Foodstuffs outlets***	***Locations***
Taradale	BNZ, Westpac, Kiwibank	1	Gloucester Street
Taupo	BNZ, Westpac, ASB, Kiwibank	1	Tongariro Street (ANZ, National, BNZ), Horomatangi Street (Westpac, ASB),
Tauranga City (two National branches)	BNZ (two branches), Westpac (two branches), ASB, Kiwibank	1	Devonport Road (ASB, Westpac), Spring Street (ANZ, National), Willow Street (BNZ), 11th Avenue (BNZ, National, Kiwibank)
Te Awamutu	BNZ, Westpac (two branches), ASB, Kiwibank	0	Alexandra Street (ANZ, National, BNZ, Westpac), Main Street (Westpac), George Street (ASB), Sloane Street (Kiwibank)
Te Kuiti	BNZ, Westpac, Kiwibank	1	Rora Street (ANZ, BNZ, Kiwibank), King Street (Westpac), Teupiri Street (National)
Te Puke	BNZ, Westpac, Kiwibank	1	Jellicoe Street
Thames	BNZ, Westpac, Kiwibank	1	Pollen Street
Timaru	BNZ, Westpac (three branches), ASB, Kiwibank	1	Stafford Street (ANZ, BNZ, ASB, Westpac), Church Street (National), Otipua Road (Westpac) Ranui Ave (Westpac), Strathallen Street (Kiwibank)
Tokoroa	BNZ, Westpac, Kiwibank	1	Bridge Street
Waikanae	BNZ, Westpac, Kiwibank	0	Main Road (BNZ, National), Mahara Place (ANZ, Westpac, Kiwibank)
Waipukurau	BNZ, Westpac, Kiwibank	1	Ruataniwha Street
Wanganui	BNZ, Westpac (two branches), ASB, Kiwibank	0	Victoria Avenue (All), Moana Street (Westpac)
Warkworth	BNZ, Westpac, ASB	1	Queen Street (ANZ, ASB, National), Neville Street (BNZ), Baxter Street (Westpac)
Whakatane	BNZ, Westpac (two branches), Kiwibank	1	The Strand (All), King Street (Westpac)

Market	***Competitors (post acquisition)***	***Number of Foodstuffs outlets***	***Locations***
Whangarei (two National branches)	BNZ, Westpac, ASB (two branches), Kiwibank	1	Rathbone Street (ANZ, ASB, Westpac, Kiwibank), Bank Street (National, BNZ), Roberts Street (National, ASB)

Source: ANZ

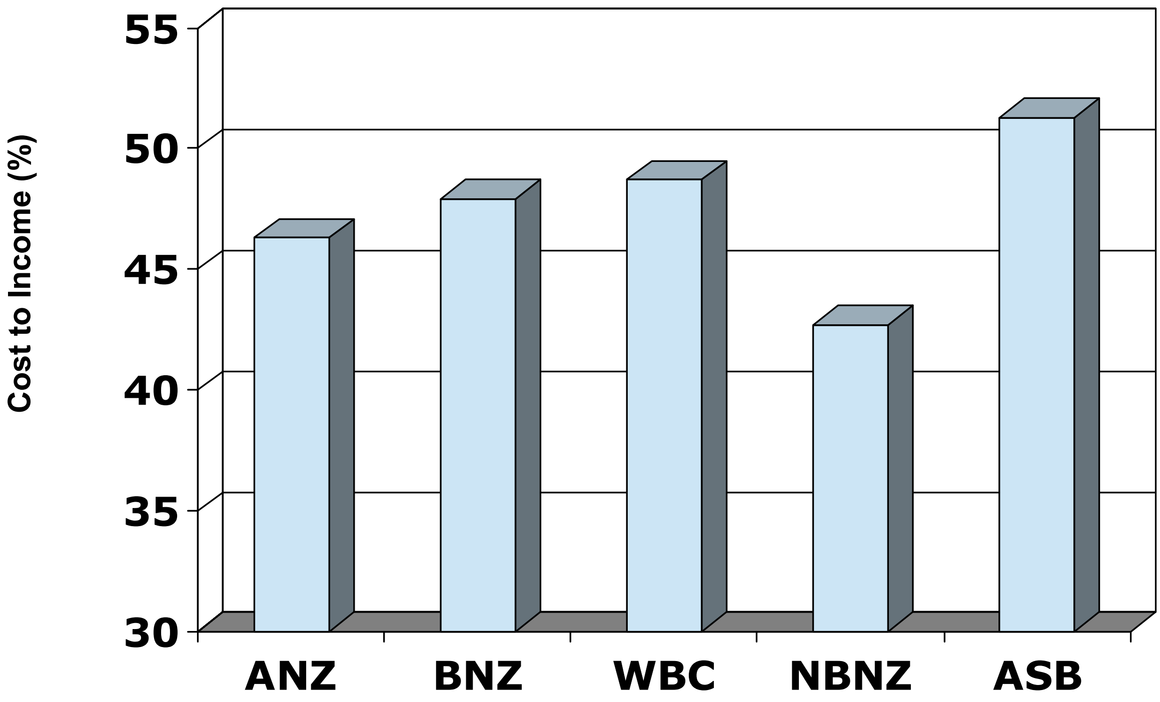
APPENDIX 5 – NEW ZEALAND / AUSTRALIA COMPARATIVE INTEREST MARGINS (FIGURE 1)



Source: KPMG Financial Institutions Survey 2003

APPENDIX 6 – COST TO INCOME VARIATIONS BETWEEN BANKS

Comparative cost performance 2002[1]



1. General Disclosure Statements

APPENDIX 7 – ALLEN CONSULTING GROUP REPORT: STATE IN THE BANKING INDUSTRY IN NEW ZEALAND (26 JUNE 2003)

26 June 2003

Report to ANZ by
The Allen Consulting Group

State of Play of the Banking Industry in New Zealand

Table of Contents

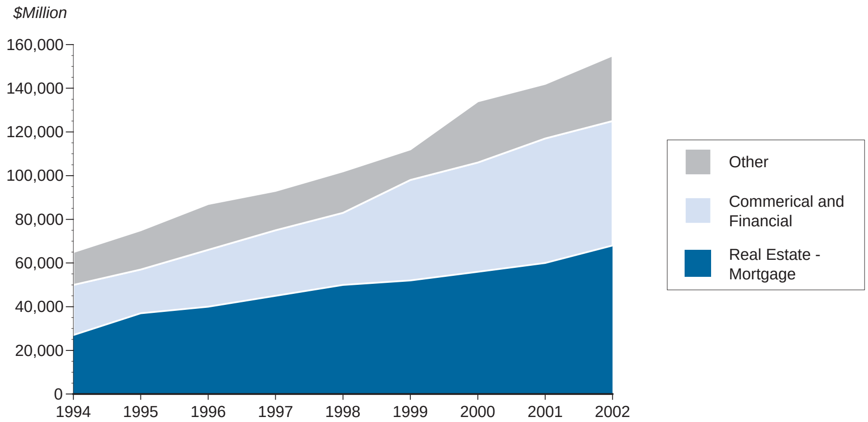
The Banking Industry in New Zealand

This report surveys the landscape of the New Zealand banking system.

The banking industry in New Zealand is in the midst of a period of robust performance, with solid asset growth (illustrated in Figure 1, below) and strongly growing profits. At the same time, the industry is highly competitive, with interest margins and interest spreads trending down, and new entrants applying significant competitive pressure to incumbent players. New technologies, especially electronic banking, are growing strongly, and banks have responded to this competitive environment by implementing significant improvements in their operating efficiencies.

Figure 1

REGISTERED BANKS: LENDING ANALYSIS



Source: KPMG Financial Institutions Survey 2003

Deleted:

Section 1 of this report describes the major players, in terms of asset size, profitability and ownership. Section 2 describes other New Zealand banks. Section 3 reviews two cases of recent entry into the New Zealand banking industry. Section 4 analyses interest margins and spreads. Section 5 describes the adoption of new technologies in the industry. Section 6 sums up.

1. Major Banks

There are five major banks in New Zealand, which between them account for 84 per cent[1] of the total assets of all registered banks that operate in New Zealand. These banks have an extensive branch network, provide a range of e-commerce products and generally provide a full range of financial services. This range includes corporate and business lending, treasury services, funds management as well as other retail products like mortgage finance and transactions services.

[1] KPMG Financial Institutions Performance Survey, 2003, p19.

In terms of assets, the largest major bank is **Westpac**, with total assets of $38.9 billion at the end of 2002. It is also the most profitable bank in New Zealand, with profits after tax of $613.5 million in the year to 30 September 2002, up from $440 million in the previous year, a rise of 39.4 per cent. Westpac has a large mortgage book with over $1 billion of securitised mortgage receivables, and net assets at the end of 2002 $5 billion. Following the purchase by Westpac's Australian parent of BT Finance in Australia and New Zealand, Westpac is New Zealand's fourth largest funds manager.

The second largest bank, also with assets of $38.9 billion (just $27 million less in assets than Westpac), is **The National Bank of New Zealand**. It is currently a wholly owned subsidiary of Lloyds TSB Group plc. The National became New Zealand's third largest bank in 1998 following its purchase of Countrywide Bank, and grew to be the second largest bank in 2002. The National Bank has a significant rural base and historical strength in wholesale banking and rural lending, the latter largely due to the purchase of The Rural Bank from Fletcher Challenge in December 1992, and subsequent growth. The National Bank recorded an after tax profit of $503 million for the year ended 31 December 2002, an increase of 20.9 per cent on the profit in the previous year of $416 million.

The third largest bank is **Bank of New Zealand**, with assets at the end of 2002 of $37 billion. The Bank of New Zealand recorded a profit after tax of in the year ended 30 September 2002 of $582 million, an increase of 32.3 per cent in profit from the previous year, of $440 million. Bank of New Zealand was majority owned by the New Zealand Government until it was sold to the National Australia Bank in November 1992.

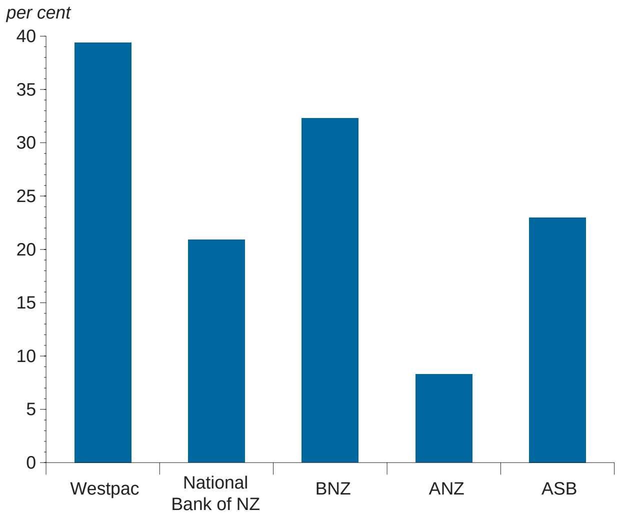
The fourth largest bank is **ANZ**, with total assets at the end of 2002 of $28 billion. ANZ achieved a profit after tax of $430 million, an increase of 8.3 per cent over the previous year's profit of $397 million. ANZ is the largest provider of retail funds management in New Zealand, following the joint venture between ANZ and ING, which commenced in May 2002.

ASB Bank is the fifth largest bank in New Zealand, with assets at the end of 2002 of $26 billion. ASB recorded an after tax profit in the year to June 2002 of $225 million, up 23 per cent on the previous year's figure of $183 million. ASB is well known as a leader in the use of technology in the banking industry.

These data are summarised in Figures 2 and 3 below.

Figure 2

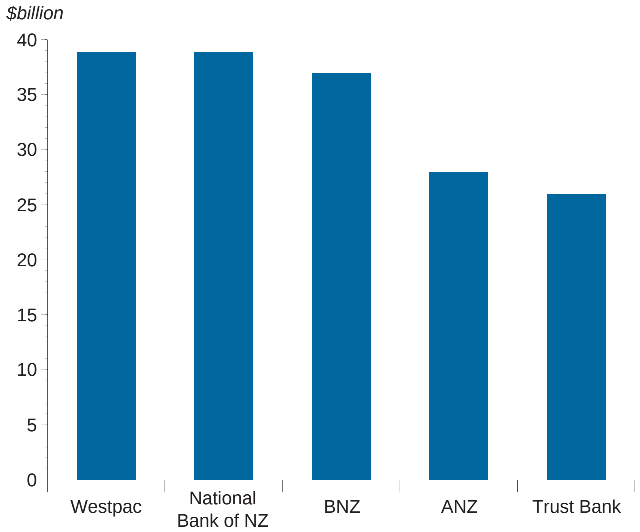
MAJOR BANKS' PROFIT GROWTH 2001–2002



Source: KPMG Financial Institutions Survey 2003

Figure 3

MAJOR BANK ASSETS 2002



Source: KPMG Financial Institutions Survey 2003

2. Other New Zealand Banks

Kiwibank is a wholly-owned subsidiary of the Government-owned New Zealand Post Limited. Kiwibank was registered on 29 November 2001 and commenced operations in February 2002. Government funding of $80 million was initially provided to establish the bank. Kiwibank's business plan relies on a take-up of between 100,000 and 150,000 customers in the first three years of operation. By December 2002 Kiwibank had signed up 100,000 customers. It reported a net loss of $10.2 million for the first five months of trading to 30 June 2002, and a net loss after tax of $6.5 million was reported for the six months to 31 December 2002.

Superbank, New Zealand's newest bank, is the trading name of St George Bank New Zealand Limited. Superbank is a joint venture between St George Bank and a New Zealand supermarket company, Foodstuffs. Superbank began operations on 23 February 2003. The business model is that banking services are distributed through a network of supermarkets throughout New Zealand.

Rabobank New Zealand is the rural banking arm of Rabobank Nederland New Zealand Banking Group. Rabobank's business model is to offer banking services to all members of the food production chain in New Zealand, from the primary producer to the retailer. Rabobank's total assets at the end of2002 were $2.52 billion. Its profits after tax in the year ended December 2002 were $19.4 million, up $6.3 million, or nearly 50 per cent, on the previous year.

TSB Bank is a small provincial bank, based primarily in the Taranaki area. It has maintained an independent ownership. At the end of December 2002 the bank had total assets of $1.8 billion. In the financial year ended 31 March 2002, TSB Bank achieved a net profit after tax of $18.5 billion, up from $16.6 million in the previous year.

Other banks operating in New Zealand are ABN Amro New Zealand, AMP bank, Bank of Tokyo-Mitsubishi (Australia), Commonwealth Bank of Australia, Citibank, Deutsche Bank, HSBC, and Kookmin Bank.

3 Entry into the New Zealand Banking System

A notable feature of the New Zealand banking industry over the past few years has been the entry of two new banks, Kiwibank and Superbank. The entry of these new banks reflects the evolution of thinking about whether and how branch networks are a barrier to entry in retail banking. Up until the mid 1990s, a branch network was thought indispensable to retail banking, and the need for a potential new entrant to establish one was thought to constitute a significant barrier to entry. However, the emergence of the Internet as the point of customer interface led to thinking that a branch network was not only unnecessary for a new entrants, it was a cost disadvantage for existing players. In Australia, ING Bank successfully established ING Direct, whose interface with its customers is almost all electronic. In both New Zealand and Australia, banks sought to cut costs by closing unprofitable branches.

Recently, however, thinking on these matters has further evolved with banks realising that a significant proportion of customers prefer to conduct their banking activities at a physical presence, rather than electronically.

KPMG's Financial Institutions Performance Survey 2003 has summarised these developments this way

> Real Estate is back. After years of driving customers to the phone and the net, there's been something of a U-turn. New branches, more tellers… these may be just the first signs of what can only be described as back to the future … Sure, telephone banking and Internet banking have been essential. Yes, they've changed the expectations of how and when customers can go the bank and how quickly they can expect to be served. And no, there's not a hope that customers will now even want to do without them. But … for many people, service is personal, the teller is still the most telling way to transact money, and nothing beats actually being in the neighbourhood for stimulating brand loyalty.

The commercial problem for banks is to satisfy this customer preference without incurring excessive branch network costs. Kiwibank and Superbank have tried to solve this problem by taking advantage of an existing distribution network which has been used for other purposes.

Kiwibank, owned by the New Zealand Post Office, is using the existing post office network and franchise operators (about 280 locations to date) as its point of physical contact with its customers. It is also using ATMs, EFTPOS, Internet and telephone banking as distribution channels. Indeed, Kiwibank relies on technology to reduce the cost of transaction processing and try to achieve its customer proposition of a cheaper banking service, which is also locally owned and more accessible. However, rather invest in its own electronic banking network, Kiwibank has obtained access to the existing payments system after reaching agreements on interchange fees with several major banks.

Kiwibank offers a current account, money management products and services, savings accounts, an interest-earning cash management account and home loans. It intends to launch a credit card in 2003 and business banking is also planned. It is ahead of schedule to reach its business case target of 150,000 customers.

Superbank, the most recent entrant, began operations in February 2003. A joint venture between St George Bank and New Zealand's largest supermarket operator, Foodstuffs, Superbank distributes its products through the telephone and Internet, with in-store point-of-sale support in 474 supermarkets throughout New Zealand. Superbank aims to "be a disruptive force" in the market, offering low (or no) fee banking products.

According to Superbank's website (www.superbank.co.nz)

> We are the new Phone and Internet bank. A revolutionary bank that combines the power of Phone and Internet Banking with the value of a supermarket. We're a bank that thinks like a supermarket and behaves like a bank should. Put simply, we're a bank that will save you money.

The supermarket theme appears to be an integral part of Superbank's marketing. On its web site, the various pages of information are labelled "Aisle 1", "Aisle 2" etc.

Superbank is modelled on the successful venture operated in the UK by Scottish banks and retailers Tesco and Sainsbury. Both Kiwibank and Superbank demonstrate that entry into the New Zealand banking system, designed specifically to exert competitive pressure on incumbent banks, is not just theoretically possible, it has actually happened. With interest margins already low (see Section 3, below), the new competitive battles between banks are likely to be fought over standards of customer service (for example, the number and type of distribution channels) and fees.

Now that the precedent has been set — twice —, it is not difficult to imagine other new entrants combining information technology and existing retail distribution channels (for example, petrol service stations) also entering the industry if the right commercial opportunities arise.

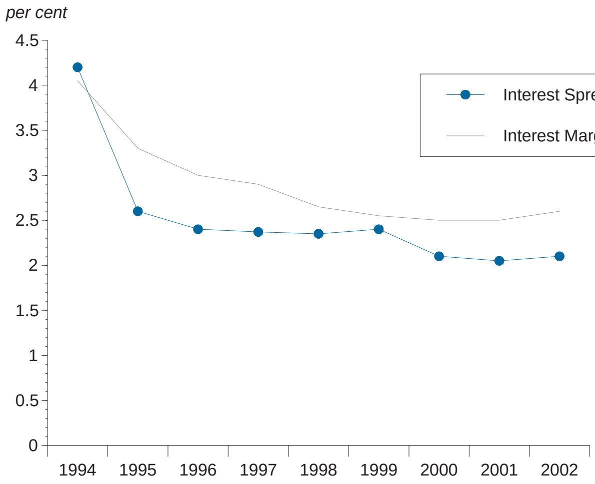
4. Interest Margins and Spreads

While New Zealand banks are profitable, this commercial success has not been achieved through higher interest margins. On the contrary, competitive pressure has resulted in a decline in both interest margins and interest spreads since the mid 1990s.

Figure 4 shows this decline. Interest margin is calculated as net interest income divided by average interest earning assets. After initial large falls in the mid 1990s, when they were over 4 per cent, interest margins in 2002 for New Zealand incorporated banks have fallen by over one-third to 2.6 per cent. The fall in interest spreads, which are the difference between the ratio of interest income to average interest earning assets and the ratio of interest expense to average interest earning liabilities, has been even more pronounced.

Figure 4

REGISTERED BANKS: INTEREST SPREADS AND MARGINS



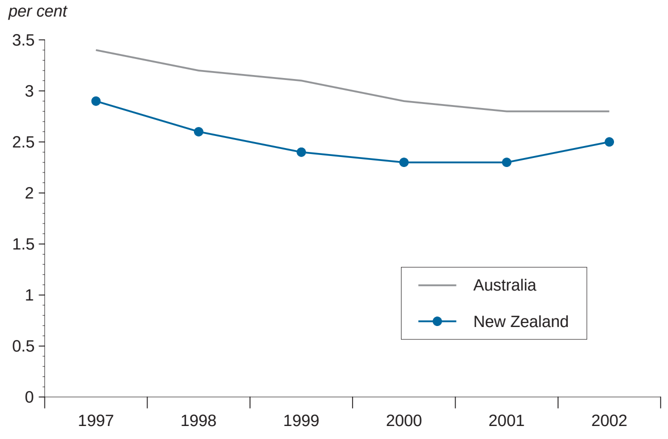
Source: KPMG Financial Institutions Survey 2003

Figure 5 shows comparative interest margins in New Zealand and Australia since 1997. While interest margins have come down in both countries, they are significantly lower in New Zealand.[2]

[2] The slight up-tick in margins in New Zealand in 2002 was largely due to the compositional effect of an increase in the proportion of fixed rate loans in NZ banks' mortgage books.

Figure 5

MAJOR NEW ZEALAND AND AUSTRALIAN BANKS: COMPARATIVE INTEREST MARGINS



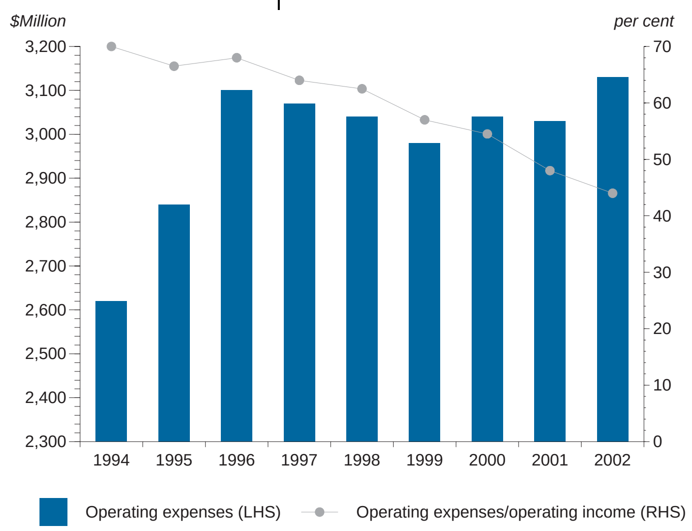
Source: KPMG Financial Institutions Survey 2003

How have New Zealand banks managed to increase their profits without increasing their prices? They have reduced their costs. Figure 6 shows that the ratio of operating expenses to operating income fell from about 70.2 per cent in 1994 to 44 per cent in 2002. (In 1990, the ratio was 78.5 per cent.) To make the same point about the productivity of New Zealand banks in a different way, between 1996 and 2003 banks increased their operating income by nearly 60 per cent, while keeping their operating expenses about constant.

Figure 6

REGISTERED BANKS: OPERATING EXPENSES VS OPERATING EXPENSES OPERATING INCOME

Deleted: /



Source: KPMG Financial Institutions Survey 2003

5. Industry Dynamism

The Adoption of New Technologies

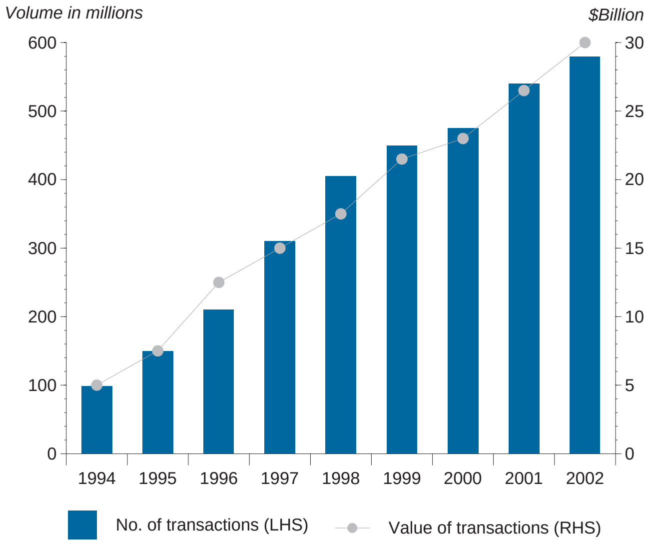
Another notable feature of the New Zealand banking industry is take up of electronic banking. In 2002, 87 per cent of all payments were made by an electronic medium.[3]

In 2002, 583 million EFTPOS transactions were carried out in New Zealand, up from 541 million in 2001. EFTPOS is a particularly popular form of payment in New Zealand, with the number of EFTPOS transactions, per capita, four times that of Australia. These transactions accounted for 35 per cent of all non cash payments and had a total value of $30.1 billion. EFTPOS payments have substituted for cheques and paper deposits, the volume of which have declined by nearly 50 per cent since 1995.

The very fast growth of in the number and value of EFTPOS transactions is shown in Figure 7.

Figure 7

NUMBER AND VALUE OF EFTPOS TRANSACTIONS



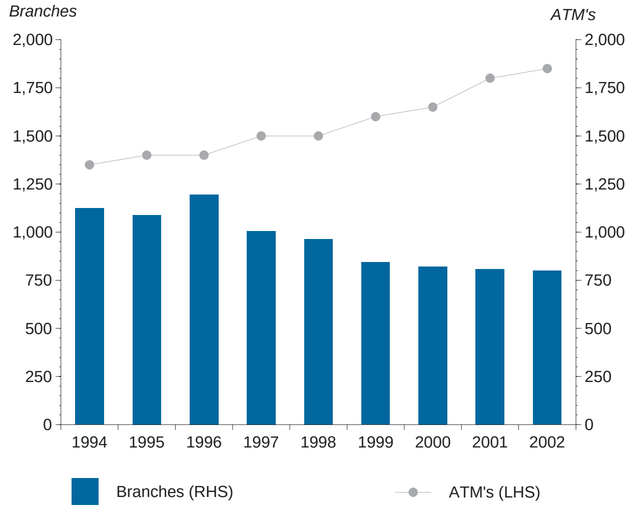
Source: KPMG Financial Institutions Survey 2003

Figure 8 shows a steady growth in the number of ATMs. Over the past decade, these have tended to be a substitute for branches, which have shown a steady decline.

[3] KPMG Financial Institutions Performance Survey 2003, p35.

Figure 8

MAJOR BANKS BRANCHES VS ATMS



Source: KPMG Financial Institutions Survey 2003

Internet banking is also very popular, with 49 per cent of banking customers having signed up for it by 2002, up from 26 per cent by 2001. About 70 per cent of those registered for the service use it 'regularly'. At the end of 2002, ANZ, Westpac and ASB all had around 250,000 Internet banking customers. The National Bank and Bank of New Zealand had around 200,000 and 100,000 Internet Customers, respectively. Most of these major banks had doubled their Internet customer base in the previous two years.

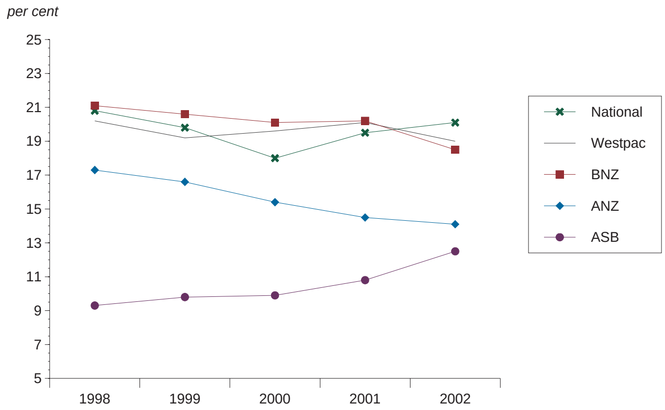
Deleted: in

Changes to Market Shares

Another example of industry dynamism is that the market shares of major banks are undergoing significant change. Since 1998, the market share (based on total assets) of the five major banks has declined from 88.8 per cent to 84.2 per cent. Within the five majors, ASB has increases its market share significantly, while the shares of ANZ and BNZ have declined. This is shown in Figure 9, below.

Figure 9

MAJOR BANKS' MARKET SHARES 1998–2002



6. Summary

The New Zealand banking industry is very healthy. Assets are growing strongly, as are profits. Five major banks account for over four-fifths of the industry's assets, with the three largest — Westpac, The National Bank and BNZ, all of about equal size. The other two major banks, ANZ and ASB Bank, are each about 70 per cent the size of the three largest banks. The industry is highly competitive, evidenced by falling interest margins and the entry of two new competitors, Kiwibank and Superbank. Productivity growth has been high, evidenced by very sharp falls in the ratio of operating expenses operating income. The industry is dynamic with both providers and customers willing to embrace new technologies, and with market shares in a state of flux.

Deleted: Trus t

APPENDIX 8 – ALLEN CONSULTING GROUP REPORT: TRENDS IN THE FINANCIAL SERVICES SECTOR (MAY 2003)

May 2003

Trends in the Financial Services Sector

Some Application to Australia

Table of Contents

Financial Services in Australia

This document outlines briefly some of the changes to the nature of banking and the provision of financial services in Australia:

- the changing nature of financial services brought around by
  - changing customer needs;
  - rapid technological innovations; and
- the changing competitive landscape.

The document also briefly outlines some the underlying trends in the various sub–sectors of the Australian financial services sectors, including:

- the deposits sub-market;
- the housing loans sub-market;
- the small business banking sub-market;
- the personal loans sub-market; and
- the transaction accounts sub-market.

Many of these underlying trends can be observed and are relevant to financial services in other jurisdictions.

The Changing Nature of Financial Services

Financial services are undergoing significant change in Australia. The Financial System Inquiry noted that the market has entered, "an era of accelerated change that is likely to continue into the next century".[1] Similarly, the *Report of the Task Force on the Future of Canadian Financial Services Sector* stated that the financial services market is being fundamentally reshaped and is in the midst of massive change.[2]

Changing Customer Needs

Changing customer needs, caused by changes in demographics and workforce patterns, have contributed to a reshaping of the financial services landscape in terms of distribution channels, products and suppliers. Customers are becoming more involved, more knowledgeable and more aware of financial product characteristics and provider choices.[3]

With this increasing sophistication, customers have also become more willing to accept non–traditional providers and adopt new technologically driven delivery methods, including electronic channels. This increased willingness has shaped and will continue to affect the way in which services are delivered, while greater focus on value will

[1] Financial System Inquiry, *Final Report,* AGPS, Canberra, 1997, p 1.

[2] Task Force on the Future of the Canadian Financial Service Sector, September 1998, *Change, Challenge, Opportunity Report of the Task Force*, Department of Finance, Ottawa, pp 23 & 26.

[3] McKinsey & Company, *The Changing Landscape for Canadian Financial Services: New Forces, New Competitors, New Choices*, Research Paper prepared for the Task Force on the Future of the Canadian Financial Services Sector, Ottawa, September 1998, p 25.

mean that only those suppliers who offer products with desired features and at an attractive price will prosper.[4] This sentiment was echoed in the ACCC's decision on the Westpac/Bank of Melbourne merger:

> "On average, consumers acquire a significantly greater number of banking-type products per person (3.19) than they do from an individual institution (1.67), which would suggest that unbundling is occurring to a considerable degree.
>
> It is considered likely that the larger the potential dollar savings available from shopping around, the greater the likelihood that consumers will not acquire all of their banking products and services as a bundle."
>
> Australian Competition and Consumer Commission, *Westpac Banking Corporation/Bank of Melbourne Ltd — Background to Decision on Merger Proposal*, p 3.

