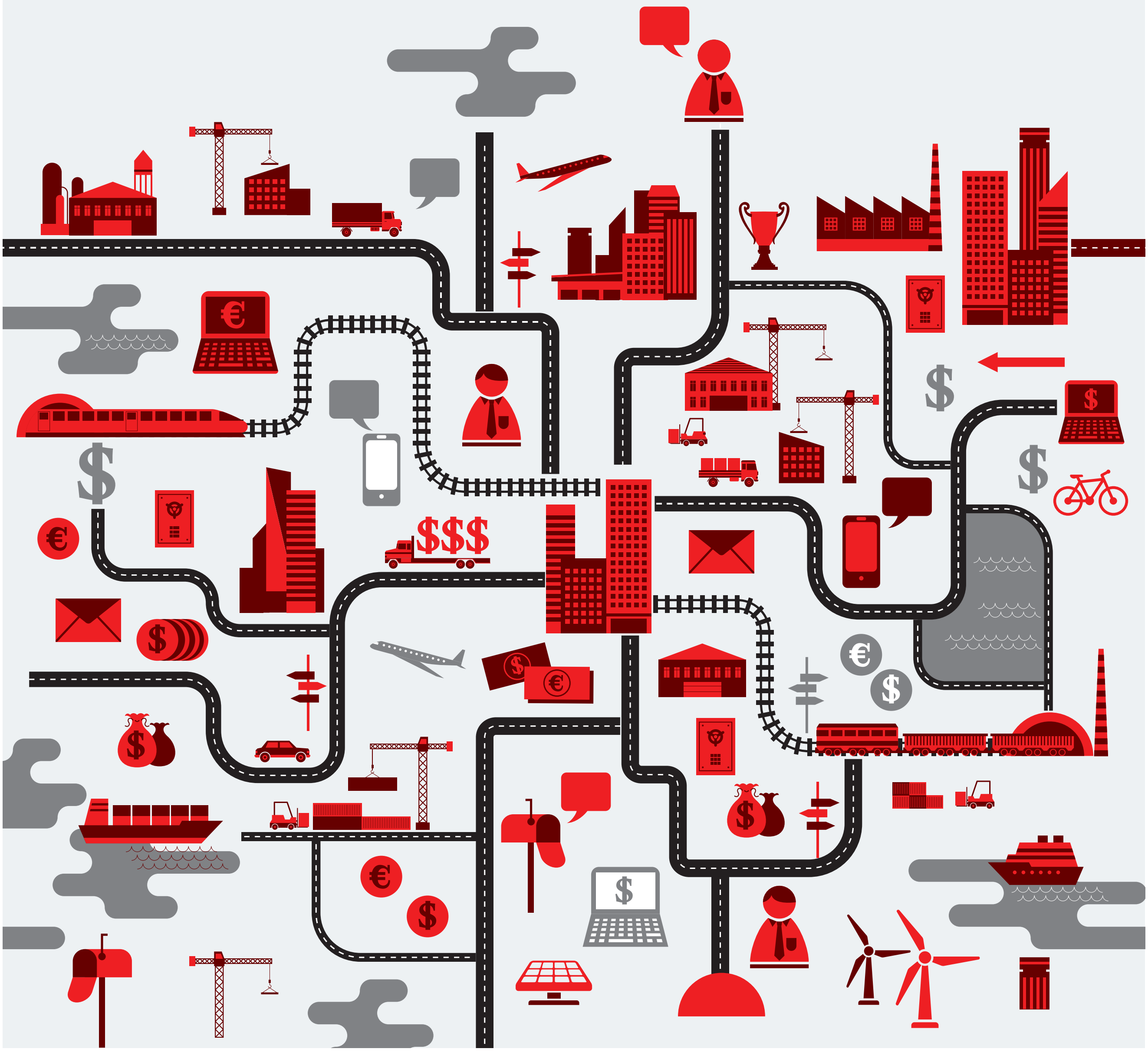
2014 Year in Review

Capital Financing



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Steve Lambert, EGM Capital Financing

2014: the year that was

Opening up new funding opportunities for our customers

Every year it surprises me how quickly we come to the end and how much we are able to deliver for our customers. This year is no different. We've been doing this magazine for three years now, and every year it seems to cover just that much more in terms of markets and capabilities. This is a great reflection of our ability to meet the needs of our customers while navigating changing market conditions.

