MACQUARIE

# Management Discussion and Analysis

## Macquarie Bank Limited

**Year ended 31 March 2018**

## NOTICE TO READERS

The purpose of this report is to provide information supplementary to the Macquarie Bank Limited Disclosure Report (U.S. Version) for the year ended 31 March 2018 and the Financial Report within the Macquarie Bank Annual Report ("the Financial Report") for the year ended 31 March 2018, including further detail in relation to key elements of Macquarie Bank Limited and its subsidiaries' ("Macquarie Bank", "the Consolidated Entity") financial performance and financial position. The report also outlines the funding and capital profile of the Consolidated Entity.

Certain financial information in this report is prepared on a different basis to that contained in the Financial Report, which is prepared in accordance with Australian Accounting Standards. Where financial information presented within this report does not comply with Australian Accounting Standards, reconciliation to the statutory information is provided.

## DATE OF THIS REPORT

This report has been prepared for the year ended 31 March 2018 and is current as at 4 May 2018.

## COMPARATIVE INFORMATION AND CONVENTIONS

Where necessary, comparative figures have been restated to conform to changes in current year financial presentation and group structures.

References to the prior year are to the 12 months ended 31 March 2017.

References to the first half are to the six months ended 30 September 2017.

References to the second half are to the six months ended 31 March 2018.

In the financial tables throughout this document "*" indicates that the absolute percentage change in the balance was greater than 300% or indicates the result was a gain in one period but a loss in another, or vice versa.

## INDEPENDENT AUDITOR'S REPORT

This document should be read in conjunction with the Financial Report for the year ended 31 March 2018, which was subject to independent review by PricewaterhouseCoopers.

PricewaterhouseCoopers' independent auditor's review report to the members of Macquarie Bank Limited dated 4 May 2018 was unqualified.

Any additional financial information in this document which is not included in the Financial Report was not subject to independent audit by PricewaterhouseCoopers.

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## DISCLAIMER

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1.1 Executive summary

# RESULT OVERVIEW

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## 1.1 EXECUTIVE SUMMARY

### Performance

Macquarie Bank's consolidated net profit attributable to ordinary equity holders of $A1,568 million for the year ended 31 March 2018 increased 28% from $A1,221 million.

### Annuity-style businesses

**Macquarie Asset Management (MAM), Corporate and Asset Finance (CAF)** and **Banking and Financial Services (BFS)** generated a combined net profit contribution for the year ended 31 March 2018 of $A1,898 million, up 8% on the prior year.

Key drivers included:

**MAM** **↑165% on prior year**

- higher net gains on sale and revaluation of equity and debt investments primarily due to income from the sell down of infrastructure debt in MSIS
- the release of accruals relating to legacy business activities
- base fees broadly in line.

**CAF** **↑1% on prior year**

- increased income from prepayments, realisations and investment-related income in the Principal Finance portfolio
- lower charges for provisions and impairments reflecting the partial reversal of collective provisions, driven by net loan repayments, and the improved credit performance of underlying portfolios
- Asset Finance contribution increased due to stronger underlying net operating lease income in Aviation and income from Vehicles which included the sale of the US commercial vehicles financing business. The remaining portfolios continued to perform well.

Partially offset by:

- lower interest income as a result of the reduction in the Principal Finance portfolio size.

**BFS** **↑9% on prior year**

- growth in Australian loan, deposit and platform average volumes
- the non-recurrence of expenses recognised in the prior year, including impairment charges predominately on certain equity positions, intangible assets and expenses in relation to the Core Banking platform.

Partially offset by:

- the non-recurrence of the net overall gain on the disposal of Macquarie Life's risk insurance business to Zurich Australia Limited and the US mortgages portfolio in the prior year.

### Capital markets facing businesses

**Commodities and Global Markets (CGM)** delivered a net profit contribution for the year ended 31 March 2018 of $A866 million, broadly in line with the prior year.

Key drivers included:

**CGM** **↓1% on prior year**

- timing of income recognition relating to tolling agreements and capacity contracts
- sustained low volatility and tighter credit spreads impacting income from interest rate and credit products
- reduced income from the sale of investments, mainly in energy and related sectors.

Partially offset by:

- improved results across the equities platform driven by rallying prices and increased volatility, notably in Asia
- reduction in impairments in commodity related sectors
- increased client demand for structured foreign exchange solutions in Asia and North America
- significant opportunities for the North American Gas and Power business to capitalise on price dislocations across regions.

## 1.1 EXECUTIVE SUMMARY CONTINUED

### Profit attributable to ordinary equity holders

# $A1,568m

**28% on prior year**

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Financial performance summary** | | | | | | |
| Net interest income | **986** | 1,032 | *(4)* | **2,018** | 2,170 | *(7)* |
| Fee and commission income | **441** | 449 | *(2)* | **890** | 820 | *9* |
| Net trading income | **1,076** | 805 | *34* | **1,881** | 1,667 | *13* |
| Net operating lease income | **468** | 469 | *(<1)* | **937** | 922 | *2* |
| Share of net profits/(losses) of associates and joint ventures accounted for using the equity method | **13** | 9 | *44* | **22** | (19) | * |
| Other operating income and charges | **325** | 90 | *261* | **415** | 261 | *59* |
| **Net operating income** | **3,309** | 2,854 | *16* | **6,163** | 5,821 | *6* |
| Employment expenses | **(722)** | (765) | *(6)* | **(1,487)** | (1,487) | - |
| Brokerage, commission and trading-related expenses | **(303)** | (316) | *(4)* | **(619)** | (626) | *(1)* |
| Occupancy expenses | **(69)** | (55) | *25* | **(124)** | (118) | *5* |
| Non-salary technology expenses | **(68)** | (65) | *5* | **(133)** | (158) | *(16)* |
| Other operating expenses | **(849)** | (798) | *6* | **(1,647)** | (1,699) | *(3)* |
| **Total operating expenses** | **(2,011)** | (1,999) | *1* | **(4,010)** | (4,088) | *(2)* |
| Operating profit before income tax | **1,298** | 855 | *52* | **2,153** | 1,733 | *24* |
| Income tax expense | **(363)** | (207) | *75* | **(570)** | (509) | *12* |
| **Profit after income tax** | **935** | 648 | *44* | **1,583** | 1,224 | *29* |
| (Profit)/loss attributable to non-controlling interests | **(4)** | 3 | * | **(1)** | 12 | * |
| **Profit attributable to equity holders of Macquarie Bank Limited** | **931** | 651 | *43* | **1,582** | 1,236 | *28* |
| Distributions paid or provided for on Macquarie Income Securities | **(7)** | (7) | - | **(14)** | (15) | *(7)* |
| **Profit attributable to ordinary equity holders of Macquarie Bank Limited** | **924** | 644 | *43* | **1,568** | 1,221 | *28* |
| **Key metrics** | | | | | | |
| Expense to income ratio (%) | **60.8** | 70.0 | | **65.1** | 70.2 | |
| Effective tax rate (%) | **28.1** | 24.1 | | **26.5** | 29.2 | |

## 1.1 EXECUTIVE SUMMARY CONTINUED

### Net operating income

Net operating income of $A6,163 million for the year ended 31 March 2018 increased 6% from $A5,821 million in the prior year. The result included lower charges for impairments and provisions and increased fee and commission income, partially offset by lower investment income.

Key drivers included:

### Net interest and trading income

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **3,899** | 3,837 |

2% on prior year

- growth in average Australian loan portfolio and deposit volumes in BFS
- lower costs of holding long-term liquidity and the impact of accounting volatility on economically hedged positions that do not qualify for hedge accounting in Corporate
- significant opportunities for the North American Gas and Power business to capitalise on price dislocations across regions in CGM.

Partially offset by:

- lower interest income as a result of the reduction in the Principal Finance portfolio in CAF
- sustained low volatility and tighter credit spreads impacting income from interest rate and credit products and timing of income recognition relating to tolling agreements and capacity contracts in CGM
- impact of Australian Government Major Bank Levy.

### Net operating lease income

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **937** | 922 |

2% on prior year

- improved underlying income from the Aviation, Energy and Technology portfolios in CAF.

### Other operating income and charges

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **415** | 261 |

59% on prior year

- lower charges for provisions and impairments across most Operating Groups due to improved credit conditions
- the release of accruals related to legacy business activities as well as higher revenue for MSIS Retail in MAM, as well as the sale of certain CAF Principal Finance assets in the US.

Partially offset by:

- lower investment income mainly due to the non-recurrence of gains in the prior year including the sale of Macquarie Life's risk insurance business to Zurich Australia Limited in BFS and the sale of a number of investments in the energy and related sectors in CGM. This was partially offset by the sell down of infrastructure debt in MAM in the current year.

### Fee and commission income

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **890** | 820 |

9% on prior year

- increase driven by demand for advisory and structured products, primarily in Asia and North America in CGM.

### Share of net profits/(losses) of associates and joint ventures accounted for using the equity method

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **22** | (19) |

significantly on prior year

- increase includes CGM's share of net profits from equity investments
- non-recurrence of equity accounted losses recognised in the prior year in Corporate, reflecting the reclassification of non-core assets to investments held for sale that were subsequently disposed of during the current year.

## 1.1 EXECUTIVE SUMMARY CONTINUED

### Operating expenses

Total operating expenses of $A4,010 million for the year ended 31 March 2018 decreased 2% from $A4,088 million in the prior year mainly driven by Occupancy and Other operating expenses and Non-salary technology expenses.

Key drivers included:

#### Employment expenses

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **1,487** | 1,487 |

– in line with prior year

– average headcount broadly in line with prior year.

#### Brokerage, commission and trading-related expenses

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **619** | 626 |

↓1% on prior year

– decrease mainly driven by a reduction in physical metals inventory levels in CGM.

Partially offset by:

– higher brokerage and commission expense in the MSIS Retail business in MAM.

#### Non-salary technology expenses

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **133** | 158 |

↓16% on prior year

– the prior year included non-recurring technology expenses in relation to the Core Banking platform in BFS.

#### Occupancy and Other operating expenses

| FULL-YEAR TO | |
|---|---|
| Mar 18 $Am | Mar 17 $Am |
| **1,771** | 1,817 |

↓3% on prior year

– lower professional fees in the current year and non-recurring Other operating expenses in the prior year in BFS
– lower Other operating expenses in CGM driven by benefits of cost synergies following the merger of Commodities and Financial Markets (CFM) and Macquarie Securities Group (MSG).

Partially offset by:

– increased deal and project related expenses in CAF.

### Income tax expense

Income tax expense for the year ended 31 March 2018 was $A570 million, a 12% increase from $A509 million in the prior year. The effective tax rate for the year ended 31 March 2018 was 26.5%, down from 29.2% in the prior year.

The increase in tax expense was mainly due to higher profit before tax, offset in part by increased benefit from permanent tax differences. The reduced effective tax rate was mainly driven by change in geographic composition and nature of earnings.

2.1 Net interest and trading income
2.2 Fee and commission income
2.3 Net operating lease income
2.4 Share of net profits of associates and joint ventures
2.5 Other operating income and charges
2.6 Operating expenses
2.7 Headcount
2.8 Income tax expense

# FINANCIAL PERFORMANCE ANALYSIS

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## 2.1 NET INTEREST AND TRADING INCOME

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| Net interest income | **986** | 1,032 | *(4)* | **2,018** | 2,170 | *(7)* |
| Net trading income | **1,076** | 805 | *34* | **1,881** | 1,667 | *13* |
| **Net interest and trading income** | **2,062** | 1,837 | *12* | **3,899** | 3,837 | *2* |

Net interest income and net trading income are recorded in accordance with Australian Accounting Standards, with net interest income brought to account using the effective interest method and net trading income predominately comprising gains and losses relating to trading activities.

For CGM, which predominately earns income from trading-related activities, the relative contribution of net interest income and net trading income from those activities can vary from period to period depending on the underlying trading strategies undertaken by the Consolidated Entity and its clients.

For businesses that predominately earn income from lending activities (CAF and BFS), derivatives that economically hedge interest rate risk are required to be carried at fair value through net trading income unless they form part of a qualifying hedge relationship. Hedge relationships are generally only recognised at a Consolidated Entity level, however for segment reporting, derivatives are accounted for on an accruals basis in the Operating Group segments and changes in fair value are recognised within the Corporate segment offset by the effect of hedge relationships at the Consolidated Entity level.

The presentation of net interest income and net trading income separately can distort the analysis of the underlying activities and drivers. For example, CAF's interest rate swaps are entered into to hedge the interest rate risk associated with loan assets. The interest income and associated funding costs are recognised in net interest income, but the related swap is recognised in net trading income. Accordingly, net interest income and net trading income are presented and discussed below in aggregate for each Operating Group, which management believes presents a more consistent overview of business performance and allows for a better analysis of the underlying activities and drivers.

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| MAM | **48** | 60 | *(20)* | **108** | 104 | *4* |
| CAF | **239** | 330 | *(28)* | **569** | 694 | *(18)* |
| BFS | **598** | 584 | *2* | **1,182** | 1,049 | *13* |
| CGM | | | | | | |
| Commodities | **685** | 388 | *77* | **1,073** | 1,122 | *(4)* |
| Credit, interest rates and foreign exchange | **233** | 270 | *(14)* | **503** | 571 | *(12)* |
| Equities | **134** | 164 | *(18)* | **298** | 289 | *3* |
| Corporate | **125** | 41 | *205* | **166** | 8 | * |
| **Net interest and trading income** | **2,062** | 1,837 | *12* | **3,899** | 3,837 | *2* |

## 2.1 NET INTEREST AND TRADING INCOME CONTINUED

Net interest and trading income of $A3,899 million for the year ended 31 March 2018 increased 2% from $A3,837 million in the prior year.

### MAM

Net interest and trading income in MAM includes income on specialised retail products and interest income from the provision of financing facilities to external funds and their investors.

Net interest and trading income of $A108 million for the year ended 31 March 2018 increased 4% from $A104 million in the prior year, primarily driven by higher interest income in the MSIS Fund Linked Product business.

### CAF

Net interest and trading income in CAF predominately relates to net income from the loan and finance lease (including vehicles and equipment financing) portfolios and the funding costs associated with the operating lease portfolios (including aviation, mining and energy assets) and Principal Finance equity investments.

Net interest and trading income of $A569 million for the year ended 31 March 2018 decreased 18% from $A694 million in the prior year, mainly as a result of the reduction in the Principal Finance portfolio.

The loan and finance lease portfolio was $A24.1 billion at 31 March 2018, a decrease of 8% from $A26.3 billion at 31 March 2017. The decrease was mainly in Principal Finance, as well as the sale of the US commercial vehicles financing business in March 2018.

### BFS

Net interest and trading income in BFS relates to interest income earned from the loan portfolio that primarily comprises residential mortgages in Australia, loans to Australian businesses, insurance premium funding and credit cards. BFS also generates income from deposits by way of a deposit premium received from Group Treasury, which uses the deposits as a source of funding for the Consolidated Entity.

Net interest and trading income of $A1,182 million for the year ended 31 March 2018 increased 13% from $A1,049 million in the prior year primarily due to a 6% growth in average Australian loan portfolio volumes and a 7% growth in average BFS deposits. This was partially offset by a $A16 million allocation of the Australian Government Major Bank Levy that came into effect from 1 July 2017.

At 31 March 2018 the Australian loan and deposit portfolio included:

- Australian mortgage volumes of $A32.7 billion, a 14% increase from $A28.7 billion at 31 March 2017;
- business lending volumes of $A7.3 billion, a 12% increase from $A6.5 billion at 31 March 2017; and
- BFS deposits of $A45.7 billion, a 3% increase from $A44.5 billion at 31 March 2017.

The remaining legacy loan portfolios were sold during the year, down from $A0.5 billion at 31 March 2017.

## 2.1 NET INTEREST AND TRADING INCOME CONTINUED

### CGM

#### Commodities

Net interest and trading income from commodity related activities is generated from the provision of hedging and risk management services and loans and working capital finance to clients across a range of commodity sectors including base and precious metals, energy and agriculture. CGM also enters into a number of tolling agreements, storage contracts and transportation agreements in order to facilitate client flow transactions as part of its commodities platform. These arrangements provide CGM with the ability to maximise opportunities where there is dislocation between the supply and demand for energy. Tolling agreements, storage contracts and transportation agreements, which are managed on a fair value basis for financial and risk management purposes, are required to be accounted for on an accruals basis for statutory reporting purposes, which may result in some volatility with timing of reported income.

Net interest and trading income from Commodities of $A1,073 million for the year ended 31 March 2018 decreased 4% from $A1,122 million in the prior year. The current year included mixed results across the commodities platform. Strong results in North American Gas and Power due to an increase in volatility, customer activity and price dislocations across regions, Bulk Commodities from volatility in iron ore and Commodity Investor Products driven by continued client growth were offset by reduced client hedging activity and trading opportunities in Global Oil, a reduction in lending and financing income and a $A147 million reduction in income due to the timing of income recognition relating to tolling agreements and capacity contracts being recognised in future years.

#### Credit, interest rates and foreign exchange

Net interest and trading income from credit, interest rates and foreign exchange related activities is generated from the provision of trading and hedging services to a range of corporate and institutional clients globally, in addition to making secondary markets in corporate debt securities, syndicated bank loans and middle market loans and providing specialty lending.