Rapid Technological Innovations

Technology is allowing innovation to occur in the financial services industry at an accelerating pace, leading to significant changes in financial relationships and market structures. Australians appear to be openly embracing much of this new technology as access to markets and products both domestically and internationally is made easier. In part, this increasing use of technology among financial services providers, and the customers they serve, is due to a decrease in information processing costs and enhanced functionality and computing power.

Technology has enabled a variety of new delivery mechanisms that permit access anywhere, any time to an increasing array of innovative financial services products.[5] Consumers are increasingly accessing financial services through:

- automatic teller machines (ATMs), and EFTPOS (see the Table below);
- the telephone; and
- the Internet (see Table 2).

Table 1

ATM USAGE AUSTRALIA-WIDE

Year	Number of EFTPOS Terminals	Number of ATM Terminals	Number of ATM Withdrawals (millions per month)
1994	43,950	6,008	40.7
1995	85,234	6,775	38.8
1996	136,645	7,718	41.6
1997	189,161	8,567	39.2
1998	243,253	9,014	42.9
1999	265,391	9,387	41.9
2000	370,372	10,818	48.4

Source: Australian Payments Clearing Association, *Annual Report 2000*, p 3.

4 Financial System Inquiry, *Final Report*, AGPS, Canberra, 1997, p 91.

5 McKinsey & Company, *The Changing Landscape for Canadian Financial Services: New Forces, New Competitors, New Choices*, Research Paper prepared for the Task Force on the Future of the Canadian Financial Services Sector, Ottawa, September 1998, p 24.

The number of ATMs and EFTPOS facilities and the value of transactions have also grown significantly, as shown in the Table below.

Table 2

TYPES OF ELECTRONIC BANKING TRANSACTIONS UNDERTAKEN BY ADULTS

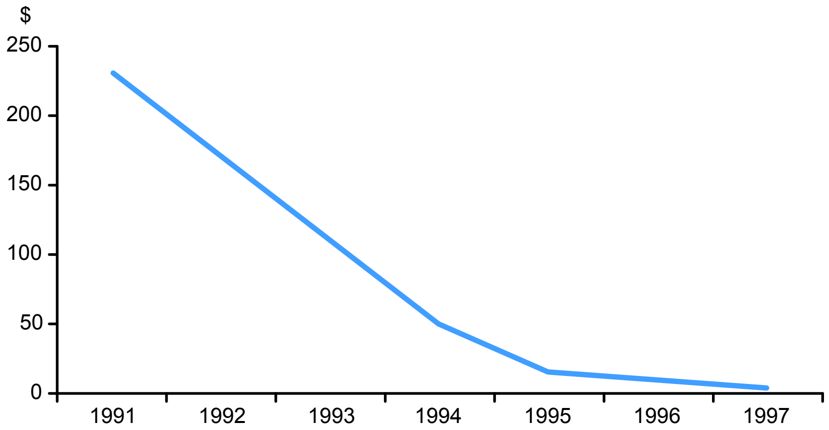
	August 1998	August 1999	August 2000
	%	%	%
Paid bills or transferred funds via Internet	1.2	3.4	8
Paid bills via an information kiosk	0.5	1.1	n.a.
Paid bills or transferred funds via phone	34.9	39.5	49
Paid bills or withdrew funds via EFTPOS	60.7	61.6	66
Transferred or withdrew funds via ATM	69.4	70.1	73

Note: n.a. — not available.
Source: Australian Bureau of Statistics, *Use of the Internet by Households*, 8147.0, August 1999 and August 2000.

New products and services have been trialed and introduced that would not have been possible to produce, sell and service economically without the advances in computing technology that we have experienced (see the Figure below).

Figure 1

COST OF A 1 MPS (MILLION PROCESSES PER SECOND) PROCESSOR



Source: Twomey, "Economic Impact of E-Commerce and the Challenge for Australian Business" presentation given at AICD & SIA's Bourse Talk, Brisbane, 29 November 1999.

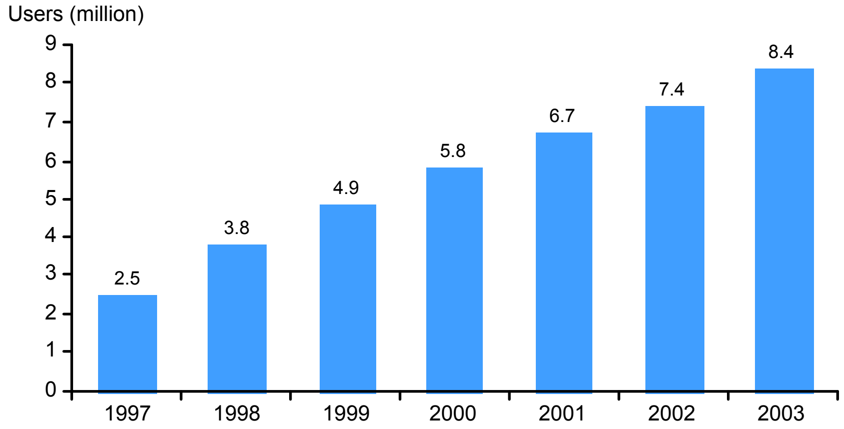
Technology is also enabling the mass customisation of financial services products to better serve the needs of particular sets of consumers. The Canadian Task Force noted that:

> "'Mono–line companies', which specialise in a single product such as credit cards or mortgages, are providing new sources of competition to traditional suppliers through the application of technology and new ways of thinking about these products. By focusing on one or a few products and by extending their geographic scope broadly, they can concentrate their technology resources in one area rather than many and defray the costs over a very large number of customers. This allows them to achieve substantial economies of scale and to exploit market niches."
>
> Task Force on the Future of the Canadian Financial Service Sector, September 1998, *Change, Challenge, Opportunity Report of the Task Force*, Department of Finance, Ottawa, p 27.

A key growth area in adopting new technologies will be in online banking over the Internet.[6] Such growth will be very dependent upon the availability and uptake of the Internet, which as the Figure below shows, is expected to increase at a significant rate.

Figure 2

INTERNET USERS IN AUSTRALIA



Note: The data for the years from 1999 to 2003 are estimates.
Source: IDC and Goldman Sachs as quoted in Goldman Sachs, *Asia Web*, October 14, 1999, pp 2&4.

The growth of Internet banking, albeit from a small base, will become more substantial, as banks further promote its use as the most cost-effective means of conducting transactions. The relative costs of alternative banking channels are shown in the Table below.

[6] See Warren Hogan "The Future of Banking: A Survey", *The Economic Record*, December 1999, p 420.

Table 3

TRANSACTION COSTS

Medium	Cost
Internet	Approximately $0.12
EFTPOS	$0.08 to $0.40
Telebanking	Approximately $0.50
ATM	$1.00 to $1.25
Over The Counter	$2.50 to $3.50

Source: Paul Buddle Communications as quoted in Paul Twomey, "*Economic Impact of E-Commerce and the Challenge for Australian Business*", presented at *AICD and SIA's Bourse Talk*, Brisbane, 29 November 1999.

While the Australian figures below are perhaps dwarfed by the experience in Germany and the United States (US), they nonetheless point to a rapid uptake of online banking services. This update is already significant in Australia — see the Table below.

Table 4

ONLINE CUSTOMERS JANUARY 2000

Bank	Online Banking Users	Proportion of Small Business Online Users Using Electronic Banking
ANZ	Approx 285,000	48%
St George Bank	Approx 100,000	N/a
Westpac	Approx 260,000	45%
National Australia Bank	Approx 165,000	45%
Commonwealth	Approx 390,000	31%

Source: Macquarie Research Equities, *Internet Bankmetrics,* January 2001, p 3. Available from www.macquarie.com.au/research on 15 February 2001. Greenwich Associates, *Small Business Monitor,* March 2000, p 108.

An example of technology lowering barriers to entry is the entry of ING, and how online technology has enabled ING to offer a branchless product with good interest rates. It is understood that within six months of opening in Victoria in February 2000, ING Direct had built a client base of 50,000 customers and $1 billion in deposits via electronic banking and without branch infrastructure.[7]

Even though such competition has been effective, actual entry is not necessary in order to impose a constraint on financial service industry incumbents. The mere threat of foreign competition operates as a significant constraint on Australian financial service provides.

The rise of e-commerce is providing a significant boost to the threat provided by international firms. For example, a global survey of senior executives from established

[7] *Australian Financial Review*, 31 July 2000, p 22.

and new finance firms demonstrated the industry's belief that global competition will become more profound within the next five years — see Table 5.

Table 5

FINANCIAL SERVICES EBUSINESS LEADERS — FIVE YEARS FROM NOW (UNPROMPTED)

	Per cent spontaneously mentioned
Global/international financial institutions	33
Local market financial institutions who are early adopters of eBusiness	21
eBusiness/internet firms which provide a range of services	13
Non-traditional financial institutions (e.g. Internet only banks)	11
Local market financial institutions who are late developers of eBusiness	9
New entrants from other industries	8

Source: Arthur Andersen, *Thriving in the New Economy: Perception vs. Reality*, Research Papers, Issue No. 2, January 2000, p 6.

The Changing Competitive Landscape

Increased competition brought about by financial deregulation has also demonstrated the capacity for entry into and exit from the financial services industry which has resulted in more players in the Australian financial industry. This has largely resulted from the blurring of division between the superannuation, life insurance and insurance markets from the banking and finance markets and also from the increased entry of building societies and credit unions into the finance industry.

The changing competitive Australian landscape is demonstrated by the range of highlights/trends shown in the Table below.

Table 5

THE CHANGING COMPETITIVE LANDSCAPE

Transaction and Bill Payment Services	Investment and Wealth Accumulation	Credit Products
Network expansion through giroPost agencies driven by non-bank service providers Network expansion through in-store banking (Ezy Banking example, others) Building societies and Credit Unions able to offer chequing facilities BPay network increases customer convenience Rapid growth of EFTPOS terminals now numbering 265,000 (from just 44,000 five years ago) ATM networks have gone global giving access to withdrawal services 24 hours a day/7 days a week anywhere in the world (9,387 in Australia, from 6,008 five years ago) Telephone banking services provided to customers 24 hours a day/7 days a week On-line funds transfer provided through Internet 24 hours a day/7 days a week On-line Foreign Exchange access provided to businesses, including small business Interest rate and foreign exchange derivatives now readily available to small businesses customers Joint ventures to develop emerging Smart Card and Stored Value Card technologies, (eg VISA Cash, Telstra SVC's) Internet based payments gateway services that support the buying and selling of goods and services over the Internet (eg eGate by ANZ, eMarket by Westpac)	Increasing range of Managed Investments on offer Increasing number of Mastertrusts and Wrap accounts driven by both taxation issues and increased consumer flexibility Compulsory superannuation has resulted in a substantial shift in the flow of funds into long-term savings products Cash Management Trust accounts offer high interest, at call, savings option Concepts such as 'Member Choice' will improve flexibility of Managed Investments Joint ventures formed with brokerage houses/share trading systems to provide on-line discount share and securities trading services Specialist 'monoline' deposit raisers able to enter market, with no effective barriers to entry. E.g. within six months of ING Direct launching in Victoria in early 2000, it passed 50,000 customers and $1 billion in deposits	Mortgage Offset Accounts significantly reduce cost of credit Home equity loans introduced Loyalty/reward programmes linked to credit card usage, with credit cards increasingly being used as a substitute payment system Credit Unions begin to offer credit card products Margins reduced through use of lower cost origination networks, putting pressure on retention of banks own branch networks 'Monoline' mortgage product providers (RAMS, Aussie) established in the marketplace and expanding into credit card products (e.g. RAMS) Widespread use of store branded credit and charge cards Store credit facilities provide consumer credit on most large ticket items, either directly by Retailer or through third party finance providers 'Infomediaries' set up to provide free electronic product comparisons, substantially increasing consumers ability to shop for the best deals on all banking products (e.g. Cannex, Quicken, Microsoft, E-Loan)

Source: ANZ

As a result of these highlights/trends, and as the range of products and providers expands , traditional distinctions between product titles and providers are becoming increasingly irrelevant. The below Figure illustrates the point. Virtually all financial services and products are now sold by organisations which previously had specialised in just a few. But at the same time, competitive dynamics within the industry have led to the emergence of niche providers of particular products.

Figure 3

COMPETITION MAP OF TRADITIONAL BANKING PRODUCTS

	Consumer Products								Small Business Products						
	Home Loans	Retail Transaction A/Cs	High Value Transaction A/Cs (a)	INVE	Personal Loans	Stored Value Cards	Bill Payments/Agency Services	Credit Cards or Charge Cards	Debit Cards	Transaction Banking	Overdrafts	Commercial Bills	Term Loans	Leasing	Credit Card Merchant Facilities
Major Banks	Currently	Currently	Currently	Currently	Currently	Possible future provider	Currently	Currently	Currently	Currently	Currently	Currently	Currently	Currently	Currently
Regional Banks	Currently	Currently	Currently	Currently	Currently	Possible future provider	Currently	Currently	Currently	Currently	Currently	Currently	Currently	Currently	Currently
Foreign Banks Subsidiaries	Currently	Currently	Currently	Currently	Currently	Possible future provider	Currently	Currently	Currently	Currently	Currently	Currently	Currently	Currently	Currently
Building Societies & Credit Unions	Currently	Currently	Currently	Currently	Currently	Possible future provider	Currently	Currently	Currently	Currently			Currently		Possible future provider
Life Companies	Currently	Possible future provider			Possible future provider	Possible future provider			Possible future provider				Currently		
Super Funds	Currently				Possible future provider								Currently		
Collective Investments	Possible future provider	Possible future provider	Possible future provider	Possible future provider	Possible future provider			Possible future provider	Possible future provider				Possible future provider		
Securitisers-includes Mtg Origs	Currently				Possible future provider			Currently			Possible future provider		Currently	Possible future provider	
Finance Cos-includes Priority 1	Currently				Currently			Possible future provider			Possible future provider		Possible future provider	Currently	
Utilities-Telstra, Aust Post, Elec.	Possible future provider	Possible future provider				Currently	Currently	Currently	Possible future provider	Possible future provider					
Credit Card Specialists					Possible future provider	Possible future provider	Possible future provider	Currently							Currently
Equipment Manufacturers													Possible future provider	Currently	
Other/Specialist Providers	Currently		Possible future provider	Possible future provider	Currently	Possible future provider	Possible future provider	Possible future provider	Possible future provider						
Merchant Banks – includes AIDC	Currently				Currently	Possible future provider		Currently			Currently	Currently	Currently	Possible future provider	

Currently   Possible future provider

(a) Accounts with minimum balances such as those offered by mutual funds in the US.
Source: Derived from the Financial System Inquiry.

The Australian Financial Services Market

The remaining sections briefly outline the funds in the sub-markets, based upon the ACCC's previous market definition, of the Australian financial services sector.

Deposits

The recent developments in voluntary superannuation contributions, cash management trusts and the traditional deposits sub-market itself illustrate the competitiveness of the deposits sub-market. However the deposits sub-market will become more competitive in the next few years. The impetus of online and phone banking will provide a further competitive threat as direct deposit institutions (for example Internet and phone-based organisations) expand operations in Australia.

The competitive nature of this sub-market can be seen by looking at three trends in the sub-market.

Firstly, cash management trusts are increasingly being offered by a range of institutions (e.g. the major banks, funds managers and stockbroking firms) and used as deposit (and transaction) accounts by consumers. The Table below includes the dollar amounts currently held in cash management trusts offered by financial institutions, excluding cash management trusts offered by other managed funds. Cash management trusts provided by financial institutions excluding other managed funds are at least seven per cent of the deposits sub-market.

Table 6

CASH MANAGEMENT TRUSTS ($ MILLION)

Annual CMT data	National
April 00/01	28,056
April 99/00	23,134
April 98/99	21,814

Source: Reserve Bank of Australia, *Bulletin*, June 2001, p s17.

Second, due to the technological advances made in relation to e-commerce and online banking, there has also recently been new entry into the deposit sub-market by branchless operators. For example, ING is understood to have built for itself a client base of 50,000 customers and $1 billion in deposits in the first six months after its opening in Victoria in late February 2000. The European and North American experience suggests that branchless deposit suppliers will increasingly make the deposit sub-market more competitive:

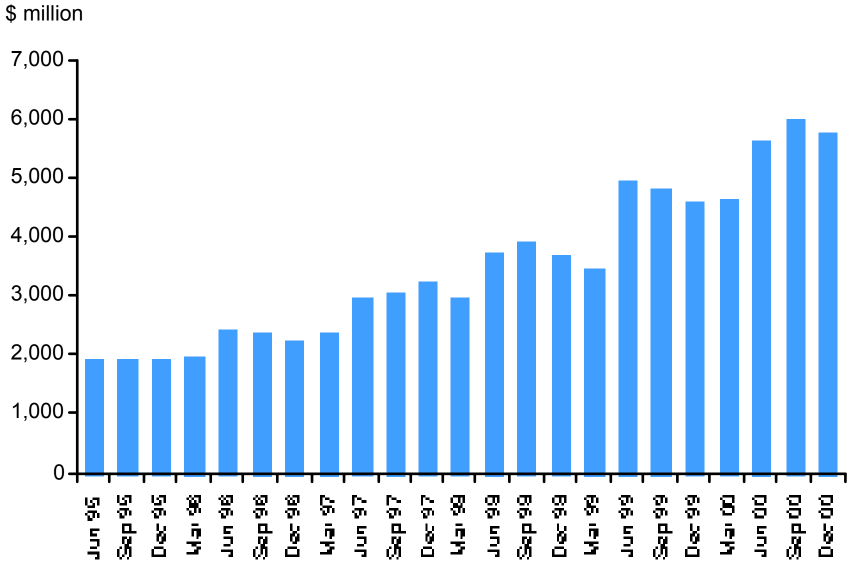
> "The 21st century promises to become the e-commerce century. Direct distribution of products and services via telephone and the Internet is booming. ING Direct, our direct response and internet bank, managed to climb to the top 10 of the banking sector in Canada within three years. The offices in Spain and Australia, which have meanwhile been started, are growing rapidly. This year, we will launch offices in France and the United States. We have set up a separate business unit for the worldwide coordination and stimulation of e-commerce activities."
>
> van der Lugt (Chairman of ING Executive Board), *ING Shareholders Bulletin*, January 2000, http://www.ing.com/uk/news/shb0001/shb01_01.html

The rapid uptake of Internet and phone-based banking has already been highlighted earlier in this document.

Third, Australians are increasingly using superannuation as a form of discretionary savings — see Figure 4. While superannuation is increasingly favoured as a long-term deposit vehicle, the imminent right to choose one's superannuation provider will further provide a competitive stimulus to this sub-market.

Figure 4

VOLUNTARY (DISCRETIONARY) SUPERANNUATION CONTRIBUTIONS AUSTRALIA-WIDE



Source: Australian Prudential Regulation Authority, *Superannuation Trends: December Quarter 2000*, Sydney, 2000, Table S3.

Housing Loans

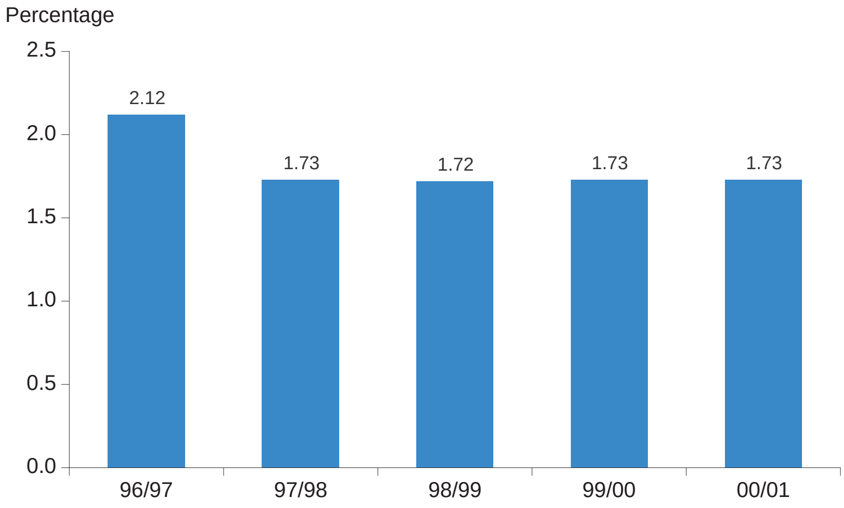
The plethora of providers and the increased consumer awareness generated by the Internet and increased media and Government scrutiny has ensured that the sub-market for home loans is a highly competitive national sub-market.

Evidence of the increased competition is provided by an analysis of home loan interest rate changes. From the previous cyclical peak in mid 1996 until April 1999 interest rates on standard variable-rate housing loans fell by four percentage points, 1.25 percentage points more than the reduction in the cash rate.[8] The decline in margins is shown in the Figure below.

[8] Reserve Bank of Australia, "Recent Developments in Interest Rates on Bank Lending", *Bulletin*, April 1999, p 1.

Figure 5

RESIDENTIAL HOME LOAN MARGINS



Source: Credit Suisse First Boston, *Equity Research Banking Trends,* February 2001, Table 28, p 72.

As show in the Table below, this margin squeeze was driven largely by mortgage originators and their lower rates. These margins are further expected to decrease given the renewed downwards pressure on interest rates in recent times.

Table 7

HOUSING INTEREST RATES

	Change from June Quarter 1996 to May 2001 (percentage points)	Current Level (per cent)
Banks		
Standard Variable	-2.75	7
Basic	-1.45	7.40
Mortgage managers		
Standard Variable	-2.35	6.55
Basic	n.a.	6.30

Source: Reserve Bank of Australia, *RBA Bulletin*, April 1999 and June 2001, Table F.5.

The RBA explained the mortgage originators' competitive advantage in these terms:

> "While banks average funding costs have remained slightly lower than mortgage managers', the latter group does not incur the substantial overheads of branch networks associated with running a retail deposit operation. By pricing housing loans at a spread of around 1.25-1.5 percentage points above the cost of issuing bills (their main source of funding), mortgage managers covered operating costs but also undercut banks on price. They gained considerable market share in the process: in the two years to June 1996, banks' share of owner-occupied housing approvals fell by almost 10 percentage points to a little over 80 per cent, due to competition form mortgage managers."

Reserve Bank of Australia Bulletin, "*Recent Developments in Interest Rates on Bank Lending*", April 1999, p 2.

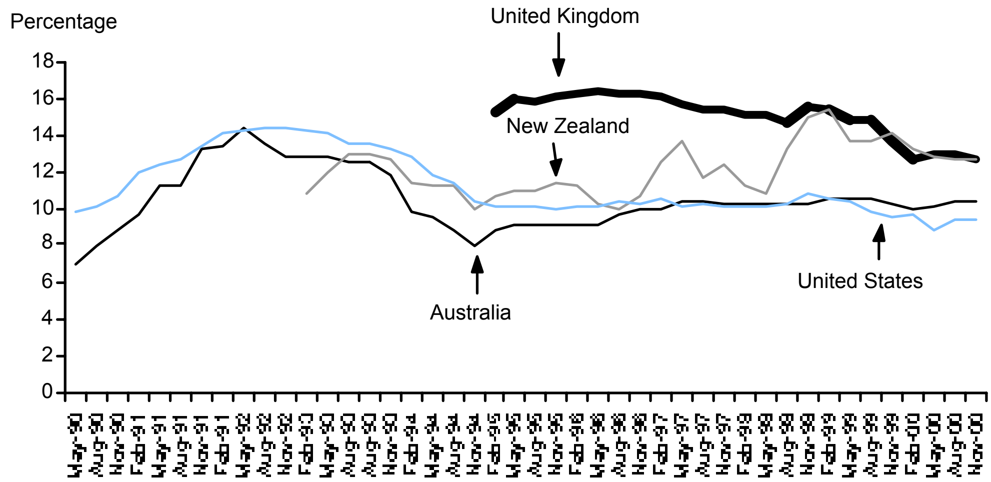
Another factor driving competition in the home loan sub-market is increased consumer awareness of switching opportunities and the best available deals (i.e. looking beyond simple headline rates). Consumer awareness of the home loans sub-market has also been encouraged by technological advances such as the Internet and scrutiny by the media and Government. Via the Internet, Australian consumers can currently compare the different products' prices, rates and conditions. Price transparency and comparability between home loan providers has changed significantly with independent institutions providing this information freely to consumers. Some examples include Quicken, Cannex, Your Mortgage and LoanNet.

Some independent institutions also calculate the cost differential between lenders, with some institutions even submitting consumer applications for competitive bidding (e.g. BankBid).

As these products also allow consumers to choose between the many different banks and the competitive fringe of home loan operators, consumers are easily able to choose the cheapest home loan alternative with fairly insignificant transaction costs. The competitiveness of the home loans sub-market is further demonstrated by the willingness of households to switch their borrowing to take advantage of the most attractive rates on offer.[9]

Figure 6

CREDIT CARD MARGINS — SPREAD OVER CASH RATE



Source: Reserve Bank of Australia, "Recent Developments in Interest Rates on Bank Lending", *RBA Bulletin*, April 1999, p 4 and Reserve Bank of New Zealand, US Federal Reserve and Bank of England data provided by Reserve Bank of Australia, 30 July 2001.

Small Business Banking

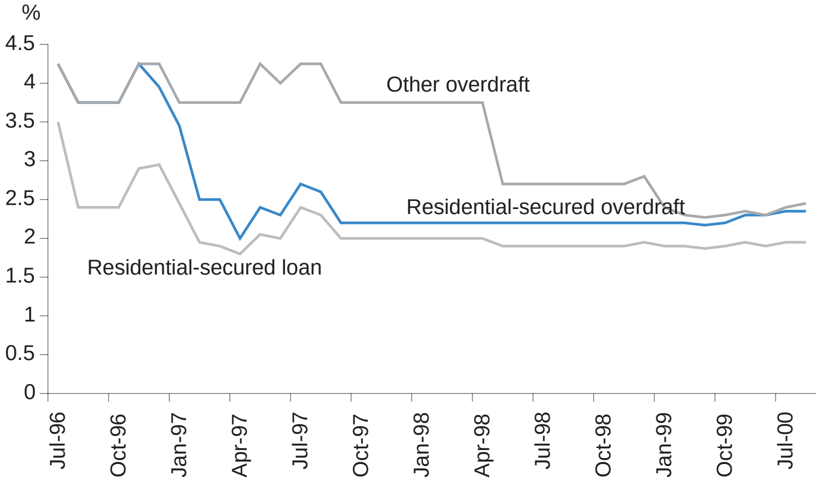
The entry of new providers and new products has increased competitive pressures in this sub-market which has reduced margins on small business lending. Furthermore, the sub-market is dynamically evolving and becoming broader (i.e. increasing the scope for interstate competitors) as a result of increased unbundling of financial products and the increasing acceptance and use of online banking by small businesses.

[9] Reserve Bank of Australia, "Recent Developments in Interest Rates on Bank Lending", *Bulletin*, April 1999, p 7.

The role of greater competitive pressures and new products has been to reduce margins on small business lending, as shown in the Figure below.

Figure 7

SMALL BUSINESS MARGINS



Source: Reserve Bank of Australia, *Bulletin*, Table F.4 — 'Indicator Lending Rates', April 1999, February 2000, July 2000, and Credit Suisse First Boston, *Equity Research Banking Trends,* February 2001, Table 28, p 72.

A comprehensive measure of the overall interest rate paid by small businesses is the weighted-average interest rate on small business loans, which comes from the Reserve Bank's quarterly *Business Finance Survey*. This measure includes indicator rates charged by banks, plus risk margins as applicable. The weighted-average interest paid on variable-loans by small business was 8.7 per cent in December 1998, down from 12.6 per cent in June 1996. Over that time, the rate had fallen by about 1.1 percentage points more than the cash rate since mid 1996.[10]

In addition, statistics from the United States suggest that margins in Australia have moved closer to those in the US (i.e. the sub-market is becoming significantly more competitive) — see the Table below.

[10] Reserve Bank of Australia, "Recent Developments in Interest Rates on Bank Lending", *Bulletin*, April 1999, p 5.

Table 8

SMALL BUSINESS MARGINS — SPREAD OVER CASH RATE

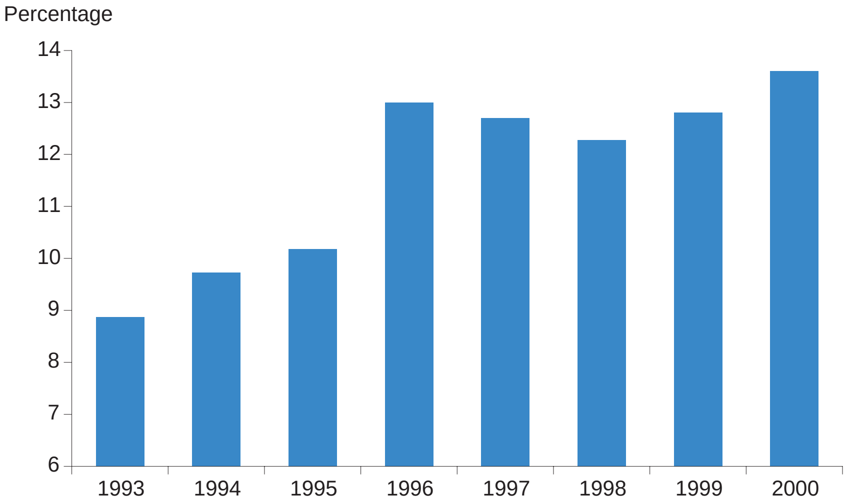
		June 1997	December 1998
Loans Under $100,000			
Australia		5.1	4.1
United States		4.3	4.1
"Larger' small business loans			
Australia			
1.0	$100,000 to $500,000	4.4	3.6
2.0	$500,000 to $2 million	4.0	3.3
United States			
3.0	$100,000 to $1 million	3.3	3.1

Note: Variable and fixed-rate loans, excluding bills. New loans for the US; outstanding loans for Australia.
Source: Reserve Bank of Australia, 'Recent Developments in Interest Rates on Bank Lending, *Bulletin,* April 1999, p 6.

Another indicator in assessing the level of competition in small business banking is the level of and reason for changing banks. As shown in the Figure below, the level of small businesses changing banks has risen from around nine per cent in 1993 to nearly thirteen per cent in 1999.

Figure 8

CHANGED PRIME BANKS IN THE LAST 2 YEARS



Note: 2000 average is derived from first quarter only.
Source: Greenwich Associates, *Small Business Monitor*, March 2000, p 79.