2014 was a story of opposites. When one market was open, or one sector issuing, another one closed. Overall, deal volume was on par in most markets and there were more deals on the go, reflecting customers' changing demands. Frequent Issuers dominated the bond market, with only a few corporates issuing late in the year. Interesting to note was the high level of university funding in the A$ market, positioning the domestic market as a viable funding option for the sector. In addition to universities, the A$ market saw the entrance of multiple BBB issuers and was quite receptive to these deals.

This year told a good story on cementing our offshore capabilities. Australia is still our dominant market – supporting our Australia and New Zealand client is at the core of NAB's strategy. However, in the US we saw renewed activity in 144a, RMBS placement, and new activity in hybrid capital. The UK also saw strong growth in Euro and Sterling denominated bonds, increasing awareness in our issuer client base. In Asia our bond issuance has increased year on year. A lot of that is thanks to our work on the team, bringing in new capabilities and products. Zero coupon callable and CNH deals were significant additions to our activity in Asia.

We continue to play a leading role in deepening the Australian Corporate Bond Market as a key pillar of funding Australia's future. This year we launched our Debt Securities Handbook - a key educational piece to help investors understand fixed interest as an asset class. We continue to drive both supply and demand sides of the bond market and education remains the key - hence pulling together this magazine each year. We also now have a solid media profile on Sky Business with Mark Todd from *Your Money, Your Call* joining the team in 2014. He hosts many guest speakers from NAB and the industry and presents an insightful show for viewers.

NAB is playing a key role in the infrastructure space and this market is becoming more important every year. We hold a solid position in Australia in the project space having been on six of the last seven PPPs in 2014. The global renewables market is also gaining strength and there's quite a bit of interesting work happening where we can play a leading role supporting our customers.

We've also been on the forefront of the Social Impact Investment market in Australia. We've been busy developing new products that we hope will come to market in early FY15. We've been working with governments and private sector organisations to fund social services. There's a growing gap in funding and NAB can play a pivotal role in identifying new models that are sustainable and tailored to these customers. In order to promote our credentials and the importance of building this market, we held a roundtable in September with some key industry leaders. I can't wait to see us make further progress next year, and hope to see NAB leading the development of this in Australia.

All these topics and more have been touched on in this magazine and I hope you enjoy reading it. As we enter 2015 we see continued volatility and uncertainty with geopolitical risks and slowing growth presenting challenges for our customers. We will continue to listen to your needs and tailor our solutions in order to provide the best outcome for our customers.

NAB thrives in finding new opportunities for customers where others tend to see barriers, and I look forward to seeing where this next year takes us.

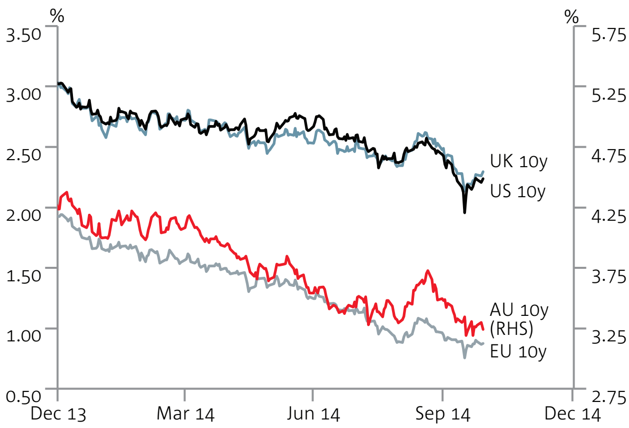
Rates and credit markets

Geopolitical concerns and weakening economic growth continued trends from last year into 2014

Rates highlights

The rates markets began 2014 with an expectation that the FOMC would complete tapering by 4Q14 and bond markets would end the year higher in yield. While the FOMC has indeed completed tapering and US economic growth has improved, bond yields are currently trading between 80-100bps below levels seen at the start of the year. Factors which have driven bond markets include subdued inflationary pressures, heightened geo-political risks, weakening European and Chinese growth and a search for yield. Volatility has remained low for most of the year, but more recently a correction in equity markets, the ECB announcing another round of QE and the Ebola crisis have contributed to an increase in trading ranges. With Australian economic data remaining on the weaker side of expectations (excluding the housing market) the Australian rates market has out-performed its peers (ex Bunds).

