Moody's Global Banking

Special Comment

November 2009

Australian & New Zealand Bank Hybrid Securities and Subordinated Debt

Supplement to Moody's Revised Rating Guidelines for Bank Hybrid Securities and Subordinated Debt

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Analyst Contacts:

Sydney 61.2.9270.8100

Patrick Winsbury 612.9270.8183
Senior Vice President

Marina Ip 612.9270.8130
Assistant Vice President-Analyst

Daniel Yu 612.9270.8198
Analyst

Singapore 65.6398.8308

Deborah Schuler 65.6398.8336
Senior Vice President

Hong Kong 852.3551.3077

Jerry Chien 852.2916.1106
Team Managing Director

Summary

Rated hybrid securities could potentially be downgraded by an average of 3 notches.

This Special Comment is a supplement to "Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt", November 2009. It dimensions the potential impact of the new guidelines on the ratings of capital-qualifying, hybrid instruments issued by Australian banks and their New Zealand subsidiaries, namely:

- "Plain vanilla" subordinated debt ratings (Lower Tier 2) are not affected
- Junior subordinated debt ratings (Upper Tier 2) could potentially be downgraded by up to 3 notches
- Preferred security ratings (Tier 1) could potentially be downgraded by 2 to 4 notches

The ratings of over A$24 billion (US$22bn) of outstanding hybrid securities could be affected.

There is no impact on the institution-level ratings of Australian and New Zealand banks – i.e. deposit ratings, issuer ratings and senior unsecured debt ratings will not change.

Moody's Investors Service

Overview of the Changes

Hybrid securities may experience more frequent and/or greater losses in the future

As outlined in "Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt", actions taken by regulators and governments in response to the financial crisis have been contrary to historical precedent and have increased the loss probability for hybrid securities. In addition, certain types of hybrids are riskier than others based on their specific features. Recent events have shown that hybrid "default"[1] probability now is clearly higher than for bank senior debt and losses could occur in a restructuring outside liquidation through coupon suspension, principal write-downs, good bank/bad bank structures, and distressed exchanges.

Consequently, our new rating guidelines have three main components:

- **In most cases, the guidelines remove systemic and regional support from bank hybrid ratings and, in some cases, from subordinated debt ratings.** Instead, these ratings will be linked to the stand-alone intrinsic strength of the bank as expressed through our Bank Financial Strength Rating (BFSR), which maps to the Baseline Credit Assessment. This is in contrast to our current practice of anchoring to the bank's senior unsecured rating or Bank Debt Rating[2] (BDR), which incorporates systemic and other forms of external support.
- **Apply wider notching among different classes of bank hybrids in order to provide greater differentiation based on the riskiness of specific features.** For example, due to their terms, non-cumulative preferred securities have proven to be more loss absorbing than junior subordinated debt with cumulative coupon skip features. Accordingly, we are proposing wider notching, as appropriate, to reflect these relative risks.
- **Provide the flexibility to position hybrid ratings based on case-specific and country-specific considerations.** While hybrids may be poised to absorb losses to varying degrees, the speed at which regulators make use of their loss absorbing features, if at all, will be driven by jurisdictional considerations. This necessitates the use of a country-specific approach with a qualitative overlay.

Explaining the revised notching

As a result of recent experience, the revised guidelines exclude the potential for systemic (regulatory) support from most hybrid ratings, by changing the reference rating – the "anchor" rating – relative to which hybrid ratings are "notched" down.

Currently the anchor rating is the Bank Debt Ratings (BDR), but under the revised approach it will be the Adjusted Baseline Credit Assessment (Adjusted BCA), For certain markets and certain types of securities (mostly Upper Tier 2), there will be a transition period.

The Adjusted BCA is arrived at in the following manner:

- Moody's Bank Financial Strength Ratings (BFSR) express the intrinsic credit profile of a bank. They do not include the potential for third-party support, and they do not include transfer risk (the risk that a sovereign may impose exchange controls)
- BFSRs can be mapped to Moody's traditional Aaa-C rating scale. This is referred to as the Baseline Credit Assessment (BCA)
- For the purpose of rating bank hybrid instruments, we add parental and cooperative support to arrive at the Adjusted BCA, which excludes systemic and regional support

[1] Under their terms, hybrids allow for missed coupon payments and/or principal write-downs, which do not result in an event of default. If these events occurred, there would not be a breach of contract, but a significant credit event that could potentially result in investor losses.