In addition, a separate survey found that while a similar percentage of small businesses had changed businesses in the previous two years, a further 32 per cent had actively considered changing banks, but decided against it. Only 56 per cent of small businesses had not considered changing banks.[11]

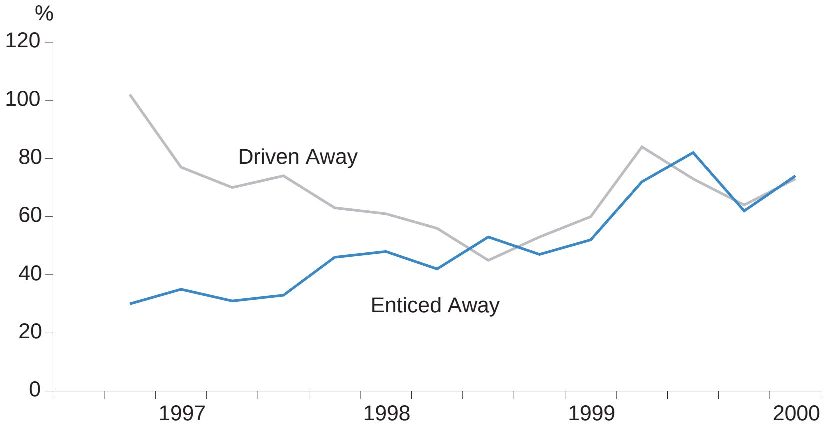
[11] Cameron, *The Australian Small Business Market for Financial Services*, 1998, p 142.

Broadly speaking, businesses are likely to change banks for two overarching reasons. Either they are driven away from the existing bank though poor service, poor relationship, or rising fees, or they are enticed to a new bank because of better performance, rates, or overall package.

The Figure below shows results of a survey conducted to ascertain reasons for changing banks. Over the life of the survey, the percentage of respondents who were enticed to another bank has almost doubled, while those driven away from their bank has remained in comparison, relatively static. This suggests that while the level of small businesses leaving for negative reasons has remained more or less constant, the level of businesses being successfully encouraged to change banks has increased substantially, signalling the advent of a more competitive sub-market.

Figure 9

REASONS FOR CHANGING BANKS



Note: Percentages are aggregates of all reasons for changing banks and permit multiple answers.
Source: Greenwich Associates, *Small Business Monitor* (prepared for ANZ in March 2000).

The increased use and accessibility of electronic banking services is further exacerbating competitive pressures in the small business sub-market.

A report prepared in the US by Arthur Anderson concluded that small businesses are committed to information technology, but that most are not receiving the full benefits that technology can provide, leaving a service gap for banks to fill. The survey also revealed that 94 per cent of small and mid-size businesses now have computers and 65 per cent use the Internet in some way.[12]

These figures are comparable to Australian figures, where 48 per cent of small businesses and 82 per cent of medium businesses are connected to the Internet.[13]

[12] "Banks Need to Tap Small Business", *FutureBanker*, January 1999, p 12

[13] Yellow Pages Small Business Index, *Survey of Computer Technology and E-Commerce in Australian Small and Medium Business*, May 1999.

Table 9

USE OF ELECTRONIC BANKING FACILITIES

	Use EFTPOS (proportion of companies)	Provide EFTPOS (proportion of companies)	Don't Use any Electronic Facilities (per cent)
NSW	16	23	57
VIC	20	20	59
QLD	14	28	63
SA	12	19	68
WA	11	26	46

Source: Greenwich Associates, *Small Business Monitor* (prepared for ANZ in March 2000).

Personal Loans

The sub-market for personal loans is broad with both banking financial institutions and NBFIs, and is getting broader. Competition in the sub-market for personal loans has been more selective than in the housing sub-market, and came somewhat later.

The reduction in personal lending rates demonstrates the competitive nature of the personal loans sub-market — see the Table below. The largest reduction in interest rates has occurred in residentially secured revolving lines of credit, or 'home equity' loans. These loans are more flexible than the traditional types of personal loans, with borrowers able to repay and redraw against a previously approved limit, more or less as they please.

Table 10

PERSONAL LENDING RATES

	Change from June quarter 1996 to March 1999 (Percentage points)
Secured	
Instalment loan	-2.15
Revolving line of credit	-4.90
Unsecured	
Credit cards -With interest-free period -Without interest-free period	-2.00
With interest-free period	-1.40
Without interest-free period	-2.25
Cash rate	**-2.75**

Source: Reserve Bank of Australia, "Recent Developments in Interest Rates on Bank Lending", *Bulletin*, April 1999, p 3.

Transaction Accounts

Recent developments in the transactions sub-market itself illustrate the competitiveness of the sub-market. However the transactions sub-market will become more competitive in the next few years. The impetus of online and phone banking will provide a further competitive threat as direct transaction account institutions (for example Internet and phone-based organisations) expand operations in Australia as has happened overseas

The Box below provides overseas and domestic evidence of transaction accounts and technological online advancements via individual case studies.

Box 1

THREE CASES STUDIES — BRANCHLESS TRANSACTION ACCOUNTS

Bank of Scotland

Sainsbury's Bank (45% owned by Bank of Scotland and 55% by retailer Sainsbury's) telephone based operation delivers growing portfolio of products to a customer base of around 700,000 – achieved in around 12 months. The business takes 10,000 calls a day into its call centre – ie 240,000 a month.

Tesco

Tesco, the biggest supermarket chain store in Britain, has established Tesco Finance. It has a full banking licence with 50% owned by the Royal Bank of Scotland and 50% owned by Tesco. It has been operating for just over 2 years and has garnered more than 600,000 customers (as at Oct 1998) – a rate of 50,000 per month.

The KPMG Report 1998 reports:

> "Tesco the supermarket chain, has entered the financial services market by offering in–store banking through a joint venture arrangement and now offers deposit accounts that pay considerably higher interest rates than those offered by United Kingdom banks. The cost of paying higher rates has been reported to be more than offset by the profits generated from directly attributable increased customer spending.
>
> While Australian supermarket chains are in an ideal position to offer similar deposit accounts, there are also other industries that might discover flow on benefits from offering financial services products.
>
> If supermarkets or other new competitors can match the banks on convenience, and subsidise account keeping costs with increased profits from other business activities as achieved by Tesco, then financial institutions might find themselves facing considerable additional pressure to reduce or eliminate some or all account keeping charges."

Woolworths Ezy Banking

The Commonwealth Bank of Australia recently announced an alliance to develop and sell co-branded bank products with Woolworths – marketed as Ezy-Banking.

Woolworths Ezy Banking lets you bank while you shop at any Woolworths Supermarket (Safeway in Victoria, Purity & Roelf Vos in Tasmania and Metro – being progressively rolled out throughout Australia).

The plan has been to introduce CBA's banking and finance products and services to Woolworths' customer base through its extensive chain of retail stores. To date, Ezy Banking has been rolled out in Queensland, Victoria and New South Wales, and will be introduced to WA in the next six months.

The company has packaged co-branded products will be offered throughout Woolworths' 680 stores.

In a status report released last November, CBA said that take-up had been stronger than initially forecast with 50 per cent of Ezy Banking's customers being first time customers of CBA.

Source: Bank of Scotland; www.tesco.co.uk and KPMG, *Financial Institutions Performance Survey*, 1998, p 4; Commonwealth Bank of Australia.

APPENDIX 9 – MERRILL LYNCH REPORT: NEW ZEALAND BANKING (APRIL 2003)

April 2003

Australian Banks Team:
Andrew Kearnan
+612 9226-5773

Hamish Carlisle
+612 9226-5694

James Ellis
+612 9226-5695
firstname_lastname@ml.com

New Zealand Banking

Structural Review of the New Zealand Banking Market

Highlights:

- Important market for Australian banks
- NZ earnings growth likely to decline
- Competition laws restrictive to M&A

Refer to important disclosures at the end of this report.

Merrill Lynch Global Securities Research & Economics Group
Global Fundamental Equity Research Department

Investors should assume that Merrill Lynch is seeking or will seek investment banking or other business relationships with the companies in this report.

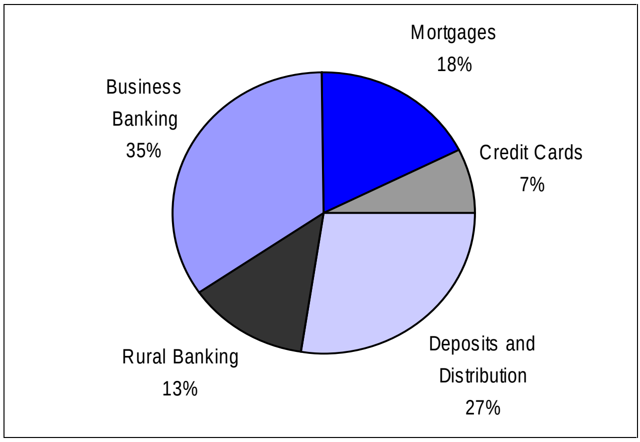
RC#60209707

Summary and Conclusions

Size & Profitability of NZ Banking Market

We estimate the New Zealand banking market currently generates NZ$2.2bn of earnings and economic value added (EVA) of NZ$1.8bn per annum. The largest contributors to industry NPAT are business banking (35%) and deposits & distribution (27%). We estimate that the banking market ROE is around 24%, with higher returns from deposits & distribution, credit cards and rural banking offset by lower returns from mortgages and business banking.

Chart A: New Zealand Banking Market



Source: Reserve Bank of New Zealand, Company reports, Merrill Lynch estimates

In earnings and EVA terms we estimate the New Zealand banking market is circa 20% the size of Australia's market. It currently contributes an average 12% to Australian bank earnings (range 5-17%).

Historical Industry Operating Performance

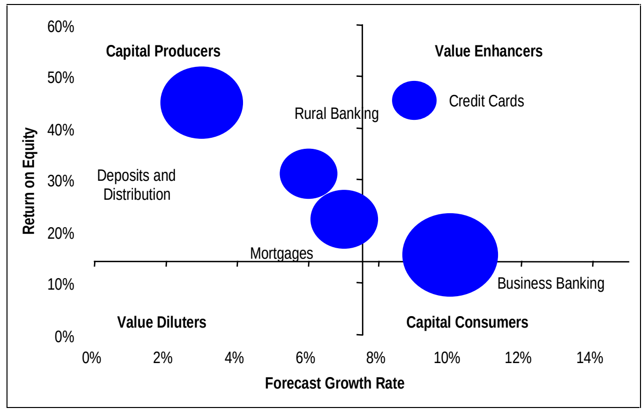
From 1995-2001, growth in the New Zealand banking industry's total revenues was a relatively modest 6% p.a., despite the benefit of increasing household gearing. However the related growth in NPAT was a more healthy 13%, largely driven by a substantial improvement in cost efficiency (which has included realised merger cost synergies).

Given total asset growth of 11% over the same period, the banks also experienced considerable margin compression. Interestingly, bad debt charges over the past decade have been remarkably moderate (averaging only 9bp of loans), reflecting the benefits of increasing industry concentration, the introduction of foreign risk management systems and the likely reporting of larger / more risky corporate loans through parent group (rather than New Zealand subsidiary) accounts.

Structural Attractiveness of Market

New Zealand's banking market is generating both positive EVA and EVA growth. Whilst the ROE is less than that reported in Australia we estimate that the return on lending assets is not too dissimilar at around 1.4%.

Chart B: Growth/Return Matrix—New Zealand Banking Market



Source: Reserve Bank of New Zealand, Company reports, Merrill Lynch estimates

From a revenue perspective one must consider both the top down environment and competitiveness dynamics. From a top down perspective we think New Zealand is a modestly lower growth economy relative to Australia—but we don't expect the difference to be overly material. Like Australia, it is a mature banking market, with low product innovation and relative product / customer saturation. Nonetheless, we think the growth outlook less structurally attractive than in the Australian banking market.

Having probably already captured most of the potential for growth through improved cost efficiency, the New Zealand banking industry now finds itself at potentially competitive cross-roads. The choice is between **diluting returns through competitive battle for market share or enhancing the return through further structural reforms**. While differing degrees of independence and management style amongst the major New Zealand banking groups leave future direction a little uncertain, our guess is that the industry is more inclined to choose the latter. This view is because—as a small, highly concentrated market—New Zealand banking appears less contestable than Australia owing to its smaller absolute size and relative absence of "fringe players". To back this view up we note evidence that at least one of the major NZ banks is considering stepping away from the broker market given its impact on return. There may well be **prospects for improving returns through the emergence of (for example) oligopoly pricing structures**, which to date appear to have been largely absent from the market.

We conclude New Zealand is not a structural unattractive banking market—but it is equally not overly that attractive. We question more the attraction to new entrants, such as SGB, rather than the attraction to incumbents.

Relative Positioning of Major Australian Banks in NZ

The New Zealand banking market is dominated by five full service banks—all foreign owned—that control more than 90% of banking assets**. The banks are National Bank of New Zealand (Lloyds TSB); ANZ Banking Group New**

Zealand (ANZ); ASB Bank (CBA); the Bank of New Zealand (NAB); and Westpac Banking Corporation New Zealand branch (WBC).

Chart C: New Zealand Banks—Lending Market Share

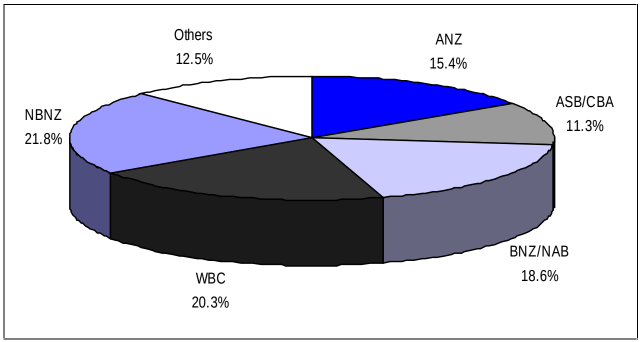
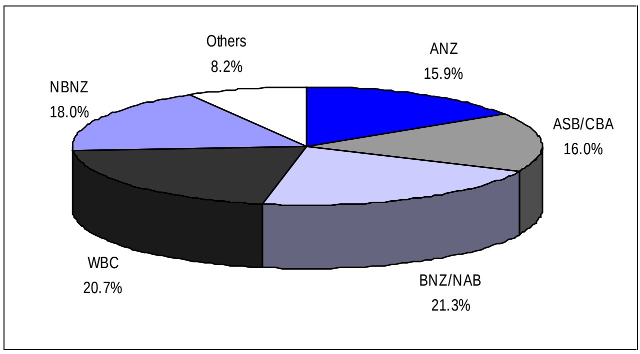


Chart D: New Zealand Banks—M3 Resident Funding Share



Source: Reserve Bank of New Zealand, Company reports, Merrill Lynch estimates

WBC & **National Bank** (Lloyd's TSB) have the strongest market shares in *total lending* while **WBC** and **BNZ** have the strongest *deposit* market shares. **ANZ** and **ASB** have the smallest lending portfolios, around two thirds the size of the other three banks. While **WBC** generates the highest return on RWA (refer table 1), it has produced half the rate of annual growth in revenue as the next best performer in the last 5 years and has similarly under performed in terms of profit momentum. This may reflect its lack of presence in the important Auckland regional market. **ANZ** and **NAB** are next best performers in terms of return but both still lag historic revenue performances of both **ASB** and **National Bank**. We don't believe that there is that much scope for further cost reduction in any of these NZ banks.

Table 1: Performance Comparison

Bank	5 Year CAGR in Revenue	5 Year CAGR in Profit	RoRWA (2002A)
ASB (CBA)	12%	19%	1.85%
ANZ	7%	23%	2.38%
BNZ (NAB)	6%	12%	2.24%
NBNZ (LTSB)	16%	32%	1.98%
WBC	3%	9%	2.56%

Source: Various Company Documents, Merrill Lynch

ASB Bank lacks both relatively strong market shares and relatively strong returns, but has driven superior growth, particularly in terms of top-line revenues. This probably has much to do with its strong position around Auckland. What it gains in revenue growth it seems to lose in return with overall returns on RWA significantly lower than the competition. The differences are both in revenue and cost structures and we suspect it is not so much opportunity as reflective of ongoing business mix.

All of the factors considered, it is difficult to rank relative position of the Australian banks in New Zealand. All have various strengths and weaknesses. ASB looks the weakest but there is little between the other banks' positioning.

New Zealand Operations in Context

The major Australian banks have been increasing the level of commitment to the New Zealand banking market via:

1. **Acquisitions** both directly through the acquisitions of New Zealand assets and indirectly through integration of their New Zealand based subsidiaries;
2. Back office **operational convergence** initiatives; and
3. The **issuance of New Zealand equity instruments**.

The contributions to major bank earnings from these New Zealand operations have been increasing in importance and comprised 12% of FY02 earnings. **WBC** has the greatest relative earnings exposure to the New Zealand market (at c17% of group earnings).

Scope for Further Market Consolidation?

For many years Lloyds TSB has been subject to conjecture regarding possible divestment of its New Zealand bank operations. This owes both to the lack of capability in the Australian market to service their New Zealand corporate client base and, more recently, the pressured group capital position. Historically, we note bank M&A transactions in New Zealand have been executed on average PE multiples of 12.1x (range 8.3x to 15.2x) and NTA multiples of 2.0x (range 1.5x to 2.7x). These multiples would suggest that Lloyd's franchise in New Zealand is worth (to an acquirer) in the range of NZ$5.0bn to NZ$6.1bn.

All of the Australian banks would structurally benefit from acquiring Lloyd's New Zealand banking business. It is our view, however, that **ANZ** and **CBA** (in that order) would get the most structural benefit from acquiring the business.

In noting this, however, we believe that any major bank in-market merger combination that involves 'National Bank' (Lloyd's TSB business) would prima facie breach the New Zealand competition law safe harbour provisions. As such, such a deal would be unlikely to automatically be granted approval by the Commission. Whilst these laws have not been tested, there may well be a good reason for that.

An option for Lloyd's TSB might be an IPO—there are no scalable New Zealand owned banking operations and such an IPO might appeal to both Government and consumer. Given the lack of available cost synergies and lower funding advantage, amongst other factors, any IPO value would be well below our estimates from an M&A perspective.

CONTENTS

1. The Market

In this section, we have defined the current size and profitability of the New Zealand banking market.

Size and Structure

In assessing the market, we have divided the industry into five key product and customer segments (spanning both personal and business banking), reflecting the current market structure and the extent of data available. These segments are:

Five market segments

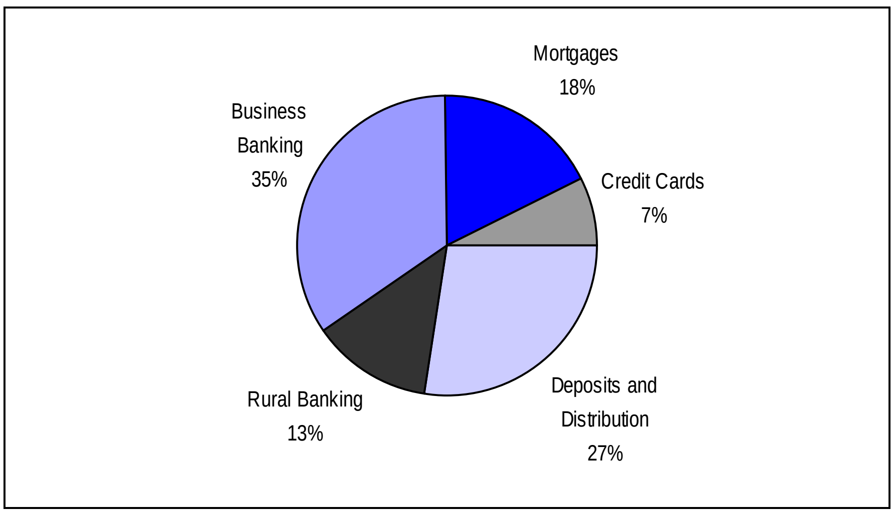
1. **Mortgages** (product manufacturing margins for housing loans);
2. **Credit cards** (product manufacturing margin);
3. **Deposits and distribution** (reflecting customer deposits and product distribution margins);
4. **Rural banking** (a specifically identifiable segment, owing to the structure of the New Zealand economy); and
5. **Business banking**.

In summarising the New Zealand Banking market we would note the following:

- We estimate that the New Zealand banking market currently generates circa **NZ$2.16bn of earnings** and **economic value add (EVA) of NZ$1.76bn** per annum (refer table on facing page);
- We estimate that the largest contributors to industry NPAT (refer chart below) are **business banking** (35%) and **deposits and distribution** (27%);
- We estimate that the **banking market ROE is c24%**, with relatively high returns from deposits and distribution, credit cards and rural banking being counter balanced by lower returns from mortgages and business banking; and
- Whilst we estimate that the NPAT contribution from Personal Banking is similar to that from Business Banking, the ROE of the former is structurally higher than the latter. This is driven by higher asset margins within Personal Banking.

High tilt to rural lending

Chart 1: New Zealand Banking Market Annual NPAT—NZ$1.76bn



Source: Reserve Bank of New Zealand, Company reports, Merrill Lynch estimates

Table 2: New Zealand Banking—Size and Profitability

	Housing	Credit Cards	Other Personal	TOTAL PERSONAL	Rural	Other Business	TOTAL BUSINESS	NZ BANKING
Industry Balance Sheet (NZ$bn):								
Lending Assets	68.8	3.5	10.3	82.7	17.5	48.9	70.4	153.1
Other Assets	0.0	0.0	41.6	0.0	0.0	0.0	0.0	0.0
Total Interest Earning Assets	**68.8**	**3.5**	**51.9**	**82.7**	**17.5**	**48.9**	**70.4**	**153.1**
Deposits / Customer Liabilities	0.0	0.0	50.6	50.6	3.4	29.9	33.4	84.0
Other Borrowings	67.1	3.2	0.0	79.3	13.2	14.1	31.3	59.9
Equity	1.7	0.4	1.3	3.4	0.9	4.9	5.8	9.1
Total Liabilities	**68.8**	**3.5**	**51.9**	**133.3**	**17.5**	**48.9**	**70.4**	**153.1**
Deposit / Lending Ratio	0%	0%	491%	61%	20%	61%	47%	55%
Equity / Assets Ratio	2.5%	10.0%	2.5%	4.1%	5.0%	10.0%	8.2%	6.0%
3 Year Forecast CAGR	**7.0%**	**9.0%**	**3.0%**	**8.1%**	**6.0%**	**10.0%**	**8.4%**	**8.3%**
Profitability Drivers:								
Net Interest Income / Assets	1.23%	9.72%	3.24%	3.47%	1.82%	1.49%	1.49%	2.56%
Other Income / Assets	0.12%	9.43%	2.00%	1.76%	2.30%	2.30%	2.17%	1.95%
Total Income / Assets	**1.36%**	**19.15%**	**5.24%**	**5.23%**	**4.12%**	**3.79%**	**3.65%**	**4.51%**
Cost / Income	35.0%	49.0%	64.2%	55.5%	40.0%	30.0%	32.8%	47.1%
Underlying Profit / Assets	**0.88%**	**9.76%**	**1.87%**	**2.33%**	**2.47%**	**2.65%**	**2.45%**	**2.39%**
Bad Debts / Lending	0.04%	3.00%	1.00%	0.29%	0.15%	0.34%	0.27%	0.28%
Profit Before Tax / Assets	**0.84%**	**6.76%**	**1.68%**	**2.04%**	**2.32%**	**2.31%**	**2.18%**	**2.10%**
Corporate Tax Rate	33%	33%	33%	33%	33%	33%	33%	33%
Return on Interest Earning Assets	**0.56%**	**4.53%**	**1.12%**	**1.37%**	**1.55%**	**1.55%**	**1.46%**	**1.41%**
Equity Multiplier	40x	10x	40x	25x	20x	10x	12x	17x
Return on Equity	**22.4%**	**45.3%**	**44.9%**	**33.5%**	**31.1%**	**15.5%**	**17.8%**	**23.6%**
Profitability (NZ$m):								
Net Interest Income	848	343	1,681	2,872	318	729	1,047	3,919
Non-Interest Income	86	333	1,039	1,457	402	1,122	1,524	2,981
Total Income	**933**	**676**	**2,719**	**4,328**	**720**	**1,851**	**2,571**	**6,900**
Non-Interest Expense	(327)	(331)	(1,746)	(2,404)	(288)	(555)	(843)	(3,247)
Underlying Profit	**607**	**345**	**974**	**1,925**	**432**	**1,296**	**1,728**	**3,653**
Bad Debt Charge	(31)	(106)	(103)	(240)	(26)	(166)	(193)	(432)
Profit before tax	**576**	**239**	**870**	**1,685**	**406**	**1,129**	**1,535**	**3,221**
Tax Expense	(190)	(79)	(287)	(556)	(134)	(373)	(507)	(1,063)
Profit after Tax	**386**	**160**	**583**	**1,129**	**272**	**757**	**1,029**	**2,158**
Economic Value Added (NZ$m)								
Profit After Tax	386	160	583	1,129	272	757	1,029	2,158
Value of Franking Credits (70%)	133	55	201	389	94	261	355	744
Cost of Equity (12.5%)	(215)	(44)	(162)	(422)	(109)	(611)	(721)	(1,142)
Economic Value Added	**304**	**171**	**622**	**1,097**	**256**	**406**	**663**	**1,760**

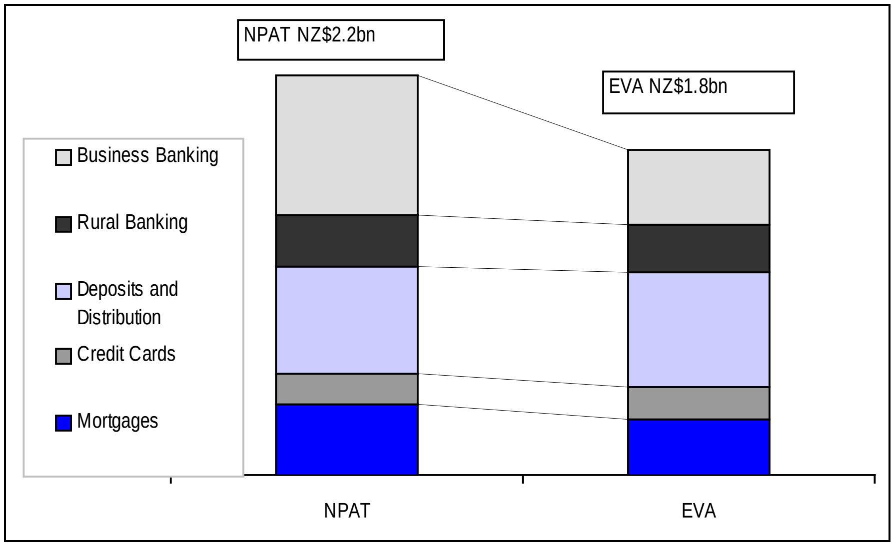
Source: reserve Bank of New Zealand, Company reports, Merrill Lynch estimates

Converting NPAT to EVA

We estimate 'Deposits and Distribution' to be the largest contributor to NZ market EVA

In the chart below we have converted our estimate of industry NPAT into industry EVA, reflecting in the process the differences in capital intensity of various lines of business. EVA adds back to NPAT the estimated value of franking credits associated with the domestically sourced income (we assume 70%) and deducts the cost of capital employed (we have assumed 12.5%). In the process, **business banking**—the largest contributor to industry NPAT—becomes supplanted by **deposits and distribution** as the largest contributor to EVA earnings.

Chart 2: New Zealand Banking Market Annual NPAT and EVA



Source: Reserve Bank of New Zealand, Company Reports, Merrill Lynch estimates

Growth and Returns for Market Segments

The charts overleaf map the Australian and New Zealand banking market forecast rate of growth and current return on equity by product category/customer segment. The scale of the circles represents the contribution to industry NPAT, whilst their positioning reflects the estimated forecast growth (horizontal axis) and return on equity (vertical axis). The charts are divided into four quadrants that delineate the attractiveness of the various segments based on growth and return characteristics.

Value enhancers should trade at price / earnings premiums

1. **Value enhancers** are businesses that combine above industry average growth prospects with above industry rates of internal capital generation (i.e. ROE). These businesses are at least self-funding from a capital perspective and often generate surplus capital despite high growth rate. We believe value enhancers should trade at price / earnings premiums to the sector.

Capital producers are the cash cows of financial services

2. **Capital producers** are often the more mature businesses where growth has slowed but where returns can continue to run above sector averages. These businesses generate significant surplus capital and are the "cash cows" of the financial services industry. Capital producers may trade at either premiums or discounts to the sector depending on the degree of excess returns relative to the extent of growth deficiency and the extent to which funds are successfully reinvested and / or returned to shareholders.

Capital consumers provide growth but lesser returns

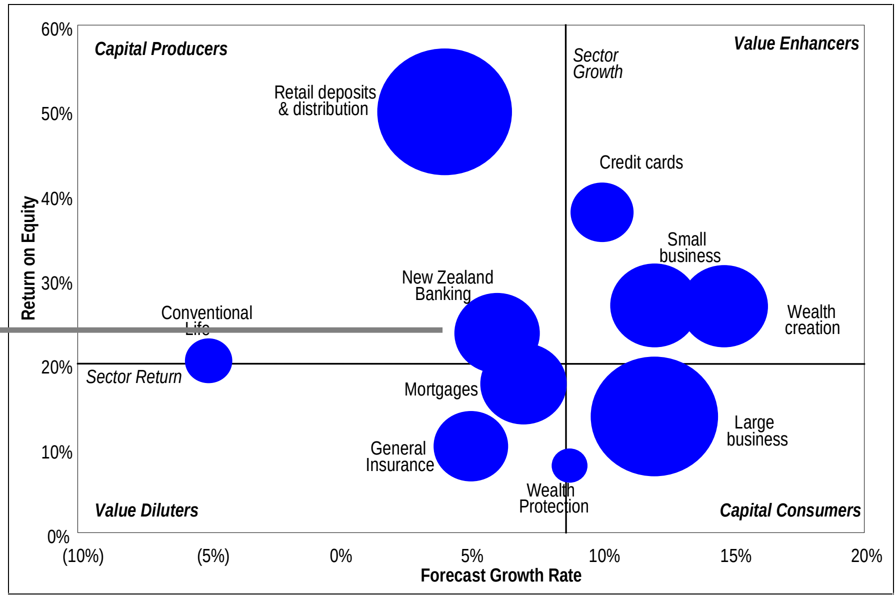
3. **Capital consumers** generate rates of return which, while in line with the cost of capital, are below the industry average. Because of their relatively strong growth profiles, these businesses are unlikely to be self funding from a capital perspective and as such require repatriation of capital from the other business units or injections of fresh equity to fuel growth. Depending on the extent of excess growth and degree to which returns exceed companies' cost of capital, these businesses could trade at either premiums or discounts to the sector.

Value diluters should trade at price / earnings discounts

4. **Value diluters** are almost always in mature markets and lack either prospect for strong growth or for strong returns. Given their low growth profiles, these businesses do generate surplus capital though not at the same rate as capital producers and should trade at price / earnings discounts to the sector.

While it is interesting to compare and contrast this analysis to similar analysis on the Australian market[1], the information available on business segment dynamics is more extensive in Australia (i.e. more granularity).