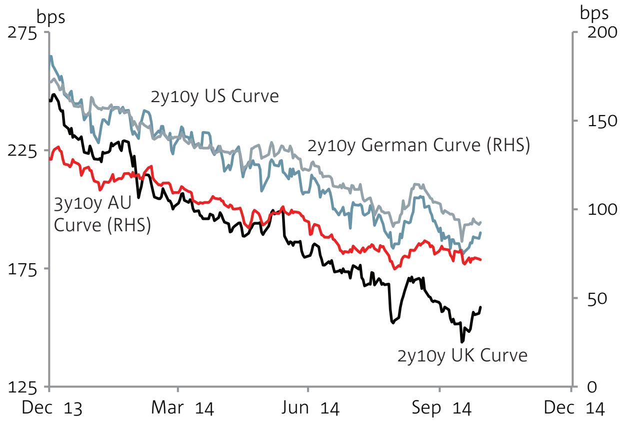
Global bond markets have rallied through 2014



Source: Bloomberg

Yield curves are generally flatter with investors maintaining expectations that at least the FOMC and BoE will begin tightening monetary policy in 2015. Investors, however, remain unconvinced about the FOMC's projected path for the FOMC funds rate which currently puts the FOMC funds at 3.75% by 2017. More recently concerns around the European situation and the impact of a higher USD has resulted in the market revising down the projected path for the FOMC funds rate which is currently priced around 1.34% by the end of 2016.

Yield curves have flattened through the year

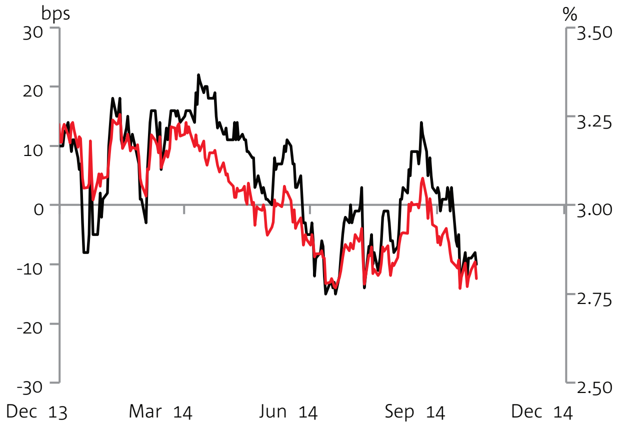


Source: Bloomberg, NAB

Subdued economic conditions kept the RBA on hold

Australia's economic conditions remained mixed in 2014. Net exports became a larger contributor to growth and house prices have risen but domestic demand has remained soft with real household income declining. In addition fewer jobs have been created. Against this backdrop, the RBA has left the cash rate unchanged at a record low of 2.50% and cash rate pricing expectations over 12 months has ranged between -15bps and +22bps. By 2H14 the 3y Government bond was trading back near the cash rate while the 3y swap yield reached a new record low of 2.725% (in mid-July). In a backdrop of an unchanged cash rate and record low swap yields, corporate hedging activity has been sporadic. This has helped to keep swap spreads in a relatively tight range (ie 9 to 25bps for 3y and 27 to 45bps for 10y).

RBA pricing expectations contained in a - 15 to + 22bps range



Source: NAB, Bloomberg

2015 outlook

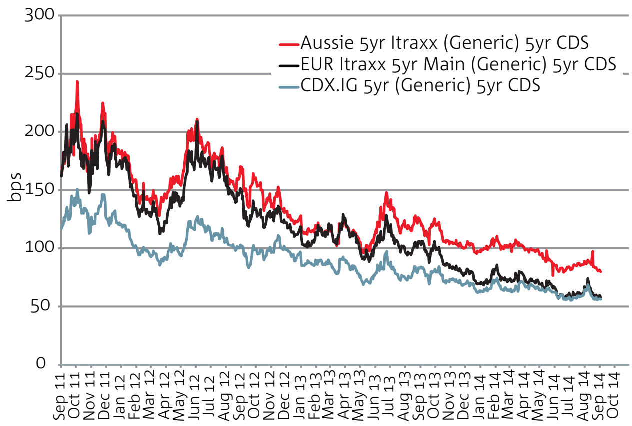
Rates markets are expected to be higher in yield in 2015 as we approach the start of the FOMC tightening cycle and the ECB balance sheet expands under QE. The 10y US Treasury yield is expected to trade in a 3.00% to 3.50% range for most of 2015 while the 10y Australian bond will move towards a 3.70% to 4.25% range. Shorter dated yields will be anchored by an unchanged cash rate for most of 2015 and so the rise in global yields should work to steepen domestic yield curves. A flattening bias will only become evident later in the year as the market begins to price in the start of the RBA tightening cycle. We see the 3y10y Australian bond curve in a 90 to 110bps trading range with the 3y10y swap curve in a 105 to 125bps range. Against this backdrop, our bias is for swap spreads to continue to range trade with 3y swap spread contained in a 25 to 35bps range while 10y swap spread should trade in a 35 to 45bps range. The diverging economic conditions between Australia and the US are expected to persist for most of 2015 and so 10y AU-US bond differential will narrow towards 70bps.