Net interest and trading income from credit, interest rates and foreign exchange related activities of $A503 million for the year ended 31 March 2018 decreased 12% from $A571 million in the prior year. Revenues were impacted by sustained low volatility and tighter credit spreads in interest rate and credit products. This was partially offset by strong client activity in structured foreign exchange products.

#### Equities

Equities net interest and trading income is generated from the issue of derivative products in key locations, the provision of equity finance solutions to institutional clients and the conduct of risk management and trading activities.

Equities net interest and trading income of $A298 million for the year ended 31 March 2018 increased 3% from $A289 million in the prior year. This reflects more favourable conditions in Asia including rallying equities, some increase in volatility, and strong demand for warrants and structured client capital solutions.

### Corporate

Net interest and trading income in the Corporate segment includes the net result of managing liquidity and funding for the Consolidated Entity, earnings on capital, funding costs associated with non-core investments held centrally and accounting volatility arising from movements in underlying rates relating to economically hedged positions where designated hedge accounting is unable to be achieved for accounting purposes.

Net interest and trading income of $A166 million for the year ended 31 March 2018 increased substantially from $A8 million in the prior year primarily due to lower costs of holding long-term liquidity and the impact of accounting volatility on economically hedged positions that do not qualify for hedge accounting. In addition, higher earnings on capital was driven by increased average capital volumes and higher USD interest rates.

## 2.2 FEE AND COMMISSION INCOME

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| Brokerage and commissions | **185** | 184 | *1* | **369** | 369 | - |
| Other fee and commission income | **256** | 265 | *(3)* | **521** | 451 | *16* |
| **Total fee and commission income** | **441** | 449 | *(2)* | **890** | 820 | *9* |

Total fee and commission income of $A890 million for the year ended 31 March 2018 increased 9% from $A820 million in the prior year.

### Brokerage and commissions

Brokerage and commissions income of $A369 million for the year ended 31 March 2018 was in line with the prior year.

### Other fee and commission income

Other fee and commission income includes fees earned on a range of BFS' products and services including the Wrap and Vision platforms, deposits, provision of wealth services in Australia, mortgages, credit cards and business loans. MAM includes distribution service fees, structuring fees and capital protection fees, while CGM includes advisory, underwriting, lending services and income on structured products.

Other fee and commission income of $A521 million for the year ended 31 March 2018 increased 16% from $A451 million in the prior year due to demand for advisory and structured products, primarily in Asia and North America in CGM. Increased platform commissions from higher funds on the Wrap and Vision platforms were offset by lower Life insurance income due to the sale of Macquarie Life's risk insurance business to Zurich Australia Limited in September 2016 by BFS.

## 2.3 NET OPERATING LEASE INCOME

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| Rental income | **1,013** | 909 | *11* | **1,922** | 1,666 | *15* |
| Depreciation on operating lease assets | **(545)** | (440) | *24* | **(985)** | (744) | *32* |
| **Net operating lease income** | **468** | 469 | *(<1)* | **937** | 922 | *2* |

Net operating lease income, which is predominately earned by CAF, totalled $A937 million for the year ended 31 March 2018, up 2% from $A922 million in the prior year due to improved underlying income from the Aviation, Energy and Technology portfolios.

CAF's operating lease portfolio was $A10.2 billion at 31 March 2018, an increase of 2% from $A10.0 billion at 31 March 2017 with growth in the Technology and Energy portfolios partially offset by depreciation and sales in the Aviation portfolio.

## 2.4 SHARE OF NET PROFITS/(LOSSES) OF ASSOCIATES AND JOINT VENTURES

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Share of net profits/(losses) of associates and joint ventures accounted for using the equity method** | **13** | 9 | *44* | **22** | (19) | * |

Share of net profits of associates and joint ventures of $A22 million for the year ended 31 March 2018 increased significantly from a net loss of $A19 million in the prior year. The increase was mainly due to CGM's share of net profits from equity investments and the non-recurrence of equity accounted losses recognised in the prior year in Corporate, reflecting the reclassification of non-core assets to investments held for sale, that were subsequently disposed of during the current year.

## 2.5 OTHER OPERATING INCOME AND CHARGES

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Investment income** | | | | | | |
| Net gain on sale of investment securities available for sale | **17** | 14 | *21* | **31** | 39 | *(21)* |
| Net gain on sale of interests in associates and joint ventures | **26** | 1 | * | **27** | 110 | *(75)* |
| Net gain on acquisition, disposing, reclassification and change in ownership interests of investments, subsidiaries and assets and businesses held for sale | **101** | 67 | *51* | **168** | 377 | *(55)* |
| Net fair value gains on financial instruments designated at fair value | **46** | - | * | **46** | - | * |
| Dividends/distributions from investment securities available for sale | **5** | 1 | * | **6** | 10 | *(40)* |
| **Total investment income** | **195** | 83 | *135* | **278** | 536 | *(48)* |
| **Impairment charges** | | | | | | |
| Impairment charge on investment securities available for sale | **(10)** | (6) | *67* | **(16)** | (32) | *(50)* |
| Impairment charge on interests in associates and joint ventures | **(3)** | (5) | *(40)* | **(8)** | (6) | *33* |
| Impairment charge on intangibles and other non-financial assets | **(10)** | (16) | *(38)* | **(26)** | (45) | *(42)* |
| **Total impairment charges** | **(23)** | (27) | *(15)* | **(50)** | (83) | *(40)* |
| **Provisions** | | | | | | |
| Individually assessed provisions for impairments | **(18)** | (42) | *(57)* | **(60)** | (150) | *(60)* |
| Collective allowance for credit losses (provided for)/reversed during the financial year | **82** | 52 | *58* | **134** | - | * |
| Amounts written off | **(67)** | (67) | - | **(134)** | (147) | *(9)* |
| Recovery of amounts previously written off | **24** | 17 | *41* | **41** | 44 | *(7)* |
| **Total provisions** | **21** | (40) | * | **(19)** | (253) | *(92)* |
| Other income | **132** | 74 | *78* | **206** | 61 | *238* |
| **Total other operating income and charges** | **325** | 90 | *261* | **415** | 261 | *59* |

## 2.5 OTHER OPERATING INCOME AND CHARGES CONTINUED

Total other operating income and charges of $A415 million for the year ended 31 March 2018 increased 59% from $A261 million in the prior year, primarily driven by reduced charges for provisions across most Operating Groups, partially offset by lower investment income mainly in BFS and CGM.

### Investment income

Investment income totalled $A278 million for the year ended 31 March 2018 decreased 48% from $A536 million in the prior year.

Investment income in the current year included gains generated by CAF from Principal Finance investments in Europe and the US and the sale of the US Vehicles financing business, and income from the sell down of infrastructure debt in MSIS.

The prior year included BFS' net overall gain on the disposal of Macquarie Life's risk insurance business to Zurich Australia Limited and the US mortgages portfolio, a gain realised on the sale of an interest in a toll road in the US by the CAF Principal Finance business, CGM's gains on the sale of a number of investments, mainly in energy and related sectors, and gains on disposal of legacy assets and a number of investments held for the purposes of managing the Consolidated Entity's liquidity in Corporate.

### Impairment charges

Impairment charges totalled $A50 million for the year ended 31 March 2018 decreased 40% from $A83 million in the prior year. The decrease predominately relates to the higher impairment of equity investments and impairments of intangibles relating to the Core Banking platform in the prior year in BFS.

### Provisions

Provisions for credit losses and write-offs of $A19 million for the year ended 31 March 2018 decreased 92% from $A253 million in the prior year. The decrease was largest in CAF which included the partial reversal of collective provisions, driven by net loan repayments, and the improved credit performance of underlying portfolios. CGM included write downs recognised on certain underperforming commodity-related loans in the prior year.

### Other Income

Other Income of $A206 million for the year ended 31 March 2018 increased significantly from $A61 million in the prior year. The increase predominately relates to the sale of Principal Finance assets in the US in CAF and the release of accruals related to legacy businesses in MAM.

## 2.6 OPERATING EXPENSES

| | HALF-YEAR TO | | | MOVEMENT | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| Employment expenses | | | | | | |
| Salary and related costs including commissions, superannuation and performance-related profit share | **(654)** | (677) | *(3)* | **(1,331)** | (1,319) | *1* |
| Share-based payments | **(68)** | (84) | *(19)* | **(152)** | (163) | *(7)* |
| Provision for long service leave and annual leave | **-** | (4) | *(100)* | **(4)** | (5) | *(20)* |
| **Total employment expenses** | **(722)** | (765) | *(6)* | **(1,487)** | (1,487) | - |
| Brokerage, commission and trading-related expenses | **(303)** | (316) | *(4)* | **(619)** | (626) | *(1)* |
| Occupancy expenses | **(69)** | (55) | *25* | **(124)** | (118) | *5* |
| Non-salary technology expenses | **(68)** | (65) | *5* | **(133)** | (158) | *(16)* |
| Other operating expenses | | | | | | |
| Professional fees | **(100)** | (89) | *12* | **(189)** | (185) | *2* |
| Travel and entertainment expenses | **(28)** | (26) | *8* | **(54)** | (51) | *6* |
| Advertising and communication expenses | **(14)** | (20) | *(30)* | **(34)** | (31) | *10* |
| Amortisation of intangibles | **(11)** | (10) | *10* | **(21)** | (11) | *91* |
| Auditor's remuneration | **(11)** | (11) | - | **(22)** | (22) | - |
| Other expenses | **(685)** | (642) | *7* | **(1,327)** | (1,399) | *(5)* |
| **Total other operating expenses** | **(849)** | (798) | *6* | **(1,647)** | (1,699) | *(3)* |
| **Total operating expenses** | **(2,011)** | (1,999) | *1* | **(4,010)** | (4,088) | *(2)* |

Total operating expenses of $A4,010 million for the year ended 31 March 2018 decreased 2% from $A4,088 million in the prior year mainly driven by non-recurring expenses in BFS and benefits of cost synergies following the merger of CFM and MSG.

Key drivers of the movement included:

- Total employment expenses of $A1,487 million for the year ended 31 March 2018 was in line with the prior year.The average headcount for the year ended 31 March 2018 was materially flat compared to the prior year.
- Brokerage, commission and trading-related expenses of $A619 million for the year ended 31 March 2018 decreased 1% from $A626 million in the prior year mainly due to reduced physical metal inventory levels in CGM, partially offset by higher expense in MSIS Retail business in MAM
- Non-salary technology expenses of $A133 million for the year ended 31 March 2018 decreased 16% from $A158 million in the prior year mainly due to non-recurring technology expenses in relation to the Core Banking platform in BFS
- Total other operating expenses of $A1,647 million for the year ended 31 March 2018 decreased 3% from $A1,699 million in the prior year due to lower professional fees and the non-recurrence of expenses in the prior year in BFS, lower expenses in CGM driven by realisation of benefits from cost synergies following the merger of CFM and MSG, partially offset by increased deal and project related expenses in CAF.

## 2.7 HEADCOUNT

| | AS AT | | | MOVEMENT | |
|---|---|---|---|---|---|
| | Mar 18 | Sep 17 | Mar 17 | *Sep 17 %* | *Mar 17 %* |
| **Headcount by Operating Group** | | | | | |
| MAM | **125** | 123 | 124 | *2* | *1* |
| CAF | **1,306** | 1,259 | 1,254 | *4* | *4* |
| BFS | **2,321** | 2,075 | 1,990 | *12* | *17* |
| CGM | **930** | 936 | 908 | *(1)* | *2* |
| Total headcount - Operating Groups | **4,682** | 4,393 | 4,276 | *7* | *9* |
| Total headcount - Discontinued Operations[1] | **57** | 68 | 59 | *(16)* | *(3)* |
| Total headcount - Corporate | **25** | 26 | 31 | *(4)* | *(19)* |
| **Total headcount** | **4,764** | 4,487 | 4,366 | *6* | *9* |
| **Headcount by region** | | | | | |
| Australia[2] | **3,505** | 3,215 | 3,108 | *9* | *13* |
| International: | | | | | |
| Americas | **493** | 503 | 496 | *(2)* | *(1)* |
| Asia | **298** | 304 | 304 | *(2)* | *(2)* |
| Europe, Middle East and Africa | **468** | 465 | 458 | *1* | *2* |
| Total headcount - International | **1,259** | 1,272 | 1,258 | *(1)* | *<1* |
| **Total headcount** | **4,764** | 4,487 | 4,366 | *6* | *9* |
| International headcount ratio (%) | **26** | 28 | 29 | | |

1. Headcount relating to the Macquarie Investment Management business within MAM relates to the business sold to Macquarie Financial Holdings Pty Limited and its subsidiaries on 15 April 2015. The employees are yet to be transferred to Macquarie Financial Holdings Pty Limited, however their employment related costs are reflected in Macquarie Financial Holdings Pty Limited and its subsidiaries.
2. Includes New Zealand

Total headcount increased 9% to 4,764 at 31 March 2018 from 4,366 at 31 March 2017 primarily driven by an increase in BFS to support business growth.

## 2.8 INCOME TAX EXPENSE

| | FULL-YEAR TO | |
|---|---|---|
| | Mar 18 $Am | Mar 17 $Am |
| Operating profit before income tax | **2,153** | 1,733 |
| Prima facie tax @ 30% | **646** | 520 |
| Income tax permanent differences | **(76)** | (11) |
| Income tax expense | **570** | 509 |
| **Effective tax rate**[1] | **26.5%** | 29.2% |

1. The effective tax rate is calculated on Operating profit before income tax and after non-controlling interests. Non-controlling interests reduced operating profit before income tax by $A1 million for the year ended 31 March 2018 (31 March 2017: increased operating profit before income tax by $A12 million).

Income tax expense for the year ended 31 March 2018 was $A570 million, a 12% increase from $A509 million in the prior year. The effective tax rate for the year ended 31 March 2018 was 26.5%, down from 29.2% in the prior year.

The increase in tax expense was mainly due to higher profit before tax, offset in part by increased benefit from permanent tax differences. The reduced effective tax rate was mainly driven by change in geographic composition and nature of earnings.

3.1 Basis of preparation
3.2 MAM
3.3 CAF
3.4 BFS
3.5 CGM
3.6 Corporate

# SEGMENT ANALYSIS

# 3

## 3.1 BASIS OF PREPARATION

### Operating Segments

AASB 8 *Operating Segments* requires the 'management approach' to disclosing information about the Consolidated Entity's reportable segments. The financial information is reported on the same basis as used internally by senior management for evaluating operating segment performance and for deciding how to allocate resources to operating segments. Such information may be produced using different measures to that used in preparing the statutory income statement.

For internal reporting, performance measurement and risk management purposes, the Consolidated Entity is divided into four Operating Groups and a Corporate segment. These segments have been set up based on the different core products and services offered. There were previously five Operating Groups, and during the prior year CFM merged with MSG to form CGM. Segment information has been prepared in accordance with the basis of preparation described below.

The Operating Groups comprise:

- **MAM** offers a range of investment solutions with an alternate fixed income focus, for its fiduciary clients within the infrastructure debt sector and balance sheet lending to shipping, export credit agency backed debt, hedge funds and private equity investors
- **CAF** operates in selected international markets, providing specialist financing, investing and asset management solutions. CAF has expertise in flexible primary financing, secondary market investing and asset finance including aircraft, vehicles, technology, healthcare, manufacturing, industrial, energy, rail and mining equipment
- **BFS** provides a diverse range of personal banking, wealth management and business banking products and services to retail clients, advisers, brokers and business clients
- **CGM** provides clients with an integrated, end-to-end offering across global markets including equities, fixed income, foreign exchange and commodities.

The **Corporate** segment, which is not considered an Operating Group, includes head office and central service groups including Group Treasury. The Corporate segment also holds certain legacy investments, assets and businesses that are no longer core for strategic reasons and not allocated to any of the Operating Groups.

Items of income and expense within the Corporate segment include the net impact of managing liquidity for the Consolidated Entity, earnings on capital, non-trading derivative volatility, earnings from investments, central overlay on impairment, provisions or valuation of assets, unallocated head office costs and costs of central service groups, the Consolidated Entity's performance-related profit share and share-based payments expense, income tax expense and certain distributions attributable to non-controlling interests and holders of loan capital.

All transactions and transfers between segments are generally determined on an arm's length basis and are included within the relevant categories of income or expense. These transactions eliminate on aggregation/consolidation.

Below is a selection of key policies applied in determining operating segment results.

### Internal funding arrangements

Group Treasury has the responsibility for managing funding for the Consolidated Entity, and Operating Groups obtain their funding from Group Treasury. The interest rates charged by Group Treasury are determined by the currency and term of the funding. Break costs are charged to Operating Groups for the early repayment of term funding.

In certain cases, Operating Groups may source funding directly from external sources - typically where the funding is secured by the assets of the Operating Group. In such cases the Operating Group bears the funding costs directly and Group Treasury may levy additional charges where appropriate.

Deposits are a funding source for the Consolidated Entity. BFS receives a deposit premium from Group Treasury on deposits they generate. This deposit premium is included within net interest and trading income for segment reporting purposes.