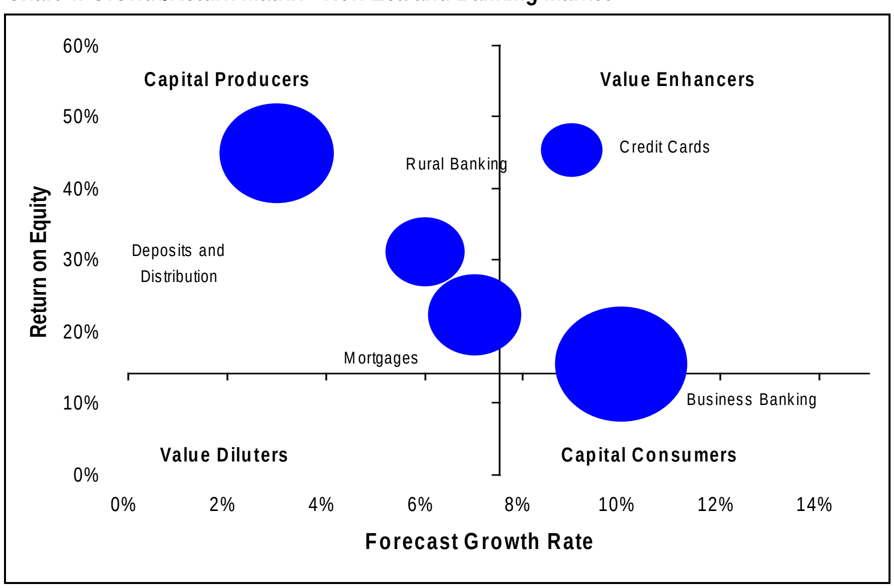
Chart 3: Growth Return Matrix—The Australian Financial Services Market (July 02)



Source: Merrill Lynch Analysis of RBA, APRA, Assirt, Plan for Life, Rice Kachor, Company accounts

Market is structurally biased towards a "capital producing" business mix

Chart 4: Growth/Return Matrix—New Zealand Banking Market



Source: Reserve Bank of New Zealand, Company Reports, Merrill Lynch estimates

[1] Please refer to our report titled *A Structural Review of the Australian Financial Services Market: Strategic Positioning of Listed Australian Banks* (9th July 2002)

From our analysis we believe most segments of the New Zealand banking market have exhibited favourable characteristics. However, we note that compared with other developed countries, the New Zealand household sector is less financially diversified and holds the bulk of its assets in housing, with far fewer assets held in the form of equities or bank deposits.

On our estimates, the identified segments all tend to show relatively attractive return prospects (placed above the horizontal line), whilst approximately half of the segments exhibit attractive growth prospects (placed to the right of the horizontal line). Importantly the mix of segments within the industry appears to be well balanced, with surplus capital generated from the **deposits and distribution** segment available to fund growth within the **business-banking** segment.

Industry Profit Trends

The table overleaf details the historical aggregate industry income statement and balance sheet for the New Zealand banks from 1992-2001. The notable features:

Modest revenue but impressive cost trends

- **The CAGR in total revenues over 1995-2001 has been a relatively modest 6% pa**, whereas related growth in underlying profit (14% pa) and growth in NPAT (13% pa) has been considerably higher. The trend primarily reflects the substantial improvement in industry cost efficiency, with the industry cost to income ratio improving from +66% to circa 48%, with CAGR in operating expenses throughout the period of 0%. **Give the contribution of cost savings (that may have peaked), it may well be that future earnings growth is less appealing.**
- **The CAGR in total assets from 1995 to 2001 of 11% has also been higher than the related growth in revenues (6% per annum),** reflecting ongoing margin compression in both spread and fee related products (although this compression has moderated in the past couple of years).

Consistently low bad debt experience but possibly a little understated

- **Bad debt charges throughout the entire 10 year period we assessed have been remarkably moderate** (averaging a mere 9bp per annum of loans) with a cycle peak in 1998 of 19bp of loans, reflecting the impact during that year of the Asia crisis and the drought. This favourable loss experience perhaps reflects the benefits of increasing industry concentration (e.g. oligopoly pricing) and the introduction of foreign risk management systems. Further, we believe that New Zealand large corporate lending activities (inherently higher risk) are reported through the parent company wholesale / institutional banking divisions (rather than directly through the New Zealand subsidiaries) creating an optically more attractive asset quality profile. It is worth noting that we believe NAB, on acquisition of BNZ, also substantially provisioned against the loan book and has subsequently written back against provisions—which may account for what seems to be a relatively low loss rate.

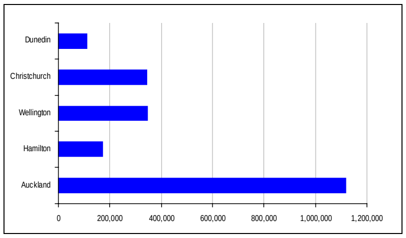
Table 3: New Zealand Banking Industry—Historical Aggregate Income Statement and Assets

(NZD, m):	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	CAGR 1995-2001
Net Interest Income	2,466	2,304	2,462	2,786	2,827	3,095	3,193	3,307	3,527	3911	
Other Income	1,334	1,492	1,401	1,596	1,638	1,705	1,862	1,865	2,140	2264	
Total Income	**3,800**	**3,796**	**3,863**	**4,383**	**4,465**	**4,800**	**5,055**	**5,172**	**5,667**	**6,175**	**6%**
Operating Expenses	(2,560)	(2,713)	(2,630)	(2,906)	(3,038)	(3,158)	(2,982)	(2,944)	(3,106)	(2,987)	0%
Underlying Profit	**1,240**	**1,083**	**1,234**	**1,476**	**1,427**	**1,642**	**2,073**	**2,228**	**2,561**	**3,188**	**14%**
Bad Debt Charges	(246)	(53)	96	9	42	(88)	(201)	(144)	(127)	(191)	
Abnormal Items						74	(130)	125	(7)	(11)	
Profit Before Tax	**994**	**1,030**	**1,330**	**1,485**	**1,469**	**1,628**	**1,742**	**2,209**	**2,427**	**2,986**	**12%**
Tax Expense	(681)	(368)	(410)	(462)	(453)	(430)	(637)	(451)	(658)	(799)	
Profit After Tax	**313**	**662**	**920**	**1,023**	**1,016**	**1,198**	**1,105**	**1,758**	**1,769**	**2,187**	**13%**
Assets (NZD, bn):											
Investments	25.6	23.0	19.0	19.4	21.5	19.2	24.3	28.2	37.1	36.5	
Mortgages	23.1	27.2	32.7	38.5	45.7	50.6	54.5	61.0	64.3	68.7	10%
Other Lending	39.6	32.2	36.2	40.1	43.9	48.3	52.5	60.3	66.3	74.3	11%
Other Assets	2.9	2.9	4.1	5.1	7.5	12.1	10.3	9.0	12.4	10.1	
Total Assets	**83.2**	**85.3**	**92.0**	**103.1**	**118.6**	**130.2**	**141.6**	**158.5**	**180.1**	**189.6**	**11%**
Profitability:											**2001 versus 1995**
Net Interest Income / Lending	3.93%	3.88%	3.57%	3.55%	3.16%	3.13%	2.98%	2.73%	2.70%	2.74%	-81bp
Other Income / Lending	2.13%	2.51%	2.03%	2.03%	1.83%	1.72%	1.74%	1.54%	1.64%	1.58%	-45bp
Total Income / Lending	6.06%	6.39%	5.60%	5.58%	4.98%	4.85%	4.72%	4.26%	4.34%	4.32%	-126bp
Cost / Income	67.4%	71.5%	68.1%	66.3%	68.0%	65.8%	59.0%	56.9%	54.8%	48.4%	
Underlying Profit / Lending	1.98%	1.82%	1.79%	1.88%	1.59%	1.66%	1.94%	1.84%	1.96%	2.23%	+35bp
Bad Debts / Lending	-0.39%	-0.09%	0.14%	0.01%	0.05%	-0.09%	-0.19%	-0.12%	-0.10%	-0.13%	
Profit Before Tax / Lending	1.59%	1.73%	1.93%	1.89%	1.64%	1.65%	1.63%	1.82%	1.86%	2.09%	
Tax Rate	68.5%	35.7%	30.8%	31.1%	30.8%	26.4%	36.6%	20.4%	27.1%	26.8%	
Profit After Tax / Lending	0.50%	1.11%	1.33%	1.30%	1.13%	1.21%	1.03%	1.45%	1.35%	1.53%	

Source: Reserve Bank of New Zealand, Merrill Lynch estimates

The Importance of the Auckland Regional Market

Chart 5: 2001 NZ Population Structure



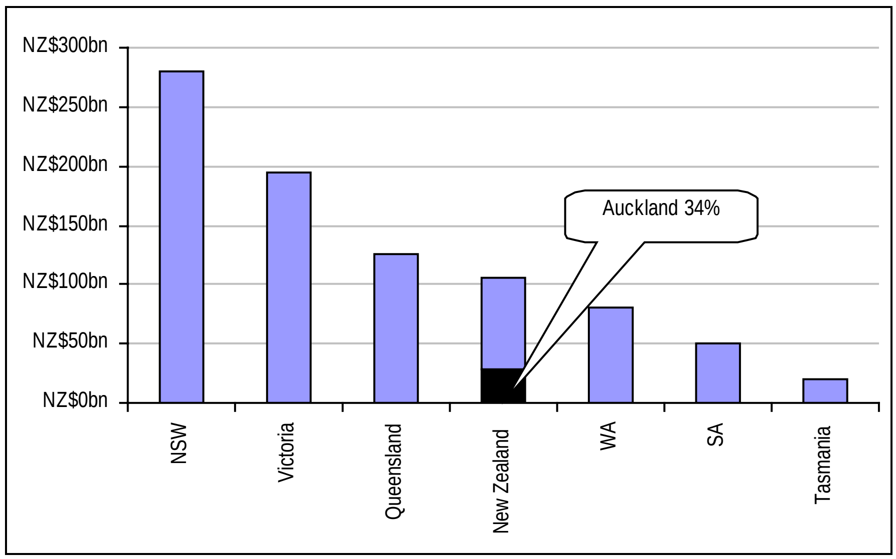
Source: AC Nielsen

New Zealand has a relatively small population of 3.9m people (mid-year 2000), which is a mere 20% of Australia's population of 19.5m (which is fairly small in itself). The chart on the left-hand side illustrates the significant proportion of the New Zealand national population that is resident in Auckland.

New Zealand banking market—fourth biggest 'Australian' State

Nevertheless, despite the relatively small size of the population, New Zealand should be regarded as a medium sized regional banking market, rather than a small national market. In the following chart, we have compared the GDP of each of the Australian states with the GDP of New Zealand, which shows New Zealand to be the fourth largest economy within the region, with a significant micro-economy based around the city of Auckland:

Chart 6: GDP Australian States and New Zealand



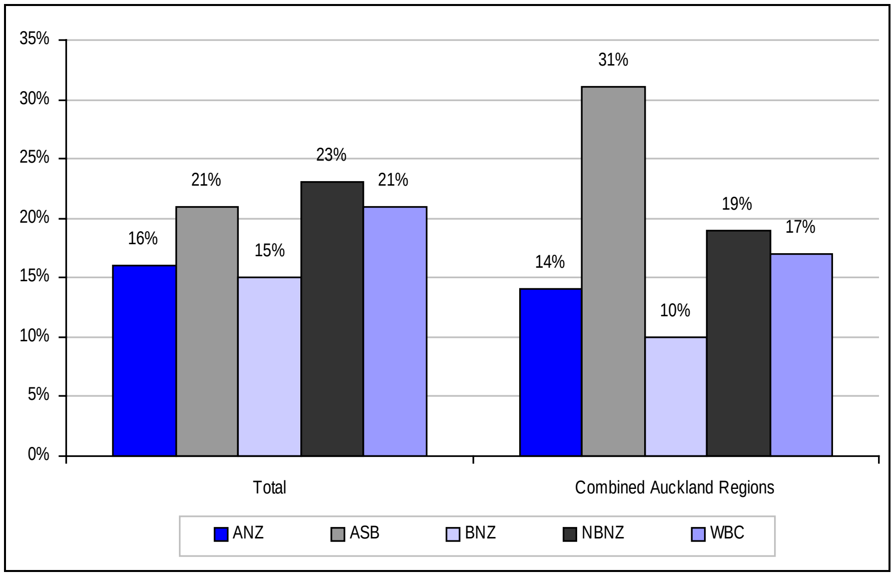
Source: WBC, Merrill Lynch

The demographic and economic profile highlights the underlying importance for New Zealand banks of holding a strong market position in the Auckland market in both Personal Banking and Business Banking (excluding Rural Banking, which is likely to be more geographically dispersed).

ASB Bank has a strong position in the Auckland market, both relative to its competitors and its national market share

The following chart benchmarks the consumer banking market shares of each of the major banks, both in Auckland and in New Zealand overall. It illustrates the relatively strong position of **ASB Bank** in the Auckland market. **ASB** is the only bank with a market share in Auckland that is higher than its national market share. By way of contrast, both **National Bank of New Zealand** and to a lesser extent **Bank of New Zealand** and **Westpac Banking Corporation** have market shares in Auckland that lag their national market shares.

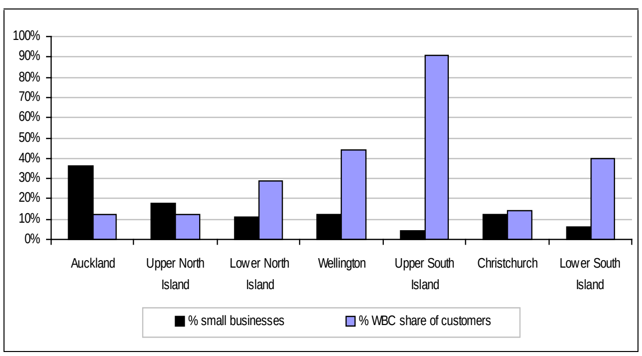
Chart 7: Consumer Banking Market Share in the Auckland Region



Source: AC Nielsen, Statistics NZ, WBC

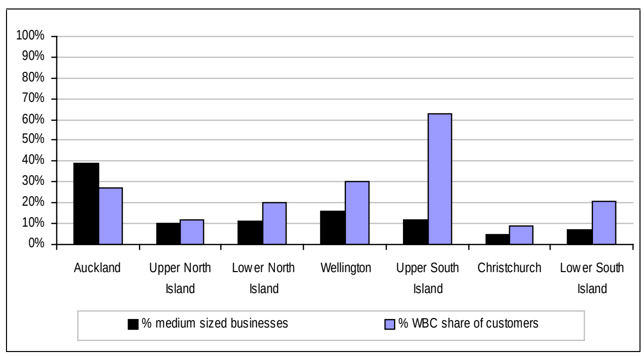
Similarly with small and medium business distribution throughout New Zealand, the following charts illustrate the importance of the Auckland market for leverage to these markets. By way of contrast, we note that WBC has a strong presence in the South Island, rather than in Auckland:

Chart 8: Distribution of Small Businesses



Note: Small businesses defined as 0-5 FTE staff
Source: WBC

Chart 9: Distribution of Medium Sized Businesses



Note: Medium sized businesses defined as having more than five FTE staff
Source: WBC

2. The Players

In this section we have benchmarked the five major banks in New Zealand in terms of operational performance, market share, parent company autonomy and consumer share of wallet.

There are eighteen registered banks in New Zealand but the five major banks account for most industry assets / revenue

The New Zealand banking market comprises eighteen registered banks (as detailed at the end of Section 2 in Table 6). It is, however, dominated by the five major full service banks, as follows:

- ***National Bank of New Zealand* (parent company Lloyds TSB);**
- ***ANZ Banking Group New Zealand* (parent company ANZ Banking Group);**
- ***ASB Bank* (parent company Commonwealth Bank);**
- ***Bank of New Zealand* (parent company National Australia Bank); and**
- ***Westpac Banking Corporation New Zealand* (a branch operation of Westpac Banking Corporation).**

Benchmarking Major Bank Operational Performance

In the table facing we have benchmarked the operational performance of the major New Zealand banks in terms of balance sheets, profitability, asset quality, capital adequacy and returns.

Key observations we have made include:

- In terms of **balance sheet size**, **WBC** has the largest portfolio of net loans and advances, although **National Bank** and **BNZ** are of a similar size (this is also the case for the quantum of net tangible assets). By way of contrast both **ANZ** and **ASB** have smaller portfolios.
- Despite having marginally the smallest portfolio of net loans and advances amongst the major banks, **ASB's** portfolio of demand deposits is the largest for the banks for which we have the data available.
- In turn, the combination of these two factors has assisted **ASB** in having a very strong loan / deposit ratio. Across the major banks, loan / deposit ratios have been stable to improving, although **National Bank** and **WBC** appear to have particularly high ratios.
- In terms of the **revenue composition**, **National Bank** and **ASB** appear to be more loan spread orientated banks, whilst ANZ's revenues appear to be more diversified. **ASB's** net interest margins appears relatively low compared with the peer group, perhaps reflecting its lending bias towards mortgages.
- Across the major banks, **cost to income ratios** have converged to the mid-40s level, with the exception of **ASB**. While the ASB cost ratio has considerably improved, it sits around 5 percentage points above the peer group levels at 51 percent. This might reflect business mix, customer skew, growth profile or other factors. Cost to assets ratios exhibit much greater dispersion.
- **Bad debt charges** appear to be moderate across the sector, particularly for both **ASB** and **BNZ**. However, the bad debt charge (and general provision coverage) appears to be structurally higher at **ANZ**. There seems to be more convergence across the major banks in terms of net write-off levels, although both **National Bank** and **ANZ** appear to be higher than the peer group (presumably problem loans within **National Bank** are all written off, given the absence of a general provision).
- Both **capital adequacy levels** and **returns** appear to be high across the major banks, although benchmarks such as ROE are less relevant for **WBC** given the branch status of its New Zealand banking operations.

Table 4: New Zealand Major Banks—Key Financials

	National Bank of New Zealand			ANZ Banking Group New Zealand			ASB Bank			Bank of New Zealand			Westpac Banking Corporation NZ Branch		
(NZD, m)	**2000**	**2001**	**2002**	**2000**	**2001**	**2002**	**2000**	**2001**	**2002**	**2000**	**2001**	**2002**	**2000**	**2001**	**2002**
Balance Sheet:															
Net Loans and Advances	23,885	31,215	33,835	21,505	21,610	21,449	14,407	16,174	19,032	27,906	29,504	30,215	26,537	31,830	32,404
Demand Deposits				6,343	7,235	7,072	4,751	6,169	7,466	5,448	6,676	6,980			
Loan/Deposits	151%	158%	155%	136%	124%	113%	103%	92%	104%	143%	125%	124%	145%	135%	142%
Net Tangible Assets	1,761	2,177	2,514	1,413	1,186	1,243	847	820	1,033	1,491	1,772	2,046	2,912	3,204	3,710
Net Tangible Assets / Share	$11.08	$13.69	$15.81	$4.62	$3.87	$4.06	$2.62	$2.54	$3.20	$0.60	$0.72	$0.83			
Profitability:															
Operating Surplus (**pre goodwill amortisation**)	384	416	503	321	398	431	150	183	225	390	441	583	434	509	657
Interest Spread	2.18%	2.07%	2.09%	2.01%	2.08%	2.19%	2.02%	1.88%	1.77%	1.96%	1.82%	1.97%	2.52%	1.94%	2.13%
Net Interest Margin	2.56%	2.44%	2.66%	2.49%	2.64%	2.76%	2.19%	2.31%	2.13%	2.13%	2.30%	2.45%	2.88%	2.46%	2.72%
Net Interest Income / Total Income	70%	71%	73%	58%	59%	59%	68%	71%	70%	58%	60%	62%	65%	64%	61%
Financial Markets Income % Non-Interest Income	24%	26%	27%	12%	16%	15%	16%	17%	19%	20%	22%	20%	16%	16%	17%
Cost to Income Ratio (pre goodwill amortisation)	46.9%	46.9%	43.9%	55.7%	46.1%	46.1%	57.3%	54.5%	51.3%	54.4%	51.9%	45.8%	50.6%	46.0%	45.6%
Costs to Average Assets (pre goodwill amortisation)	1.60%	1.58%	1.56%	2.3%	1.95%	1.99%	2.02%	1.89%	1.68%	1.90%	1.77%	1.69%	2.07%	1.62%	2.05%
Effective Tax Rate	27%	30%	29%	25%	29%	29%	34%	35%	33%	24%	25%	22%	29%	24%	25%
Asset Quality:															
Bad Debt Charge / Average Loans	0.10%	0.05%	0.12%	0.21%	0.26%	0.30%	0.08%	0.09%	0.10%	0.05%	0.04%	-0.05%	0.13%	0.16%	0.13%
Write-offs / Average Loans	0.32%	0.30%	0.24%	0.24%	0.30%	0.30%	0.02%	0.03%	0.03%	0.10%	0.08%	0.09%	0.13%	0.06%	0.14%
Impaired Assets / Total Assets	0.43%	0.34%	0.31%	0.33%	0.36%	0.16%	0.05%	0.36%	0.35%	0.25%	0.12%	0.08%	0.37%	0.38%	0.24%
Specific Provisions / Impaired Assets	69%	62%	64%	40%	40%	53%	46%	66%	78%	20%	43%	23%	23%	26%	16%
General Provisions / Risk Weighted Assets	No general provisions for doubtful debts held			0.94%	0.95%	1.10%	0.49%	0.53%	0.55%	0.84%	0.72%	0.60%	0.32%	0.29%	0.28%
Capital Adequacy:															
Tier 1 Ratio	8.52%	8.94%	9.50%	7.83%	6.53%	6.89%	7.64%	7.25%	7.90%	6.25%	6.80%	7.88%	Capital adequacy managed at a group level		
Capital Adequacy Ratio	10.57%	10.63%	11.32%	12.17%	10.25%	10.69%	9.57%	10.07%	10.44%	10.80%	10.98%	11.96%			
Tangible Equity / Assets	5.6%	6.0%	6.5%	5.2%	4.4%	4.6%	4.9%	4.1%	4.3%	4.3%	4.7%	5.7%	4.1%	4.5%	5.9%
Returns:															
ROE	23.3%	21.1%	21.4%	24.7%	30.6%	35.3%	18.9%	22.0%	24.3%	27.1%	26.7%	30.3%	15.2%	15.0%	17.4%
ROA	1.25%	1.23%	1.34%	1.24%	1.47%	1.58%	0.94%	0.99%	1.02%	1.18%	1.21%	1.58%	1.34%	1.39%	1.74%
RoRWA	1.90%	1.85%	1.98%	1.84%	2.20%	2.38%	1.54%	1.70%	1.85%	1.72%	1.77%	2.24%	1.85%	2.03%	2.56%

Note: ANZ 2002 includes $36m pre-tax gain on sale of funds management operations; NAB 2002 includes $56m pre-tax gain on sale of subsidiaries; WBC 2002 includes $104.9m pre-tax gain on sale of AGC. Securitised mortgages added back to WBC Net Loans and Advances. Financial year-end: NBNZ December; ANZ September; ASB June; BNZ September; WBC September.
Source: Company reports, Merrill Lynch estimates

Market Shares of the New Zealand Major Banks

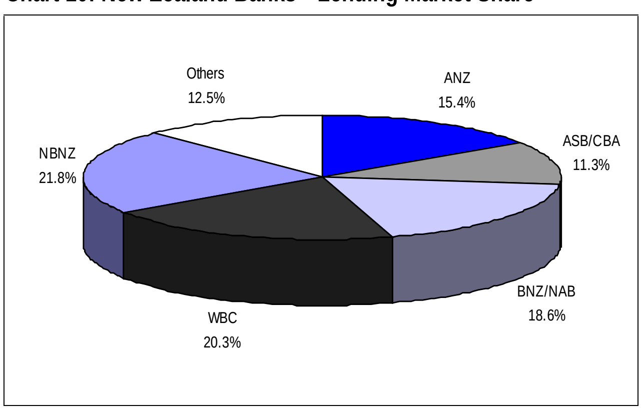
WBC and National Bank (Lloyd's) seem best positioned

In the charts below we have estimated the market shares as at the end FY01 for each of the major banks, using loan disclosures within company general disclosure statements and Reserve Bank of New Zealand statistics.

The key observations we have made include:

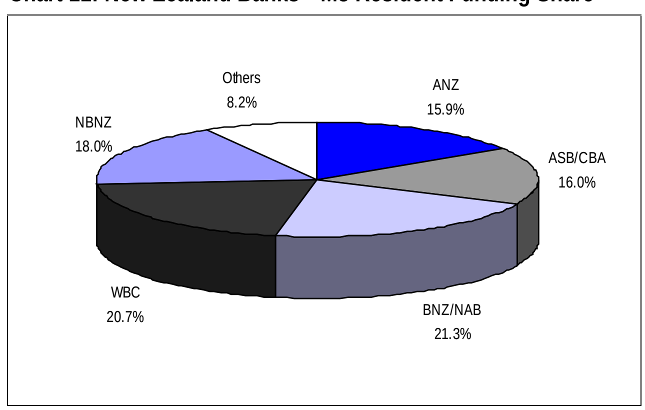
- The upper two charts indicate that **WBC** and **National Bank** (Lloyd's) have strongest market shares in total lending, with **WBC** and **BNZ** (NAB) enjoying the strongest market shares in deposits (we have used M3 Resident Funding as a proxy). New Zealand (like Australia) is one of the few developed banking markets not to have some form of deposit insurance.
- Comparing the loan to deposit mix, **ASB** and **BNZ** appear to have stronger shares in deposits than in lending. Conversely, **National Bank** appears to have a weaker share in deposits than in lending.
- There appears to be little dispersion in mortgage market shares amongst the five major banks (refer lower left chart), with **ASB** enjoying a marginally greater market share than **ANZ** and **BNZ**, owing to (amongst other things) their strong presence in the important Auckland mortgage market (larger population, higher average house prices). By way of contrast, **ASB** has a much lower market share in other lending (which is predominantly business). Conversely, the "other lending" market share of **BNZ** (which is also heavily focused on the Auckland market), is much higher than their corresponding mortgage market share.
- Amongst the five major banks, **ASB** appears to have relatively weaker market shares on most measures (particularly in business lending). This may reflect the fact that—unlike each of the other major banks—**ASB** has not undertaken a transforming banking merger in its recent history.
- It would seem **WBC** and **National Bank** appear to have the strongest market positions overall, followed by **BNZ (NAB)** and then **ANZ** and **ASB (CBA).** We conclude that ANZ and CBA, particularly the latter, would be most likely to benefit from acquisition of National Bank of New Zealand (should it be for sale). We explore this possibility later in the report.

Chart 10: New Zealand Banks—Lending Market Share



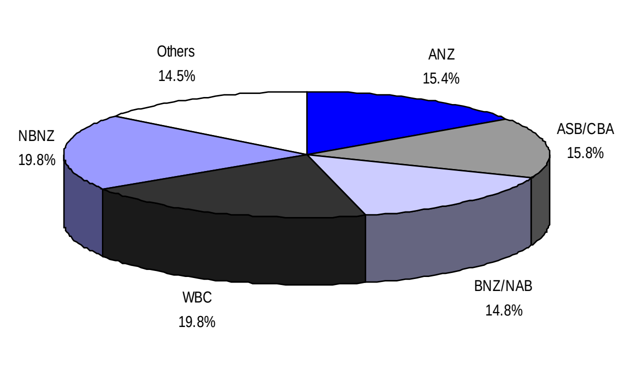
Source: Company reports, Reserve Bank of New Zealand, Merrill Lynch estimates

Chart 11: New Zealand Banks—M3 Resident Funding Share



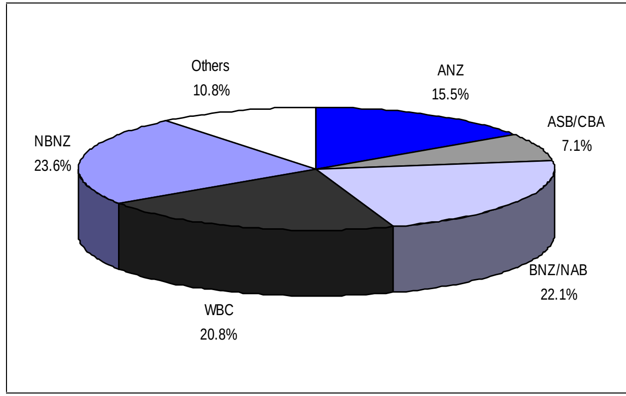
Source: Company reports, Reserve Bank of New Zealand, Merrill Lynch estimates

Chart 12: New Zealand Banks—Mortgages Market Share



Source: Company reports, Reserve Bank of New Zealand, Merrill Lynch estimates

Chart 13: New Zealand Banks—Other Lending Market Share



Source: Company reports, Reserve Bank of New Zealand, Merrill Lynch estimates

Control: Autonomy or Trans-Tasman Benefits?

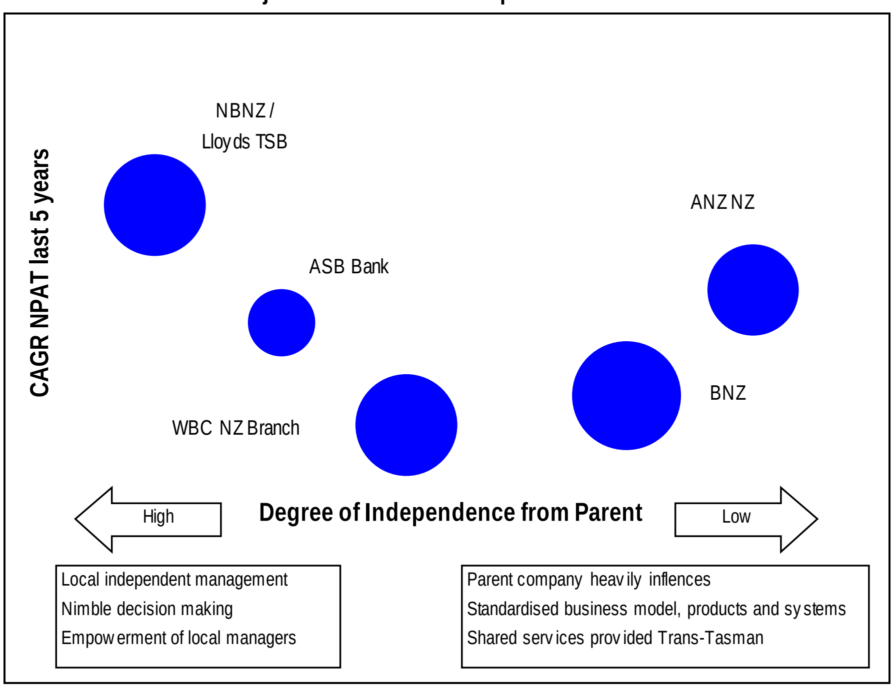
More than 99% of New Zealand banking assets foreign owned

The foreign ownership of banking assets is particularly high in New Zealand—in excess of 99% of the industry being foreign owned (up from c40% in 1985). In fact, there are now only two New Zealand owned banks in the country, namely TSB and the New Zealand Post's Kiwibank. All of the other banks operating in New Zealand have parents domiciled in a range of countries, including Australia, the UK, the Netherlands, Korea and the US (refer Table 6 at the end of this section).

In the chart below we've conceptually mapped the perceived degree of operational independence of each of the major banks from their respective parents (horizontal axis) against historical profit growth (vertical axis). The objective of this exercise was to measure the relationship between profit growth and management style. The foreign ownership structures of the five major banks provide various management options for the respective parent companies.

Higher growth banks have either had a high level of autonomy or a high level of parent company integration—but not a combination of both

Chart 14: New Zealand Major Banks—Growth/Independence Matrix



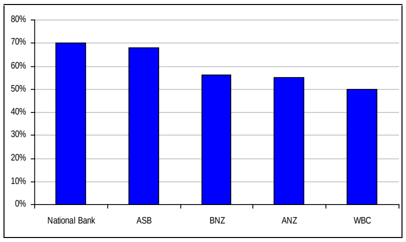
Source: Company reports, WBC, Merrill Lynch estimates

Whilst the profit growth for National Bank has been positively distorted by the impact of a merger of equals during the period examined, the results nevertheless seem to argue for a clear strategy either towards a high level of autonomy or high level of parent integration—but not a combination of both.