Credit market highlights

Ample liquidity and a search for yield in a low rate environment pushed credit spreads further tighter through much of 2014, continuing the trend established since 2012. That said, the degree of spread tightening slowed in the second half of the year, even mildly reversing from September as a confluence of geopolitical concerns, economic growth worries (particularly applying to Europe, China and possibly also Japan) and the Ebola outbreaks saw global credit spreads nudge higher. The Australian credit market was no exception and spreads across most corporate credit sectors followed the global trend.

Within the credit derivative market, Credit Default Swap (CDS) spreads were quick to respond to the rising risk-aversion and indices observably widened across Europe, the US and Asia-Pacific, breaking out of what had been a steady year-long tightening trend. But, despite the recent widening, indices are still at relatively tight levels and the major investment grade indices within 10-15bps of the post GFC tights.

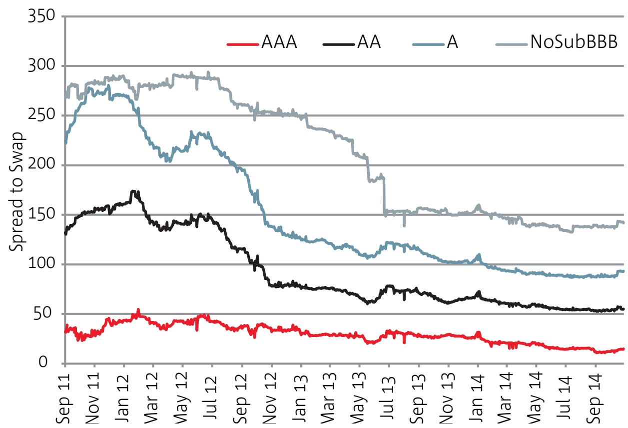
Credit Default Swap regional indices



Source: NAB Credit Research, Bloomberg

As is often the case, physical cash bond spreads were far slower to respond. Again though, while pushing most spreads off post GFC lows, the recent sell-off still left credit spreads at comparatively tight levels. While the recent degree of risk aversion has seen investors reluctant to add aggressively to positions and chase yields lower, that has been balanced by the longer term dynamic of a weight of money seeking the higher yield offered by corporate bonds.

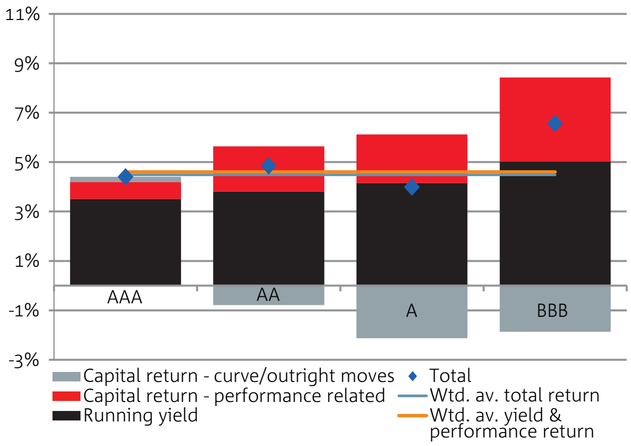
AUD Corporate Credit Spread to Swap (3yr duration)



Source: NAB Credit Research

The yield chasing theme was also reflected in the outright bond sector performances over the year. As displayed in the chart below, the higher yielding BBB rated sector has outperformed, with total returns boosted not only by the higher running yield offered, but also by further capital appreciation as investors chased the higher yields.