### Transactions between Operating Groups

Operating Groups that enter into arrangements with other Operating Groups must do so on commercial terms or as agreed by the Consolidated Entity's Chief Executive Officer or Chief Financial Officer. There is a requirement for accounting symmetry in such transactions.

Internal transactions are recognised in each of the relevant categories of income and expense as appropriate.

### Accounting for derivatives that economically hedge interest rate risk

For businesses that predominately earn income from lending activities (CAF and BFS), derivatives that economically hedge interest rate risk are required to be carried at fair value through net trading income unless they form part of a qualifying hedge relationship. Hedge relationships are generally only recognised at a Consolidated Entity level; however for segment reporting, derivatives are accounted for on an accruals basis in the Operating Group segments and changes in fair value are recognised within the Corporate segment offset by the effect of hedge relationships at the total Consolidated Entity level.

### Central service groups

Central service groups recover their costs from Operating Groups generally on either a time and effort allocation basis or a fee for service basis. Central service groups include Corporate Operations Group (COG), Financial Management Group (FMG), Risk Management Group (RMG), Legal and Governance and Central Executive.

### Performance-related profit share and share-based payments expense

Performance-related profit share and share-based payments expense relating to the Macquarie Group Employee Retained Equity Plan (MEREP) is recognised in the Corporate segment and not allocated to Operating Groups.

## 3.1 BASIS OF PREPARATION CONTINUED

### Income tax

Income tax expense and benefits are recognised in the Corporate segment and not allocated to Operating Groups. However, to recognise an Operating Group's contribution to permanent income tax differences, an internal management revenue or charge is used. These internal management revenue/charges are offset by an equal and opposite amount recognised in the Corporate segment such that they are eliminated on aggregation.

### Presentation of segment income statements

The income statements in the following pages for each of the reported segments are in some cases summarised by grouping non-material balances together. Where appropriate, all material or key balances have been reported separately to provide users with information relevant to the understanding of the Consolidated Entity's financial performance. The financial information disclosed relates to ordinary activities.

## 3.1 BASIS OF PREPARATION CONTINUED

| | MAM $Am | CAF $Am | BFS $Am | Annuity-Style Businesses $Am |
|---|---|---|---|---|
| **Full-year ended 31 March 2018** | | | | |
| Net interest and trading income | 108 | 569 | 1,182 | **1,859** |
| Fee and commission income/(expense) | 65 | 43 | 463 | **571** |
| Net operating lease income | 3 | 929 | - | **932** |
| Share of net (losses)/profits of associates and joint ventures accounted for using the equity method | - | (3) | 3 | **-** |
| Other operating income and charges | | | | |
| Impairment charges, write-offs and provisions, net of recoveries | - | (15) | (26) | **(41)** |
| Other operating income and charges | 106 | 351 | 13 | **470** |
| Internal management revenue/(charge) | 8 | 4 | 3 | **15** |
| Net operating income | 290 | 1,878 | 1,638 | **3,806** |
| Total operating expenses | (147) | (676) | (1,081) | **(1,904)** |
| Operating profit/(loss) before income tax | 143 | 1,202 | 557 | **1,902** |
| Income tax expense | - | - | - | **-** |
| Profit/(loss) after Income Tax | 143 | 1,202 | 557 | **1,902** |
| (Profit)/loss attributable to non-controlling interests | - | (4) | - | **(4)** |
| Profit/(loss) attributable to equity holders | 143 | 1,198 | 557 | **1,898** |
| Distributions paid or provided for on MIS | - | - | - | **-** |
| **Net profit/(loss) contribution** | **143** | **1,198** | **557** | **1,898** |
| **Full-year ended 31 March 2017** | | | | |
| Net interest and trading income | 104 | 694 | 1,049 | **1,847** |
| Fee and commission income/(expense) | 65 | 58 | 469 | **592** |
| Net operating lease income | 13 | 904 | - | **917** |
| Share of net profits/(losses) of associates and joint ventures accounted for using the equity method | - | - | 6 | **6** |
| Other operating income and charges | | | | |
| Impairment charges, write-offs and provisions, net of recoveries | 1 | (111) | (91) | **(201)** |
| Other operating income and charges | (13) | 233 | 205 | **425** |
| Internal management revenue/(charge) | 1 | 40 | 5 | **46** |
| Net operating income | 171 | 1,818 | 1,643 | **3,632** |
| Total operating expenses | (117) | (631) | (1,133) | **(1,881)** |
| Operating profit/(loss) before income tax | 54 | 1,187 | 510 | **1,751** |
| Income tax expense | - | - | - | **-** |
| Profit/(loss) after Income Tax | 54 | 1,187 | 510 | **1,751** |
| Loss/(profit) attributable to non-controlling interests | - | 1 | - | **1** |
| Profit/(loss) attributable to equity holders | 54 | 1,188 | 510 | **1,752** |
| Distributions paid or provided for on MIS | - | - | - | **-** |
| **Net profit/(loss) contribution** | **54** | **1,188** | **510** | **1,752** |

| CGM $Am | Capital Markets Facing Businesses $Am | Corporate $Am | Total $Am |
|---|---|---|---|
| 1,874 | **1,874** | 166 | **3,899** |
| 390 | **390** | (71) | **890** |
| - | **-** | 5 | **937** |
| 22 | **22** | - | **22** |
| (90) | **(90)** | 62 | **(69)** |
| 45 | **45** | (31) | **484** |
| 4 | **4** | (19) | **-** |
| 2,245 | **2,245** | 112 | **6,163** |
| (1,379) | **(1,379)** | (727) | **(4,010)** |
| 866 | **866** | (615) | **2,153** |
| - | **-** | (570) | **(570)** |
| 866 | **866** | (1,185) | **1,583** |
| - | **-** | 3 | **(1)** |
| 866 | **866** | (1,182) | **1,582** |
| - | **-** | (14) | **(14)** |
| **866** | 866 | **(1,196)** | 1,568 |
| 1,982 | **1,982** | 8 | **3,837** |
| 339 | **339** | (111) | **820** |
| - | **-** | 5 | **922** |
| - | **-** | (25) | **(19)** |
| (157) | **(157)** | 22 | **(336)** |
| 148 | **148** | 24 | **597** |
| 11 | **11** | (57) | **-** |
| 2,323 | **2,323** | (134) | **5,821** |
| (1,447) | **(1,447)** | (760) | **(4,088)** |
| 876 | **876** | (894) | **1,733** |
| - | **-** | (509) | **(509)** |
| 876 | **876** | (1,403) | **1,224** |
| (1) | **(1)** | 12 | **12** |
| 875 | **875** | (1,391) | **1,236** |
| - | **-** | (15) | **(15)** |
| **875** | 875 | **(1,406)** | 1,221 |

## 3.2 MAM

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Net interest and trading income** | **48** | 60 | *(20)* | **108** | 104 | *4* |
| **Fee and commission income** | | | | | | |
| Base fees | **20** | 20 | - | **40** | 39 | *3* |
| Other fee and commission income | **2** | 23 | *(91)* | **25** | 26 | *(4)* |
| Total fee and commission income | **22** | 43 | *(49)* | **65** | 65 | - |
| **Net operating lease income** | **2** | 1 | *100* | **3** | 13 | *(77)* |
| **Other operating income and charges** | | | | | | |
| Net gains on sale and revaluation of equity and debt investments and non-financial assets | **46** | 6 | * | **52** | 15 | *247* |
| Other income/(charges) | **11** | 43 | *(74)* | **54** | (27) | * |
| Total other operating income and charges | **57** | 49 | *16* | **106** | (12) | * |
| **Internal management revenue** | **8** | - | * | **8** | 1 | * |
| **Net operating income** | **137** | 153 | *(10)* | **290** | 171 | *70* |
| **Operating expenses** | | | | | | |
| Employment expenses | **(18)** | (16) | *13* | **(34)** | (27) | *26* |
| Brokerage, commission and trading-related expenses | **(12)** | (40) | *(70)* | **(52)** | (27) | *93* |
| Other operating expenses | **(34)** | (27) | *26* | **(61)** | (63) | *(3)* |
| **Total operating expenses** | **(64)** | (83) | *(23)* | **(147)** | (117) | *26* |
| **Net profit contribution** | **73** | 70 | *4* | **143** | 54 | *165* |
| **Non-GAAP metrics** | | | | | | |
| MAM assets under management ($A billion) | **6.4** | 5.3 | *21* | **6.4** | 5.5 | *16* |
| Headcount | **125** | 123 | *2* | **125** | 124 | *1* |

Net profit contribution of $A143 million for the year ended 31 March 2018, up 165% from the prior year:

- Higher net gains on sale and revaluation of equity and debt investments primarily due to income from the sell down of infrastructure debt in MSIS
- Other operating income includes the release of accruals relating to legacy business activities as well as higher revenue for MSIS Retail
- Base fees broadly in line

Partially offset by:

- Higher brokerage, commission and trading-related expenses in MSIS Retail

## 3.2 MAM CONTINUED

### Net interest and trading income

Net interest and trading income in MAM includes income on specialised retail products and interest income from the provision of financing facilities to external funds and their investors.

Net interest and trading income of $A108 million for the year ended 31 March 2018 increased 4% from $A104 million in the prior year, primarily driven by higher interest income in the MSIS Fund Linked Product business.

### Base fees

Base fee income of $A40 million for the year ended 31 March 2018 was broadly in line with the prior year. Base fee income benefited from growth in the MSIS Infrastructure Debt business.

### Other fee and commission income

Other fee and commission income includes distribution service fees, structuring fees, capital protection fees and brokerage and commission income. Distribution service fees and brokerage and commission income are offset by associated expenses that, for accounting purposes, are recognised in brokerage, commission and trading-related expenses.

Other fee and commission income of $A25 million for the year ended 31 March 2018 was broadly in line with the prior year.

### Other operating income and charges

Net other operating income of $A106 million for the year ended 31 March 2018 significantly increased from $A12 million charge in the prior year. The current year included income from the MSIS Retail business, sell down of infrastructure debt in MSIS and the release of accruals related to legacy businesses.

### Operating expenses

Total operating expenses of $A147 million for the year ended 31 March 2018 increased 26% from $A117 million in the prior year. The current year included higher brokerage and commission expense in MSIS Retail.

## 3.3 CAF

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Net interest and trading income** | **239** | 330 | *(28)* | **569** | 694 | *(18)* |
| **Fee and commission income** | **20** | 23 | *(13)* | **43** | 58 | *(26)* |
| **Net operating lease income** | **464** | 465 | *(<1)* | **929** | 904 | *3* |
| **Share of net losses of associates and joint ventures accounted for using the equity method** | **(3)** | - | * | **(3)** | - | * |
| **Other operating income and charges** | | | | | | |
| Impairment charge on equity investments, intangibles and other non-financial assets | **(11)** | (11) | - | **(22)** | (28) | *(21)* |
| Gain on disposal of operating lease assets | **21** | 6 | *250* | **27** | 16 | *69* |
| Net gain on acquiring, disposing, reclassification and change in ownership interests of investments, subsidiaries and businesses held for sale | **122** | 66 | *85* | **188** | 142 | *32* |
| Provisions for impairment, write-offs and collective allowance for credit losses | **(5)** | 12 | * | **7** | (83) | * |
| Other income | **103** | 33 | *212* | **136** | 75 | *81* |
| Total other operating income and charges | **230** | 106 | *117* | **336** | 122 | *175* |
| **Internal management revenue** | **3** | 1 | *200* | **4** | 40 | *(90)* |
| **Net operating income** | **953** | 925 | *3* | **1,878** | 1,818 | *3* |
| **Operating expenses** | | | | | | |
| Employment expenses | **(142)** | (131) | *8* | **(273)** | (265) | *3* |
| Brokerage, commission and trading-related expenses | **(6)** | (3) | *100* | **(9)** | (9) | - |
| Other operating expenses | **(218)** | (176) | *24* | **(394)** | (357) | *10* |
| **Total operating expenses** | **(366)** | (310) | *18* | **(676)** | (631) | *7* |
| **Non-controlling interests**[1] | **(4)** | - | * | **(4)** | 1 | * |
| **Net profit contribution** | **583** | 615 | *(5)* | **1,198** | 1,188 | *1* |
| **Non-GAAP metrics** | | | | | | |
| Loan and finance lease portfolio[2] ($A billion) | **24.1** | 25.4 | *(5)* | **24.1** | 26.3 | *(8)* |
| Operating lease portfolio ($A billion) | **10.2** | 9.9 | *3* | **10.2** | 10.0 | *2* |
| Headcount | **1,306** | 1,259 | *4* | **1,306** | 1,254 | *4* |

1. "Non-controlling interests" adjusts reported consolidated profit or loss for the share that is attributable to non-controlling interests, such that the net profit contribution represents the net profit attributable to ordinary equity holders.
2. Includes equity portfolio of $A0.4 billion (FY17: $A0.4 billion)

Net profit contribution of $A1,198 million for the year ended 31 March 2018, broadly in line with the prior year:
– Increased income from prepayments, realisations and investment-related income in the Principal Finance portfolio
– Lower charges for provisions and impairments reflecting the partial reversal of collective provisions, driven by net loan repayments, and the improved credit performance of underlying portfolios
– Asset Finance contribution increased due to stronger underlying net operating lease income in Aviation and income from Vehicles which included the sale of the US commercial vehicles financing business. The remaining portfolios continued to perform well
Partially offset by:
– Lower interest income as a result of the reduction in the Principal Finance portfolio size

## 3.3 CAF CONTINUED

### Net interest and trading income

Net interest and trading income in CAF predominately relates to net income from the loan and finance lease (including vehicles and equipment financing) portfolios and the funding costs associated with the operating lease portfolios (including aviation, mining and energy assets) and Principal Finance equity investments.

Net interest and trading income of $A569 million for the year ended 31 March 2018 decreased 18% from $A694 million in the prior year, mainly as a result of the reduction in the Principal Finance portfolio.

The loan and finance lease portfolio was $A24.1 billion at 31 March 2018, a decrease of 8% from $A26.3 billion at 31 March 2017. The decrease was mainly in Principal Finance, as well as the sale of the US commercial vehicles financing business in March 2018.

### Net operating lease income

Net operating lease income of $A929 million for the year ended 31 March 2018 increased 3% from $A904 million in the prior year due to improved underlying income from the Aviation, Energy and Technology portfolios.

The operating lease portfolio was $A10.2 billion at 31 March 2018, an increase of 2% from $A10.0 billion at 31 March 2017 with growth in the Technology and Energy portfolios partially offset by depreciation and sales in the Aviation portfolio.

### Impairment charge on equity investments, intangibles and other non-financial assets

The impairment charge on equity investments, intangibles and other non-financial assets of $A22 million for the year ended 31 March 2018 predominately related to the impairment of a legacy Asset Finance business and impairments of certain Aviation assets.

### Gain on disposal of operating lease assets

The gain on disposal of operating lease assets of $A27 million for the year ended 31 March 2018 predominately related to gains recognised on the sale of five aircraft.

### Net gain on acquiring, disposing, reclassification and change in ownership interests of investments, subsidiaries and businesses held for sale

The net gain on acquiring, disposing, reclassification and change in ownership interests of investments, subsidiaries and businesses held for sale was $A188 million for the year ended 31 March 2018. Gains were generated from Principal Finance investments in Europe and the US and the sale of the US commercial vehicles financing business.

The prior year result of $A142 million primarily related to a gain realised on the sale of an interest in a toll road in the US by the Principal Finance business.

### Provisions for impairment, write-offs and collective allowance for credit losses

Provisions for impairment, write-offs and collective allowance for credit losses was a gain of $A7 million for the year ended 31 March 2018. The improvement from the $A83 million provision expense in the prior year was due to the partial reversal of collective provisions, driven by net loan repayments, and the improved credit performance of underlying portfolios.

### Other income

Other income of $A136 million for the year ended 31 March 2018 increased 81% from $A75 million in the prior year. The increase was primarily due to the sale of Principal Finance assets in the US.

### Operating expenses

Total operating expenses of $A676 million for the year ended 31 March 2018 increased 7% from $A631 million in the prior year mainly due to increased deal and project related expenses.