Whilst either strategy appears capable of driving robust profit growth, banks that have recorded the historically highest rate of growth have either allowed their subsidiaries to operate with a high degree of autonomy (namely, **National Bank** and **ASB**) or have extracted maximum Trans-Tasman synergies (namely, **ANZ**). Relatively poor performers (namely, **WBC** and **BNZ**) appear to have lacked a clear strategy either way.

Share of Wallet

Chart 15: Customer Satisfaction 2002



Source: AC Nielsen CFM, Merrill Lynch

Finally, looking at positioning within the consumer market, the following table details the share of wallet amongst various customer segments, particularly from the perspective of **WBC**. It shows **ASB** Bank enjoying relatively good penetration of the "youth", "starting out" and "retired" segments and **National Bank** enjoying relatively good penetration of the "nester" and "high net worth" segments:

Table 5: New Zealand Banks Share of Wallet by Customer Segment

	Youth	Coper	Starting Out*	Nester	High Net Worth*	Transition*	Retired
WBC	78%	38%	64%	54%	47%	50%	49%
...market position	3rd	5th	5th	4th	3rd	3rd	4th
Best Competitor	94%	99%	83%	68%	65%	69%	64%
...who is	ASB	BNZ	ASB	NBNZ	NBNZ	ASB	ASB

*Seen as key opportunity segments by WBC
Source: WBC, AC Nielsen

Registered Banks in New Zealand

Table 6: New Zealand Registered Banks

Bank	Owned by	Country	Date Registered	Credit rating
ABN Amro Bank	ABN Amro	Netherlands	2 Mar 1998	AA/Aa3
AMP Bank	AMP	Australia	12 Oct 1998	A-
ANZ Banking Group	ANZ Banking Group	Australia	1 Apr 1987	AA-/Aa3
ASB Bank	Commonwealth Bank	Australia	11 May 1989	AA-
Bank of New Zealand	National Australia Bank	Australia	1 Apr 1987	AA
Bank of Tokyo Mitsubishi	Bank of Tokyo Mitsubishi	Australia/Japan	18 Sep 1996	BBB+
Citibank	Citibank	USA	22 Jul 1987	Aa1/AA
Commonwealth Bank	Commonwealth Bank	Australia	23 Jun 2000	AA-/Aa3
Deutsche Bank	Deutsche Bank	Germany	8 Nov 1996	Aa3/AA-
Kiwi Bank	Kiwi Bank	New Zealand	29 Nov 2001	AA-
Kookmin Bank	Kookmin Bank	Korea	14 Jul 1997	A3/BBB
St George Bank New Zealand	St George Bank	Australia	3 Feb 2003	BBB-
Rabobank New Zealand	Rabobank	Netherlands	7 Jul 1999	AAA
Rabobank Nederland	Rabobank	Netherlands	1 Apr 1996	AAA/Aaa
HSBC	HSBC	Hong Kong/UK	22 Jul 1987	Aa3
National Bank of New Zealand	Lloyds TSB	UK	1 Apr 1987	AA-/Aa1
TSB Bank	TSB Community Trust	New Zealand	8 Jun 1989	BBB-
Westpac Banking Corporation	Westpac Banking Corp	Australia	1 Apr 1987	AA-/Aa3

Source: Reserve Bank of New Zealand

3. New Zealand and Australian Banks

New Zealand bank operations a meaningful contributor to the major Australian bank profits…

In this section we have placed the New Zealand banking operations of the major Australian banks into the context of their global operations. Each of the major banks in Australia has a meaningful wholly owned New Zealand subsidiary or branch operation, as follows:

- **ANZ Banking Group—ANZ Banking Group New Zealand;**
- **Commonwealth Bank—ASB Bank;**
- **National Australia Bank—Bank of New Zealand; and**
- **Westpac Banking Corporation—Westpac (branch operation).**

Contribution to Earnings

The contributions to major bank earnings from these New Zealand operations have been increasing in importance and have **comprised 12% of FY02 earnings**. **WBC** has greatest relative earnings exposure to the New Zealand market (see chart below).

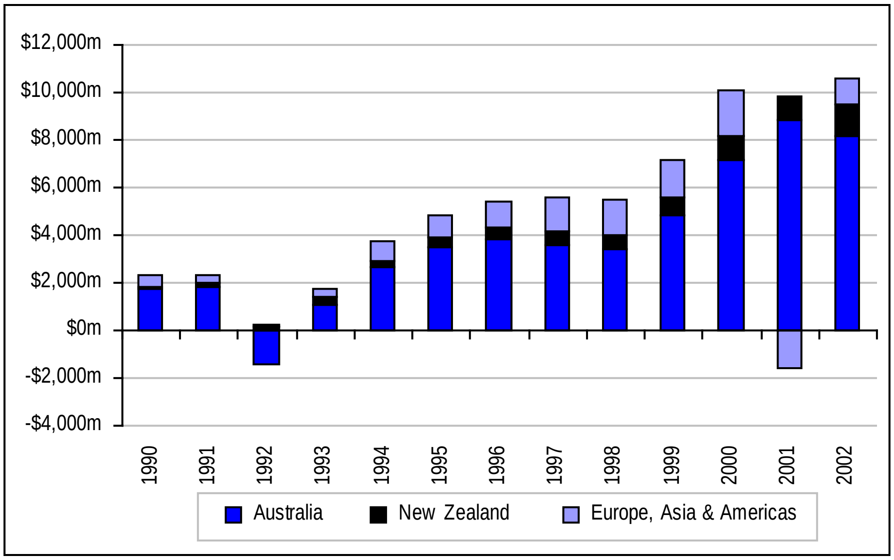
…contributing at least 12% to FY02 cash earnings (more if the wholesale banking and life insurance operations included)

However, we note that these subsidiaries do not comprise the entirety of the New Zealand sourced earnings for the major Australian banks. For example, wholesale banking earnings are usually reported outside of these subsidiaries. Further, we note that the results for ASB Life Assurance are not reported as part of the **ASB Bank** annual report/general disclosure statement.

The chart below places the significance of New Zealand earnings in the context of total earnings of the Australian major banks, illustrating over time an increasing contribution to aggregate earnings. During the period 1994-2002, New Zealand contributed on average 11% to aggregate earnings of the Australian major banks.

We wonder whether the presence of Australian major banks in the New Zealand market reflects the interdependence between the economies of New Zealand and Australia. Both countries have significant trade linkages (with Australia currently New Zealand's largest single trading partner) and there are various institutional factors linking Australia and New Zealand (for example, in 1983, the Australia & New Zealand Closer Economic Relations Trade Agreement (CER) was established to provide for free trade):

Chart 16: Australian Major Bank Earnings—Geographic Segments (A$m)



Note: ANZ segments estimated from 2000-2002 based on domicile of assets; NAB New Zealand segments in 2002 based on Financial Services New Zealand plus 10% of Wholesale Financial Services earnings.
Source: Company reports, Merrill Lynch estimates

Importance of New Zealand has Increased

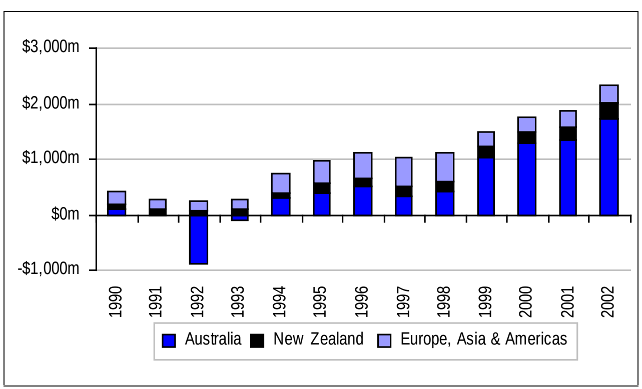
Since the late 1980s, all of the major Australian banks have increased their relative commitment to the New Zealand banking market through:

- **Acquisitions**, either directly by the parent company or sponsored through the respective New Zealand subsidiary. There have also been indirect acquisitions through integration of New Zealand subsidiaries of Australian acquisitions;
- Back and mid-office office **operational convergence** (e.g. "Trans-Tasman" initiatives)—most notably for both **ANZ** and **WBC**. In the late 1990s, some Australian banks operationally moved towards more "global management" of business lines, so that functional management in the New Zealand operations of the respective banking subsidiaries reported directly to functional heads outside of New Zealand (rather than to the local MD). As part of this initiative some Australian banks centralised aspects of New Zealand support services such as information technology, dealing operations, back office support and finance and accounting to Australia; and
- **Issuance of equity instruments** offering a New Zealand franked distribution—such instruments were issued by **WBC** in 1999 (NZ Class shares) and **CBA** in 2002 (ASB preference shares), but were also examined by **ANZ** in 1999. In 1999 **WBC** also issued USD denominated trust preferred securities from their New Zealand branch, ostensibly for taxation purposes.

Following **NAB's** exit from the USA market and unwinding of its global strategy in 2002, **New Zealand has now been defined as one of three key retail financial services regions for the NAB Group** (along with Australia and Europe). Although less significant, we also note that in 2002 **SGB** announced the establishment of a 50% joint venture with dominant New Zealand food retailer Foodstuffs, initially providing a direct deposit offering similar to the Australian Dragondirect product.

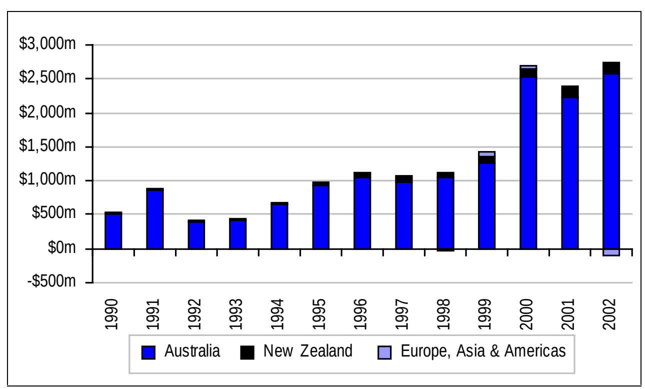
Nevertheless, amongst each of the major banks the relative 1994 to 2002 earnings contributions from New Zealand have varied, with a relatively greater contribution being derived from **WBC** and relatively smaller contribution being derived from **CBA**, as depicted in the following charts:

Chart 17: ANZ Banking Group—*14% Average Earnings Contribution* from New Zealand 1994-2002



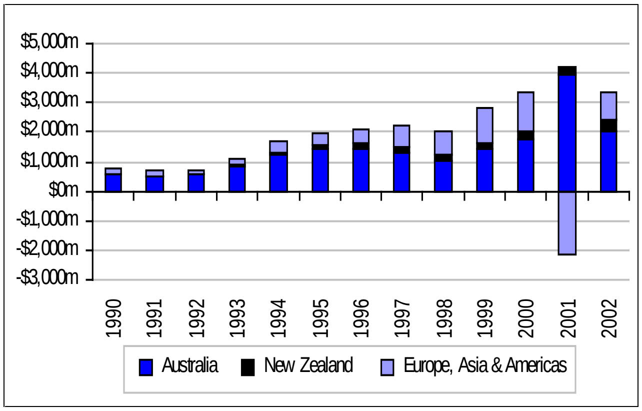
ANZ segments estimated from 2000-2002 based on domicile of assets
Source: Company reports, Merrill Lynch estimates

Chart 18: Commonwealth Bank—*5% Average Earnings Contribution* from New Zealand 1994-2002



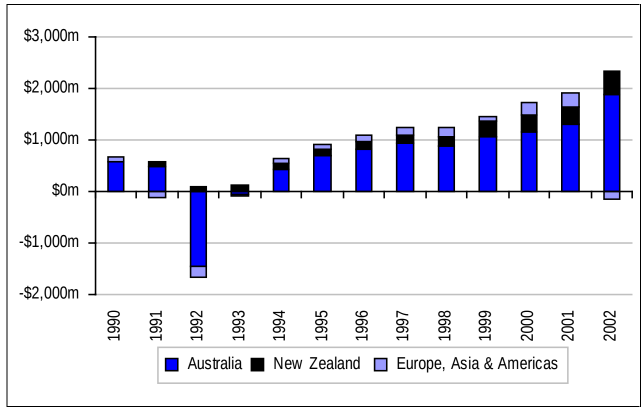
Source: Company reports, Merrill Lynch estimates

Chart 19: National Australia Bank—*9% Average Earnings Contribution* from New Zealand 1994-2002



NAB New Zealand segments in 2002 based on Financial Services New Zealand plus 10% of Wholesale Financial Services earnings
Source: Company reports, Merrill Lynch estimates

Chart 20: Westpac Banking Corporation—*17% Average Earnings Contribution* from New Zealand 1994-2002



Source: Company reports, Merrill Lynch estimates

4. Market Consolidation

In this section we have reviewed the history of, and prospects for, further M&A within the New Zealand banking industry, with a particular focus on the National Bank of New Zealand.

Concentrated Market Limits Opportunities

New Zealand has a relatively highly concentrated banking industry—which limits M&A opportunities

New Zealand has a relatively highly concentrated banking industry, with the five major banks collectively controlling more than 90% of all the bank assets in New Zealand. The two dominant banks are **WBC** and **National Bank**, although there are strong niches enjoyed by both **ASB** (mortgages) and **BNZ** (corporate banking). This high level of concentration perhaps reflects the relatively small size of the market.

Given this existing high degree of concentration, further meaningful M&A activity is only likely to occur through either:

- **Out-of-market activity—**e.g. should the parent companies of New Zealand's major banks merge (i.e. mergers amongst major banks in Australia or a major bank in Australia merging with Lloyds TSB in the UK). We have already seen this occur on a small scale with the **CBA** / Colonial merger in 2000 and the **WBC** / BT Financial merger in 2002; or
- **Parent company divestments—**one or more of the parent companies of the New Zealand banks divesting their New Zealand subsidiary. We have already seen this with the Bank of Scotland divestment of Countrywide Bank in 1998 and the divestment of **WBC's** AGC subsidiary in New Zealand and Australia in 2002.

In particular, we note that consolidation has been one of the key drivers behind the dominant market positions of both **WBC** and **National Bank** / Lloyds TSB.

Historical Bank M&A Multiples

Recent major New Zealand M&A transactions have been executed on an average historical PE multiple of 12.1x and a price/NTA of 2.0x

The following table details recent major New Zealand M&A transactions. This table does not include smaller transactions, such as the acquisition of Westland Bank by ASB in 1992, the acquisition of United Bank by Countrywide Bank in 1992 and the acquisition of the Rural Bank by the National Bank of New Zealand in 1992. Nor does it include non-bank financial services transactions, such as the acquisition of Sovereign Limited by ASB Bank in 1998.

These transactions have been executed on an average historical PE multiple of 12.1x (range 8.3x to 15.2x) and a price/NTA of 2.0x (range 1.5x to 2.7x). The broad trend has been for transaction multiples to increase throughout this period, perhaps reflecting the capitalisation of in-market merger synergies into acquisition prices:

Table 7: Recent Major New Zealand Bank M&A Transactions (NZD)

Date	Target	Acquirer	Value	Price/NTA	PE Historical
March 1989	Post Bank	ANZ	$679m	1.8x	8.9x
May 1989	ASB (75%)	CBA	$252m	1.7x	8.3x
June 1992	Countrywide Bank	Bank of Scotland	$149m	1.3x	15.3x
November 1992	Bank of New Zealand	NAB	$1,481m	2.2x	10.0x
December 1995	BNZ Finance	NAB/BNZ	$280m	1.5x	12.2x
April 1996	Trust Bank	WBC	$1,274m	2.3x	13.6x
August 1998	Countrywide	Lloyds TSB/NBNZ	$850m	2.6x	15.2x
August 2000	ASB (25%)	CBA	$560m	2.7x	13.1x

Source: Merrill Lynch

Can We Expect More Consolidation?

Lloyds TSB lacks sufficient capabilities in the Australian market to service its New Zealand corporate client base and more recently their capital position has been pressured

Despite increasing their commitment to the New Zealand market in 1998 through a merger of equals (the National Bank acquisition of Countrywide), **Lloyds TSB has been the subject of perennial conjecture regarding the ownership of its New Zealand operations**.

The conventional wisdom is that—unlike each of the Australian major banks—Lloyds TSB lacks sufficient capabilities in the Australian market to service its New Zealand corporate client base. More recently, Lloyds' capital position in the UK has come under pressure, although we acknowledge the recent indications from the company that their life assurance operations will not require additional capital until the FTSE reaches 3,000 (at which point less than 300m pounds would be required). **Nevertheless, we believe that these events might hasten a strategic review of the National Bank subsidiary.**

In the table below we have calculated some hypothetical divestment multiples, based upon recent transactions and upon the multiples that Lloyds TSB acquired Countrywide Banking Corporation:

Table 8: Hypothetical M&A Pricing for National Bank

(NZD)	PE Historical	Price/NTA	
Based on recent transactions:			
…average	12.1x $503m = $6.1bn	2.0x $2.514bn	$5.0bn
…low	8.3x $503m = $4.2bn	1.5x $2.514bn	$3.8bn
…high	15.2x $503m = $7.6bn	2.7x $2.514bn	$6.8bn
Based on Countrywide transaction	15.2x $503m = $7.6bn	2.6x $2.514bn	$6.5bn

Source: Merrill Lynch

National Bank divestment valuation +NZ$4.4bn

We consider the average multiple of recent transactions to be a reasonable basis for establishing a National Bank divestment valuation. This is because the lower historical multiples reflected distressed circumstances and local banks seeking strong parent company support, whilst the higher historical multiples reflected the capitalised value of in-market merger synergies and occurred during a time of relatively more buoyant equity markets. On this basis, we would value National Bank at between NZ$5.0bn and NZ$6.1bn.

Lloyds TSB's own acquisition of Countrywide Banking Corporation was priced at or near peak M&A multiples. As a result, Lloyds TSB could be reluctant to divest National Bank for less than the multiples for which Countrywide was originally acquired. Potential variables in the pricing on the upside could be the existence of any merger synergies (in the event of an in-market merger) and, on the downside, any capital deficiency within Lloyds TSB (thereby forcing a divestment).

In our view, the realistic potential acquirers of National Bank include (in order of likelihood):

ANZ and CBA are likely to be structurally the most attracted to the National Bank platform

- **ANZ Banking Group:** ANZ lacks any leading positions in the New Zealand banking market and lacks the degree of scale that is already enjoyed by WBC. Acquisition of National Bank would enable ANZ to capture a greater share of the considerable trade finance and foreign exchange trading business across Australia, New Zealand and the Pacific Islands (all core geographic markets and lines of business for ANZ). ANZ could utilise the rural finance expertise of National Bank to assist in increasing its penetration of the regional banking market in Australia.
- **Commonwealth Bank:** While ASB Bank has historically experienced strong growth (and thereby might not need an acquisition), as the smallest of the five major banks in New Zealand, ASB Bank would also have less difficulty in satisfying New Zealand's "competition law business acquisition tests" (refer below). Further, National Bank would provide ASB with a strong presence in business, which it currently lacks and, to that extent, would be a transforming deal.

- **National Australia Bank:** NAB has clearly defined New Zealand as a core retail banking market (along with Australia and Europe). The acquisition of National Bank would provide a dominant position in a core market (including a stronger share position in the core NAB market of rural banking), although might distract NAB from further building its position in Europe.

New Zealand Bank M&A Competition Policy

Acquisitions assessed on impact (lessening) on competition…

The Commerce Commission administers competition law in New Zealand. All business acquisitions are assessed under Section 47 of the Commerce Act under the framework of whether or not the acquisition would substantially lessen the competition within one or more relevant markets. The standard has been drafted to be consistent with the corresponding Australian test and the Act prohibits business acquisitions that result in such substantial lessening of competition in any relevant market. Chart 21 (over leaf) schematically details the Commission's approach to the assessment of business acquisitions.

…but the competitive landscape is not well defined

There have been few precedents as to how the Commission defines the 'discrete' markets within the New Zealand financial services industry. Nonetheless, in the 2000 CBA / Colonial business acquisition ruling, the Commission identified life insurance, managed funds / superannuation and investment administration services as discrete national markets for competition review. Further, in the 2002 GE Capital Finance / AGC business acquisition ruling, the Commission identified that consumer finance products (not including motor vehicles), retail merchant finance (as a conservative alternative) and business finance were discrete national markets for competition purposes. Notably, in both instances, the relevant markets were found to be national in their geographic scope.

Safe harbours of 40% market share or 70% market share if at least one competitor has 15% or more of the market

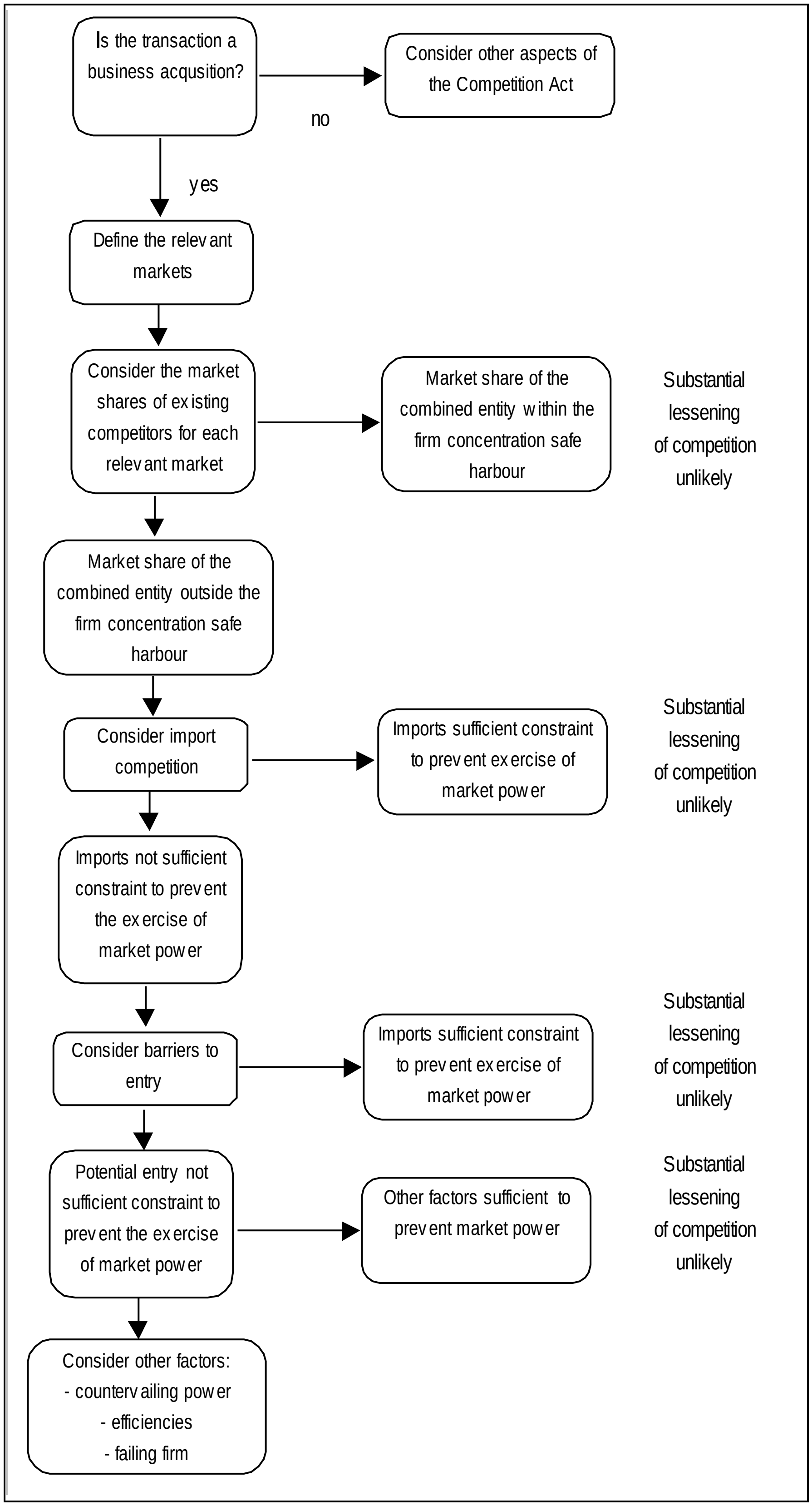
The Commission has established "safe harbour" provisions in its interpretation of the legislation, defining the market share concentration thresholds below which the substantial lessening of competition is prima facie unlikely to be found. The relevant test to be used turns on whether the largest three competitors have more or less than 70% share in the relevant market. More particularly, the Commission considers a business acquisition unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exists:

- **No unilateral market power:** Where the three-firm concentration ratio (including any interconnected or associated shares) in the relevant market is below 70%, **the combined entity has less than in the order of a 40% market share**; or
- **No coordinated market power:** Where the three-firm concentration ratio (including any interconnected or associated shares) in the relevant market is above 70%, **the market share of the combined entity is less than in the order of 20%**.

New Zealand M&A regulations are less restrictive than the corresponding Australian tests

This second safe harbour provision is a little less restrictive than the corresponding Australian test (which applies a **four** firm concentration ratio to the relatively low thresholds of 75% and 15% respectively), owing ostensibly to the smaller size of the New Zealand economy and its generally more concentrated industry structures. Further, we note that whilst the geographic definition of markets in New Zealand competition law is usually national in scope, many financial services markets in Australia have been more restrictively defined from a geographical perspective (such as state-wide).

Chart 21: Competition Commission Approach to Assessment of Business Acquisitions



Source: Commerce Commission

Any major bank merger involving National Bank would breach safe harbour provisions

In the following table we apply the three-firm concentration ratio across four product markets within the New Zealand banking market. We acknowledge some limitations in our analysis. In particular, we believe the Commission would likely identify a larger number of more discrete markets for any specific bank merger proposal and, further, we have assumed that in each instance the relevant market identified would be national (rather than regional) in its scope. Perhaps the market likely to be of greatest competitive concern for bank mergers in New Zealand would be small business lending, where non-banks do not traditionally contest.

Nevertheless, using the available data, we observe that the application of the three-firm concentration ratio involving a hypothetical in-market merger of National Bank of New Zealand with any of the four Australian major banks New Zealand operations would result in market shares of more than 70% in each of the markets identified. As a result, the first "safe harbour" test would be breached, and the second test (market share of the combined entity of less than in the order of 20%) would apply.

On that note, we calculate that in each of the markets identified a merger involving National Bank and any of the other major banks would result in a market share well in excess of 20% (indeed, National Bank already has more than a 20% market share in its own right in many markets).

On this basis, a major bank merger involving National Bank would prima facie breach New Zealand competition law "safe harbour" provisions. This might make further material market consolidation a problematic activity.

Table 9: New Zealand Banking Market—Three Firm Concentration Ratios

	Total loans and Advances	Total deposits	Mortgages	Other lending
National Bank of New Zealand	21.8%	21.4%	19.9%	23.6%
#1 (excluding NBNZ)	20.3%	25.3%	19.8%	22.1%
#2 (excluding NBNZ)	18.6%	24.6%	15.8%	20.8%
#3 (excluding NBNZ)	15.4%	19.0%	15.4%	15.5%
Three firm concentration ratio	76.2%	90.3%	70.8%	82.0%

Source: Company reports, Merrill Lynch estimates

Given market shares of any hypothetical combined entity involving National Bank would likely be outside of the concentration ratio safe harbour, the Commission would need to consider other factors, including:

- **The constraint on the exercise of market power from import competition:** In this regard, we note that import competition is likely to be limited given that the four major Australian banks (who dominate banking markets throughout Australia and the Pacific) already control circa 70% of banking assets in New Zealand (N.B. St George recently entered New Zealand with its Foodstuffs JV). Further, while there are several overseas incorporated banks already in New Zealand, the trend recently has been for exit from (rather than entry to) the New Zealand banking market (e.g. BNP Paribas exited in March 2001). Accordingly, we do not see much constraint on the exercise of market power from import competition.
- **The constraint on the exercise of market power from the threat of new entrants:** Under New Zealand competition law, a business acquisition is unlikely to result in a substantial lessening of competition if there is a real threat of timely and meaningful market entry and expansion from new firms. As a result the Commission will examine industry barriers to entry and the history of past market entry as an indicator of the likelihood of future entry. However, again we do not see much constraint on the exercise of market power from the threat of new competition. In particular, we note that the Australian insurer AMP exited the New Zealand banking market in late 2002

after registering as a bank in New Zealand four years previously, following the acquisition of the local retail banking business of Citibank in 1998.

- **Efficiencies:** New Zealand competition law recognises that combined entities in business acquisitions might be able to make unit cost efficiency gains that are not obtainable by other means, thereby facilitating price reductions. Where a sound and credible case can be made that: 1) such efficiencies will be realised, 2) they cannot be realised without the acquisition, and 3) they will enhance competition in the relevant market, the Commission will include them in the competition analysis. The Commission, however, has stated that they envisage efficiency claims will rarely overturn findings that competition would otherwise be substantially lessened.

The following table examines efficiency profiles of New Zealand banks involved in M&A transactions. In each of the six transactions reviewed, the acquiring bank was larger than the target bank, although not (in general) more efficient. With the exception of ANZ's acquisition of PostBank, merged banks achieved most of their efficiency gains by reducing employee numbers and retrenching branches. This might be used to argue for consideration of efficiencies by the Commission in the merger analysis:

Table 10: New Zealand Banking Mergers

Acquirer	NBNZ	WBC	Countrywide	NBNZ	BNZ	ANZ
Acquiree	Countrywide	Trust Bank	United	Rural Bank	NAB (NZ)	PostBank
Year	1998	1996	1992	1992	1992	1989
Size Before	$18bn	$13bn	$1.8bn	$7.4bn	$18.9bn	$6.7bn
Size After	$29bn	$27bn	$4.7bn	$14.7bn	$19.1bn	$10.4bn
Increase	61%	108%	161%	99%	1%	55%
Cost to Income Ratio	72.3% to 66.9%	61.4% to 58.2%	75.3% to 75.7%	75.9% to 70.0%	81.4% to 71.2%	64.3% to 78.6%
Cost to Assets Ratio	2.52% to 1.84%	2.82% to 2.70%	3.55% to 3.20%	4.88% to 3.05%	4.22% to 3.88%	4.82% to 4.31%
Employee Productivity Before	$164,000	$171,000	$96,000	$129,000	$127,000	NA
Employee Productivity After	$237,000	$186,000	$162,000	$162,000	$179,000	$130,000

Note: Data used is for the two years before and after the respective mergers (2000 data not included)
Source: B. Liu and D. Tripe, "New Zealand Banking Mergers and Efficiency Gains", December 2001; Merrill Lynch

We conclude that any major bank merger involving National Bank is unlikely to be automatically granted approval by the Commission.

New Zealand Bank M&A Prudential Policy

Apart from the standard review by competition authorities, there is also the issue as to whether proposed bank mergers require review by the prudential regulators as well.

To date in New Zealand, the involvement of the Reserve Bank of New Zealand as prudential regulator in bank M&A transactions is not obvious. Whilst the Reserve Bank has an oversight role in the case of significant changes in ownership, no explicit approval criteria have in fact been specified, apart from the issue of the transaction not resulting in "material loss of standing in the financial market" for the New Zealand banking industry.