[2] For purposes of this piece, we have defined the Bank Debt Rating as the senior unsecured rating of the bank rather than the Bank Deposit Rating. In this way, we have allowed for the possibility that there may be differentiation between these two ratings in the future, depending on the potential for depositor preference relative to senior unsecured creditors in a given jurisdiction.

- Bank Debt Ratings, in contrast, include the potential for all types of third-party support, including systemic support[3].

The notching ranges for various classes of hybrids relative to the Adjusted BCA (and in some cases the Bank Debt Rating) is summarized in the table below:

Moody's Revised Bank Hybrid and Subordinated Debt Rating Guidelines

	Hybrid Subordination	Typical Regulatory Treatment	Coupon Non-Payment	Number of Notches below Adjusted BCA (Adj. BCA = BCA + Parental and/or Cooperative Support)
1	**"Plain Vanilla" Subordinated Debt**	Lower Tier 2	None	Generally, will receive uplift from Adjusted BCA to BDR – 1*
2	**Junior Subordinated Debt**	Upper Tier 2	Optional, cumulative	Adjusted BCA - 1 or – 2**
3	**Preferred Securities**	Tier 1	Optional/mandatory, cumulative, non-cumulative, or non-cash cumulative (ACSM) settlement	Adjusted BCA - 2 to – 4***

* *In countries where this class of subordinated debt has absorbed losses or if the probability of incurring losses has increased, the notching will be Adjusted BCA - 1.*

** *For junior subordinated debt, depending on jurisdiction, ratings may incorporate some uplift for systemic support as banks transition from a period of extraordinary government support to a more normal operating environment.*

*** *Capped at a maximum of Baa1 for non-cumulative Tier 1 securities with a net loss trigger. Certain Australian securities have the option, which may or may not be explicit in the hybrid security documentation, to override a trigger breach and pay the coupon anyway, subject to regulatory approval, and they are exempted from the Baa1 cap.*

Impact of the revised guidelines on the ratings of Australian and New Zealand bank hybrid securities

Please refer to the Appendix for a complete listing of affected securities

"Plain vanilla" subordinated debt ratings (Lower Tier 2) will not change

- In Australia and New Zealand, the rating for "plain vanilla" subordinated debt will continue to incorporate uplift for systemic support from the Adjusted BCA, to a level that is one notch below the Bank Debt Rating in order to capture subordination risk. Since we view Australia to be a "high support" country for the purpose of our joint default analysis rating approach, and New Zealand to be a "medium support" country, subordinated debt ratings of banks in these countries will continue to incorporate systemic support.
- Since subordinated debt issued by Australian and New Zealand banks is already rated at one notch below the level of the Bank Debt Rating, the revised methodology does not have any impact on outstanding subordinated debt ratings.

Junior subordinated debt ratings (Upper Tier 2) could eventually be downgraded by up to 3 notches, but there may be a transition period

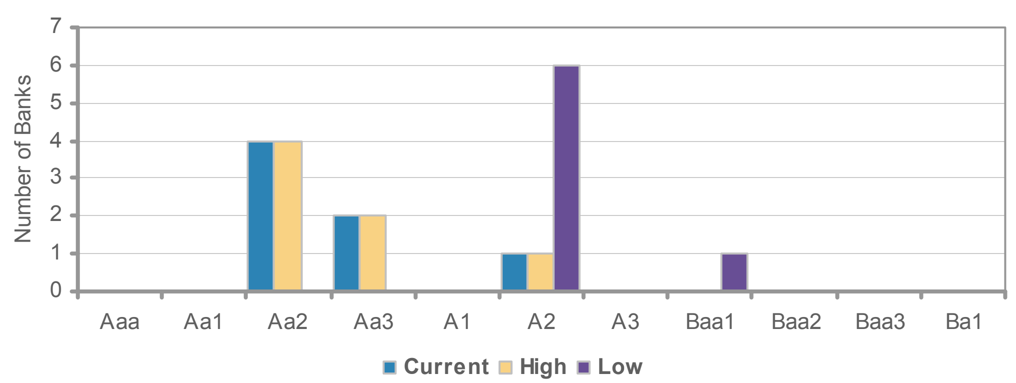
- Junior subordinated securities are currently rated one notch below the Bank Debt Rating of a given bank, which incorporates uplift for the potential for systemic support.
- The new guidelines envisage that most junior subordinated debt ratings will eventually be positioned one notch below a bank's Adjusted BCA.. Consequently, given that the ratings are already positioned one notch below the Bank Debt Rating, there would only be lower ratings to the extent that the anchor migrates from the Bank Debt Rating, which incorporates systemic support, to the Adjusted BCA, which does not incorporate systemic support.