## 3.4 BFS

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Net interest and trading income** | **598** | 584 | *2* | **1,182** | 1,049 | *13* |
| **Fee and commission income** | | | | | | |
| Wealth management fee income | **166** | 167 | *(1)* | **333** | 310 | *7* |
| Banking fee income | **64** | 66 | *(3)* | **130** | 132 | *(2)* |
| Life insurance income | **-** | - | - | **-** | 27 | *(100)* |
| Total fee and commission income | **230** | 233 | *(1)* | **463** | 469 | *(1)* |
| **Share of net profits of associates and joint ventures accounted for using the equity method** | **3** | - | * | **3** | 6 | *(50)* |
| **Other operating income and charges** | | | | | | |
| Impairment charge on equity investments, intangibles and other non-financial assets | **(8)** | - | * | **(8)** | (53) | *(85)* |
| Net gain on acquiring, disposing, reclassification and change in ownership interests of investments, subsidiaries and businesses held for sale | **1** | 1 | - | **2** | 192 | *(99)* |
| Provisions for impairment, write-offs and collective allowance for credit losses | **(10)** | (8) | *25* | **(18)** | (38) | *(53)* |
| Other income | **6** | 5 | *20* | **11** | 13 | *(15)* |
| Total other operating income and charges | **(11)** | (2) | * | **(13)** | 114 | * |
| **Internal management revenue** | **-** | 3 | *(100)* | **3** | 5 | *(40)* |
| **Net operating income** | **820** | 818 | *<1* | **1,638** | 1,643 | *(<1)* |
| **Operating expenses** | | | | | | |
| Employment expenses | **(173)** | (158) | *9* | **(331)** | (326) | *2* |
| Brokerage, commission and trading-related expenses | **(107)** | (104) | *3* | **(211)** | (208) | *1* |
| Technology expenses[1] | **(143)** | (135) | *6* | **(278)** | (321) | *(13)* |
| Other operating expenses | **(124)** | (137) | *(9)* | **(261)** | (278) | *(6)* |
| **Total operating expenses** | **(547)** | (534) | *2* | **(1,081)** | (1,133) | *(5)* |
| **Net profit contribution** | **273** | 284 | *(4)* | **557** | 510 | *9* |
| **Non-GAAP metrics** | | | | | | |
| Funds on platform[2] ($A billion) | **82.5** | 78.9 | *5* | **82.5** | 72.2 | *14* |
| Australian loan portfolio[3] ($A billion) | **40.6** | 37.6 | *8* | **40.6** | 35.8 | *13* |
| Legacy loan portfolios[4] ($A billion) | **-** | - | - | **-** | 0.5 | *(100)* |
| BFS deposits[5] ($A billion) | **45.7** | 46.4 | *(2)* | **45.7** | 44.5 | *3* |
| Headcount | **2,321** | 2,075 | *12* | **2,321** | 1,990 | *17* |

1. Technology expenses include technology staff expenses, depreciation of technology assets, amortisation of capitalised software and maintenance costs.
2. Funds on platform includes Macquarie Wrap and Vision.
3. The Australian loan portfolio comprises residential mortgages, loans to businesses, insurance premium funding and credit cards.
4. The legacy loan portfolios primarily comprise residential mortgages in Canada and the US.
5. BFS Deposits excludes corporate/wholesale deposits.

Net profit contribution of $A557 million for the year ended 31 March 2018, up 9% from the prior year:

– Growth in Australian loan, deposit and platform average volumes
– The non-recurrence of expenses recognised in the prior year, including impairment charges predominately on certain equity positions, intangible assets and expenses in relation to the Core Banking platform

Partially offset by:

– The non-recurrence of the net overall gain on the disposal of Macquarie Life's risk insurance business to Zurich Australia Limited and the US mortgages portfolio in the prior year

## 3.4 BFS CONTINUED

### Net interest and trading income

Net interest and trading income in BFS relates to interest income earned from the loan portfolio that primarily comprises residential mortgages in Australia, loans to Australian businesses, insurance premium funding and credit cards. BFS also generates income from deposits by way of a deposit premium received from Group Treasury, which uses the deposits as a source of funding for the Consolidated Entity.

Net interest and trading income of $A1,182 million for the year ended 31 March 2018 increased 13% from $A1,049 million in the prior year primarily due to a 6% growth in average Australian loan portfolio volumes and a 7% growth in average BFS deposits. This was partially offset by a $A16 million allocation of the Australian Government Major Bank Levy that came into effect from 1 July 2017.

At 31 March 2018 the Australian loan and deposit portfolio included:

- Australian mortgage volumes of $A32.7 billion, a 14% increase from $A28.7 billion at 31 March 2017;
- business lending volumes of $A7.3 billion, a 12% increase from $A6.5 billion at 31 March 2017; and
- BFS deposits of $A45.7 billion, a 3% increase from $A44.5 billion at 31 March 2017.

The remaining legacy loan portfolios were sold during the year, down from $A0.5 billion at 31 March 2017.

### Wealth management fee income

Wealth management fee income relates to fees earned on a range of BFS' products and services including the Wrap and Vision platforms, deposits and the provision of wealth services in Australia.

Wealth management fee income of $A333 million for the year ended 31 March 2018 increased 7% from $A310 million in the prior year driven by platform commissions from higher funds on the Wrap and Vision platforms.

Funds on platform closed at $A82.5 billion at 31 March 2018, an increase of 14% from $A72.2 billion at 31 March 2017 due to the successful migration of holdings onto the Vision Platform, net inflows and positive market movements.

### Banking fee income

Banking fee income relates to fees earned on a range of BFS' products including mortgages, credit cards, business loans and deposits.

Banking fee income of $A130 million for the year ended 31 March 2018 was in line with the prior year.

### Life insurance income

Macquarie Life's risk insurance business was sold to Zurich Australia Limited in September 2016.

### Impairment charge on equity investments, intangibles and other non-financial assets

The impairment charge on equity investments, intangibles and other non-financial assets of $A8 million for the year ended 31 March 2018 decreased from $A53 million in the prior year due to higher impairment of equity investments and impairments of intangibles relating to the Core Banking platform in the prior year.

### Net Gain on acquiring, disposing, reclassification and change in ownership interests of investments, subsidiaries and businesses held for sale

The net gain on acquiring, disposing, reclassification and change in ownership interests of investments, subsidiaries and businesses held for sale of $A2 million for the year ended 31 March 2018 was down from $A192 million in the prior year, which included the sale of Macquarie Life's risk insurance business to Zurich Australia Limited, partially offset by losses on the sale of the US mortgages portfolio.

### Provisions for impairment, write-offs and collective allowance for credit losses

Provisions for impairment, write-offs and collective allowance for credit losses of $A18 million for the year ended 31 March 2018 decreased 53% from $A38 million in the prior year due to higher business lending provisions taken on a small number of loans in the prior year.

### Other income

Other income of $A11 million for the year ended 31 March 2018 decreased 15% from $A13 million in the prior year and includes dividend income from equity investments.

### Operating expenses

Total operating expenses of $A1,081 million for the year ended 31 March 2018 decreased 5% from $A1,133 million in the prior year, which was impacted by non-recurring expenses.

Employment expenses of $A331 million for the year ended 31 March 2018 were broadly in line with the prior year driven by 4% higher average headcount, partially offset by higher contractor expenses in the prior year.

Brokerage, commission and trading-related expenses of $A211 million for the year ended 31 March 2018 were broadly in line with the prior year.

Technology expenses of $A278 million for the year ended 31 March 2018 decreased 13% from $A321 million in the prior year. The decrease was mainly due to non-recurring technology expenses recognised in the prior year upon the successful completion of the Core Banking platform.

Other operating expenses of $A261 million decreased 6% from $A278 million in the prior year due to lower professional fees and non-recurring expenses recognised in the prior year.

## 3.5 CGM

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | Movement % | Mar 18 $Am | Mar 17 $Am | Movement % |
| **Net interest and trading income** | | | | | | |
| Commodities | **685** | 388 | *77* | **1,073** | 1,122 | *(4)* |
| Credit, interest rates and foreign exchange | **233** | 270 | *(14)* | **503** | 571 | *(12)* |
| Equities | **134** | 164 | *(18)* | **298** | 289 | *3* |
| Net interest and trading income | **1,052** | 822 | *28* | **1,874** | 1,982 | *(5)* |
| **Fee and commission income** | | | | | | |
| Brokerage and commissions | **146** | 142 | *3* | **288** | 274 | *5* |
| Other fee and commission income | **62** | 40 | *55* | **102** | 65 | *57* |
| Total fee and commission income | **208** | 182 | *14* | **390** | 339 | *15* |
| **Share of net profits of associates and joint ventures accounted for using the equity method** | **14** | 8 | *75* | **22** | - | * |
| **Other operating income and charges** | | | | | | |
| Net gains on sale of equity and debt investments | **17** | 12 | *42* | **29** | 120 | *(76)* |
| Impairment charge on equity investments, intangibles and other non-financial assets | **(3)** | (11) | *(73)* | **(14)** | (19) | *(26)* |
| Provisions for impairment and collective allowance for credit losses | **(31)** | (45) | *(31)* | **(76)** | (138) | *(45)* |
| Other income | **13** | 3 | * | **16** | 28 | *(43)* |
| Total other operating income and charges | **(4)** | (41) | *(90)* | **(45)** | (9) | * |
| **Internal management revenue/(charge)** | **(1)** | 5 | * | **4** | 11 | *(64)* |
| **Net operating income** | **1,269** | 976 | *30* | **2,245** | 2,323 | *(3)* |
| **Operating expenses** | | | | | | |
| Employment expenses | **(155)** | (140) | *11* | **(295)** | (295) | - |
| Brokerage, commission and trading-related expenses | **(178)** | (169) | *5* | **(347)** | (379) | *(8)* |
| Other operating expenses | **(389)** | (348) | *12* | **(737)** | (773) | *(5)* |
| **Total operating expenses** | **(722)** | (657) | *10* | **(1,379)** | (1,447) | *(5)* |
| **Non-controlling interests**[1] | **-** | - | - | **-** | (1) | *(100)* |
| **Net profit contribution** | **547** | 319 | *71* | **866** | 875 | *(1)* |
| **Non-GAAP metrics** | | | | | | |
| Headcount | **930** | 936 | *(1)* | **930** | 908 | *2* |

1. "Non-controlling interests" adjusts reported consolidated profit or loss for the share that is attributable to non-controlling interests, such that the net profit contribution represents the net profit attributable to ordinary equity holders.

Net profit contribution of $A866 million for the year ended 31 March 2018, down 1% from the prior year driven by:

- Timing of income recognition relating to tolling agreements and capacity contracts
- Sustained low volatility and tighter credit spreads impacting income from interest rate and credit products
- Reduced income from the sale of investments, mainly in energy and related sectors

Partially offset by:

- Improved results across the equities platform driven by rallying prices and increased volatility, notably in Asia
- Reduction in impairments in commodity related sectors
- Increased client demand for structured foreign exchange solutions in Asia and North America
- Significant opportunities for the North American Gas and Power business to capitalise on price dislocations across regions

## 3.5 CGM CONTINUED

### Commodities net interest and trading income

Net interest and trading income from commodity related activities is generated from the provision of hedging and risk management services and loans and working capital finance to clients across a range of commodity sectors including base and precious metals, energy and agriculture. CGM also enters into a number of tolling agreements, storage contracts and transportation agreements in order to facilitate client flow transactions as part of its commodities platform. These arrangements provide CGM with the ability to maximise opportunities where there is dislocation between the supply and demand for energy. Tolling agreements, storage contracts and transportation agreements, which are managed on a fair value basis for financial and risk management purposes, are required to be accounted for on an accruals basis for statutory reporting purposes, which may result in some volatility with timing of reported income.

Net interest and trading income from commodities of $A1,073 million for the year ended 31 March 2018 decreased 4% from $A1,122 million in the prior year. The current year included mixed results across the commodities platform. Strong results in North American Gas and Power due to an increase in volatility, customer activity and price dislocations across regions, Bulk Commodities from volatility in iron ore and Commodity Investor Products driven by continued client growth were offset by reduced client hedging activity and trading opportunities in Global Oil, a reduction in lending and financing income and a $A147 million reduction in income due to the timing of income recognition relating to tolling agreements and capacity contracts being recognised in future years.

### Credit, interest rates and foreign exchange net interest and trading income

Net interest and trading income from credit, interest rates and foreign exchange related activities is generated from the provision of trading and hedging services to a range of corporate and institutional clients globally, in addition to making secondary markets in corporate debt securities, syndicated bank loans and middle market loans and providing specialty lending.

Net interest and trading income from credit, interest rates and foreign exchange related activities of $A503 million for the year ended 31 March 2018 decreased 12% from $A571 million in the prior year. Revenues were impacted by sustained low volatility and tighter credit spreads in interest rate and credit products. This was partially offset by strong client activity in structured foreign exchange products.

### Equities net interest and trading income

Equities net interest and trading income is generated from the issue of derivative products in key locations, the provision of equity finance solutions to institutional clients and the conduct of risk management and trading activities.

Equities net interest and trading income of $A298 million for the year ended 31 March 2018 increased 3% from $A289 million in the prior year. This reflects more favourable conditions in Asia including rallying equities, some increase in volatility, and strong demand for warrants and structured client capital solutions.

### Fee and commission income

Fee and commission income of $A390 million for the year ended 31 March 2018 increased 15% from $A339 million in the prior year.

The increase in fee and commission income was driven by demand for advisory and structured products, primarily in Asia and North America.

### Net gains on sale of equity and debt investments

Net gains on sale of equity and debt investments of $A29 million for the year ended 31 March 2018 decreased 76% from $A120 million in the prior year, which included gains on the sale of a number of investments, mainly in energy and related sectors.

### Impairment charge on equity investments, intangibles and other non-financial assets

The impairment charge on equity investments, intangibles and other non-financial assets of $A14 million for the year ended 31 March 2018 decreased 26% from $A19 million in the prior year. Impairments in the current year relate to certain metals, mining, and energy positions.

### Provisions for impairment and collective allowance for credit losses

Provisions for impairment and collective allowances for credit losses of $A76 million for the year ended 31 March 2018 decreased 45% from $A138 million in the prior year with write-downs recognised on certain underperforming commodity-related loans in the prior year.

### Operating expenses

Total operating expenses of $A1,379 million for the year ended 31 March 2018 decreased 5% from $A1,447 million in the prior year.

Employment expenses of $A295 million for the year ended 31 March 2018 and the average headcount were broadly in line with the prior year.

Brokerage, commission and trading-related expenses include fees paid in relation to trading-related activities. Brokerage, commission and trading-related expenses of $A347 million for the year ended 31 March 2018 decreased 8% from $A379 million in the prior year mainly due to reduced physical metal inventory levels, partially offset by higher volumes relating to new business.

Other operating expenses of $A737 million for the year ended 31 March 2018 decreased 5% from $773 million in the prior year. This reflects the realisation of benefits from cost synergies following the merger of CFM and MSG.

## 3.6 CORPORATE

| | HALF-YEAR TO | | | FULL-YEAR TO | | |
|---|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | *Movement %* | Mar 18 $Am | Mar 17 $Am | *Movement %* |
| **Net interest and trading income** | **125** | 41 | *205* | **166** | 8 | * |
| **Fee and commission expense** | **(39)** | (32) | *22* | **(71)** | (111) | *(36)* |
| **Net operating lease income** | **2** | 3 | *(33)* | **5** | 5 | - |
| **Share of net (losses)/profits of associates and joint ventures accounted for using the equity method** | **(1)** | 1 | * | **-** | (25) | *(100)* |
| **Other operating income and charges** | | | | | | |
| Net gains/(losses) on sale and reclassification of debt and equity securities | **-** | (4) | *(100)* | **(4)** | 48 | * |
| Impairment write-back/(charge) on investments, intangibles and other non-financial assets, and provisions for impairment and collective allowance for credit losses | **67** | (5) | * | **62** | 22 | *182* |
| Other income and charges | **(14)** | (13) | *8* | **(27)** | (24) | *13* |
| Total other operating income and charges | **53** | (22) | * | **31** | 46 | *(33)* |
| **Internal management charge** | **(10)** | (9) | *11* | **(19)** | (57) | *(67)* |
| **Net operating income** | **130** | (18) | * | **112** | (134) | * |
| **Operating expenses** | | | | | | |
| Employment expenses | **(233)** | (320) | *(27)* | **(553)** | (574) | *(4)* |
| Brokerage, commission and trading-related expenses | **1** | (1) | * | **-** | (3) | *(100)* |
| Other operating expenses | **(80)** | (94) | *(15)* | **(174)** | (183) | *(5)* |
| **Total operating expenses** | **(312)** | (415) | *(25)* | **(727)** | (760) | *(4)* |
| Income tax expense | **(363)** | (207) | *75* | **(570)** | (509) | *12* |
| Macquarie Income Securities | **(7)** | (7) | - | **(14)** | (15) | *(7)* |
| Non-controlling interests[1] | **-** | 3 | *(100)* | **3** | 12 | *(75)* |
| **Net loss contribution** | **(552)** | (644) | *(14)* | **(1,196)** | (1,406) | *(15)* |
| **Non-GAAP metrics** | | | | | | |
| Headcount | **25** | 26 | *(4)* | **25** | 31 | *(19)* |

1. "Non-controlling interests" adjusts reported consolidated profit or loss for the share that is attributable to non-controlling interests, such that the net profit contribution represents the net profit attributable to ordinary equity holders.

The Corporate segment comprises head office and central service groups, including Group Treasury, certain legacy investments, assets and businesses that are no longer core for strategic reasons and costs that are not allocated to Operating Groups, including performance-related profit share and share-based payments expense, and income tax expense.

## 3.6 CORPORATE CONTINUED

### Net interest and trading income

Net interest and trading income in the Corporate segment includes the net result of managing liquidity and funding for the Consolidated Entity, earnings on capital, funding costs associated with non-core investments held centrally and accounting volatility arising from movements in underlying rates relating to economically hedged positions where designated hedge accounting is unable to be achieved for accounting purposes.

Net interest and trading income of $A166 million for the year ended 31 March 2018 increased substantially from $A8 million in the prior year primarily due to lower costs of holding long-term liquidity and the impact of accounting volatility on economically hedged positions that do not qualify for hedge accounting. In addition, higher earnings on capital was driven by increased average capital volumes and higher USD interest rates.