In any event, it is not clear whether this policy would apply to a change of ownership of a foreign owner, which might only come within the jurisdictions of the relevant parent company's home prudential regulators.

As a result, we do not foresee any prudential issues with a major bank merger involving National Bank (just competition issues).

Hypothetical In-Market Merger Scenarios

An ANZ (NZ) or ASB Bank merger with National Bank would increase New Zealand earnings contribution to group earnings for ANZ and CBA to 29% and 22% respectively

Based on our view that ANZ and CBA are likely to be the most attracted to National Bank from a structural perspective, we've explored some hypothetical merger scenarios involving **National Bank** with each of **ANZ Banking Group (NZ)** and **ASB Bank** respectively. For simplicity, in our calculations, we:

1. Accrue full cost synergies equivalent to 30% of National Bank's cost base immediately (rather than over a more likely two to three year period)
2. Assume no revenue synergies or revenue / market share attrition, and
3. Do not include any funding costs.

In both the scenarios, the pro forma earnings and market shares of the combined entities are substantially enhanced (tabled below). We remind that the competition laws present a barrier to completion of such hypothetical deals.

Table 11: National Bank Merger Scenarios— Pro forma New Zealand Earnings

(NZD, m)	NBNZ	ANZ (NZ)	ASB	ANZ / NBNZ Combined	ASB / NBNZ Combined
Net Interest Income	977	717	508	1,694	1,485
Other Income	357	500	215	857	572
Total Income	**1,334**	**1,217**	**724**	**2,551**	**2,058**
Operating Expenses	(586)	(545)	(371)	(955)	(781)
Underlying Profit	**748**	**672**	**353**	**1,596**	**1,277**
Cost Synergies @ 30%	176				
Bad Debts	(39)	(65)	(18)	(104)	(57)
Profit Before Tax	**885**	**607**	**335**	**1,492**	**1,220**
Tax Expense and OEI	(206)	(177)	(110)	(383)	(316)
Profit After Tax	**679**	**430**	**225**	**1,109**	**904**

Note: Uses NBNZ, ANZ (NZ) and ASB Bank 2002 accounts
Source: Company reports, Merrill Lynch estimates

Table 12: National Bank Merger Scenarios—Pro forma New Zealand Market Shares

	NBNZ	ANZ (NZ)	ASB	ANZ / NBNZ Combined	ASB / NBNZ Combined
Total Lending	21.8%	15.4%	11.3%	37.3%	33.1%
Deposits (M3 Resident Funding)	21.4%	18.9%	19.0%	40.2%	40.4%
Lending - Mortgages	19.9%	15.4%	15.8%	35.3%	35.7%
Other Lending (primarily Business)	23.6%	15.5%	7.1%	39.1%	30.8%

Source: Company reports, Merrill Lynch estimates

Table 13: National Bank Merger Scenarios—Pro forma Group Earnings Profiles for ANZ and CBA

(AUD, m)	ANZ	NBNZ	ANZ / NBNZ Combined	CBA	NBNZ	CBA / NBNZ Combined
Australia	1,713		1,713	2,569		2,569
New Zealand	302	611	913	178	611	789
Europe, Asia & Americas	308		308	(92)		(92)
TOTAL	**2,322**		**2,933**	**2,655**		**3,266**
Australia	74%		58%	97%		79%
New Zealand	***13%***		***31%***	***7%***		***24%***
Europe, Asia & Americas	13%		10%	-3%		-3%
TOTAL	**100%**		**100%**	**100%**		**100%**

Note: Assumed NZD/AUD rate of 0.90 for translation of NBNZ earnings (inclusive of assumed synergies); NBNZ, ANZ and CBA earnings are 2002
Source: Company reports, Merrill Lynch estimates

New Zealand Major Banks

National Bank of New Zealand

ANZ Banking Group (New Zealand)

ASB Bank

Bank of New Zealand

Westpac Banking Corporation New Zealand branch

National Bank of New Zealand

Table 14: NBNZ 2001

Head Office	Wellington
FTE Employees	4,579
Branches	159
Owned ATMs	240
Other Accessible ATMs	1,616

Source: KPMG 2002 FIPS

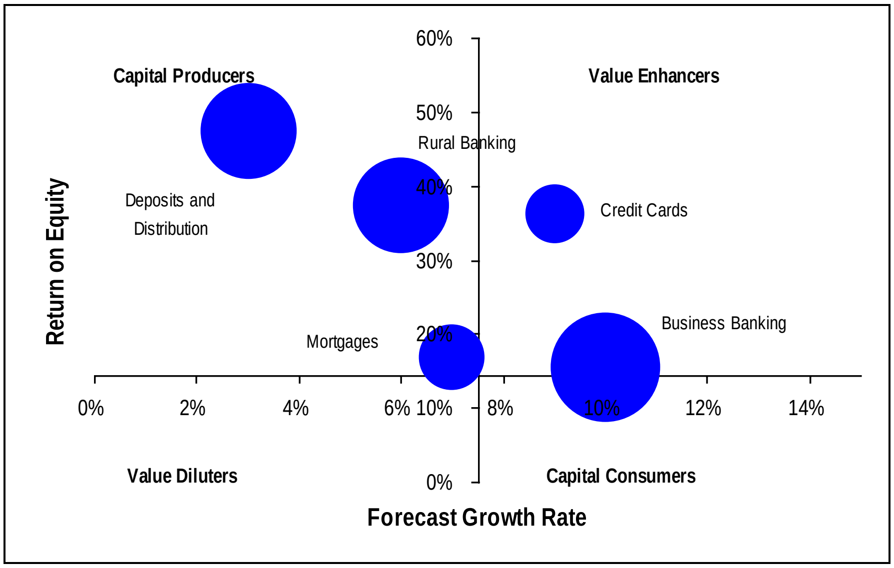
Parent Company: Lloyds TSB

Lloyds TSB acquired National Bank in 1966. Whilst both Lloyds TSB and National Bank always have had directors in common, National Bank is operated independently from its parent. The Bank was managed from London until 1978 when head office was moved to Wellington.

National Bank traditionally been strong in wholesale banking and rural lending, and is also a significant participant in the securities and derivatives markets. Its strength in rural lending derives predominantly from its acquisition of The Rural Bank from Fletcher Challenge in December 1992. National Bank sold its funds management subsidiary (Southpac Investment Management) to AMP in late 1997.

In 1998 Lloyds TSB acquired Countrywide Banking Corporation from Bank of Scotland. Countrywide Bank itself had been formed by the amalgamation of several building societies. The acquisition of Countrywide brought National Bank specialist skills in leasing, including a number of specialist leasing subsidiaries.

Chart 22: National Bank of New Zealand—Business Portfolio



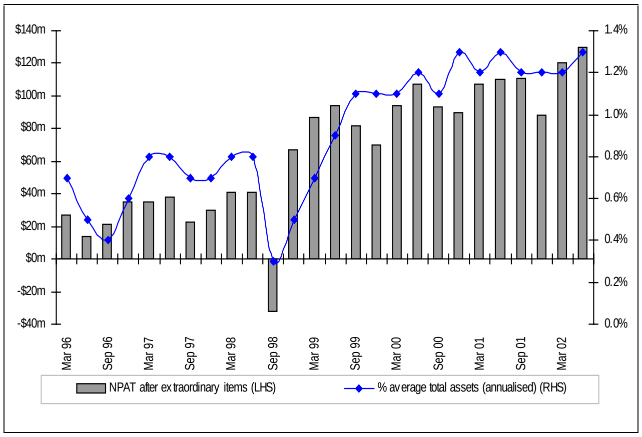
Source: Company reports, Merrill Lynch estimates

Table 15: National Bank of New Zealand—Key Financials

(NZD)	1995	1996	1997	1998	1999	2000	2001	2002	5 Year CAGR
Profit and Loss Statement:									
Net Interest Income	374	347	437	530	688	730	811	977	17%
Other Income	259	226	193	248	340	314	334	357	13%
Total Income	**633**	**573**	**630**	**778**	**1,028**	**1,044**	**1,145**	**1,334**	**16%**
Operating Expenses	(420)	(440)	(427)	(482)	(541)	(490)	(537)	(586)	7%
Underlying Profit	**213**	**133**	**203**	**296**	**487**	**554**	**608**	**748**	**30%**
Bad Debts	(12)	(3)	(24)	(22)	(32)	(25)	(15)	(39)	10%
Profit Before Tax	**201**	**130**	**179**	**274**	**455**	**529**	**593**	**709**	**32%**
Tax Expense and OEI	(52)	(33)	(53)	(37)	(122)	(145)	(177)	(206)	31%
Profit After Tax	**149**	**97**	**126**	**237**	**333**	**384**	**416**	**503**	**32%**
Abnormal Restructuring Expenses				(120)					
Profit After Tax and Restructuring	149	97	126	117	333	384	416	503	32%
Assets (NZD, bn):									
Mortgages	3.8	5.6	6.1	12.7	7.3	13.0	13.7	14.8	20%
Other Lending	11.8	13.9	16.0	23.6	24.8	12.9	17.5	19.0	4%
Total Assets	**15.5**	**17.0**	**19.7**	**28.9**	**29.8**	**31.5**	**36.4**	**38.9**	**15%**
Customer Deposits	8.5	9.5	9.4	13.8	14.0	15.4	17.9	20.0	16%
Impaired Assets	84	47	106	182	190	133	114	117	2%
Equity	0.9	0.9	1.0	1.4	1.5	1.8	2.2	2.5	20%
Return on Average Equity	17.7%	10.8%	13.2%	10.4%	22.9%	23.3%	21.1%	21.4%	
Return on Average Total Assets	1.0%	0.6%	0.7%	0.5%	1.1%	1.3%	1.2%	1.3%	
Profitability:									
Net Interest Income / Lending	2.39%	1.78%	1.98%	1.46%	2.14%	2.82%	2.60%	2.40%	
Other Income / Lending	1.66%	1.16%	0.87%	0.68%	1.06%	1.21%	1.07%	0.99%	
Total Income / Lending	4.05%	2.94%	2.85%	2.14%	3.20%	4.03%	3.67%	3.94%	
Cost / Income	66.4%	76.8%	67.8%	62.0%	52.6%	46.9%	46.9%	43.9%	
Underlying Profit / Lending	1.36%	0.68%	0.92%	0.81%	1.52%	2.14%	1.95%	2.21%	
Bad Debts / Lending	-0.08%	-0.02%	-0.11%	-0.06%	-0.10%	-0.10%	-0.05%	-0.12%	
Profit Before Tax / Lending	1.29%	0.67%	0.81%	0.75%	1.42%	2.04%	1.90%	2.10%	
Tax Rate	25.9%	25.4%	29.6%	13.5%	26.8%	27.4%	29.8%	29.1%	
Profit After Tax / Lending	0.95%	0.50%	0.57%	0.65%	1.04%	1.48%	1.33%	1.49%	

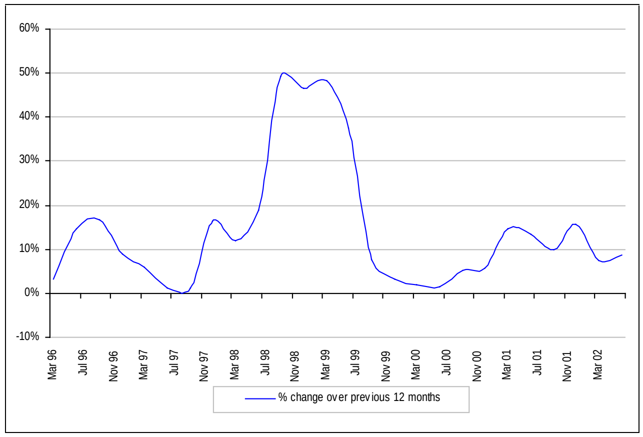
Source: Company reports, Merrill Lynch estimates

Chart 23: National Bank—Profit and Profitability (NZD)



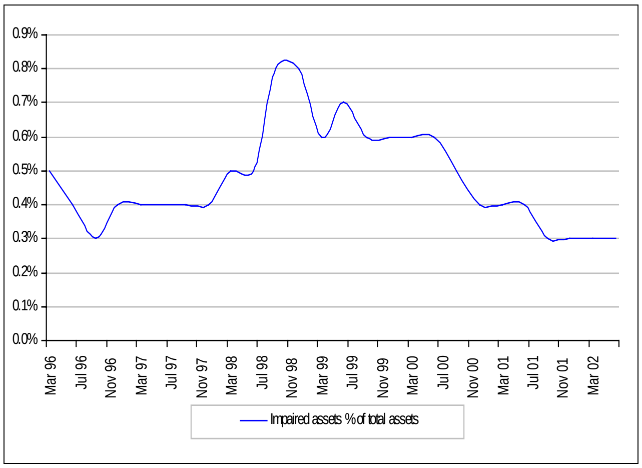
Source: Company reports, Merrill Lynch estimates

Chart 24: National Bank—Growth in Total Assets (NZD)



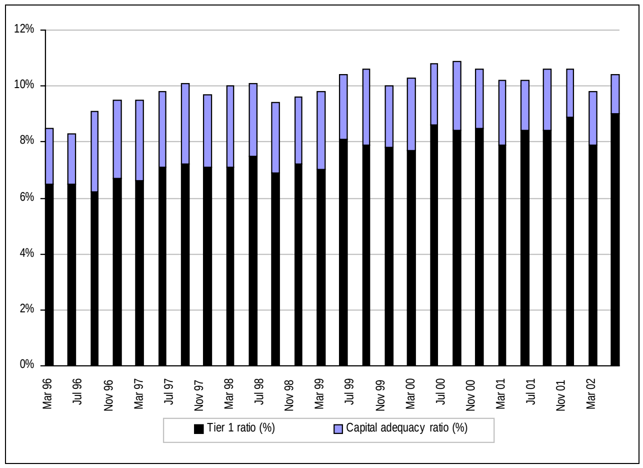
Source: Company reports

Chart 25: National Bank—Asset Quality (NZD)



Source: Company reports

Chart 26: National Bank—Capital Adequacy (NZD)



Source: Company reports

ANZ Banking Group (New Zealand)

Table 16: ANZ NZ 2001

Head Office	Auckland
FTE Employees	3,463
Branches	143
Owned ATMs	386
Other Accessible ATMs	1,422

Source: KPMG 2002 FIPS

Parent company: ANZ Banking Group

ANZ acquired New Zealand's Post Office Savings Bank (or PostBank) in 1988, operating it for approximately five years as a separately registered bank before amalgamating the legal entity with ANZ's existing New Zealand operations on the 1st December 1994. A few years later ANZ commenced amalgamating the ANZ and PostBank brand names. The PostBank transaction reflected, from the vendor's point of view, the New Zealand Government's proposed divestment of PostBank and, from the purchaser's point of view, the attraction to ANZ was acquiring an inexpensive deposit base. ANZ has been in the New Zealand market since 1840.

ANZ's states that its New Zealand business is comprised of 7,000 SME customers and one million personal customers. ANZ owns UDC Finance, which is a leading New Zealand finance company, specialising in asset backed financing.

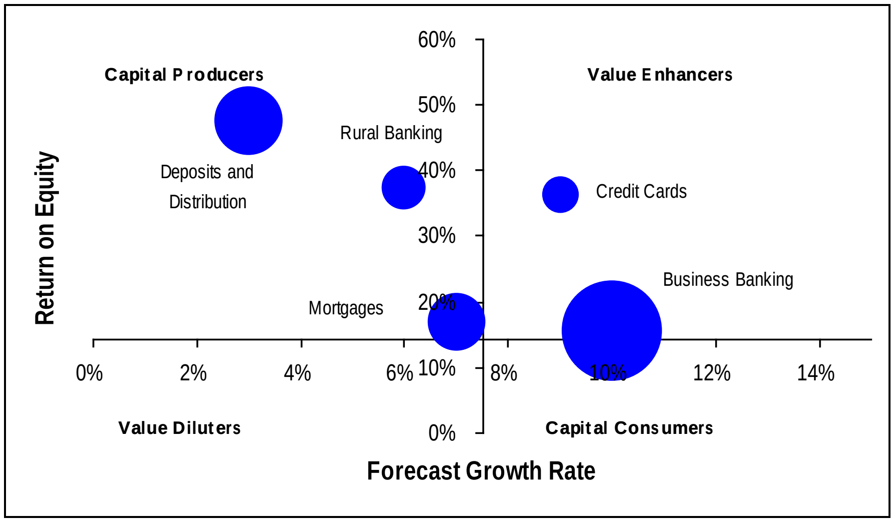
In late 2002 ANZ appointed Greg Camm as CEO of New Zealand operations.

Mr. Camm indicated in early 2003 that he thought ANZ's branch network in New Zealand was too lean for the size of their customer base, and that centralisation to Australia had been too great. ANZ believes that their New Zealand footprint is a little underweight, with 143 branches (15% total branches) and 394 ATMs (21% of total ATMs). New Zealand staff now report directly to Mr. Camm rather than through divisions to head office.

Going forward, ANZ's stated strategy is longer-term growth in personal banking through targeting improved customer satisfaction, improved service delivery and reduced queues, improved sales productivity / growth in specialist sales forces and growth in key segments (including wealth and a focus on faster growing regions).

ANZ believes that the 'Restoring Customer Faith' program will underwrite these initiatives.

Chart 27: ANZ Banking Group New Zealand—Business Portfolio



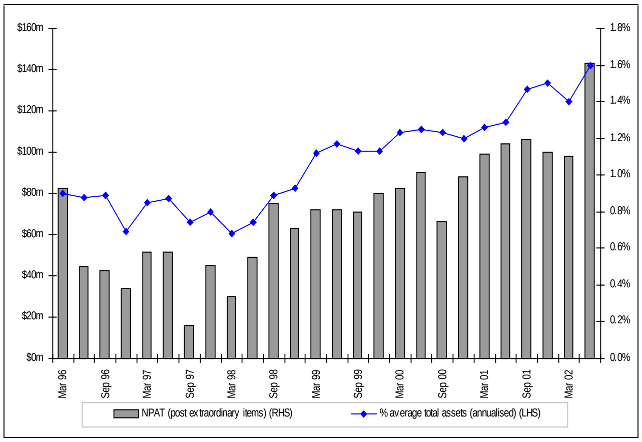
Source: Company reports, Merrill Lynch estimates

Table 17: ANZ Banking Group New Zealand—Key Financials

Year end September (NZD, m)	1995	1996	1997	1998	1999	2000	2001	2002	5 YR CAGR
Profit and Loss Statement:									
Net Interest Income	564	576	541	549	593	621	673	717	6%
Other Income	278	288	337	379	403	446	475	500*	8%
Total Income	**842**	**863**	**878**	**928**	**996**	**1,067**	**1,148**	**1,217**	**7%**
Operating Expenses	(567)	(592)	(674)	(578)	(563)	(596)	(533)	(545)	-4%
Underlying Profit	**275**	**272**	**204**	**350**	**433**	**471**	**615**	**672**	**27%**
Bad Debts	(23)	(22)	9	(62)	(45)	(44)	(57)	(65)	
Profit Before Tax	**252**	**250**	**213**	**289**	**388**	**427**	**558**	**607**	**23%**
Tax Expense and OEI	(72)	(80)	(60)	(90)	(110)	(108)	(161)	(177)	
Profit After Tax	**180**	**170**	**153**	**199**	**278**	**319**	**397**	**430**	**23%**
Assets (NZD, bn):									
Mortgages			7.9	8.7	9.9	10.6	10.5	10.4	6%
Other Lending			8.4	9.7	9.8	11.4	11.5	11.6	7%
Total Assets	**17.8**	**20.2**	**21.1**	**24.3**	**25.0**	**26.9**	**27.2**	**27.4**	**5%**
Impaired Assets (NZD, m)	223.6	198.1	161.7	143.9	63.4	78.0	97.0	43.0	-23%
Liabilities	16.6	19.3	20.0	23.2	23.9	25.5	26.0	26.1	
Equity	1.2	0.9	1.0	1.1	1.1	1.4	1.2	1.2	4%
Profitability:									
Net Interest Income / Lending	na	na	3.32%	2.99%	3.01%	2.83%	3.05%	3.26%	
Other Income / Lending	na	na	2.07%	2.06%	2.05%	2.03%	2.15%	2.28%	
Total Income / Lending	na	na	5.39%	5.05%	5.06%	4.86%	5.20%	5.54%	
Cost / Income	67.4%	68.5%	76.7%	62.2%	56.6%	55.9%	46.4%	44.8%	
Underlying Profit / Lending	na	na	1.25%	1.91%	2.20%	2.15%	2.78%	3.06%	
Bad Debts / Lending	na	na	0.06%	-0.34%	-0.23%	-0.20%	-0.26%	-0.30%	
Profit Before Tax / Lending	na	na	1.31%	1.57%	1.97%	1.94%	2.53%	2.76%	
Tax Rate	29%	32%	28%	31%	28%	25%	29%	29%	
Profit After Tax / Lending	na	na	0.94%	1.08%	1.41%	1.45%	1.80%	1.96%	

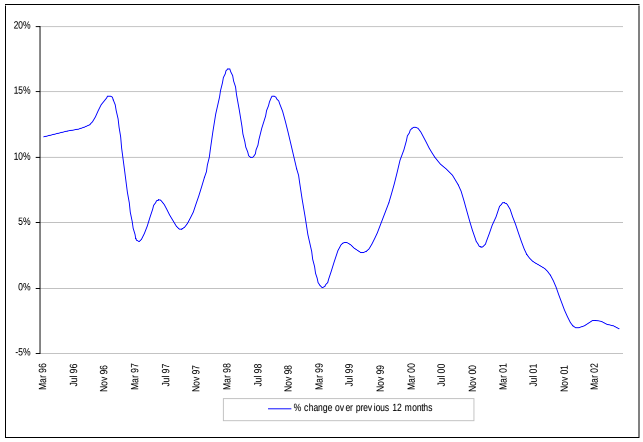
Note: Includes Countrywide Banking Corporation from 1 September 1998
* Includes net gain on sale of funds management of $36m
Source: Company reports, Merrill Lynch estimates

Chart 28: ANZ NZ—Profit and Profitability (NZD)



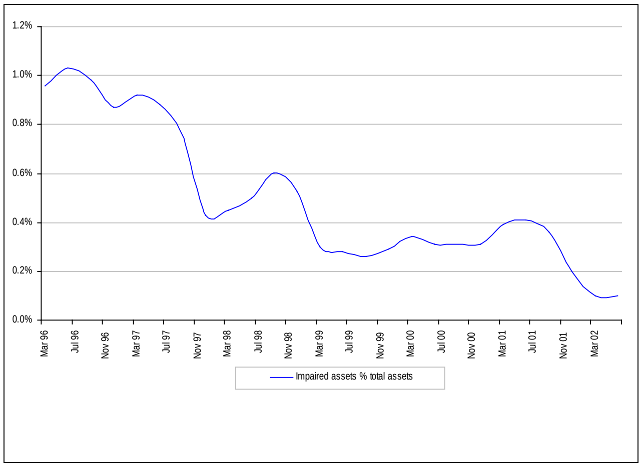
Source: Company reports, Merrill Lynch estimates

Chart 29: ANZ NZ—Growth in Total Assets (NZD)



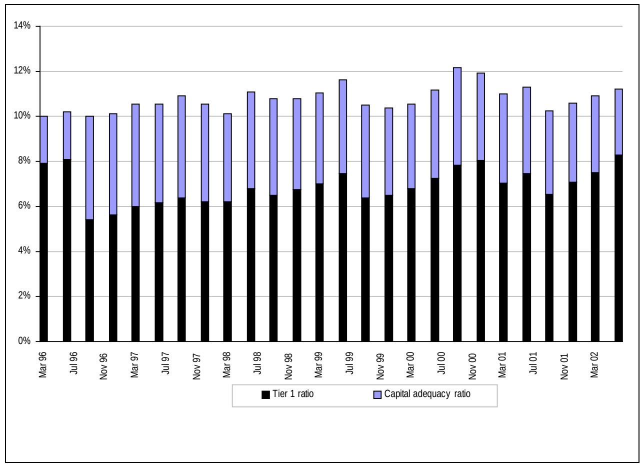
Source: Company reports

Chart 30: ANZ NZ—Asset Quality (NZD)



Source: Company reports

Chart 31: ANZ NZ—Capital Adequacy (NZD)



Source: Company reports

ASB Bank

Table 18: ASB Bank 2001

Head Office	Auckland
FTE Employees	2,937
Branches	116
Owned ATMs	315
Other Accessible ATMs	1,482

Source: KPMG 2002 FIPS

Parent company: Commonwealth Bank

ASB Bank was established in 1847 as a trustee bank and throughout most of its history has operated as a regional savings bank in Auckland and Northland.

CBA acquired an initial 75% interest in ASB Group in February 1989, with the remaining 25% held by the ASB Bank Community Trust, which is a philanthropic institution. Both parties held pre-emptive rights to acquire the other party's interests. The 1989 acquisition was the result of approaches made by ASB Bank (then wholly owned by the Community Trust), which had recognised the need for international banking affiliations and had determined that an Australian bank offered the most advantages in this regard.

In 1991 ASB commenced national expansion: thereafter achieving average growth in advances at twice the market average. In 1994, ASB adopted a formal growth strategy, involving organic growth (establishment of 30 branches), business line diversification (into commercial and rural banking, managed funds, life insurance and stock broking) and acquisitions. On 4th December 1998 ASB Bank acquired risk insurance company Sovereign Ltd (adding an estimated 175,000 Sovereign customers to ASB's existing customer base) and in June 1999 ASB Bank announced the acquisition of the retail stock broking operations of Warburg Dillon Read (re-named ASB Securities). Following the Sovereign acquisition, in 1998 the ASB Group was formed, incorporating banking (ASB Bank and the direct offering BankDirect) and life assurance (ASB Life and Sovereign).

Following CBA's acquisition of Colonial in Australia in 2000 CBA acquired the ASB Bank Community Bank's 25% interest in ASB Group in 2001. This allowed CBA to resolve the issue of shareholder value leakage to the ASB minorities from the ASB Group / Colonial New Zealand merger integration.

An important factor behind ASB's strong organic growth has been the effective deployment of IT (former CEO Ralph Norris had an IT background), which has provided ASB with good customer information systems, enhanced back office efficiency and new customer acquisition through direct channels.

ASB's market presence is strongest in the important Auckland region (with a 35% market share—twice that of the next largest player), which is a key centre because of the number of housing loans and the higher housing loan average draw downs (house prices).

Strong, above-system balance sheet growth has been achieved as part of corporate strategy on the back of strong sales and service focus and (along with both ANZ and Westpac Trust) extensive use of mortgage brokers.

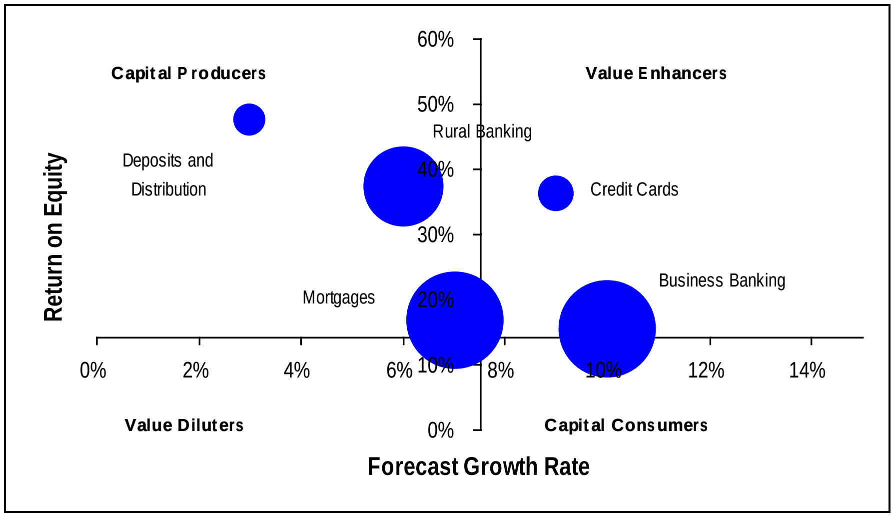
ASB Bank has its own board of directors and management operates autonomously from that of CBA.

Following the CBA / Colonial merger, the enlarged ASB Bank / Colonial became the second largest retail fund manager in New Zealand after Tower Group.

ASB's returns in New Zealand have generally been lower than those achieved by other full service banks in New Zealand, which is likely attributable to their efforts to expand business operations to cover the whole of New Zealand, beyond the original Auckland base.

ASB Bank is the smallest of the five major trading banks in New Zealand, with a customer base of 800,000 customers.