Total returns by sector



Source: NAB Credit Research

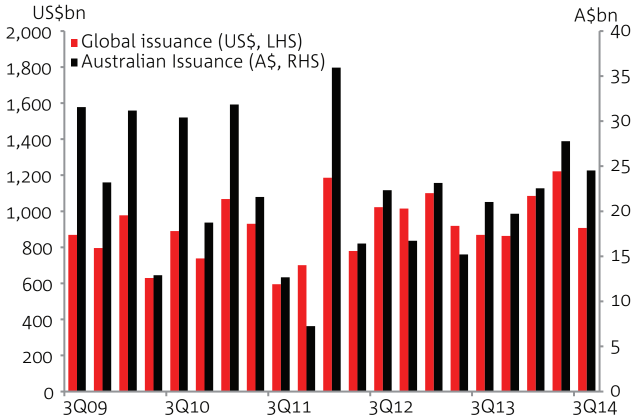
While there was a noticeable spread widening from September, perhaps a larger impact for global credit markets was a rapid drying up of liquidity. Corporate primary bond issuance almost stopped during several weeks in October and secondary market bond trading, which had already been at comparatively low levels, also fell further.

But that period had followed on from what were very strong conditions earlier in the year. In fact the calendar year second quarter global issuance was a record US$1.22tr (equivalent) and followed on from what was also a very strong first quarter.

The Australian corporate bond market remains solid

The Australian market also saw solid levels of corporate bond issuance. A notable feature of the local market was the re-emergence of solid issuance from offshore kangaroo issuers, while ‘true corporate’ (non-financial institution) issuance is falling below prior year levels. Rather than reflecting any investor reticence, the lower true corporate issuance reflects a lack of supply, driven by corporates’ ongoing reluctance to invest and to borrow. Indeed those non-financial corporate deals that have entered the market this year have generally been very eagerly taken up by investors. Additionally, further evidence of the positive development of the Australian corporate bond market was provided, with a number of smaller and unrated issuers successfully pricing inaugural deals during the year.

Corporate bond issuance global and Australian 2015 outlook



Source: Bloomberg, NAB FICC Credit Research

2015 outlook

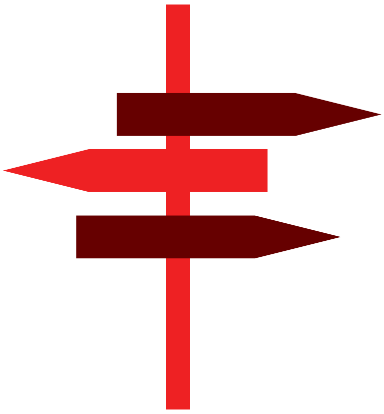
With corporations still reluctant to invest, debt issuance from both corporations themselves and the banks that fund them is expected to remain constrained. The US may well prove to be the bright spot in 2015 and there will be some expectation for rising investment - and the debt issuance required to fund it - there. But the outlook for European (and Australian) originated issuance looks to be something of a repeat of 2014. For the Australian market, that wouldn’t be disappointing in a broader sense - issuance after all was a very healthy A$95bn. It was however buoyed by returning kangaroo issuance and the current trends would suggest that it will be that sector that largely determines the level of primary issuance seen by the market in 2015.

But, it can also be expected that, short of a sharp credit shock event, investor demand for diversity and for yield will continue. While the latter driver may be a waning influence if the US economy markedly accelerates, we expect investor demand for quality corporate paper to remain very strong. Deterioration in risk appetite and lengthy continuation of the periods of market disruption evident in September and October would obviously threaten that scenario, but that is not our current expectation.

With some constraint on issuance supply expected, and investor demand anticipated to remain strong, we see the compression pressure on credit spreads remaining. Nevertheless, investors have increasingly shown reluctance to push spreads ever-tighter and it could be reasonably suggested that current levels are towards the tighter end of what may be a relatively narrow trading range for the next six to twelve months.

Australian Bond Market

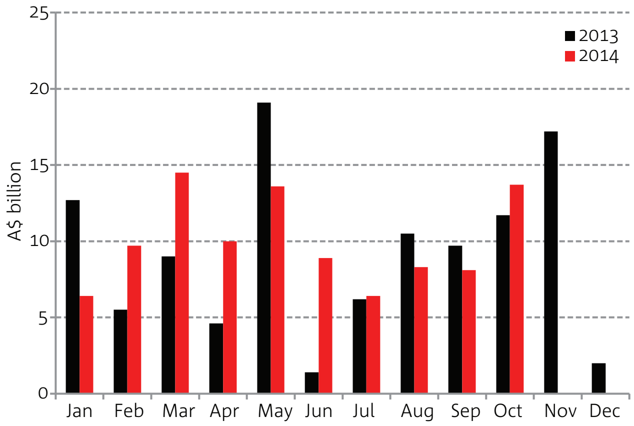
A diverse range of issuers entered the market to overcome a slow start to the year



In a year characterised by geopolitical risk and concerns about slowing global economic growth, the Australian bond market continues to provide a stable platform for domestic and offshore issuers to access Australian dollars.