### Fee and commission expense

Fee and commission expense in the Corporate segment primarily comprises internal transactions between the Corporate segment and other segments within the Bank Group, and transactions between the Bank and Non-Bank Groups.

Fee and commission expense of $A71 million for the year ended 31 March 2018 decreased from $A111 million in the prior year. This was primarily due to a decrease in the recovery of costs by the central service groups from the Bank Group.

### Share of net (losses)/profits of associates and joint ventures accounted for using the equity method

Share of net profits of associates and joint ventures was nil for the year ended 31 March 2018, up from a net loss of $A25 million in the prior year. The movement reflects the reclassification of non-core assets to investments held for sale that were subsequently disposed of during the current year.

### Net gains/(losses) on sale and reclassification of debt and equity securities

Net losses on sale and reclassification of debt and equity securities were $A4 million for the year ended 31 March 2018 down from net gains of $A48 million in the prior year. The gain in the prior year resulted from the disposal of legacy assets and a number of investments held for the purposes of managing the Consolidated Entity's liquidity.

### Impairment write-back/(charge) on investments, intangibles and other non-financial assets, and provisions for impairment and collective allowance for credit losses

Impairment write-back on investments, intangibles and other non-financial assets, and provisions for impairment and collective allowance for credit losses was $A62 million for the year ended 31 March 2018, compared to $A22 million in the prior year. The current year result is primarily driven by a partial reduction of central management overlay provisions to reflect changes in credit conditions. The prior year result reflects changes in the underlying performance of central investments, which include certain legacy and other non-core assets.

### Employment expenses

Employment expenses in the Corporate segment relate to employment costs associated with the Consolidated Entity's central service groups including COG, FMG, RMG, Legal and Governance, and Central Executive, as well as performance-related profit share and share-based payments expense for the Consolidated Entity and the impact of fair value adjustments to Directors' Profit Share liabilities.

Employment expenses of $A553 million for the year ended 31 March 2018 decreased 4% from $A574 million in the prior year. This was primarily due to decreased share-based payments expense relating to retained equity awards granted in previous years.

### Other operating expenses

Other operating expenses in the Corporate segment include non-employment related operating costs of central service groups, offset by the recovery of central service groups costs (including employment-related costs) from the Operating Groups including transactions between the Bank and Non-Bank Groups.

Other operating expenses of $A174 million for the year 31 March 2018 decreased 5% from $A183 million in the prior year. This was primarily due to an increase in the recovery of costs recovered from the Bank Group.

4.1 Statement of financial position
4.2 Loan assets
4.3 Equity investments MAM

# BALANCE SHEET

4

## 4.1 STATEMENT OF FINANCIAL POSITION

| | AS AT | | | MOVEMENT | |
|---|---|---|---|---|---|
| | Mar 18 $Am | Sep 17 $Am | Mar 17 $Am | *Sep 17 %* | *Mar17 %* |
| **Assets** | | | | | |
| Receivables from financial institutions | **36,629** | 38,360 | 25,565 | *(5)* | *43* |
| Trading portfolio assets | **14,894** | 18,179 | 26,637 | *(18)* | *(44)* |
| Derivative assets | **12,695** | 12,161 | 12,067 | *4* | *5* |
| Investment securities available for sale | **5,322** | 3,909 | 5,182 | *36* | *3* |
| Other assets | **9,287** | 9,335 | 8,646 | *(1)* | *7* |
| Loan assets held at amortised cost | **80,143** | 75,833 | 75,550 | *6* | *6* |
| Other financial assets at fair value through profit or loss | **707** | 692 | 760 | *2* | *(7)* |
| Due from related body corporate entities | **1,383** | 1,075 | 1,733 | *29* | *(20)* |
| Property, plant and equipment | **11,074** | 10,673 | 10,743 | *4* | *3* |
| Interests in associates and joint ventures accounted for using the equity method | **727** | 579 | 203 | *26* | *258* |
| Intangible assets | **214** | 242 | 193 | *(12)* | *11* |
| Deferred tax assets | **143** | 179 | 162 | *(20)* | *(12)* |
| **Total assets** | **173,218** | 171,217 | 167,441 | *1* | *3* |
| **Liabilities** | | | | | |
| Trading portfolio liabilities | **7,938** | 7,209 | 4,922 | *10* | *61* |
| Derivative liabilities | **11,788** | 10,663 | 11,101 | *11* | *6* |
| Deposits | **59,379** | 58,987 | 57,682 | *1* | *3* |
| Other liabilities | **8,845** | 9,211 | 9,375 | *(4)* | *(6)* |
| Payables to financial institutions | **11,653** | 15,341 | 14,236 | *(24)* | *(18)* |
| Due to related body corporate entities | **13,993** | 5,101 | 7,367 | *174* | *90* |
| Debt issued at amortised cost | **39,685** | 45,648 | 43,137 | *(13)* | *(8)* |
| Other debt issued at fair value through profit or loss | **1,992** | 1,789 | 1,934 | *11* | *3* |
| Deferred tax liabilities | **586** | 461 | 484 | *27* | *21* |
| **Total liabilities excluding loan capital** | **155,859** | 154,410 | 150,238 | *1* | *4* |
| **Loan capital** | **4,256** | 4,246 | 4,615 | *<1* | *(8)* |
| **Total liabilities** | **160,115** | 158,656 | 154,853 | *1* | *3* |
| **Net assets** | **13,103** | 12,561 | 12,588 | *4* | *4* |
| **Equity** | | | | | |
| Contributed equity | **9,928** | 9,915 | 9,911 | *<1* | *<1* |
| Reserves | **477** | 312 | 373 | *53* | *28* |
| Retained earnings | **2,686** | 2,329 | 2,296 | *15* | *17* |
| **Total capital and reserves attributable to ordinary equity holders of Macquarie Bank Limited** | **13,091** | 12,556 | 12,580 | *4* | *4* |
| Non-controlling interests | **12** | 5 | 8 | *140* | *50* |
| **Total equity** | **13,103** | 12,561 | 12,588 | *4* | *4* |

## 4.1 STATEMENT OF FINANCIAL POSITION CONTINUED

The Consolidated Entity's statement of financial position has been impacted by changes in business activities and Treasury management initiatives during the year ended 31 March 2018.

### Assets

Total assets of $A173.2 billion at 31 March 2018 increased 3% from $A167.4 billion at 31 March 2017 mainly due to an increase in Receivables from financial institutions, Loan assets held at amortised cost, Other assets, Derivative assets and Interests in associates and joint ventures accounted for using the equity method. These increases were partially offset by a decrease in Trading portfolio assets.

- Receivables from financial institutions of $A36.6 billion at 31 March 2018 increased 43% from $A25.6 billion at 31 March 2017 mainly due to an increase in stock borrowing and reverse repurchase trades in CGM driven by short term funding opportunities and client flow
- Loan assets held at amortised cost of $A80.1 billion at 31 March 2018 increased 6% from $A75.6 billion at 31 March 2017 mainly due to net new loans written in BFS' mortgages and business lending portfolios, and an increase in CGM's lending in Fixed Income Currencies and Futures businesses. This was partially offset by a decrease of 8% in CAF's loan and finance lease portfolio to $A24.1 billion at 31 March 2018 from $A26.3 billion at 31 March 2017 primarily due to repayments in Principal Finance
- Other assets of $A9.3 billion at 31 March 2018 increased 7% from $A8.6 billion at 31 March 2017 mainly due to an increase in unsettled trade balances in CGM and Held for sale investments in CAF. The receivable following the sale of the Canadian mortgages portfolio in BFS in the prior year was partially offset by the receivable on the sale of CAF's US commercial vehicles financing business in the current year
- Derivative assets of $A12.7 billion at 31 March 2018 increased 5% from $A12.1 billion at 31 March 2017 mainly due an increase in US Gas derivatives due to the acquisition of Cargill and positive price movements on energy derivatives in CGM
- Interests in associates and joint ventures accounted for using the equity method of $A0.7 billion increased significantly from $A0.2 billion at 31 March 2017 mainly due to an additional investment by CAF, which resulted in the reclass of an investment from Available for sale to Associate
- Trading portfolio assets of $A14.9 billion at 31 March 2018 decreased 44% from $A26.6 billion at 31 March 2017 mainly due to a decrease in long equity positions and a reduction in the holdings of physical commodities and volume of oil contracts.

### Liabilities

Total liabilities of $A160.1 billion at 31 March 2018 increased 3% from $A154.9 billion at 31 March 2017 mainly driven by an increase in Due to related body corporate entities, Trading portfolio liabilities, Deposits and Derivative liabilities. These increases were partially offset by a decrease in Debt issued at amortised cost, Payables to financial institutions, Other liabilities and Loan Capital.

- Due to related body corporate entities of $A14.0 billion at 31 March 2018 increased 90% from $A7.4 billion at 31 March 2017 mainly due to new non-bank debt issuances placed by MGL and other entities with MBL
- Trading portfolio liabilities of $A7.9 billion at 31 March 2018 increased 61% from $A4.9 billion at 31 March 2017 mainly due to an increase in short equity positions
- Deposits of $A59.4 billion at 31 March 2018 increased 3% from $A57.7 billion at 31 March 2017 mainly due to an increase in transaction and savings accounts and business deposit volumes
- Derivative liabilities of $A11.8 billion increased 6% from $A11.1 billion at 31 March 2017 reflecting increased activity in CGM's Commodity business
- Debt issued at amortised cost of $A39.7 billion at 31 March 2018 decreased 8% from $A43.1 billion at 31 March 2017, mainly driven by a reduction in CAF leasing facilities and bond repayments in BFS Mortgages. This was partially offset by Treasury's funding and liquidity management activities which included US commercial paper issuance
- Payables to financial institutions of $A11.7 billion at 31 March 2018 decreased 18% from $A14.2 billion at 31 March 2017 mainly due to a net repayment of Treasury funding facilities and a decrease in cash collateral on securities lent in CGM
- Other liabilities of $A8.8 billion at 31 March 2018 decreased 6% from $A9.4 billion at 31 March 2017 mainly due a decrease in unsettled trade balances in CGM
- Loan capital of $A4.3 billion decreased 8% from $A4.6 billion mainly due to the redemption of Exchangeable Capital Securities notes during the year.

### Equity

Total equity of $A13.1 billion at 31 March 2018 increased 4% from $A12.6 billion at 31 March 2017.

The increase was mainly due to the retained earnings generated during the year ended 31 March 2018 (net of dividends paid), an increase in the Foreign currency translation reserve and Cash flow hedge reserve, partially offset by a decrease in the Available for sale reserve due to the reclassification of investments from Available for sale to Associates during the year ended 31 March 2018.

## 4.2 LOAN ASSETS

Reconciliation between the statement of financial position and the funded balance sheet:

| | AS AT | | | MOVEMENT | |
|---|---|---|---|---|---|
| | Mar 18 $Ab | Sep 17 $Ab | Mar 17 $Ab | *Sep 17 %* | *Mar17 %* |
| **Loan assets at amortised cost per the statement of financial position** | **80.1** | 75.8 | 75.6 | *6* | *6* |
| Other loans held at fair value[1] | **0.1** | 0.1 | 0.2 | - | *(50)* |
| Operating lease assets | **10.2** | 9.9 | 10.0 | *3* | *2* |
| Other reclassifications[2] | **0.8** | 1.2 | 1.1 | *(33)* | *(27)* |
| Less: loans held by consolidated SPEs which are available as security to noteholders and debt providers[3] | **(9.0)** | (11.4) | (13.4) | *(21)* | *(33)* |
| Less: segregated funds[4] | **(5.4)** | (5.2) | (4.6) | *4* | *17* |
| Less: margin balances (reclassed to trading)[5] | **(2.5)** | (1.4) | (2.7) | *79* | *(7)* |
| **Total loan assets including operating lease assets per the funded balance sheet[6]** | **74.3** | 69.0 | 66.2 | *8* | *12* |

1. Excludes other loans held at fair value that are self-funded.
2. Reclassification between loan assets and other funded balance sheet categories.
3. Excludes notes held by Macquarie Bank in consolidated Special Purpose Entities (SPE).
4. These represent the assets and liabilities that are recognised where Macquarie Bank holds segregated client monies. The client monies will be matched by assets held to the same amount and hence does not require funding.
5. For the purposes of the funded balance sheet, margin balances are treated as trading assets rather than loan assets.
6. Total loan assets including operating lease assets per the funded balance sheet includes self-securitised assets.

## 4.2 LOAN ASSETS CONTINUED

Loan assets[1] including operating lease assets by Operating Group per the funded balance sheet are shown in further detail below:

| | | AS AT | | | MOVEMENT | |
|---|---|---|---|---|---|---|
| | Notes | Mar 18 $Ab | Sep 17 $Ab | Mar 17 $Ab | *Sep 17 %* | *Mar17 %* |
| CAF | | | | | | |
| Asset Finance: | 1 | | | | | |
| Finance lease assets | | **14.7** | 13.4 | 12.0 | *10* | *23* |
| Operating lease assets | | **10.2** | 9.9 | 10.0 | *3* | *2* |
| Total Asset Finance | | **24.9** | 23.3 | 22.0 | *7* | *13* |
| Principal Finance | 2 | **4.8** | 5.7 | 6.5 | *(16)* | *(26)* |
| **Total CAF** | | **29.7** | 29.0 | 28.5 | *2* | *4* |
| BFS | | | | | | |
| Retail Mortgages: | 3 | | | | | |
| Australia[2] | | **28.7** | 25.4 | 23.0 | *13* | *25* |
| Canada, US and Other | | **-** | - | 0.5 | - | *(100)* |
| Total Retail Mortgages | | **28.7** | 25.4 | 23.5 | *13* | *22* |
| Business banking[2] | 4 | **7.9** | 7.7 | 7.1 | *3* | *11* |
| **Total BFS** | | **36.6** | 33.1 | 30.6 | *11* | *20* |
| CGM | | | | | | |
| Resources and commodities | 5 | **3.1** | 2.6 | 2.5 | *19* | *24* |
| Other | 6 | **2.3** | 2.1 | 2.6 | *10* | *(12)* |
| **Total CGM** | | **5.4** | 4.7 | 5.1 | *15* | *6* |
| MAM | | | | | | |
| Structured investments | 7 | **2.6** | 2.2 | 2.0 | *18* | *30* |
| **Total** | | **74.3** | 69.0 | 66.2 | *8* | *12* |

1. Total loan assets including operating lease assets per the funded balance sheet includes self-securitised assets.
2. Securitised business banking portfolio with underlying residential mortgages was included in Retail Mortgages: Australia has been reclassed to business banking and restated accordingly in March 2017.

## 4.2 LOAN ASSETS CONTINUED

### Explanatory notes concerning asset security of funded loan asset portfolio

#### 1. Asset Finance

Secured by underlying financed assets.

#### 2. Principal Finance

Diversified corporate and real estate lending portfolio, predominately consisting of loans which are senior, secured, well covenanted and with a hold to maturity horizon.

#### 3. Retail Mortgages

Secured by residential property.

#### 4. Business banking

Secured relationship managed loan portfolio to professional and financial services firms, real estate industry clients, insurance premium funding, mortgages to business banking clients and other small business clients. Secured largely by real estate, working capital, business cash flows and credit insurance. The portfolio also includes other retail lending including credit cards.

#### 5. Resources and commodities

Diversified loan portfolio primarily to the resources sector that are secured by the underlying assets.

#### 6. CGM Other

Predominately relates to recourse loans to financial institutions, as well as financing for real estate and other sectors.

#### 7. Structured investments

Loans to retail and wholesale counterparties that are secured against equities, investment funds or cash, or are protected by capital guarantees at maturity.

## 4.3 EQUITY INVESTMENTS

Equity investments are reported in the following categories in the statement of financial position:

- other financial assets at fair value through profit or loss;
- investment securities available for sale; and
- interests in associates and joint ventures accounted for using the equity method.

### Equity investments reconciliation

| | AS AT | | | MOVEMENT | |
|---|---|---|---|---|---|
| | Mar 18 $Ab | Sep 17 $Ab | Mar 17 $Ab | *Sep 17 %* | *Mar17 %* |
| **Equity investments** | | | | | |
| **Statement of financial position** | | | | | |
| Equity investments within other financial assets at fair value through profit or loss | **0.3** | 0.3 | 0.4 | - | *(25)* |
| Equity investments within investment securities available for sale | **0.1** | 0.2 | 0.6 | *(50)* | *(83)* |
| Interests in associates and joint ventures accounted for using the equity method | **0.7** | 0.6 | 0.2 | *17* | *250* |
| **Total equity investments per statement of financial position** | **1.1** | 1.1 | 1.2 | - | *(8)* |
| **Adjustment for funded balance sheet** | | | | | |
| Equity hedge positions[1] | **(0.3)** | (0.3) | (0.4) | - | *(25)* |
| **Total funded equity investments** | **0.8** | 0.8 | 0.8 | - | - |
| **Adjustments for equity investments analysis** | | | | | |
| Available for sale and associates' reserves[2] | **-** | (0.1) | (0.1) | *(100)* | *(100)* |
| **Total adjusted equity investments[3]** | **0.8** | 0.7 | 0.7 | *14* | *14* |

1. These relate to assets held for the purposes of economically hedging Macquarie Bank's fair valued liabilities to external parties arising from various equity linked instruments. Consequently, these have been excluded from the analysis of equity investment exposures.
2. Available for sale reserve on equity investments (gross of tax) that will be released to income upon realisation of the investment, excluding investments in which Macquarie Bank has no economic exposure; Associates' reserves (gross of tax) that will be released to income upon realisation of the investment.
3. The adjusted book value represents the total net exposure to Macquarie Bank.