Chart 32: ASB Bank—Business Portfolio



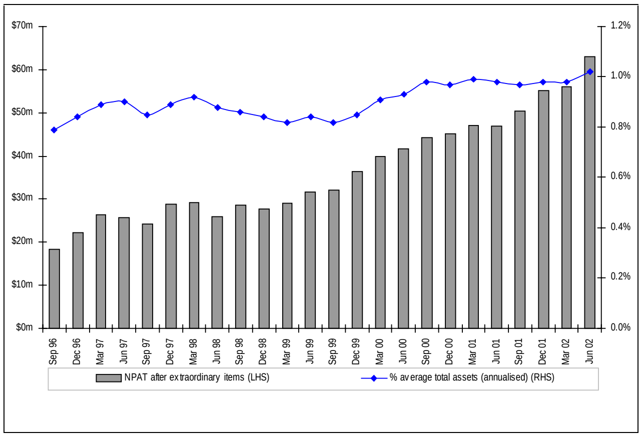
Source: Company reports, Merrill Lynch estimates

Table 19: ASB Bank—Key Financials

Year end June (NZD)	1995	1996	1997	1998	1999	2000	2001	2002	5 YR CAGR
Profit and Loss Statement									
Net interest income	206	231	276	320	328	385	457	508	13%
Other income	111	117	132	121	137	177	187	215	10%
Total income	**317**	**349**	**408**	**441**	**465**	**562**	**645**	**724**	**12%**
Operating expenses	(210)	(228)	(260)	(267)	(275)	(322)	(351)	(371)	7%
Underlying profit	**107**	**120**	**148**	**174**	**189**	**240**	**294**	**353**	**19%**
Bad debts	(6)	(9)	(10)	(11)	(13)	(11)	(14)	(18)	
Profit before tax	**101**	**111**	**138**	**163**	**177**	**229**	**280**	**335**	**19%**
Tax expense and OEI	(36)	(39)	(45)	(55)	(60)	(78)	(97)	(110)	
Profit after tax	**65**	**72**	**93**	**108**	**117**	**150**	**183**	**225**	**19%**
Assets (NZD, bn)									
Mortgages	3.6	4.8	6.1	7.2	8.2	9.6	10.9	13.0	16%
Other lending	2.4	2.9	3.2	10.8	4.2	4.8	5.3	6.0	13%
Total assets	**7.4**	**9.1**	**11.0**	**12.9**	**14.7**	**17.2**	**20.0**	**24.2**	**17%**
Impaired assets (NZD, m)	13.0	8.0	6.0	24.4	31.2	16.2	31.2	35.2	42%
Liabilities	7.0	8.6	10.4	12.2	14.0	16.3	19.2	23.2	
Equity	0.4	0.5	0.6	0.7	0.7	0.8	0.8	1.0	12%
Profitability									
Net interest income / Lending	3.47%	3.02%	2.97%	1.78%	2.63%	2.67%	2.83%	2.67%	
Other income / Lending	1.87%	1.53%	1.42%	0.67%	1.10%	1.23%	1.16%	1.13%	
Total income / Lending	5.34%	4.56%	4.39%	2.45%	3.73%	3.90%	3.99%	3.80%	
Cost / Income	66.3%	65.5%	63.7%	60.6%	59.3%	57.3%	54.5%	51.3%	
Underlying profit / Lending	1.80%	1.57%	1.59%	0.96%	1.52%	1.67%	1.82%	1.85%	
Bad debts / Lending	-0.09%	-0.12%	-0.11%	-0.06%	-0.10%	-0.08%	-0.08%	-0.09%	
Profit before tax / Lending	1.71%	1.45%	1.48%	0.90%	1.42%	1.59%	1.73%	1.76%	
Tax rate	35.4%	35.4%	32.8%	33.7%	33.8%	34.3%	34.5%	32.9%	
Profit after tax / Lending	1.10%	0.94%	0.99%	0.60%	0.94%	1.04%	1.13%	1.18%	

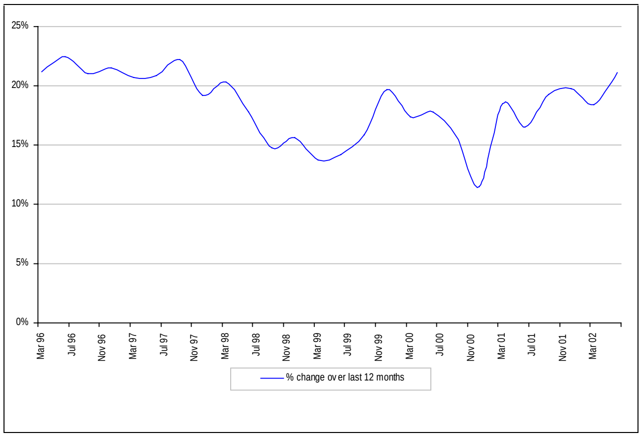
Source: Company reports, Merrill Lynch estimates

Chart 33: ASB Bank—Profit and Profitability



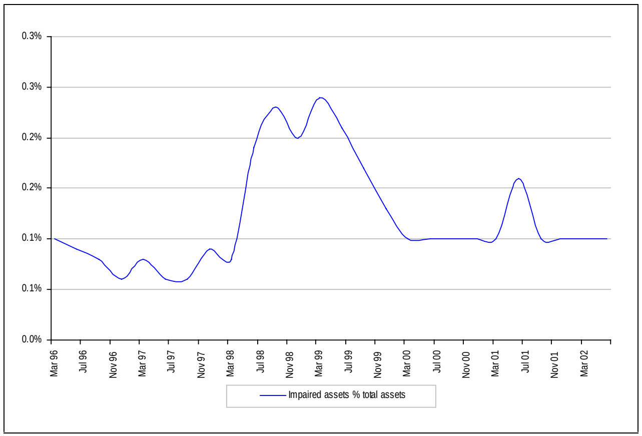
Source: Company reports, Merrill Lynch estimates

Chart 34: ASB Bank—Growth in Total Assets



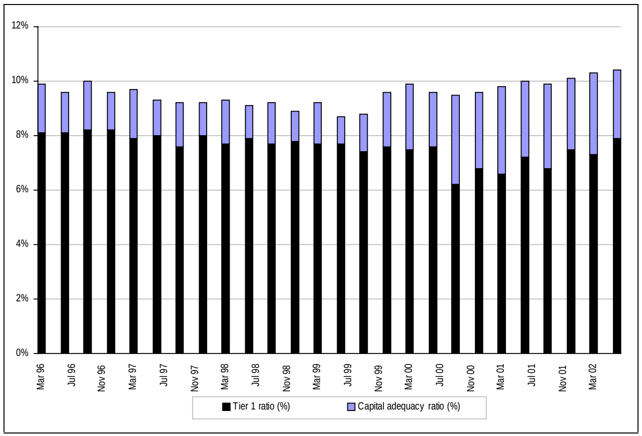
Source: Company reports

Chart 35: ASB Bank—Asset Quality



Source: Company reports

Chart 36: ASB Bank—Capital Adequacy



Source: Company reports

Bank of New Zealand

Parent company: National Australia Bank

Table 20: BNZ 2001

Head Office	Auckland
FTE Employees	4,751
Branches	189
Owned ATMs	374
Other Accessible ATMs	1,433

Source: KPMG 2002 FIPS

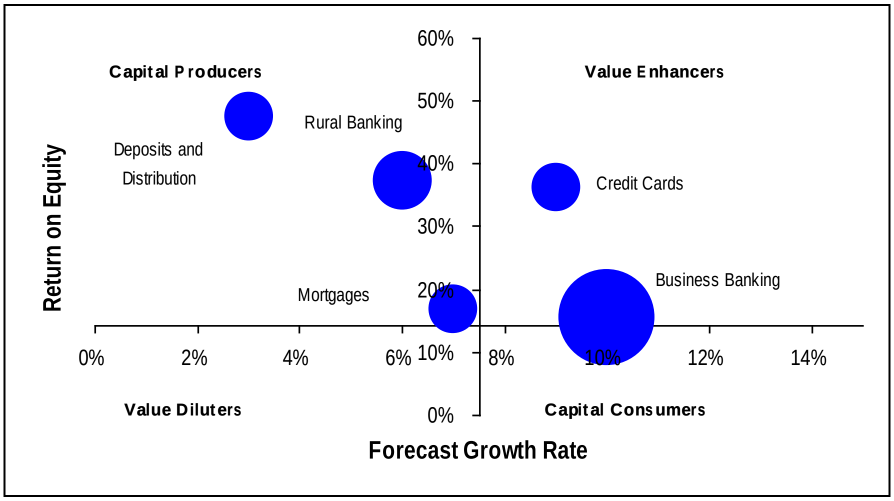
NAB commenced its expansion into New Zealand in 1985 with the establishment of a merchant banking operation and the acquisition of a small finance company. This was followed by the acquisition of Broadbank Corporation (a larger finance company) in early 1987. At the time, this acquisition was seen as a foundation for a retail banking operation that NAB sought to establish following the issuance of the first banking New Zealand licences to foreign banks in 1987. NAB was issued a New Zealand banking license in July 1987.

NAB then acquired BNZ in 1992, which at the time was majority owned by the New Zealand government & financially distressed. The operation rapidly absorbed NAB's existing operations in New Zealand, which had been trading as National Australia Bank, New Zealand. Following the merger, BNZ experienced a decline in profitability in 1993 following the adoption of NAB's accounting policies and procedures. The profitability of NAB's New Zealand operations was thereafter significantly improved, although considerably assisted by continuing write-backs of loan loss provisions raised at the time of the acquisition.

One of the key objectives of NAB's initial expansion into New Zealand was the desire to protect its existing relationships with Australian corporate customers that were undertaking business in New Zealand.

BNZ has a strong presence amongst New Zealand corporations and has more than 960,00 customers in New Zealand.

Chart 37: Bank of New Zealand—Business Portfolio



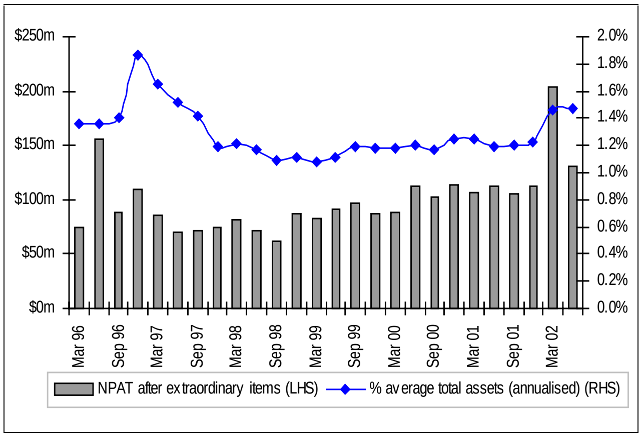
Source: Company reports, Merrill Lynch estimates

Table 21: Bank of New Zealand—Key Financials

Year end September (NZD)	1995	1996	1997	1998	1999	2000	2001	2002	5 YR CAGR
Profit and Loss Statement:									
Net Interest Income	638	681	704	682	623	665	753	837	4%
Other Income	300	308	321	337	407	491	494	522	10%
Total Income	**938**	**989**	**1,025**	**1,019**	**1,030**	**1,156**	**1,247**	**1,359**	**6%**
Operating Expenses	(586)	(601)	(572)	(605)	(570)	(630)	(648)	(624)	2%
Underlying Profit	**352**	**388**	**453**	**414**	**460**	**526**	**599**	**735**	**10%**
Bad Debts	103	80	6	(33)	(22)	(13)	(12)	15	
Profit Before Tax	**455**	**468**	**459**	**381**	**438**	**513**	**587**	**750**	**10%**
Tax expense and OEI	(153)	(150)	(124)	(93)	(80)	(124)	(147)	(168)	
Profit After Tax	**302**	**318**	**335**	**288**	**358**	**389**	**440**	**582**	**12%**
Assets (NZD, bn):									
Mortgages	na	na	7.4	8.0	8.8	9.3	10.2	10.9	8%
Other Lending	na	na	12.0	13.6	15.2	15.6	16.4	16.4	7%
Total Assets	**22.0**	**23.5**	**23.6**	**29.3**	**31.0**	**35.3**	**37.8**	**36.0**	**9%**
Impaired Assets	0.3	0.2	0.1	0.1	0.1	0.1	0.0	0.0	-25%
Liabilities	21.0	22.5	22.5	28.1	29.6	33.8	36.1	33.9	
Equity			1.1	1.3	1.4	1.5	1.8	2.1	
Profitability:									
Net Interest Income / Lending	na	na	3.63%	3.15%	2.59%	2.67%	2.83%	3.06%	
Other Income / Lending	na	na	1.66%	1.56%	1.69%	1.97%	1.86%	1.91%	
Total Income / Lending	na	na	5.29%	4.71%	4.29%	4.64%	4.69%	4.97%	
Cost / Income	62.5%	60.8%	55.8%	59.4%	55.3%	54.5%	52.0%	45.9%	
Underlying Profit / Lending	na	na	2.34%	1.91%	1.92%	2.11%	2.25%	2.69%	
Bad Debts / Lending	na	na	0.03%	-0.15%	-0.09%	-0.05%	-0.05%	0.05%	
Profit Before Tax / Lending	na	na	2.37%	1.76%	1.82%	2.06%	2.21%	2.74%	
Tax Rate	34%	32%	27%	24%	18%	24%	25%	22%	
Profit After Tax / Lending	na	na	1.73%	1.33%	1.49%	1.56%	1.66%	2.13%	

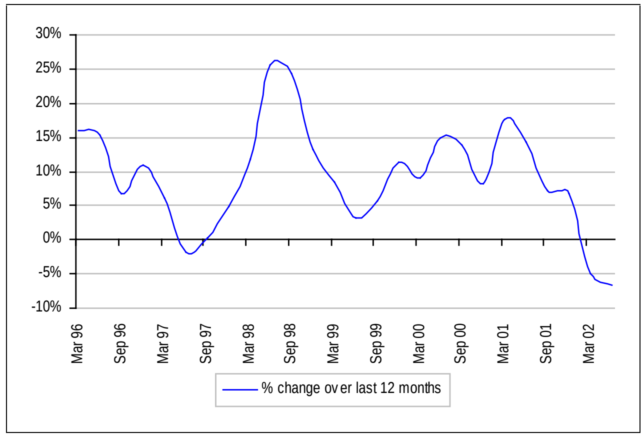
Source: Company reports, Merrill Lynch estimates

Chart 38: Bank of New Zealand NZ—Profit and Profitability



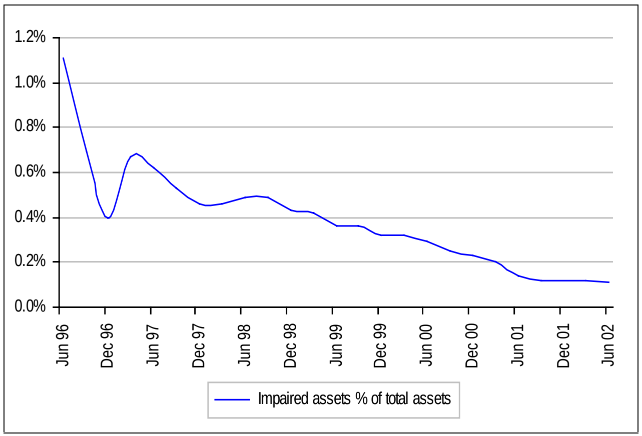
Source: Company reports, Merrill Lynch estimates

Chart 39: Bank of New Zealand—Growth in Total Assets



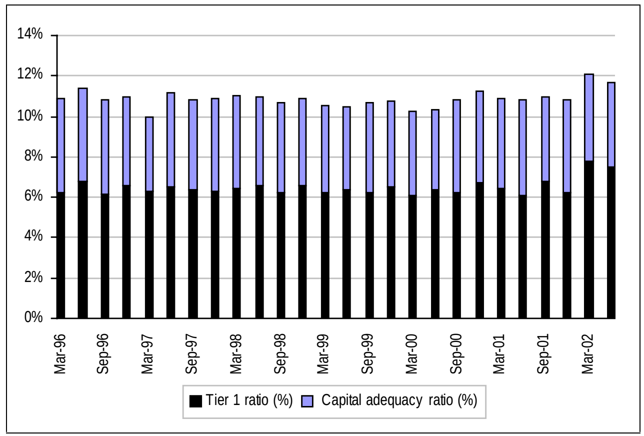
Source: Company reports

Chart 40: Bank of New Zealand—Asset Quality



Source: Company reports

Chart 41: Bank of New Zealand—Capital Adequacy



Source: Company reports

Westpac Banking Corporation NZ Branch

Table 22: WBC NZ 2001

Head Office	Auckland
FTE Employees	5,735
Branches	201
Owned ATMs	493
Other Accessible ATMs	1,339

Source: KPMG 2002 FIPS

Branch operation of Westpac Banking Corporation

The Trust Bank Group was formed in 1986, combining nine Trustee Savings Banks from around the country to become New Zealand's largest specialised retail bank (TSB Bank and ASB Bank were the only trustee banks not to joint the Trust Bank consortium). In 1988 the Group became Trust Bank New Zealand.

WBC acquired Trust Bank New Zealand on 24th May 1996—one of three regional banks acquired by WBC in Australasia as part of the rebuilding of WBC following the losses of the early 1990s. At the time of the transaction, WBC and Trust Bank had 15% and 10% respectively of bank net loans and advances. WBC had been operating in the New Zealand market since 1861.

WBC executed the Trust Bank acquisition to expand its business footprint in New Zealand, which was otherwise seen as too small to justify continued involvement. There was also an opportunistic dimension, inasmuch as one reason for the acquisition was that Trust Bank was available for sale.

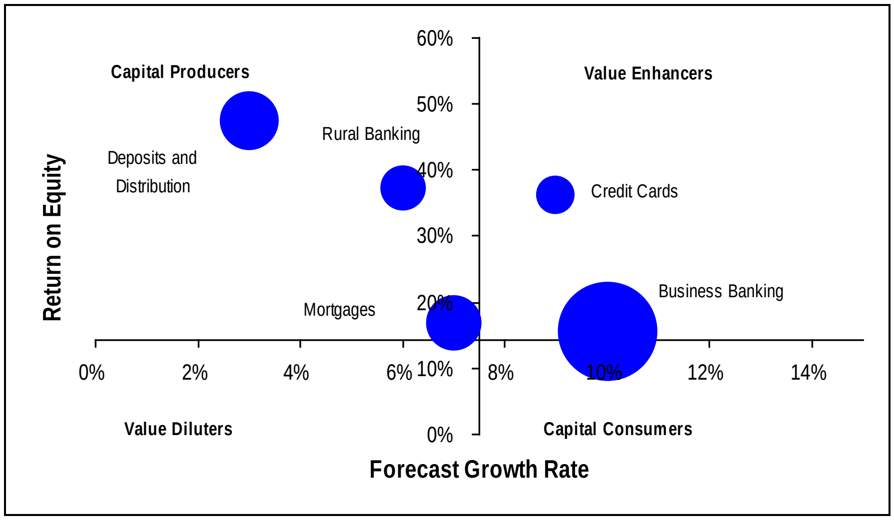
At the time of this transaction, WBC was the largest of the (then six) New Zealand major banks, based on both total asset and total deposit measures. The acquisition particularly provided WBC with improved market shares in areas like Canterbury, Southland and Waikato.

WBC has stated that they have 1.3m customers in New Zealand, with one in three people in New Zealand having a banking relationship with WBC. The position is particularly dominant in the South Island, and there are 200 branches and 484 ATMs nationwide. WBC has stated they have a #1 position in consumer banking, #2 positions in business and corporate banking and a #5 position in the wealth management arena. WBC is the leading provider of banking services to small to medium business (with over 100,000 business customers), the largest provider of card processing (merchant) services and is the official banker to the New Zealand government. WBC's 2002 acquisition of BT Financial and divestment of AGC included the respective New Zealand operations of these companies.

In October 2002, WBC announced: 1) The appointment of Ann Sherry as Group Executive New Zealand and Pacific Banking and CEO of WestpacTrust; 2) The transfer of the head office of WestpacTrust to Auckland (effective 1st October 2002) from Wellington; and 3) The renaming of 'WestpacTrust' to 'Westpac' "in order to gain full leverage of the Westpac brand name and to assist in standardising customer services throughout Australasia".

WBC operates in New Zealand as a branch bank. Branch banks are not required to maintain capital adequacy standards in New Zealand, but rather satisfy capital adequacy requirements of their home regulator. The Reserve Bank of New Zealand passed legislation in March 2001 empowering them to require banks to be locally incorporated as a condition of registration. This power has been exercised with regard to AMP and HSBC (whom have since exited the retail market in New Zealand). This policy change reflects the Reserve Bank's desire to be able to identify the assets of the New Zealand business with as much certainty as possible, to help ensure a close connection between the assets available in a crisis and those published in General Disclosure Statements, and to ensure, for example, that, if the Reserve Bank is required to place an entity into statutory management, there is a self-contained entity available for this purpose. WBC is currently continuing discussions with the Reserve Bank regarding incorporation. We understand WBC argues New Zealand depositors currently have more protection than they would have if the bank were locally incorporated, given that New Zealand depositors rank ahead of other unsecured creditors of the Overseas Bank in respect of claims against New Zealand assets (i.e. the security cover for deposit holders is greater than the "capital buffer" that would be their only protection through local incorporation).

Chart 42: Westpac Banking Corporation New Zealand Branch—Business Portfolio



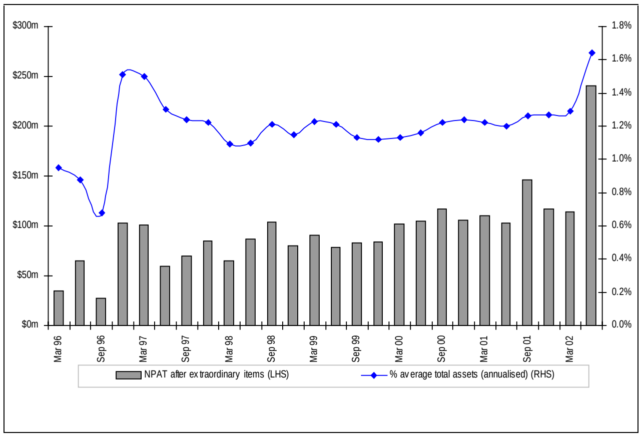
Source: Company reports, Merrill Lynch estimates

Table 23: Westpac Banking Corporation NZ branch—Key Financials

Year end September (NZD)	1995	1996	1997	1998	1999	2000	2001	2002	5 YR CAGR
Profit and Loss Statement:									
Net Interest Income	385	495	760	857	805	808	825	916	4%
Other Income	220	252	466	397	413	459	469	488	1%
Total Income	**605**	**746**	**1,226**	**1,254**	**1,218**	**1,266**	**1,294**	**1,403**	**3%**
Operating Expenses	(391)	(527)	(720)	(723)	(687)	(656)	(639)	(685)	-1%
Underlying Profit	**214**	**219**	**506**	**531**	**531**	**610**	**656**	**718**	**7%**
Bad Debts	(37)	(26)	(16)	(24)	(36)	(32)	(45)	(41)	
Profit Before Tax	**177**	**193**	**490**	**506**	**495**	**578**	**610**	**678**	**7%**
Tax Expense and OEI	(64)	(66)	(157)	(166)	(163)	(170)	(145)	(173)	
Profit After Tax *	**113**	**127**	**333**	**341**	**332**	**408**	**465**	**505**	**9%**
Assets (NZD, bn):									
Mortgages	na	na	12.2	11.9	12.5	12.8	13.6	13.7	2%
Other Lending	na	na	10.2	10.6	11.8	13.9	15.5	17.6	12%
Total Assets	**14.3**	**26.4**	**27.5**	**28.8**	**29.6**	**35.0**	**39.1**	**37.6**	**6%**
Securitised Mortgages	na	na		0.2	0.9	1.0	1.0	0.1	
Impaired Assets	248.6	240.9	162.2	151.7	127.5	150.8	146.2	91.6	-11%
Liabilities	14.1	26.2	25.8	27.1	26.8	34.4	34.3	33.1	
Equity	0.2	0.1	1.7	1.8	2.8	0.6	4.8	4.4	20%
Profitability:									
Net Interest Income / Lending	na	na	3.40%	3.82%	3.31%	3.03%	2.84%	2.92%	
Other Income / Lending	na	na	2.08%	1.77%	1.69%	1.72%	1.61%	1.56%	
Total Income / Lending	na	na	5.48%	5.58%	5.00%	4.75%	4.46%	4.48%	
Cost / Income	64.6%	70.7%	58.7%	57.7%	56.4%	51.8%	49.3%	48.8%	
Underlying Profit / Lending	na	na	2.26%	2.36%	2.18%	2.29%	2.26%	2.29%	
Bad Debts / Lending	na	na	-0.07%	-0.11%	-0.15%	-0.12%	-0.16%	-0.13%	
Profit Before Tax / Lending	na	na	2.19%	2.25%	2.03%	2.17%	2.10%	2.16%	
Tax Rate	36%	34%	32%	33%	33%	29%	24%	25%	
Profit After Tax / Lending	na	na	1.49%	1.52%	1.36%	1.53%	1.60%	1.61%	

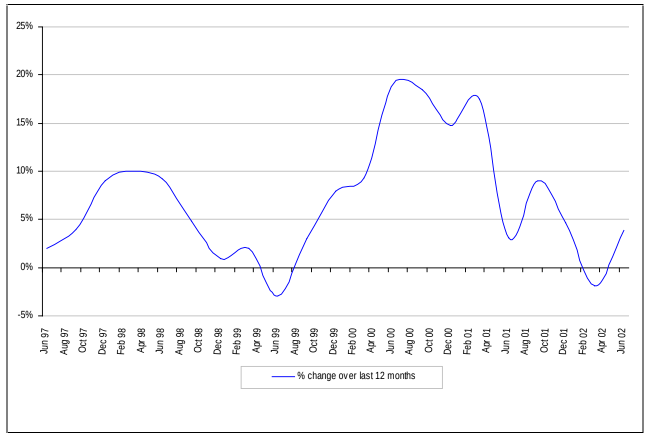
Source: Company reports, Merrill Lynch estimates * Note that the NPAT line includes considerable goodwill amortisation costs which distort ratio comparisons relative to other banks. Table 3 normalises for the goodwill amortisation deduction and this is the better place to look at relative bank performance.

Chart 43: WBC NZ Branch—Profit and Profitability (NZD)



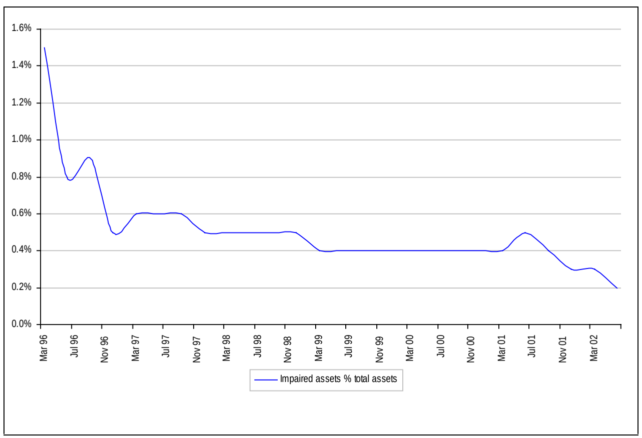
Source: Company reports, Merrill Lynch estimates

Chart 44: WBC NZ Branch—Growth in Total Assets (NZD)



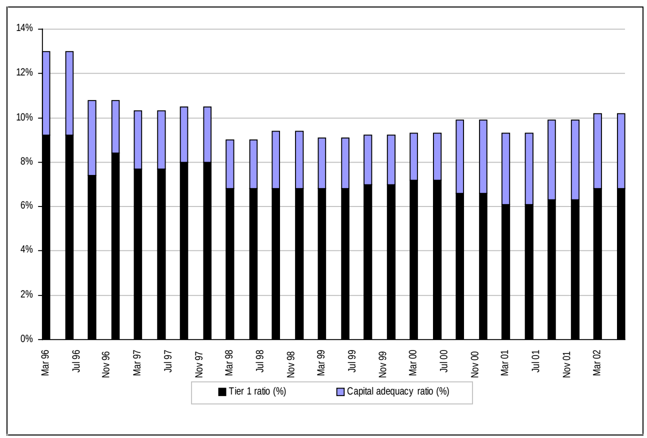
Source: Company reports

Chart 45: WBC NZ Branch—Asset Quality (NZD)



Source: Company reports

Chart 46: WBC NZ Branch—Capital Adequacy (NZD)



Source: Company reports

WBC– Ranking of Local Creditors in a Winding-Up

The *Banking Act 1959 (Australia)* gives priority over Australian assets of the Overseas Bank to Australian depositors. Accordingly, New Zealand depositors will rank after Australian depositors of the Overseas Bank in relation to claims against Australian assets.

However, the *Westpac Banking Corporation Act 1982 (New Zealand)* gives New Zealand depositors priority to the New Zealand assets of the Overseas Bank. Accordingly, WBC New Zealand depositors will rank ahead of other unsecured creditors of the Overseas Bank in respect of claims against the New Zealand assets of the Overseas Bank. Based on the audited statement of financial position as at 30th September 2002 the value of the WBC New Zealand assets is greater than the New Zealand deposit liabilities. The WBC New Zealand Bank has at all times held in New Zealand assets (other than goodwill) of not less than the value of the New Zealand Bank's total deposit liabilities in New Zealand.