[3] For a more in-depth discussion of BFSRs and Moody's approach to incorporating third-party support into BDRs, please refer to Moody's BFSR methodology and Joint Default Analysis methodology, referenced at the end of this report.

Australian & New Zealand Bank Hybrid Securities and Subordinated Debt

- A transition period is envisaged for the anchor, and hence junior subordinated debt ratings to be adjusted to the new level. The length of of the transition will reflect country-specific legal and regulatory issues, as well as political pressure for holders of capital qualifying instruments to share in the cost of bank recapitalizations.
- Because the Australian and New Zealand banking systems have not experienced severe stress during the global financial crisis, there is no case history to illuminate if and how regulatory attitudes may be changing. However, we continue to view the Australian regulator as being highly "supportive" (see discussion below), and consequently we will be giving careful consideration as the appropriate speed of transition for junior subordinated debt ratings.
- Approximately one quarter of Australian banks and their New Zealand subsidiaries rated by Moody's would be affected by the new guidelines as they relate to Upper Tier 2 securities.
- Three banks have rated junior subordinated debt outstanding: ANZ National Bank, which is the New Zealand subsidiary of Australia and New Zealand Banking Group (ANZ),, National Australia Bank (NAB) and Westpac Banking Corporation (Westpac).
- Six institutions have the ability to issue junior subordinated instruments out of their debt programmes: three of the four major banks: ANZ, NAB and Westpac; regional banks Suncorp-Metway and Bank of Western Australia (BankWest) - now a subsidiary of Commonwealth Bank of Australia (CBA); and Bank of New Zealand (a subsidiary of NAB).
- The ratings of ANZ, NAB, and Westpac currently include two notches of systemic support because of their prominent market positions. Consequently, the junior subordinated debt ratings of these banks would eventually be expected to drop by at least two notches, if and when systemic support is removed.
- The ratings of Suncorp Metway and ANZ National Bank currently include one notch of systemic support. Consequently, the junior subordinated debt ratings of these banks would eventually be expected to drop by at least one notch, if and when systemic support is removed.

Upper Tier 2 Ratings:
Current & Potential Distribution by Bank



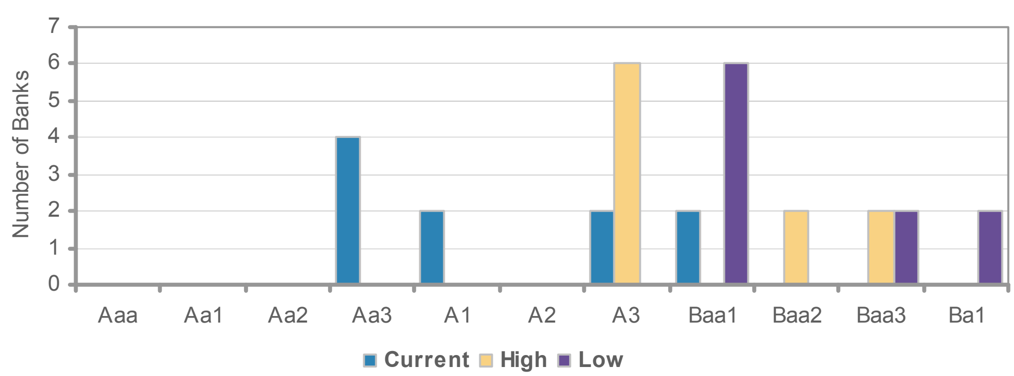
Preferred security ratings (Tier 1) could be downgraded 2 to 4 notches

- Preferred securities are currently rated two notches below the Bank Debt Rating of a given bank, which incorporates the potential for systemic support. Under the revised methodology, for all preferred securities, we would remove systemic support and notch from the Adjusted BCA. From this unsupported rating starting point, we would then notch wider or narrower based on the hybrid's features.
- The new guidelines envisage that non-cumulative preferred securities will be positioned three notches below a bank's Adjusted BCA, which does not include the potential for systemic support.