5.1 Liquidity Risk Governance and Management Framework
5.2 Management of Liquidity Risk
5.3 Funded balance sheet
5.4 Funding profile
5.5 Explanatory notes concerning funding sources and funded assets

# FUNDING AND LIQUIDITY

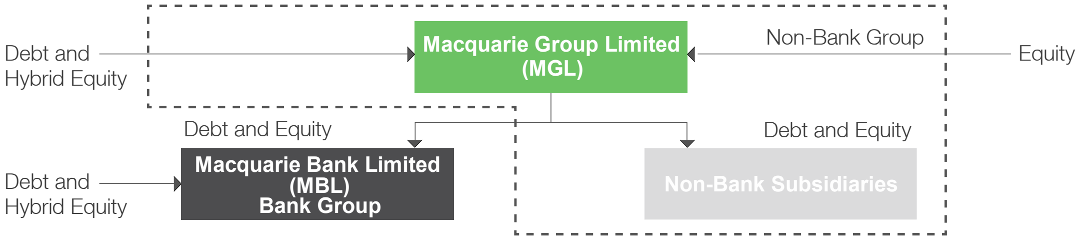
5

## 5.1 LIQUIDITY RISK GOVERNANCE AND MANAGEMENT FRAMEWORK

### Governance and oversight

Macquarie Group's two primary external funding vehicles are Macquarie Group Limited (MGL) and Macquarie Bank Limited (MBL). MGL provides funding principally to the Non-Bank Group and limited funding to some MBL subsidiaries. MBL provides funding to the Bank Group.

The high level funding structure of the Group is shown below:




Macquarie Group's liquidity risk management framework is designed to ensure that it is able to meet its funding requirements as they fall due under a range of market conditions.

Liquidity management is performed centrally by Group Treasury, with oversight from the Asset and Liability Committee (ALCO) and the Risk Management Group (RMG). Macquarie Group's liquidity policy is approved by the MGL and MBL Boards after endorsement by the ALCO and liquidity reporting is provided to the Boards on a monthly basis. The ALCO includes the MGL Chief Executive Officer, MBL Chief Executive Officer, Chief Financial Officer, Chief Risk Officer, Group Treasurer, Head of Balance Sheet Management and Operating Group Heads.

RMG provides independent oversight of liquidity risk management, including ownership of liquidity policies and key limits and approval of material liquidity scenario assumptions.

### Liquidity policy and risk appetite

The MGL and MBL liquidity policy is designed so that each of the Macquarie Group, the Bank Group and the Non-Bank Group maintains sufficient liquidity to meet its obligations as they fall due. In some cases, certain entities within Macquarie Group may also be required to have a standalone liquidity policy. In these cases, the principles applied within the entity-specific liquidity policies are consistent with those applied in the broader MGL and MBL policy.

Macquarie Group establishes a liquidity risk appetite for both MGL and MBL, which is defined within the liquidity policy. The risk appetite is approved by the MGL and MBL Boards and represents an articulation of the nature and level of liquidity risk that is acceptable in the context of achieving Macquarie Group's strategic objectives.

Macquarie Group's liquidity risk appetite is set to ensure that Macquarie Group is able to meet all of its liquidity obligations during a period of liquidity stress: a twelve month period, with constrained access to funding markets for MBL, no access to funding markets for MGL and with only a limited reduction in Macquarie Group's franchise businesses.

MBL is an Authorised Deposit-taking Institution (ADI) and is funded mainly with capital, long-term liabilities and deposits.

## 5.1 LIQUIDITY RISK GOVERNANCE AND MANAGEMENT FRAMEWORK CONTINUED

### Liquidity risk tolerance and principles

Macquarie Group's liquidity risk appetite is supported by a number of risk tolerances and principles applied to managing liquidity risk in both MGL and MBL.

#### Risk tolerances

- term assets must be funded by term liabilities and short term assets must exceed short term wholesale liabilities;
- cash and liquid assets must be sufficient to cover the expected outflow under a twelve month stress scenario and meet minimum regulatory requirements;
- cash and liquid assets held to cover stress scenarios and regulatory minimums must be high quality unencumbered liquid assets and cash;
- diversity and stability of funding sources is a key priority;
- balance sheet currency mismatches are managed within set tolerances; and
- funding and liquidity exposures between entities within Macquarie Group are subject to constraints where required.

#### Liquidity management principles

- Macquarie Group has a centralised approach to liquidity management;
- liquidity risk is managed through stress scenario analysis and setting limits on the composition and maturity of assets and liabilities;
- a regional liquidity framework is maintained that outlines Macquarie Group's approach to managing funding and liquidity requirements in offshore subsidiaries and branches;
- the liquidity position is managed to ensure all obligations can be met as required on an intraday basis;
- a liquidity contingency plan is maintained that provides an action plan in the event of a liquidity 'crisis';
- a funding strategy is prepared annually and monitored on a regular basis;
- internal pricing allocates liquidity costs, benefits and risks to areas responsible for generating them;
- strong relationships are maintained to assist with managing confidence and liquidity; and
- the MGL and MBL Boards and Senior Management receive regular reporting on Macquarie Group's liquidity position, including compliance with liquidity policy and regulatory requirements.

### Liquidity contingency plan

Group Treasury maintains a liquidity contingency plan, which outlines how a liquidity crisis would be managed. The plan defines roles and responsibilities and actions to be taken in a liquidity event, including identifying key information requirements and appropriate communication plans with both internal and external parties.

Specifically, the plan details factors that may constitute a crisis, the officer responsible for enacting the contingency management, a committee of senior executives responsible for managing a crisis, the information required to effectively manage a crisis, a communications strategy, a high level checklist of possible actions to conserve or raise additional liquidity and contact lists to facilitate prompt communication with all key internal and external stakeholders. The plan also incorporates a retail run management plan (RRMP) that outlines the Bank's processes and operational plans for managing a significant increase in customer withdrawals during a potential deposit 'run' on Macquarie Group.

In addition, Macquarie Group monitors a range of early warning indicators on a daily basis that might assist in identifying emerging risks in Macquarie Group's liquidity position. These indicators are reviewed by Senior Management and are used to inform any decisions regarding invoking the plan.

The liquidity contingency plan is subject to regular review by both Group Treasury and RMG. It is submitted to the ALCO and MGL and MBL Boards for approval.

Macquarie Group is a global financial institution, with branches and subsidiaries in a variety of countries. Regulations in certain countries may require some branches or subsidiaries to have specific local contingency plans. Where that is the case, the liquidity contingency plan contains a supplement providing the specific information required for those branches or subsidiaries.

### Funding strategy

Macquarie Group prepares a funding strategy on an annual basis and monitors progress against the strategy throughout the year. The funding strategy aims to maintain Macquarie Group's diversity of current and projected funding sources, ensure ongoing compliance with all liquidity policy requirements and facilitate forecast asset growth. The funding strategy is reviewed by the ALCO and approved by the respective Boards.

## 5.2 MANAGEMENT OF LIQUIDITY RISK

### Scenario analysis

Scenario analysis is central to Macquarie Group's liquidity risk management framework. In addition to regulatory defined scenarios, Group Treasury models a number of additional liquidity scenarios covering both market-wide and Macquarie Group specific crises. Scenario analysis performs a range of functions within the liquidity risk management framework, including:

– monitoring compliance with internal liquidity risk appetite statements by ensuring all repayment obligations can be met in the corresponding scenarios;
– determining Macquarie Group's minimum level of cash and liquid assets;
– determining the appropriate minimum tenor of funding for Macquarie Group's assets; and
– determining the overall capacity for future asset growth.

The scenarios separately consider the requirements of the Bank Group, the Non-Bank Group and Macquarie Group. They are run over a number of timeframes and a range of conservative assumptions are used regarding the level of access to capital markets, deposit outflows, contingent funding requirements and asset sales.

As an example, one internal scenario projects the expected cash and liquid asset position during a combined market-wide and Macquarie Group name-specific crisis over a twelve month time frame. This scenario assumes no access to new funding sources, a significant loss of customer deposits and contingent funding outflows resulting from undrawn commitments, market moves impacting derivatives and other margined positions combined with a multiple notch credit rating downgrade. Macquarie Group's cash and liquid asset portfolio must exceed the minimum requirement as calculated in this scenario at all times.

### Liquid asset holdings

Group Treasury centrally maintains a portfolio of highly liquid unencumbered assets in the Consolidated Group to ensure adequate liquidity is available in all funding environments, including worst case wholesale and retail market conditions. The minimum level of cash and liquid assets is calculated with reference to internal scenario projections and regulatory requirements.

The cash and liquid asset portfolio contains only unencumbered assets that can be relied on to maintain their liquidity in a crisis scenario. Specifically, cash and liquid assets held to meet minimum internal and regulatory requirements must be held in cash, qualifying High Quality Liquid Assets (HQLA) or be an asset type that is eligible as collateral in the Reserve Bank of Australia's (RBA) Committed Liquidity Facility (CLF) – so called 'Alternative Liquid Assets' (ALA). Composition constraints are also applied to ensure appropriate diversity and quality of the assets in the portfolio.

The cash and liquid asset portfolio is held in a range of currencies to ensure Macquarie Group's liquidity requirements are broadly matched by currency. Certain other business units also hold cash and liquid assets as part of their operations. The Bank Group had $A23.6 billion cash and liquid assets as at 31 March 2018 (31 March 2017: $A20.0 billion).

### Funds transfer pricing

An internal funds transfer pricing framework is in place that has been designed to produce appropriate incentives for business decision-making by reflecting the true funding costs arising from business actions. Under this framework, each business is allocated the full cost of the funding required to support its products and business lines, recognising the actual and contingent funding-related exposures their activities create for Macquarie Group as a whole. Businesses that raise funding are compensated at a level that is appropriate for the liquidity benefit provided by the funding.

## 5.2 MANAGEMENT OF LIQUIDITY RISK CONTINUED

### Credit ratings[1] at 31 March 2018 are detailed below.

| | Macquarie Bank Limited | | |
|---|---|---|---|
| | Short term rating | Long term rating | Outlook |
| Moody's Investors Service | P-1 | A2 | Stable |
| Standard and Poor's[2] | A-1 | A | Negative |
| Fitch Ratings | F-1 | A | Stable |

1. A security rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by an assigning rating agency and any rating should be evaluated independently of any other information.
2. Standard and Poor's does not place outlook statements on short-term ratings.

### Regulatory developments

The Australian Prudential Regulation Authority's (APRA) liquidity standard (APS210) details the local implementation of the Basel III liquidity framework for Australian banks. In addition to a range of qualitative requirements, the standard incorporates the Liquidity Coverage Ratio (LCR), and as of 1 January 2018, the Net Stable Funding Ratio (NSFR). The LCR and NSFR apply specifically to Macquarie Bank as the regulated ADI in Macquarie Group.

#### Liquidity coverage ratio

The LCR requires sufficient levels of unencumbered HQLA to be held to meet expected net cash outflows under a combined 'idiosyncratic' and market-wide stress scenario lasting 30 calendar days. In Australia, HQLA includes cash, balances held with the RBA, Commonwealth Government and semi-government securities, as well as any CLF allocation. The LCR determines Macquarie Bank's regulatory minimum required level of liquid assets.

Macquarie Bank's 3-month average LCR to 31 March 2018 was 162% (average based on daily observations). For a detailed breakdown of Macquarie Bank's LCR, please refer to Macquarie Group's regulatory disclosures (available on Macquarie Group's website).

#### Net stable funding ratio

NSFR is a 12-month structural funding metric, requiring that 'available stable funding' be sufficient to cover 'required stable funding', where 'stable' funding has an actual or assumed maturity of greater than twelve months. The NSFR became a regulatory requirement on 1 January, 2018. Macquarie Bank's NSFR at 31 March 2018 was 112%.

## 5.3 FUNDED BALANCE SHEET

The Bank Group's statement of financial position is prepared based on Australian Accounting Standards and includes certain accounting gross-ups and non-recourse self-funded assets that do not represent a funding requirement of the Bank Group.

The table below reconciles the reported assets of the Bank Group to the net funded assets as at 31 March 2018.

| | Notes | AS AT Mar 18 $Ab | AS AT Mar 17 $Ab |
|---|---|---|---|
| Total assets per the Bank Group's statement of financial position | | **173.2** | 167.4 |
| Accounting deductions: | | | |
| Self-funded trading assets | 1 | **(16.6)** | (14.4) |
| Derivative revaluation accounting gross-ups | 2 | **(11.7)** | (10.6) |
| Segregated funds | 3 | **(9.8)** | (9.6) |
| Outstanding trade settlement balances | 4 | **(2.9)** | (3.4) |
| Short-term working capital assets | 5 | **(4.5)** | (4.0) |
| Intercompany gross-ups | | **(14.0)** | (7.3) |
| Non-recourse funded assets: | | | |
| Securitised assets and other non-recourse funding | 6 | **(9.0)** | (13.5) |
| **Net funded assets** | | **104.7** | 104.6 |

### Explanatory notes concerning net funded assets

#### 1. Self-funded trading assets

The Bank Group enters into stock borrowing and lending as well as repurchase agreements and reverse repurchase agreements in the normal course of trading activity that it conducts with its clients and counterparties. Also as part of its trading activities, the Bank Group pays and receives margin collateral on its outstanding derivative positions. These trading related asset and liability positions are presented gross on the statement of financial position but are viewed as being self-funded to the extent that they offset one another and, therefore, are netted as part of this adjustment.

#### 2. Derivative revaluation accounting gross-ups

The Bank Group's derivative activities are mostly client driven with client positions hedged by offsetting positions with a variety of counterparties. The derivatives are largely matched and this adjustment reflects that the matched positions do not require funding.

#### 3. Segregated funds

These represent the assets and liabilities that are recognised where the Bank Group provides products such as investment-linked policy contracts or where the Bank Group holds segregated client monies. The policy (contract) liability and client monies will be matched by assets held to the same amount and hence do not require funding.

#### 4. Outstanding trade settlement balances

At any particular time the Bank Group will have outstanding trades to be settled as part of its brokering business and trading activities. These amounts (payables) can be offset in terms of funding by amounts that the Bank Group is owed on other trades (receivables).

#### 5. Short-term working capital assets

As with the outstanding trade settlement balances above, the Bank Group through its day-to-day operations generates working capital assets (e.g. receivables and prepayments) and working capital liabilities (e.g. creditors and accruals) that produce a 'net balance' that either requires or provides funding.

#### 6. Securitised assets and other non-recourse funding

These represent assets that are funded by third parties with no recourse to the Bank Group including lending assets (mortgages and leasing) sold down into external securitisation entities.

## 5.4 FUNDING PROFILE

### Funded balance sheet

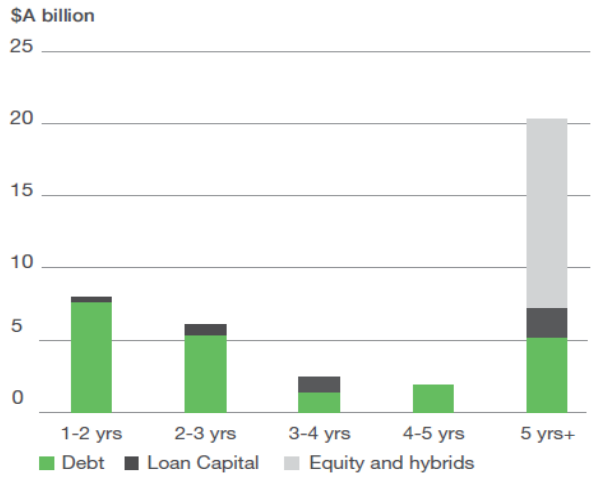
| | Notes | AS AT Mar 18 $Ab | AS AT Mar 17 $Ab |
|---|---|---|---|
| **Funding sources** | | | |
| Wholesale issued paper: | 1 | | |
| Certificates of deposit | | **0.6** | 0.9 |
| Commercial paper | | **8.4** | 5.7 |
| Net trade creditors | 2 | **1.1** | 1.6 |
| Structured notes | 3 | **2.1** | 2.6 |
| Secured funding | 4 | **4.4** | 4.4 |
| Bonds | 5 | **20.7** | 21.7 |
| Other loans | 6 | **1.1** | 0.3 |
| Syndicated loan facilities | 7 | **0.8** | 2.4 |
| Customer deposits | 8 | **48.1** | 47.8 |
| Loan capital | 9 | **4.3** | 4.6 |
| Equity and hybrids | 10 | **13.1** | 12.6 |
| **Total** | | **104.7** | 104.6 |
| **Funded assets** | | | |
| Cash and liquid assets | 11 | **23.6** | 20.0 |
| Self-securitisation | 12 | **15.5** | 16.5 |
| Net trading assets | 13 | **17.1** | 21.8 |
| Loan assets including operating lease assets less than one year | 14 | **14.1** | 13.6 |
| Loan assets including operating lease assets greater than one year | 14 | **44.7** | 36.1 |
| Debt investment securities | 15 | **1.3** | 1.9 |
| Non-Bank Group deposit with MBL | | **(12.9)** | (6.7) |
| Co-investment in Macquarie-managed funds and other equity investments | 16 | **0.8** | 0.8 |
| Property, plant and equipment and intangibles | | **0.5** | 0.6 |
| **Total** | | **104.7** | 104.6 |

See Section 5.5 for notes 1–16.