New Zealand Banking Industry: Chart Summary

Interest Rates and Credit Growth

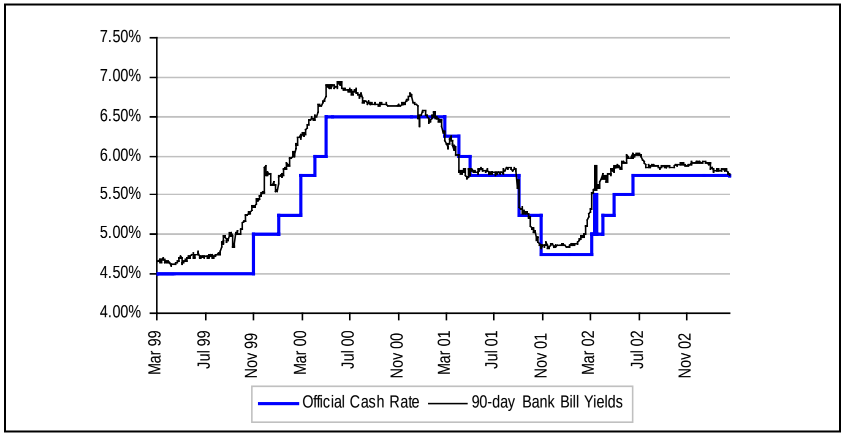
Macroeconomics

Bank Sector Operational Trends

Payments and Distribution

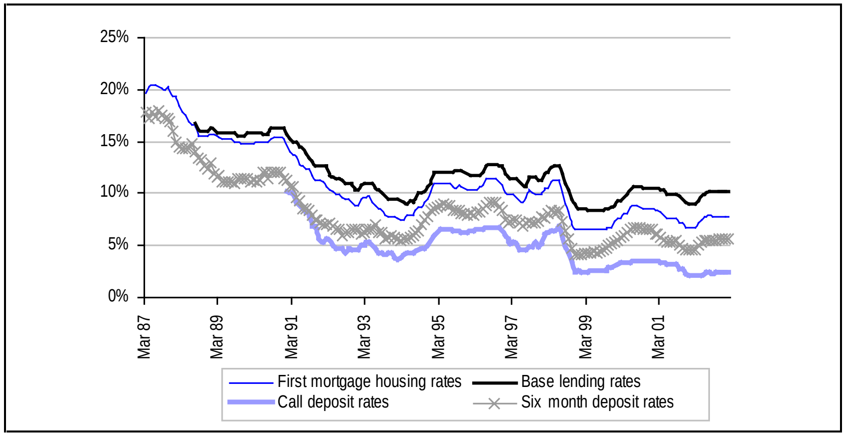
Interest Rates and Credit Growth

Chart 47: New Zealand Cash/90-day Bill Spread



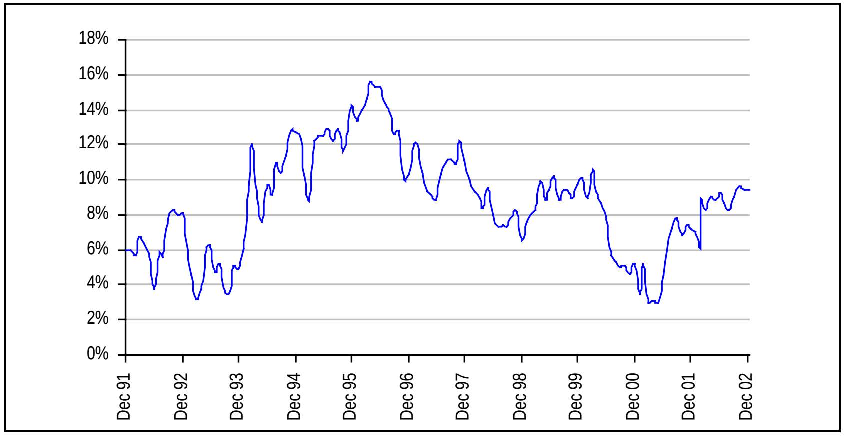
Note: Average spread 25bp, with a maximum of 102bp and a minimum of –40bp
Source: Reserve Bank of New Zealand statistics, Table B2

Chart 49: New Zealand Interest Rates on Lending and Deposits



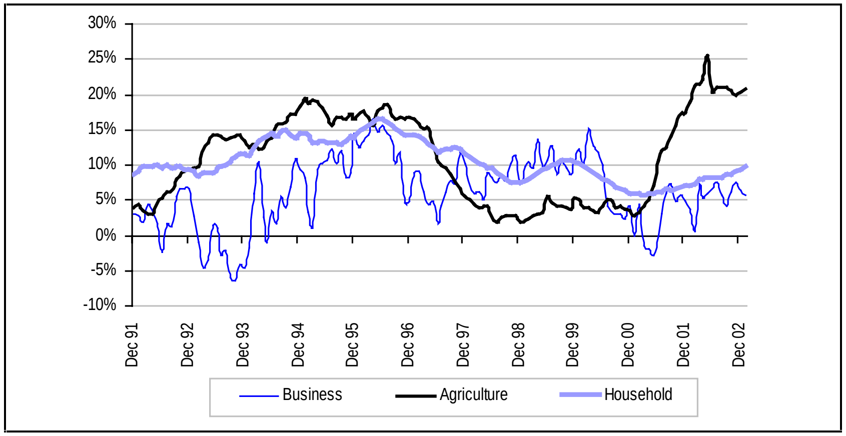
Note: First mortgage housing rates in January 2003 at a 208bp premium over the Official Cash Rate
Source: Reserve Bank of New Zealand statistics, Table B3

Chart 48: New Zealand Credit Growth (y-o-y)



Note: Data adjusted for securitisation
Source: Reserve Bank of New Zealand statistics, Table C2

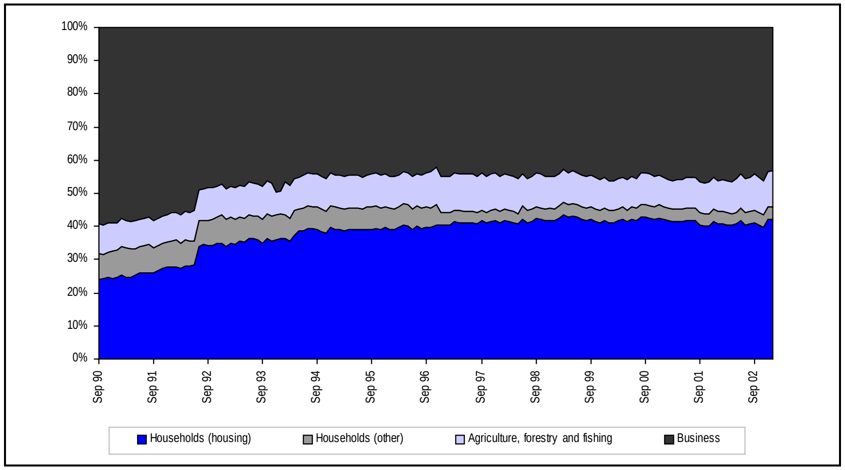
Chart 50: New Zealand Credit Growth Aggregates (y-o-y)



Note: Composition of January 2003 stock of system credit—business 33%; household 55%; agriculture 12%
Source: Reserve Bank of New Zealand statistics, Table C5

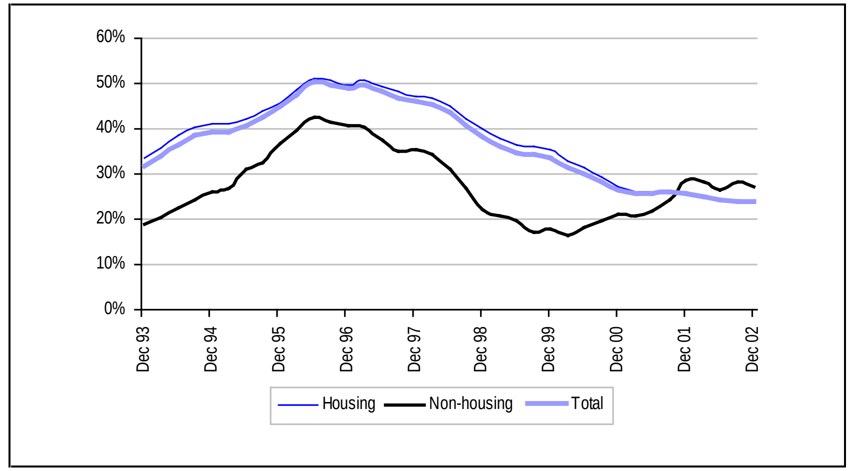
Interest Rates and Credit Growth (continued)

Chart 51: New Zealand—Composition of Bank Credit Exposures



Source: Reserve Bank of New Zealand, Table C7

Chart 53: New Zealand—Growth in Personal Loans (y-o-y)

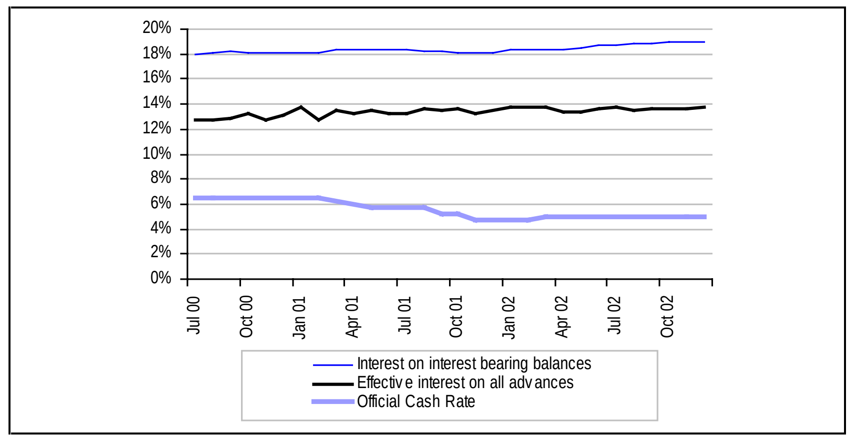


Source: Reserve Bank of New Zealand

Chart 52: New Zealand—Growth in Period End Balances for All Credit Cards

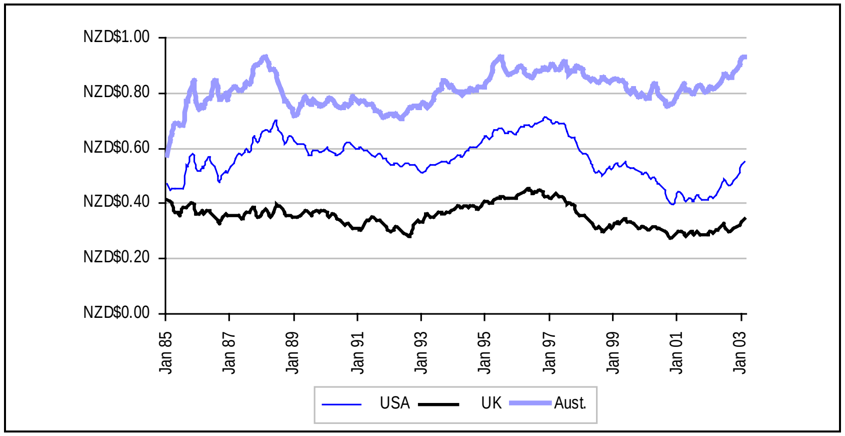
Source: Reserve Bank of New Zealand, Table C12

Chart 54: New Zealand—Interest Rates on Personal Credit Cards



Source: Reserve Bank of New Zealand, Table C12

Chart 55: New Zealand Dollar Exchange Rates



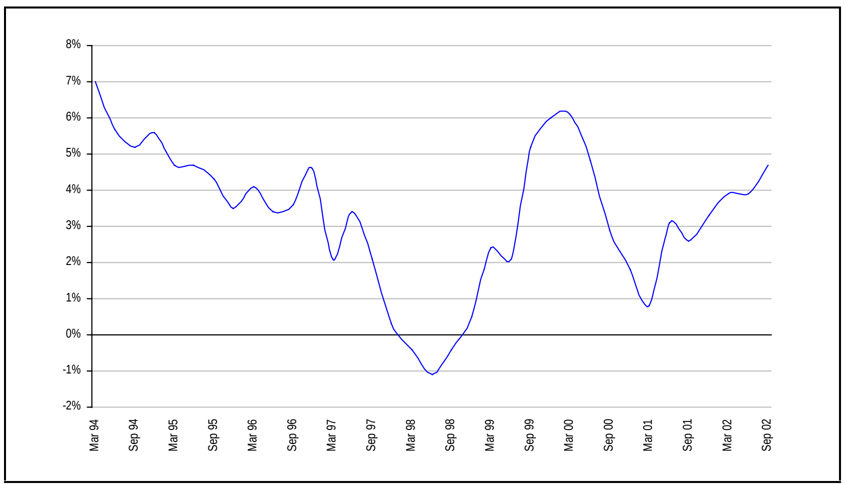
Note: Average monthly rates used; mid-rates all quoted to NZ$1
Source: Reserve Bank of New Zealand statistics, Table B1

Chart 57: New Zealand and Australia Economic Forecasts

Growth y-o-y		1999	2000	2001	2002E	2003E	2004E
GDP	New Zealand	4.0%	3.8%	2.5%	4.2%	2.9%	2.7%
	Australia	4.5%	2.8%	2.7%	3.8%	3.1%	3.7%
Investment	New Zealand*	4.7%	7.7%	-1.5%	6.8%	6.2%	4.0%
	Australia**	6.2%	-2.6%	0.7%	10.5%	9.8%	6.0%
Consumption	New Zealand	3.9%	2.0%	2.4%	3.4%	2.5%	2.2%
	Australia	4.9%	3.2%	3.0%	4.1%	3.2%	3.3%
Consumer Prices	New Zealand	-0.1%	2.6%	2.6%	2.7%	2.0%	2.1%
	Australia	1.5%	4.5%	4.4%	3.0%	2.7%	2.5%
Unemployment Rate	New Zealand	6.8%	6.0%	5.4%	5.1%	5.3%	5.3%
	Australia	7.0%	6.3%	6.8%	6.3%	6.1%	6.0%

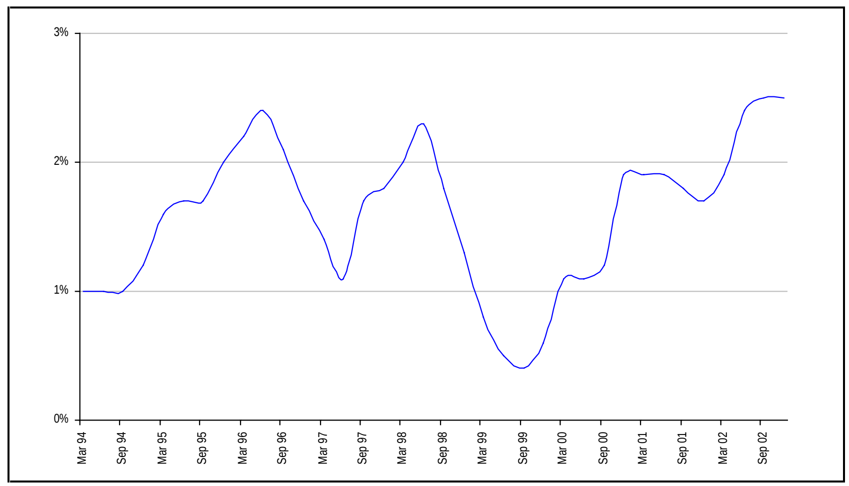
Note: * Gross fixed investment; ** Business investment
Source: Consensus economics

Chart 56: New Zealand Real GDP growth



Note: Quarterly data, y-o-y growth
Source: Statistics NZ

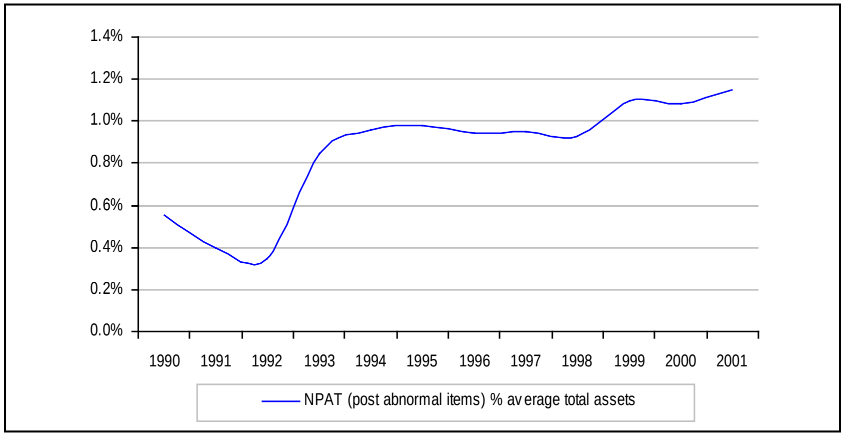
Chart 58: New Zealand Inflation Rate



Note: Weighted median inflation; quarterly data y-o-y growth
Source: Statistics NZ

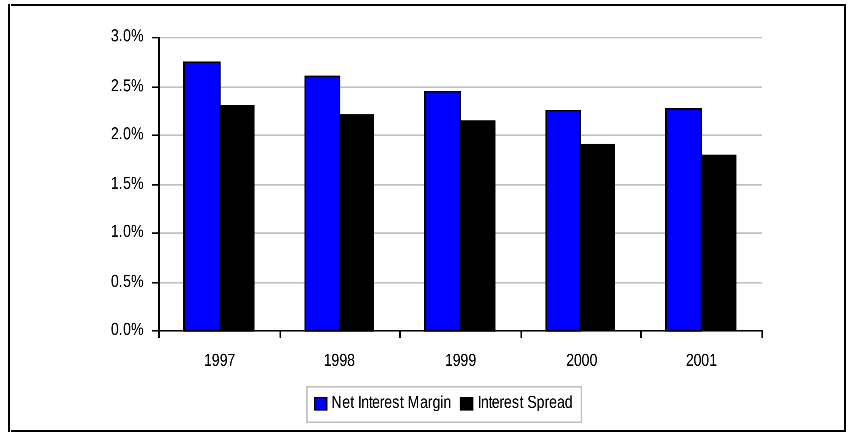
Bank Sector Operational Trends

Chart 59: New Zealand Banks—Profitability



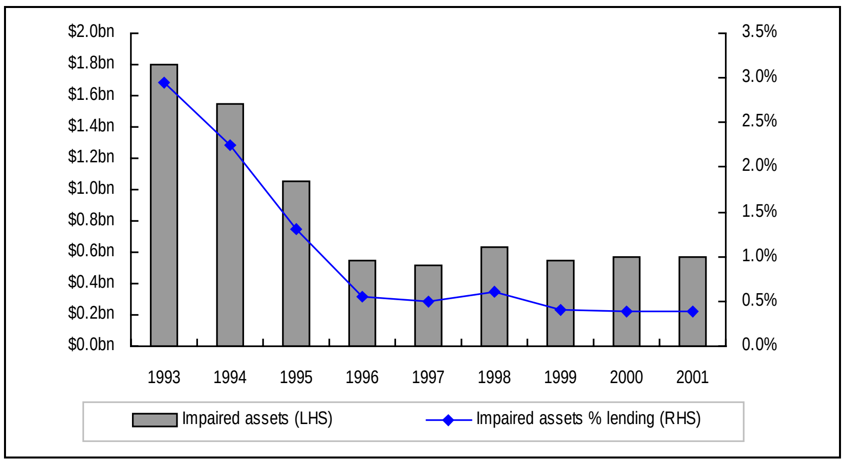
Source: Reserve Bank of New Zealand

Chart 61: New Zealand Banks—Margins and Spreads



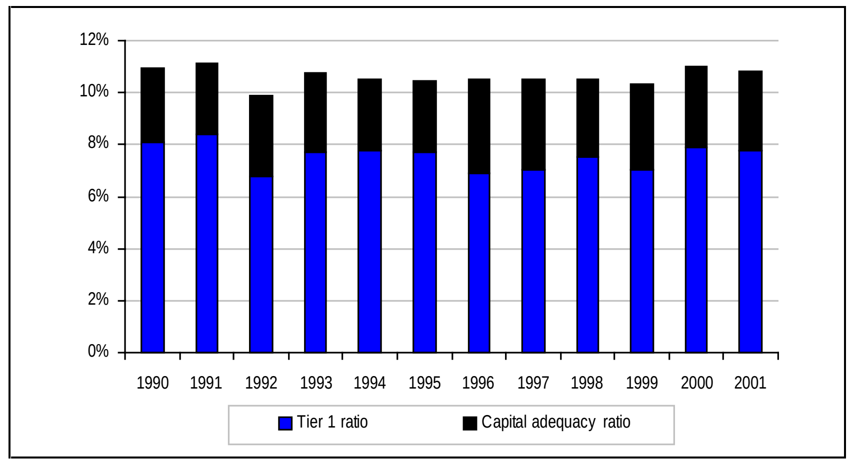
Source: Reserve Bank of New Zealand

Chart 60: New Zealand Banks—Asset Quality



Source: Reserve Bank of New Zealand

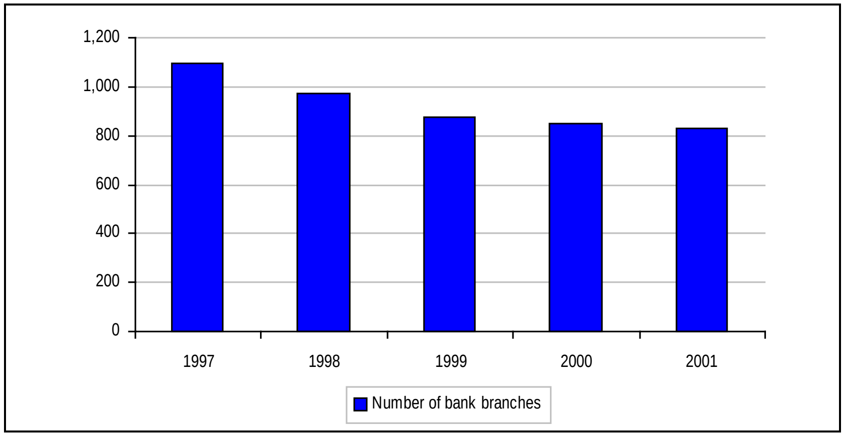
Chart 62: New Zealand Banks—Capital Adequacy



Source: Reserve Bank of New Zealand

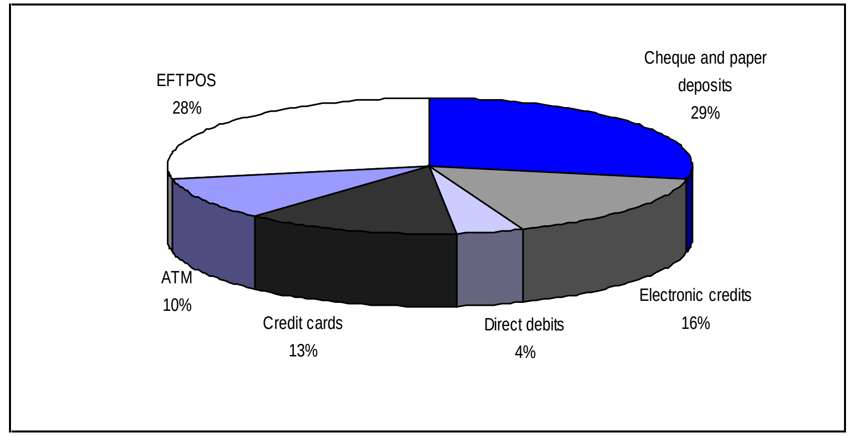
Payments and Distribution

Chart 63: New Zealand—Number of Bank Branches



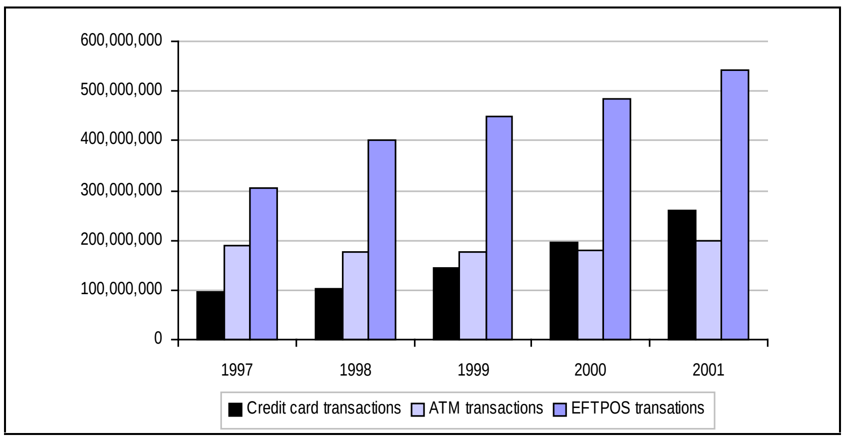
Source: New Zealand Bankers' Association

Chart 65: New Zealand Payment Methods 2001—% Total Transactions by Volume



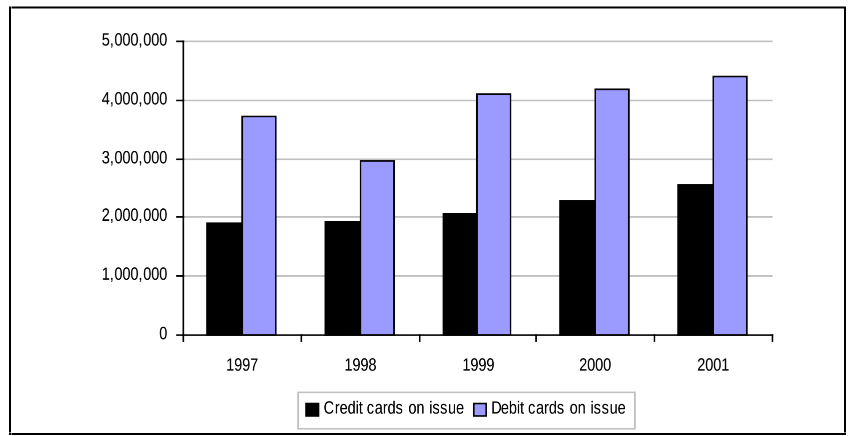
Note: 1997 data: Cheques 27%; Electronic 22%; Direct debits 4%; Credit cards 8%; ATM 15%; EFTPOS 25%
Source: New Zealand Bankers' Association

Chart 64: New Zealand—Number of Non-Cash Transactions Per Annum



Source: New Zealand Bankers' Association

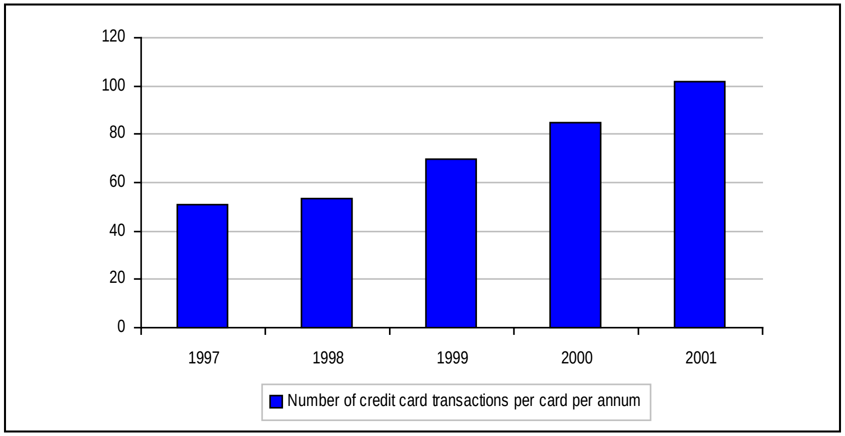
Chart 66: New Zealand—Number of Cards on Issue



Source: New Zealand Bankers' Association

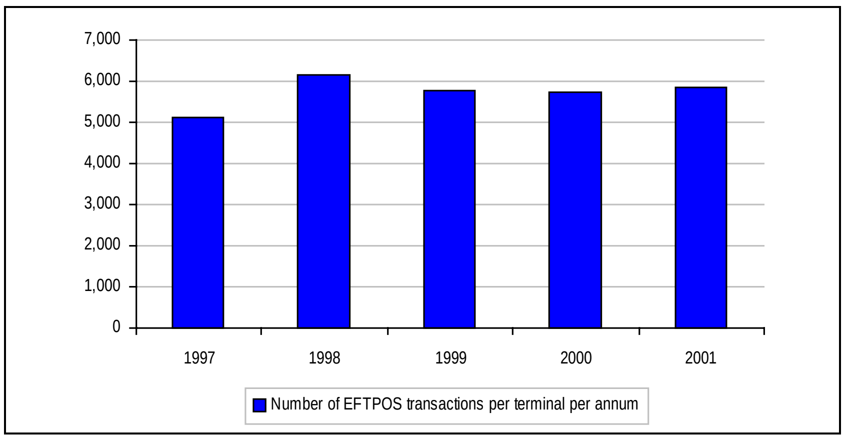
Payments and Distribution (continued)

Chart 67: New Zealand—Intensity of Credit Card Usage



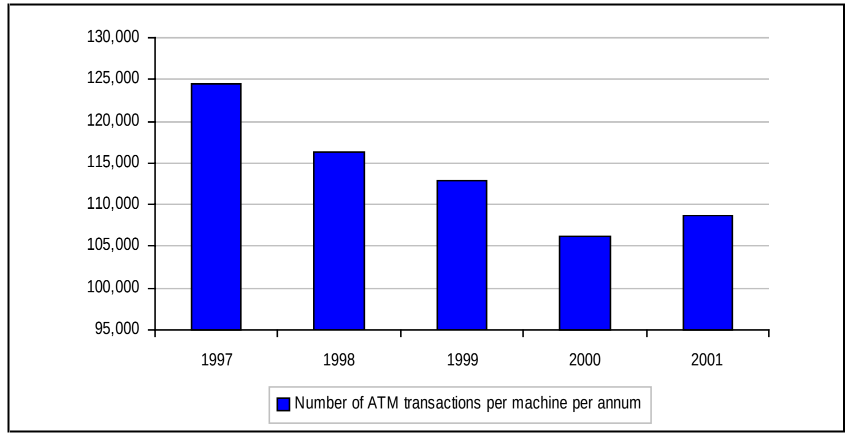
Source: New Zealand Bankers' Association, Merrill Lynch estimates

Chart 68: New Zealand—Intensity of EFTPOS Machine Usage



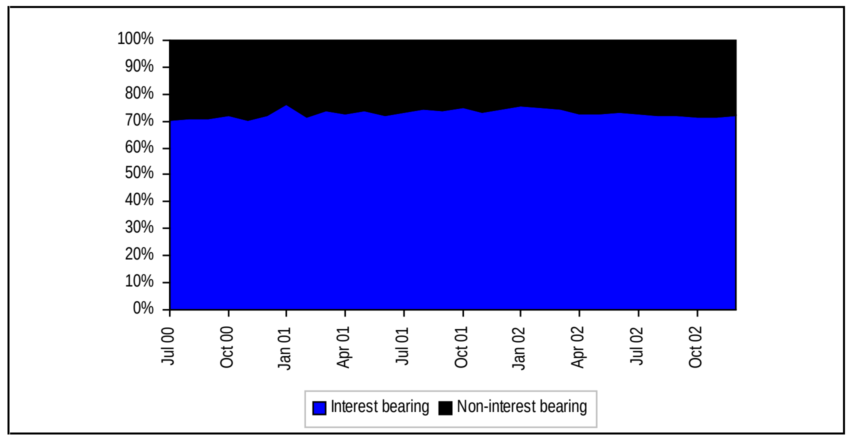
Source: New Zealand Bankers' Association, Merrill Lynch estimates

Chart 69: New Zealand—Intensity of ATM Usage



Source: New Zealand Bankers' Association, Merrill Lynch estimates

Chart 70: New Zealand—Advances Outstanding on Personal Credit Cards



Source: Reserve Bank of New Zealand, Table C12

Investment Rating Distribution: Banks Group (as of 31 March 2003)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	67	37.22%	Buy	30	44.78%
Neutral	94	52.22%	Neutral	38	40.43%
Sell	19	10.56%	Sell	6	31.58%

Investment Rating Distribution: Financial Services Group (as of 31 March 2003)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	81	46.55%	Buy	44	54.32%
Neutral	82	47.13%	Neutral	37	45.12%
Sell	11	6.32%	Sell	1	9.09%

Investment Rating Distribution: Global Group (as of 31 March 2003)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1027	42.02%	Buy	358	34.86%
Neutral	1229	50.29%	Neutral	304	24.74%
Sell	188	7.69%	Sell	39	20.74%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

Price charts for the equity securities referenced in this research report are available at http://www.ml.com/research/pricecharts.asp**, or call 1-888-ML-CHART to have them mailed.**

[NAB, NAUBF] One or more analysts responsible for covering the securities in this report owns such securities.

[NAB, ANZ, WBK] MLPF&S or one or more of its affiliates acts as a market maker for the recommended securities to the extent that MLPF&S or such affiliate is willing to buy and sell such securities for its own account on a regular and continuous basis.

[NAB, NAUBF, WEBNF, WBK, CBAUF] MLPF&S or an affiliate was a manager of a public offering of securities of this company within the last 12 months.

[NAB, NAUBF, ANZ, ANEWF, WEBNF, WBK, CBAUF] MLPF&S was a manager of the most recent public offering of securities of this company within the last three years.

[NAUBF, ANEWF, WEBNF, CBAUF, AMLTF] In the US, retail sales and/or distribution of this report may be made only in states where these securities are exempt from registration or have been qualified for sale.

[NAB, NAUBF] MLPF&S or an affiliate has received compensation for investment banking services from this company within the past 12 months.

[NAB, NAUBF, WEBNF, WBK, CBAUF, AMLTF] MLPF&S or an affiliate expects to receive or intends to seek compensation for investment banking services from this company within the next three months.

Investors should assume that Merrill Lynch is seeking or will seek investment banking or other business relationships with the companies in this report.

In Germany, this report should be read as though Merrill Lynch has acted as a member of a consortium which has underwritten the most recent offering of securities during the last five years for companies covered in this report and holds 1% or more of the share capital of such companies.

The analyst(s) responsible for covering the securities in this report receive compensation based upon, among other factors, the overall profitability of Merrill Lynch, including profits derived from investment banking revenues.

OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. VOLATILITY RISK RATINGS, indicators of potential price fluctuation, are: A - Low, B - Medium, and C - High. INVESTMENT RATINGS, indicators of expected total return (price appreciation plus yield) within the 12-month period from the date of the initial rating, are: 1 - Buy (10% or more for Low and Medium Volatility Risk Securities - 20% or more for High Volatility Risk securities); 2 - Neutral (0-10% for Low and Medium Volatility Risk securities - 0-20% for High Volatility Risk securities); 3 - Sell (negative return); and 6 - No Rating. INCOME RATINGS, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure); 8 - same/lower (dividend not considered to be secure); and 9 - pays no cash dividend.

Neither the information nor any opinion expressed constitutes an offer, or an invitation to make an offer, to buy or sell any securities or any options, futures or other derivatives related to such securities ("related investments"). MLPF&S, its affiliates, directors, officers, employees and employee benefit programs may have a long or short position in any securities of this issuer(s) or in related investments. MLPF&S or its affiliates may from time to time perform investment banking or other services for, or solicit investment banking or other business from, any entity mentioned in this report.

This research report is prepared for general circulation and is circulated for general information only. It does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may receive this report. Investors should seek financial advice regarding the appropriateness of investing in any securities or investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Investors should note that income from such securities, if any, may fluctuate and that each security's price or value may rise or fall. Accordingly, investors may receive back less than originally invested. Past performance is not necessarily a guide to future performance.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or related investment mentioned in this report. In addition, investors in securities such as ADRs, whose values are influenced by the currency of the underlying security, effectively assume currency risk.