Australian & New Zealand Bank Hybrid Securities and Subordinated Debt

- For non-cumulative securities with "net loss triggers" (coupon distributions must be suspended if the issuing bank does not report positive earnings), the rating will normally be positioned 4 notches below the Adjusted BCA, and in addition will be rated no higher than Baa1. Almost all rated Australian and New Zealand hybrid Tier 1 securities contain "distributable profits" triggers that effectively reference the prior twelve months of earnings.
- However, the revised guidelines note that Australian banks have the option, which may or may not be explicit in the hybrid security documentation, to override a trigger breach and pay the coupon anyway, subject to regulatory approval. Given the dependence of Australian banks on foreign wholesale funding, there is a high probability that the breach of an earnings-related trigger would be overridden by the bank or regulators despite the absence of explicit language. As a result, the ratings for these securities, in certain cases, may be positioned three notches below the Adjusted BCA instead of four notches, and be excluded from the Baa1 cap.
- Approximately half of the Australian banks and their New Zealand subsidiaries rated by Moody's would be affected by the new guidelines as they relate to Tier 1 securities
- 11 institutions have preferred instruments outstanding: the "Four Majors" ANZ, CBA, NAB, and Westpac; two regional banks, Bank of Queensland and Suncorp-Metway; investment banking house Macquarie Group and its subsidiary Macquarie Bank; and New Zealand banks ANZ National Bank, ASB Bank and Bank of New Zealand (subsidiaries of ANZ, CBA and NAB respectively).
- The ratings of preferred instruments issued by the four major banks could decline by three or four notches under the new guidelines. The exception-basis notching of the Adjusted BCA minus three notches described above could potentially apply to many of these securities.
- The ratings of Suncorp-Metway, Bank of Queensland, Macquarie Group, Macquarie Bank, ANZ National Bank, ASB Bank and Bank of New Zealand include only one notch of systemic support, as compared to the two notches of systemic support in the ratings of the "Four Majors". Hence their hybrid Tier 1 ratings would potentially fall by two to three notches (although one specific security issued by Suncorp-Metway could fall by three to four notches). Again, the exception-based notching may be applicable in many cases.
- A small number of preferred securities do not contain net loss triggers, and could potentially decline by a lesser number of notches: one of ANZ's preferred securities by three notches and one of ASB Bank's preferred securities by two notches.

Tier 1 Ratings:
Current & Potential Distribution by Bank



The operating and regulatory environment

As discussed above, the pace and extent of rating changes will be dictated by careful consideration of the local operating and regulatory environment. Below are some of the key issues that will have a bearing on the ratings of Australian and New Zealand bank hybrid securities.

Emphasis on problem prevention

Australia's Banking Act requires that, in liquidation, Australian depositors are to be repaid in priority to all other creditors. The bank regulator, the Australian Prudential Regulation Authority (APRA), also regularly highlights the protection of bank depositors as a key priority.

Despite its focus on protecting depositors, APRA's approach has always been highly pro-active, with a strong emphasis on problem-prevention that has protected bank creditors also. The regulator has been accorded a wide range of powers to resolve emerging issues.

As a result, we have not seen hybrid instruments being used to absorb losses. When stress has arisen at a particular institution, APRA (and its regulatory predecessors) typically appear to have favoured alternative solutions. For example, the Australian regulatory authorities have historically permitted issuers to make distributions on preferred securities, despite having tripped coupon suspension triggers – but it is noteworthy that on such occasions the issuers simultaneously raised additional equity.[4]

Nevertheless, it is hard to extrapolate future regulatory behaviour from past events, as hybrids are instruments that count as part of regulatory capital and therefore exist to absorb loss in case of stress. Furthermore, we have seen a global trend during the financial crisis of regulators being increasingly willing to impose losses on hybrids outside of liquidation. These facts underlie the overall downward re-rating of hybrid securities under the new guidelines.

Balance of payments deficit

A particular feature of the Australian economy is its large and persistent balance of payments deficit. The banking system plays a key role in financing the deficit. Australian bank foreign liabilities have historically comprised as much as two-thirds of the country's foreign funding requirement. And foreign funding (largely wholesale) has constituted as much as a quarter of Australian bank funding.

Accordingly, we believe that there is a strong incentive for the Australian authorities to maintain a high level of investor confidence in the financial strength of Australia's banks – and to provide support if required. We believe that this may have contributed to the regulatory override of coupon suspension triggers on preferred securities in the past. And looking forward, even though we believe the global regulatory trend to emphasize the loss-absorbing role of hybrid instruments will be felt in the Australian market, it may be somewhat moderated by the reality imposed by the funding profile of Australia and its banks.