## 5.4 FUNDING PROFILE CONTINUED

### Term funding profile

### Detail of drawn term funding maturing beyond one year




| | AS AT MAR 18 | | | | | |
|---|---|---|---|---|---|---|
| | 1-2yrs $Ab | 2-3yrs $Ab | 3-4yrs $Ab | 4-5yrs $Ab | 5yrs+ $Ab | Total $Ab |
| Structured notes [1] | - | - | 0.1 | 0.1 | 1.6 | **1.8** |
| Secured funding | 0.3 | 1.1 | 0.2 | 1.2 | 0.2 | **3.0** |
| Bonds | 7.2 | 3.4 | 1.0 | 0.6 | 3.2 | **15.4** |
| Other Loans | 0.1 | - | - | - | - | **0.1** |
| Syndicated loan facilities | - | 0.8 | - | - | - | **0.8** |
| **Total debt** | **7.6** | **5.3** | **1.3** | **1.9** | **5.0** | **21.1** |
| Loan capital [2] | 0.4 | 0.8 | 1.1 | - | 2.0 | **4.3** |
| Equity and hybrids | - | - | - | - | 13.1 | **13.1** |
| **Total funding sources drawn** | **8.0** | **6.1** | **2.4** | **1.9** | **20.1** | **38.5** |
| Undrawn | - | - | - | - | - | **-** |
| **Total funding sources drawn and undrawn** | **8.0** | **6.1** | **2.4** | **1.9** | **20.1** | **38.5** |

1. Structured notes are profiled using a behavioural maturity profile.
2. Included in this balance are securities with conditional repayment obligations. These securities are disclosed using the earlier repricing dates instead of contractual maturity.

The Bank Group has diversity of funding by both source and maturity. The weighted average term to maturity of term funding maturing beyond one year (excluding equity which is a permanent source of funding) was 3.9 years at 31 March 2018.

As at 31 March 2018, customer deposits represented $A48.1 billion, or 46% of the Bank Group's total funding, short-term (maturing in less than 12 months) wholesale issued paper represented $A9.0 billion, or 9% of total funding, and other debt funding maturing within 12 months represented $A9.1 billion, or 9% of total funding.

## 5.4 FUNDING PROFILE CONTINUED

### Term funding initiatives

The Bank Group has a liability driven approach to balance sheet management, where funding is raised prior to assets being taken on to the balance sheet. Since 1 April 2017, the Bank Group has continued to raise term wholesale funding across various products and currencies.

Details of term funding raised between 1 April 2017 and 31 March 2018:

| | | Bank Group $Ab |
|---|---|---|
| Secured Funding | – Term securitisation | 2.2 |
| Issued paper | – Senior | 3.1 |
| Macquarie Air Finance Term Loan[1] | – Unsecured and secured term loan | 5.1 |
| **Total** | | **10.4** |

The Bank Group has continued to develop its major funding markets and products during the year ended 31 March 2018.

From 1 April 2017 to 31 March 2018, the Bank Group raised $A10.4 billion of term funding including:

- $A2.2 billion of term secured finance comprising of $A1.2 billion of SMART auto and equipment ABS and $A1.0 billion of PUMA RMBS.
- $A3.1 billion of term wholesale issued paper comprising of $A3.1 billion in private placements and structured notes.
- $A5.1 billion of Macquarie Air Finance Term Loan comprising of a $A3.8 billion secured term loan and $A1.3 billion unsecured term loan[1].

1. The Macquarie Air Finance Term Loan is a refinance and upsize of the current outstanding AWAS Term Loan. Commitment letters for the Macquarie Air Finance Term Loan were signed prior to 31 March 2018.

## 5.4 FUNDING PROFILE CONTINUED

The key tools used for accessing wholesale debt funding markets for MBL, which primarily funds the Bank Group are as follows:

- $US25 billion Regulation S Debt Instrument Program, including Euro Commercial Paper, Euro Certificate of Deposit, Euro-Medium Term Notes, senior and subordinated fixed/floating rate notes, and Transferable Deposits. The Debt Instrument Program had $US9.3 billion debt securities outstanding at 31 March 2018;
- $US15 billion Commercial Paper Program under which $US6.4 billion of debt securities were outstanding at 31 March 2018;
- $US20 billion US Rule 144A/Regulation S Medium Term Note Program under which $US9.0 billion of issuances were outstanding at 31 March 2018;
- $US5 billion Structured Note Program under which $US1.6 billion of funding from structured notes was outstanding at 31 March 2018;
- £0.4 billion Sterling Facility under which £0.4 billion was outstanding at 31 March 2018;
- $A5 billion Covered Bond Programme under which $A0.8 billion of debt securities were outstanding at 31 March 2018; and
- $US1.5 billion AWAS term loan under which $US1.5 billion of secured funding was outstanding at 31 March 2018[1].

Macquarie Bank accesses the Australian capital markets through the issuance of Negotiable Certificates of Deposit. At 31 March 2018, Macquarie Bank had $A0.6 billion of these securities outstanding.

At 31 March 2018, Macquarie Bank had internally securitised $A15.5 billion of its own mortgages.

Macquarie Bank, as an ADI, has access to liquidity from the RBA daily market operations.

### Deposit strategy

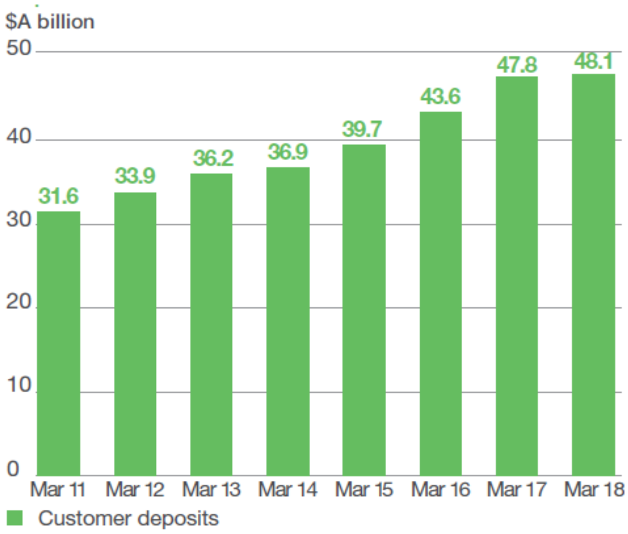
MBL continues to pursue a deposit strategy that is consistent with the core liquidity management tolerance of achieving diversity and stability of funding sources. The strategy is focused on growing the BFS deposit base, which represents a stable and reliable source of funding and reduces Macquarie Group's reliance on wholesale funding markets.

In particular, MBL has focused on the quality and composition of the deposit base, targeting transactional and relationship based deposits.

The majority of MBL's deposits continue to be covered by the Financial Claims Scheme. The value cap on the deposits is set at $A250,000 per account holder.

The chart below illustrates the customer deposit growth since 31 March 2011.

### Deposit trend




1. The Macquarie Air Finance Term Loan is a refinance and upsize of the current outstanding AWAS Term Loan. Commitment letters for the Macquarie Air Finance Term Loan were signed prior to 31 March 2018.

## 5.5 EXPLANATORY NOTES CONCERNING FUNDING SOURCES AND FUNDED ASSETS

### 1. Wholesale issued paper

Unsecured short-term wholesale funding comprised of both Certificates of Deposit and Commercial Paper.

### 2. Net trade creditors

Short-term working capital balances (debtors and creditors) are created through the Bank Group's day-to-day operations. A net funding use (or source) will result due to timing differences in cash flows.

### 3. Structured notes

Includes debt instruments on which the return is linked to a number of variables including interest rates, currencies, equities and credit. They are generally issued as part of structured transactions with clients and are hedged with positions in underlying assets or derivative instruments.

### 4. Secured funding

Certain funding arrangements secured against an asset (or pool of assets).

### 5. Bonds

Unsecured long-term wholesale funding.

### 6. Other loans

Unsecured loans provided by financial institutions and other counterparties.

### 7. Syndicated loan facilities

Loan facilities provided by a syndicate of wholesale lenders.

### 8. Customer deposits

Unsecured funding from BFS, corporate and wholesale depositors. The Australian Government Financial Claims Scheme covers eligible deposits in Macquarie Bank.

### 9. Loan capital

Long term subordinated debt, Macquarie Additional Capital Securities, Bank Capital Notes, and Exchangeable Capital Securities.

### 10. Equity and hybrids

Equity balances are comprised of issued capital, retained earnings and reserves. Hybrid instruments include MIS.

### 11. Cash and liquid assets

Cash and liquid assets generally consist of amounts due from banks and liquid debt investment securities available for sale. Liquid assets are almost entirely repo eligible with central banks or are very short dated.

### 12. Self-securitisation

This represents Australian mortgages which have been internally securitised and is a form of collateral on the RBA's list of eligible securities for repurchase agreements.

### 13. Net trading assets

The net trading asset balance consists of financial markets and equity trading assets including the net derivative position and any margin or collateral balances. It also includes trading assets which are hedging structured notes issued.

### 14. Loan assets including operating lease assets

This represents loans provided to retail and wholesale borrowers, as well as assets held under operating leases.

See section 4.2 for further information.

### 15. Debt investment securities

These include various categories of debt securities including asset backed securities, bonds, commercial mortgage backed securities and residential mortgage backed securities.

### 16. Co-investment in Macquarie-managed funds and other equity investments

These equity securities include co-investments in Macquarie-managed funds.

6.1 Overview
6.2 Bank Group capital

# 6 CAPITAL

## 6.1 OVERVIEW

As an Australian Prudential Regulation Authority (APRA) authorised and regulated Non-Operating Holding Company, MGL is required to hold adequate regulatory capital to cover the risks for Macquarie Group, including the Non-Bank Group. MGL and APRA have agreed a capital adequacy framework for Macquarie Group, based on APRA's capital standards for ADIs and Macquarie Group's Board-approved Economic Capital Adequacy Model (ECAM).

Macquarie Group's capital adequacy framework requires it to maintain minimum regulatory capital requirements calculated as the sum of:

- The Bank Group's minimum Tier 1 capital requirement, based on a percentage of risk-weighted assets plus Tier 1 deductions using prevailing APRA ADI Prudential Standards; and
- The Non-Bank Group's capital requirement, calculated using Macquarie Group's ECAM. Transactions internal to Macquarie Group are eliminated.

Eligible regulatory capital of Macquarie Group consists of ordinary share capital, retained earnings and certain reserves plus eligible hybrid instruments. Eligible hybrid instruments as at 31 March 2018 include the Macquarie Income Securities (MIS), Macquarie Bank Capital Notes (BCN), Macquarie Additional Capital Securities (MACS), Macquarie Group Capital Notes (MCN) and Macquarie Group Capital Notes 2 (MCN2).

Macquarie Group has announced that it intends to redeem MCN in June 2018. An offer of Macquarie Group Capital Notes 3 (MCN3) hybrid securities, including a rollover offer for MCN holders and a security holder offer will be launched subsequent to 31 March 2018.

Capital disclosures in this section include Harmonised Basel III[1] and APRA Basel III[2]. The former is relevant for comparison with banks regulated by regulators other than APRA, whereas the latter reflects Macquarie Group's regulatory requirements under APRA Basel III rules.

### Pillar 3

The APRA ADI Prudential Standard APS 330 Capital Adequacy: Public Disclosure of Prudential Information (Pillar 3) details the market disclosure requirements for Australian domiciled banks. APS 330 requires qualitative and quantitative disclosure of risk management practices and capital adequacy. Pillar 3 documents are available on Macquarie Group's website.

1. Harmonised Basel III relates to the Basel III guidelines defined by the Basel Committee on Banking Supervision, documented in the following: 'Basel III: a global regulatory framework for more resilient banks and banking systems', published December 2010 (revised June 2011) by the Bank for International Settlements (BIS).
2. APRA Basel III relates to the ADI Prudential Standards released by APRA for the period effective from 1 January 2013.

## 6.2 BANK GROUP CAPITAL

The Bank Group is accredited by APRA under the Basel Foundation Internal Ratings Based approach (FIRB) for credit risk, the Advanced Measurement Approach (AMA) for operational risk, the internal model approach for market risk and the internal model approach for interest rate risk in the banking book (IRRBB).

These advanced approaches place a higher reliance on a bank's internal capital measures and therefore require a more sophisticated level of risk management and risk measurement practices.

### Common Equity Tier 1 capital

The Bank Group's Common Equity Tier 1 capital under Basel III consists of ordinary share capital, retained earnings and certain reserves.

### Tier 1 capital

Tier 1 capital consists of Common Equity Tier 1 capital and Additional Tier 1 capital (hybrids). Additional Tier 1 capital as at 31 March 2018 consists of MIS, BCN and MACS. MBL periodically pays dividends to MGL and is recapitalised by MGL as required to support projected business growth.

MIS are a perpetual instrument with no conversion rights. MIS were listed for trading on the Australian Stock Exchange (now known as the Australian Securities Exchange) in 1999. MIS distributions are paid quarterly at a floating rate of BBSW plus 1.7% per annum and payment is subject to certain conditions including profitability of the Bank. MIS are eligible for transitional arrangements under Basel III rules.

BCN were issued by MBL in October 2014 and are quoted on the Australian Securities Exchange. The BCN pay discretionary, semi-annual floating rate cash distributions equal to six month BBSW plus 3.30% per annum margin, adjusted for franking credits. These instruments are non-cumulative and unsecured and may be redeemed at face value on 24 March 2020, 24 September 2020 and 24 March 2021 (subject to certain conditions being satisfied) or earlier in specified circumstances. The BCN can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 24 March 2023; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL or MBL); or where APRA determines MBL would be non-viable without an exchange or a public sector injection of capital (or equivalent support). APRA has confirmed that BCN are eligible for inclusion as Additional Tier 1 capital.

MACS were issued by MBL, acting through its London Branch in March 2017. MACS are subordinated, unsecured notes that pay discretionary, non-cumulative, semi-annual fixed rate cash distributions. Subject to certain conditions the MACS may be redeemed on 8 March 2027, or every 5th anniversary thereafter. MACS can be exchanged for a variable number of fully paid MGL ordinary shares on an acquisition event (where a person acquires control of MBL or MGL), where MBL's common equity Tier 1 capital ratio falls below 5.125%, or where APRA determines MBL would be non-viable without an exchange or a public sector injection of capital (or equivalent support). APRA has confirmed that MACS are eligible for inclusion as Additional Tier 1 capital.