Tier 1 hybrids purchased by retail investors

Tier 1 hybrids issued by the larger Australian banks, in particular, are popular with retail investors, who are attracted by the yields offered relative to deposits, the strong intrinsic financial condition of the banks themselves – and what appears to be a widespread assumption amongst the general public that a high level of systemic support for the banks would be forthcoming in case of need.[5] Indeed, Australia's banks have been able to tap the retail Tier 1 market throughout much of the global financial crisis, with the exception being in the immediate aftermath of Lehman's collapse.

[4] For example, major banks ANZ and Westpac paid distributions on their preferred securities in 1992, after recording losses during Australia's last financial crisis – but they simultaneously raised additional capital to underpin their financial condition. Similarly, insurer AMP also paid distributions on its preferred securities after recording a loss in 2003 but also raised equity as part of its de-merger that year.

[5] For example, a pre-crisis survey suggested roughly two-thirds of Australian retail depositors expected the government to ensure the safety of their deposits, in the case that a bank experienced stress.

Australian banks dominate the New Zealand banking system

The subsidiaries of Australia's four major banks collectively account for over 90% of New Zealand banking system assets. This creates a unique political and regulatory dynamic.

It is worth noting that in 2006, both the Australian Banking Act of 1959 and the Reserve Bank of New Zealand Act were amended to include clauses on trans-Tasman cooperation. In the Australian Act, Section 8A requires of the Australian regulator that:

1. In performing and exercising its functions and powers, APRA must "to the extent reasonably practicable, avoid any action that is likely to have a detrimental effect on financial system stability in New Zealand."

At the margin, we would interpret this as increasing the probability that the Australian regulator would permit its major banks to support their New Zealand subsidiaries, if required. Furthermore, and separately to the trans-Tasman provision of the Act, there is a track record of the Australian regulator allowing Australian financial institutions to support their foreign subsidiaries.

No impact on institution-level ratings

We continue to expect a high degree of governmental and regulatory support for the deposits and senior obligations of Australia's banks

In common with many other countries, the Australian authorities have taken a number of extraordinary measures to support the banking system during the global financial crisis – notably including a guarantee scheme for bank deposits and debt obligations and broadened central bank repo facilities. While these remain in place, the ratings of Australian banks will remain closely aligned to that of the sovereign: we have indicated that we see the ratings of the major banks remaining within the Aa category and the regional banks within the Single A category for the duration of the crisis.

As discussed, even after the crisis-related support measures run off, we expect that a significant degree of systemic support will continue to be available to Australia's larger banks, as for the purposes of our Joint Default Analysis, we judge Australia to be a "high support" country.

Potential changes to equity credit calculation are very unlikely to impact issuer-level ratings

As part of the review, we have also indicated that we may reconsider the way we classify hybrid securities in terms of the relative amount of debt and equity that they contribute to calculations of a bank's adjusted capital ratios. However, we do not expect this to impact bank ratings.

As part of this reevaluation, we have suggested that greater "equity credit" may be given for deeply subordinated, non-cumulative instruments, while less may be given for hybrids without these features. Hence, on a net basis, there may be little change.

Moreover, the impact of equity credit on Australian bank capital ratios is not material: they currently fall into the expected range for their ratings, whether or not it is included.

Appendix 1: Impact of proposal on the ratings of Australian bank capital-qualifying instruments

Australian & New Zealand Bank Hybrid Securities and Subordinated Debt

Issuer Name	Hybrid Security Name	Currency	Face Amount (millions)	ISIN	Hybrid Security: Existing Rating	Group's Debt Rating	Group's BFSR	Group's BCA	Group's "Adjusted BCA"	Hybrid Security: New Guideline (High)	Hybrid Security: New Guideline (Low)
Australia											
Tier 1 Securities											
ANZ Capital Trust I	Non-cumulative Trust Securities	USD	350	US001822AA36	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
ANZ Capital Trust II	Non-cumulative Trust Securities	USD	750	US001822AB19	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
ANZ Capital Trust III	Non-cumulative Trust Securities	Euro	500	XS0207513127	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Australia and New Zealand Banking Group Limited	Non-cumulative mandatory convertible stapled securities	GBP	450	XS0304110132	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Australia and New Zealand Banking Group Limited	Convertible Preference Shares ("September 2008 CPS")	AUD	1,081	AU0000ANZPB7	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Australia and New Zealand Banking Group Limited	Perpetual capital subordinated notes	USD	300	GB0040024555	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Bank of Queensland Limited	Perpetual Equity Preferred Shares	AUD	200	AU0000BOQPC0	Baa1	A2	C	A3	A3	Baa3	Ba1
CBA Capital Trust I	Trust Preferred Securities	USD	550	US124789AA60	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
CBA Capital Trust II	Trust Preferred Securities	USD	700	US12479BAA08	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Commonwealth Bank of Australia	PERLS IV	AUD	1,465	AU0000CBAPB1	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Preferred Capital Limited	PERLS III	AUD	1,166	AU0000PCAPA3	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Macquarie Capital Funding L.P.	6.177% Non-cumulative Perpetual Preference shares	GBP	350	XS0201559811	A3	A1	C+	A2	A2	Baa2	Baa3
Macquarie Finance Limited	Macquarie Income Securities	AUD	400	AU0000MBLHB4	A3	A1	C+	A2	A2	Baa2	Baa3
Macquarie CPS Trust	Convertible Preference Securities	AUD	600	AU0000MQCPA6	Baa1	A2	n/a	n/a	A3	Baa3	Ba1
National Australia Bank Limited	National Income Securities	AUD	2,000	AU0000NABHA7	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Australia Bank Limited (New York Branch)	Stapled Securities	AUD	300		Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Australia Bank Limited (New York Branch)	Convertible Notes	AUD	300		Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Australia Bank Limited (New York Branch)	Perpetual Capital Notes	USD	600	XS0347918723	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Australia Bank Limited (New York Branch)	2009 Stapled Securities	AUD	500		Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Capital Instruments [Euro] LLC2	National Capital Instruments	Euro	400	XS0269714464	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Capital Trust I	Trust Preferred Securities	GBP	400	XS0177403937	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1

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National Capital Trust II	Trust Preferred Securities II	USD	800	US635192AA58	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
National Capital Trust III	National Capital Instruments	AUD	400	AU3FN0000121	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Suncorp-Metway Ltd.	Reset Preference Shares ("RPS") SUNPA ASX	AUD	144	AU0000SUNPA2	A3	A1	C+	A2	A2	Baa2	Baa3
Suncorp-Metway Ltd.	Converting Preference Shares ("CPS") SUNPB ASX	AUD	735	AU0000SUNPB0	A3	A1	C+	A2	A2	Baa2	Baa3
Suncorp-Metway Ltd.	Resetting Floating Rate Capital Notes ("FRCN") SUNHB ASX (A)	AUD	170	AU0000SUNHB7	A2	A1	C+	A2	A2	Baa2	Baa3
Westpac Banking Corporation	Westpac SPS	AUD	1,036	AU0000WBCPA7	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Westpac Banking Corporation (New York branch)	Westpac SPS II	AUD	908	AU0000WBCPB5	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Westpac Capital Trust III	Trust Preferred Securities	USD	750	US96122BAA44	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
WestPac Capital Trust IV	Trust Preferred Securities	USD	525	US96122CAA27	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Westpac TPS Trust	Westpac Trust Preferred Securities 2006	AUD	762	AU0000WCTPA9	Aa3	Aa1	B	Aa3	Aa3	A3	Baa1
Upper Tier 2 Securities											
National Australia Bank Limited	Subordinated Perpetual Notes	AUD	190	GB0006241326	Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
Westpac Banking Corporation	Subordinated Perpetual Notes	USD	390	GB0009573998	Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
Upper Tier 2: Programmes under which securities may be issued											
Australia and New Zealand Banking Grp. Ltd.	EMTN programme	USD	60,000		Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
Bank of Western Australia	Programme for the issuance of Debt Instruments	USD	5,000		Aa2	Aa1	C	A3	Aa3	Aa2	A2
National Australia Bank Limited	Global MTN Programme	USD	100,000		Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
National Australia Bank Limited	Debt Issuance Programme		Unlimited		Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
Suncorp-Metway Ltd.	Domestic MTN, TD and Other Debt Instruments Programme		Unlimited		A2	A1	B	Aa3	A2	A2	Baa1
Westpac Banking Corporation	Debt Issuance Programme		Unlimited		Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
Westpac Banking Corporation	Programme for the issuance of Debt Instruments	USD	50,000		Aa2	Aa1	B	Aa3	Aa3	Aa2	A2
Westpac Banking Corporation	Euro Transferable Certificate of Deposit Programme	USD	2,500		Aa2	Aa1	B	Aa3	Aa3	Aa2	A2