## 6.2 BANK GROUP CAPITAL CONTINUED

### Bank Group Basel III Tier 1 Capital

| | AS AT MAR 18 | | AS AT SEP 17 | | *MOVEMENT* | |
|---|---|---|---|---|---|---|
| | Harmonised Basel III $Am | APRA Basel III $Am | Harmonised Basel III $Am | APRA Basel III $Am | *Harmonised Basel III %* | *APRA Basel III %* |
| **Common Equity Tier 1 capital** | | | | | | |
| Paid-up ordinary share capital | **9,537** | **9,537** | 9,523 | 9,523 | *<1* | *<1* |
| Retained earnings | **2,647** | **2,647** | 2,348 | 2,348 | *13* | *13* |
| Reserves | **478** | **478** | 355 | 355 | *35* | *35* |
| **Gross Common Equity Tier 1 capital** | **12,662** | **12,662** | 12,226 | 12,226 | *4* | *4* |
| **Regulatory adjustments to Common Equity Tier 1 capital:** | | | | | | |
| Goodwill | **40** | **40** | 39 | 39 | *3* | *3* |
| Deferred tax assets | **65** | **142** | 54 | 167 | *20* | *(15)* |
| Net other fair value adjustments | **12** | **12** | (86) | (86) | *(114)* | *(114)* |
| Intangible component of investments in subsidiaries and other entities | **63** | **63** | 51 | 51 | *24* | *24* |
| Loan and lease origination fees and commissions paid to mortgage originators and brokers | **–** | **397** | – | 384 | – | *3* |
| Shortfall in provisions for credit losses | **401** | **428** | 339 | 364 | *18* | *18* |
| Equity exposures | **–** | **1,201** | – | 1,137 | – | *6* |
| Other Common Equity Tier 1 capital deductions | **144** | **251** | 152 | 271 | *(5)* | *(7)* |
| Total Common Equity Tier 1 capital deductions | **725** | **2,534** | 549 | 2,327 | *32* | *9* |
| **Net Common Equity Tier 1 capital** | **11,937** | **10,128** | 11,677 | 9,899 | *2* | *2* |
| **Additional Tier 1 Capital** | | | | | | |
| Additional Tier 1 capital instruments | **1,592** | **1,592** | 1,619 | 1,619 | *(2)* | *(2)* |
| **Gross Additional Tier 1 capital** | **1,592** | **1,592** | 1,619 | 1,619 | *(2)* | *(2)* |
| Deduction from Additional Tier 1 capital | **–** | **–** | – | – | – | – |
| **Net Additional Tier 1 capital** | **1,592** | **1,592** | 1,619 | 1,619 | *(2)* | *(2)* |
| **Total Net Tier 1 capital** | **13,529** | **11,720** | 13,296 | 11,518 | *2* | *2* |

## 6.2 BANK GROUP CAPITAL CONTINUED

### Bank Group Basel III Risk-Weighted Assets (RWA)

| | AS AT MAR 18 | | AS AT SEP 17 | | *MOVEMENT* | |
|---|---|---|---|---|---|---|
| | Harmonised Basel III $Am | APRA Basel III $Am | Harmonised Basel III $Am | APRA Basel III $Am | *Harmonised Basel III %* | *APRA Basel III %* |
| **Credit risk** | | | | | | |
| Subject to IRB approach: | | | | | | |
| Corporate | **27,136** | **27,136** | 26,736 | 26,736 | *1* | *1* |
| SME Corporate | **3,234** | **3,234** | 2,962 | 2,962 | *9* | *9* |
| Sovereign | **182** | **182** | 226 | 226 | *(19)* | *(19)* |
| Bank | **1,576** | **1,576** | 1,315 | 1,315 | *20* | *20* |
| Residential mortgage | **5,678** | **12,654** | 5,228 | 11,597 | *9* | *9* |
| Other retail | **4,466** | **4,466** | 4,093 | 4,093 | *9* | *9* |
| Retail SME | **3,093** | **3,101** | 3,040 | 3,056 | *2* | *1* |
| **Total RWA subject to IRB approach** | **45,365** | **52,349** | 43,600 | 49,985 | *4* | *5* |
| **Specialised lending exposures subject to slotting criteria** | **5,392** | **5,392** | 4,939 | 4,939 | *9* | *9* |
| Subject to Standardised approach: | | | | | | |
| Corporate | **701** | **701** | 938 | 938 | *(25)* | *(25)* |
| Residential mortgage | **1,630** | **1,630** | 1,635 | 1,635 | *(<1)* | *(<1)* |
| Other Retail | **3,771** | **3,771** | 4,847 | 4,847 | *(22)* | *(22)* |
| **Total RWA subject to Standardised approach** | **6,102** | **6,102** | 7,420 | 7,420 | *(18)* | *(18)* |
| **Credit risk RWA for securitisation exposures** | **609** | **609** | 529 | 529 | *15* | *15* |
| **Credit Valuation Adjustment RWA** | **3,712** | **3,712** | 3,014 | 3,014 | *23* | *23* |
| **Exposures to Central Counterparties RWA** | **842** | **1,274** | 1,059 | 1,423 | *(20)* | *(10)* |
| **RWA for Other Assets** | **8,892** | **8,276** | 9,674 | 8,976 | *(8)* | *(8)* |
| **Total Credit risk RWA** | **70,914** | **77,714** | 70,235 | 76,286 | *1* | *2* |
| **Equity risk exposures RWA** | **4,441** | **–** | 4,057 | – | *9* | – |
| **Market risk RWA** | **3,303** | **3,303** | 3,314 | 3,314 | *(<1)* | *(<1)* |
| **Operational risk RWA** | **9,960** | **9,960** | 10,025 | 10,025 | *(1)* | *(1)* |
| **Interest rate risk in banking book RWA** | **–** | **753** | – | – | – | *100* |
| **Total Bank Group RWA** | **88,618** | **91,730** | 87,631 | 89,625 | *1* | *2* |
| Capital ratios | | | | | | |
| Bank Group Common Equity Tier 1 capital ratio (%) | **13.5** | **11.0** | 13.3 | 11.0 | | |
| Bank Group Tier 1 capital ratio (%) | **15.3** | **12.8** | 15.2 | 12.9 | | |

7.1 Glossary

# GLOSSARY

# 7

## 7.1 GLOSSARY

| | |
|---|---|
| AASB | Australian Accounting Standards Board. |
| ABS | Asset Backed Securities. |
| ADI | Authorised Deposit-taking Institution. |
| Additional Tier 1 Capital | A capital measure defined by APRA comprising high quality components of capital that satisfy the following essential characteristics:<br>– provide a permanent and unrestricted commitment of funds;<br>– are freely available to absorb losses;<br>– rank behind the claims of depositors and other more senior creditors in the event of winding up of the issuer; and<br>– provide for fully discretionary capital distributions. |
| Additional Tier 1 Deductions | An amount deducted in determining Additional Tier 1 Capital, as defined in Prudential Standard APS 111 Capital Adequacy: Measurement of Capital. |
| ALCO | The Asset and Liability Committee. |
| AMA | Advanced Measurement Approach (for determining operational risk). |
| APRA | Australian Prudential Regulation Authority. |
| Asset Finance | Global provider of specialist finance and asset management solutions, with global expertise in aircraft, vehicles, technology, healthcare, manufacturing, industrial, energy, rail, and mining equipment, within CAF. |
| Assets under Management (AUM) | AUM is calculated as the proportional ownership interest in the underlying assets of funds and mandated assets that Macquarie actively manages or advises for the purpose of wealth creation, adjusted to exclude cross-holdings in funds and reflect Macquarie's proportional ownership interest of the fund manager. AUM excludes uninvested equity in MIRA. |
| Associates | Associates are entities over which Macquarie Bank has significant influence, but not control.<br>Investments in associates may be further classified as Held for Sale ('HFS') associates. HFS associates are those that have a high probability of being sold within 12 months to external parties. Associates that are not held for sale are carried at cost and equity-accounted. Macquarie Bank's share of the investment's post-acquisition profits and losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised within equity. |
| AVS | Available for sale. AVS assets are investments where Macquarie Bank does not have significant influence or control and are intended to be held for an indefinite period. AVS investments are initially carried at fair value plus transaction costs and revalued in subsequent periods to recognise changes in the assets' fair value with these revaluations included in the AVS reserve in equity. If and when the AVS asset is derecognised or impaired, the cumulative gain or loss will be recognised in the income statement. |
| Bank Group | MBL and its subsidiaries. |
| Bank Group Capital | Level 2 regulatory group capital. |
| Basel III IRB Formula | A formula to calculate RWA, as defined in Prudential Standard APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk. |
| BCN | On 8 October 2014, MBL issued 4.3 million Macquarie Bank Capital Notes (BCN) at face value of $A100 each. BCN are subordinated, unsecured notes that pay discretionary, non-cumulative, semi-annual floating rate cash distributions and may be redeemed at face value on 24 March 2020, 24 September 2020 or 24 March 2021 (subject to certain conditions being satisfied) or earlier in specified circumstances.<br>BCN can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 24 March 2023; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL or MBL); where MBL's common equity Tier 1 capital ratio falls below 5.125%, or where APRA determines MBL would be non-viable without an exchange or a public sector injection of capital (or equivalent support). |
| BBSW | Bank Bill Swap Rate. |
| BFS | Banking and Financial Services. |
| BFS deposits | BFS deposits are those placed with Banking and Financial Services and include products such as the Cash Management Account, Term Deposits and Relationship Banking deposits. Counterparties primarily consist of individuals, self-managed super funds and small-medium enterprises. |

## 7.1 GLOSSARY CONTINUED

| | |
|---|---|
| **BIS** | Bank for International Settlements. |
| **CAF** | Corporate and Asset Finance. |
| **CCB** | Capital Conservation Buffer. |
| **Central Service Groups** | The Central Service Groups consist of the Corporate Operations Group, Financial Management Group, Risk Management Group, Legal and Governance and Central Executive. |
| **CGM** | Commodities and Global Markets. |
| **CLF** | Committed Liquidity Facility. |
| **CMA** | Cash Management Account. |
| **Collective allowance for credit losses** | The provision relating to losses inherent in a portfolio of loan assets or debt investment securities available for sale that have not yet been specifically identified. |
| **Common Equity Tier 1 Capital** | A capital measure defined by APRA, comprising the highest quality components of capital that fully satisfy all the following essential characteristics:<br>– provide a permanent and unrestricted commitment of funds;<br>– are freely available to absorb losses;<br>– do not impose any unavoidable servicing charge against earnings; and<br>– rank behind the claims of depositors and other creditors in the event of winding up.<br>– Common Equity Tier 1 Capital comprises paid up capital, Retained earnings, and certain reserves. |
| **Common Equity Tier 1 Capital Ratio** | Common Equity Tier 1 Capital net of Common Equity Tier 1 deductions expressed as a percentage of RWA. |
| **Common Equity Tier 1 Deductions** | An amount deducted in determining Common Equity Tier 1 Capital, as defined in Prudential Standard APS 111 Capital Adequacy: Measurement of Capital. |
| **Compensation ratio** | The ratio of Compensation Expense to Net Operating Income. |
| **Directors' Profit Share (DPS)** | The DPS plan comprises exposure to a notional portfolio of Macquarie-managed funds. Retained amounts for Executive Directors are notionally invested over the retention period. This investment is described as 'notional' because Executive Directors do not directly hold securities in relation to this investment. However, the value of the retained amounts will vary as if these amounts were due directly invested in actual securities, giving the Executive Directors an effective economic exposure to the performance of the securities. If the notional investment results in a notional loss, this loss will be offset against any future notional income until the loss is completely offset. |
| **Earnings on capital and certain corporate income items** | Net operating income includes the income generated by Macquarie Bank's Operating Groups, income from the investment of Macquarie Bank's capital, and certain items of operating income not attributed to Macquarie Bank's Operating Groups. Earnings on capital and certain corporate income items is net operating income less the net operating income generated by Macquarie Bank's Operating Groups. |
| **Earnings per share** | A performance measure that measures earnings attributable to each ordinary share, defined in AASB 133 'Earnings Per Share'. |
| **ECAM** | Economic Capital Adequacy Model. |
| **ECS** | On 26 March 2012, MBL, acting through its London Branch, issued $US250 million of Exchangeable Capital Securities (ECS). ECS were subordinated, unsecured notes that paid discretionary, non-cumulative, semi-annual floating rate cash distributions. ECS were bought back on 20 June 2017. |
| **Effective tax rate** | The income tax expense as a percentage of the profit before income tax, both adjusted for amounts attributable to non-controlling interests. The effective tax rate differs from the Australian company tax rate due to permanent differences arising from the income tax treatment of certain income and expenses as well as tax rate differentials on some of the income earned offshore. |
| **Expense/Income ratio** | Total operating expenses expressed as a percentage of net operating income. |
| **Financial Report** | The Financial Report within the Macquarie Bank Annual Report. |
| **FIRB** | Foundation Internal Ratings Based Approach (for determining credit risk). |
| **FY2017** | The year ended 31 March 2017. |
| **FY2018** | The year ended 31 March 2018. |
| **Headcount** | Headcount represents Macquarie Bank's active permanent and variable workforce, and includes Macquarie Bank employees (permanent and casual) and its contingent workers (contractors, agency workers and secondees). Macquarie Bank's non-executive directors are not included. |
| **HQLA** | High-quality liquid assets. |

## 7.1 GLOSSARY CONTINUED

| | |
|---|---|
| **International income** | Operating income is classified as 'international' with reference to the geographic location from which the operating income is reported from a Management perspective. This may not be the same geographic location where the operating income is recognised for reporting purposes. For example, operating income generated by work performed for clients based overseas but recognised in Australia for reporting purposes could be classified as 'international' income. Income earned in the Corporate segment is excluded from the analysis of international income. |
| **LGD** | Loss given default is defined as the economic loss which arises upon default of the obligator. |
| **Macquarie Bank, the Consolidated Entity** | Macquarie Bank Limited and its subsidiaries. |
| **Macquarie Group** | MGL and its subsidiaries. |
| **Macquarie Income Securities (MIS)** | Macquarie Income Securities (MIS) are perpetual, subordinated instruments that have no conversion rights to ordinary shares. Discretionary distributions are paid quarterly. They are treated as equity in the statement of financial position. There are four million $A100 face value MIS on issue. |
| **MACS** | On 8 March 2017, MBL, acting through its London Branch, issued $US750 million of Macquarie Additional Capital Securities (MACS). MACS are subordinated, unsecured notes that pay discretionary, non-cumulative, semi-annual fixed rate cash distributions.<br>Subject to certain conditions the MACS may be redeemed on 8 March 2027, or every 5th anniversary thereafter. MACS can be exchanged for a variable number of fully paid MGL ordinary shares on an acquisition event (where a person acquires control of MBL or MGL), where MBL's common equity Tier 1 capital ratio falls below 5.125%, or where APRA determines MBL would be non-viable without an exchange or a public sector injection of capital (or equivalent support). |
| **MAM** | Macquarie Asset Management. |
| **MBL, the Company** | Macquarie Bank Limited ABN 46 008 583 542. |
| **MCN** | On 7 June 2013, MGL issued six million Macquarie Group Capital Notes (MCN) at a face value of $A100 each. MCN are subordinated, non-cumulative, unsecured notes that that pay discretionary, non-cumulative, semi-annual floating rate cash distributions and may be redeemed at face value on 7 June 2018, 7 December 2018 or 7 June 2019 (subject to certain conditions being satisfied) or earlier in specified circumstances.<br>MCN can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 7 June 2021; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL); or where APRA determines MGL would be non-viable without an exchange or a public sector injection of capital (or equivalent support). |
| **MCN2** | On 18 December 2015, MGL issued 5.3 million Macquarie Group Capital Notes 2 (MCN2) at a face value of $A100 each. MCN2 are subordinated, non-cumulative, unsecured notes that that pay discretionary, non-cumulative, semi-annual floating rate cash distributions and may be redeemed at face value on 17 March 2021, 17 September 2021 or 17 March 2022 (subject to certain conditions being satisfied) or earlier in specified circumstances.<br>MCN2 can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 18 March 2024; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL); or where APRA determines MGL would be non-viable without an exchange or a public sector injection of capital (or equivalent support). |
| **MCN3** | MGL intends to make an offer of Macquarie Group Capital Notes 3 (MCN3) subsequent to 31 March 2018. |
| **MEREP** | Macquarie Group Employee Retained Equity Plan. |
| **MFHPL** | Macquarie Financial Holdings Pty Limited. |
| **MGL** | Macquarie Group Limited ABN 94 122 169 279. |
| **MIM** | Macquarie Investment Management. |
| **MSIS** | Macquarie Specialised Investment Solutions. |
| **Net loan losses** | The impact on the income statement of loan amounts provided for or written off during the period, net of the recovery of any such amounts which were previously written-off or provided for in the income statement. |
| **Net tangible assets per ordinary share** | (Total equity less Macquarie Income Securities less non-controlling interest less the Future Income Tax Benefit plus the Deferred Tax Liability less Intangible assets) divided by the number of ordinary shares on issue at the end of the period. |

## 7.1 GLOSSARY CONTINUED

| | |
|---|---|
| **Net Trading Income** | Income that comprises gains and losses related to trading assets and liabilities and includes all realised and unrealised fair value changes and foreign exchange differences. |
| **Non-Bank Group** | MGL, MFHPL and its subsidiaries. |
| **Non-GAAP metrics** | Non-GAAP metrics include financial measures, ratios and other information that are either not required or defined under Australian Accounting Standards. |
| **Operating Groups** | The Operating Groups consist of MAM, CAF, BFS and CGM. |
| **Principal Finance** | Principal Finance is a division of CAF and provides flexible primary financing solutions and engages in secondary market investing, across the capital structure. Operating globally in both corporate and real estate sectors, the team has experience across a variety of industry groups including real estate, infrastructure, telecommunications, media, entertainment and technology, leisure and healthcare. |
| **RBA** | Reserve Bank of Australia. |
| **Risk-weighted assets (RWA)** | A risk-based measure of an entity's exposures, which is used in assessing its overall capital adequacy. |
| **RMBS** | Residential Mortgage-Backed Securities. |
| **SPEs** | Special purpose entities. |
| **Subordinated debt** | Debt issued by Macquarie Bank for which agreements between Macquarie Bank and the lenders provide, in the event of liquidation, that the entitlement of such lenders to repayment of the principal sum and interest thereon is and shall at all times be and remain subordinated to the rights of all other present and future creditors of Macquarie Bank. Subordinated debt is classified as liabilities in the Macquarie Bank financial statements and may be included in Tier 2 Capital. |
| **Tier 1 Capital** | Tier 1 capital comprises of (i) Common Equity Tier 1 Capital; and (ii) Additional Tier 1 Capital. |
| **Tier 1 Capital Deductions** | Tier 1 capital deductions comprises of (i) Common Equity Tier 1 Capital deductions; and (ii) Additional Tier 1 Capital deductions. |
| **Tier 1 Capital Ratio** | Tier 1 Capital net of Tier 1 Capital Deductions expressed as a percentage of RWA. |
| **UK** | The United Kingdom. |
| **US** | The United States of America. |