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Issuer Name	Hybrid Security Name	Currency	Face Amount (millions)	ISIN	Hybrid Security: Existing Rating	Group's Debt Rating	Group's BFSR	Group's BCA	Group's "Adjusted BCA"	Hybrid Security: New Guideline (High)	Hybrid Security: New Guideline (Low)
New Zealand											
Tier 1 Securities											
ASB Capital Limited	Perpetual Preference Shares	NZD	200	NZASBD0001S7	A1	Aa2	B-	A1	Aa3	A3	Baa1
BNZ Income Securities Limited	BNZ Income Securities	NZD	448	NZBISD0001S0	A1	Aa2	C+	A2	Aa3	A3	Baa1
BNZ Income Securities Limited - II	BNZ income Securities II	NZD	260	NZBNSDP001C9	A1	Aa2	C+	A2	Aa3	A3	Baa1
Upper Tier 2 Securities											
ANZ National Bank Ltd	Perpetual callable subordinated bonds	NZD	835	NZANBD0006S7	Aa3	Aa2	C+	A2	Aa3	Aa3	A2
Upper Tier 2: Programmes under which securities may be issued											
ANZ National (International) Hong Kong Branch	Euro MTN Programme	USD	2,000		Aa3	Aa2	C+	A2	Aa3	Aa3	A2
BNZ International Funding Limited (London Branch)	Global MTN Programme	USD	100,000		Aa3	Aa2	C+	A2	Aa3	Aa3	A2

Appendix 2: Characteristics of Australian Hybrid Instruments

Tier 1 instruments

"Stapled" Structures

Australian Tier 1 instruments may be issued by the bank or through a trust, and often employ tax-efficient "stapled" structures. They typically have a mandatory conversion into equity or preference shares after 5 years and an option for the issuer to redeem or sell the issue for cash, subject to regulatory approval.

Australian stapled structures consist of (i) a perpetual, unsecured, non-cumulative, subordinated note and (ii) a preference share issued by a bank. The note and preference share are "stapled" together when issued and comprise a single stapled security. This stapled security is registered and traded: the note and preference share cannot be traded separately whilst they are stapled. Interest is payable on the notes only whilst they are stapled.

The note and preference share are "unstapled" upon an "assignment event" or a "trigger event (depending on whether the preference share was initially issued paid or unpaid). Such events would include (i) the date immediately prior to conversion or redemption, (ii) an event of default or, (iii) the appointment of a regulator as statutory manager to the bank. Upon unstapling, the note is automatically assigned back to the bank and the investor continues to hold the preference share.

Moody's rates such stapled securities on the basis of the credit risk of the preference share, which is the security that an investors would ultimately hold in case of an assignment or trigger event. No rating is separately assigned to the note.

Common features

- Securities rank pari passu with preferred stock in bankruptcy
- Most Tier 1 securities have a distributable profits test, which in Australia amounts to an earnings test . Coupons must be suspended if there is a breach. Some instruments contain language which provide for the payment of coupons even when there has been a breach, in the case that regulatory approval is obtained. In rare cases the coupon deferral trigger is a capital adequacy test.
- Non-Cumulative

Junior Subordinated securities (Upper Tier 2)

A number of Australian banks are able to issue undated subordinated debt off their debt issuance programmes that would qualify as Upper Tier 2 securities. However there is only one outstanding rated issue.

Common features

- Securities typically rank subordinate to "plain vanilla" subordinated debt
- Deferral of coupons is typically required if there is a solvency test breach, and in rare cases optional in case of an earnings test breach.
- Cumulative

Moody's Related Research

Rating Methodologies:

- Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt", November 2009 (120307)
- Frequently Asked Questions: Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt, November 2009 (120614)
- Bank Financial Strength Ratings: Global Methodology, February 2007 (102151)
- Incorporation of Joint-Default Analysis into Moody's Bank Ratings: A Refined Methodology, March 2007 (102639)

To access these reports, click on the entries above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

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Author	Production Associate
Patrick Winsbury	Diana Brimson

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