The relatively stable conditions allowed for a steady flow of issuance with the market pausing from time to time allowing investors time to digest the regularity of supply. Overall issuance volume has risen to ~A$100 billion vs. A$90 billion in 2013 (as at 31 October).

Monthly issuance volume



Source: Bloomberg

Financials

One of the year's highlights was the diversity of financial issuers who have visited the Australian dollar market. As expected, Financials were the largest contributor with 42% of total issuance. It was excellent to see a good representation from European and American kangaroo issuers making up more than 10% of issuance, and a number of debut entrants to the A$ market.

Foreign branch ADIs also featured heavily; a theme which continued this year as European, Chinese and Japanese bank branches build out their curve in Australian dollars.

In high grade, Sovereign, Supranational and Agency (SSA) issuance persisted, as the basis pick up continued to support European issuers, particularly in the longer end of the curve.

Covered Bonds

Although covered bond issuance in Australia remains infrequent, the diversification value and conducive pricing evident this year has promoted financial borrowers to access this source of funding. Investors have shown solid appetite for low beta, highly rated covered bond transactions in the face of increasing volatility. Activity in the AUD covered bond market has been dominated by the local major banks in 10-year maturity, with only Suncorp (5-year) and two Kangaroo borrowers (RBC & TD) registering covered bond transactions in 2014.

Non-financial corporates

It took until late February for the non-financial corporate market to open and it was not until May, when the gears really started turning.

A key theme in 2014 has been a lack of supply, with corporate transactions seeing heavy oversubscription and significant price tension.

It was pleasing to see the university sector take A$450 million out of the market, positioning the domestic market as a viable funding option for the sector going forward.

The 7yr tenor has become the sweet spot for corporate issuers accounting for over 50% YTD, with a number of investors indicating that they would support even longer trades if shown the right credit and price.

The BBB rated band has been well supported and this demand drove several debut entrants to the market. This year also saw its first sub-investment grade A$ corporate transaction lead by NAB. NEXTDC raised A$60 million in 5yr funds, and the market seems to be much more receptive of these trades, with Qantas and G8 Education both returning with successful transactions. The other most notable transaction was from AGL Energy which issued the largest ever BBB band corporate transaction in Australia.

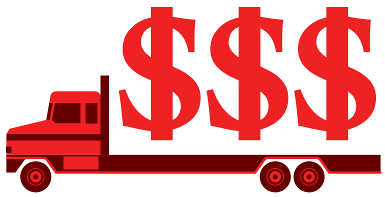
Credit spreads

The first half of the year saw credit spreads steadily grind tighter, as markets seemingly brushed aside any negative sentiment driven by geopolitical risk or news that the US FOMC would begin tapering its bond buying program. Issuers took advantage of this and issued into what was a very conducive market.

However in October the market eventually backed out as the negative headlines persisted and the risks from the Ukraine, Middle East and the Ebola outbreak widened. A period of subdued issuance then followed as spreads pushed wider across most segments.

More recently we've seen some stability allowing primary issuance to resume however an element of fragility still exists.

The ASX-Listed Hybrid Market sees interesting developments in 2014



Financial Issuers dominate total volume in the ASX listed market

The listed market in 2014 has been dominated by banks and insurers bringing both new and rollover money into regulatory capital issuance at a volume of just over $7 billion in total. This volume represents a total of seven transactions across major Australian banks ANZ, CBA and Westpac and names such as Suncorp, Bendigo Bank, Macquarie Bank and Challenger Limited. In contrast, a continued lack of supply in Corporate issuance continues to be an ongoing theme with the only Corporate activity seen from Bentham IMF that priced its $50 million senior bond issue in April 2014.

In terms of diversity within the Financials, the bulk of the total year's volume took the form of Tier 1 capital issues. A majority of the primary Tier 1 issuance was seen in September when four Australian financial institutions priced an aggregate of over $4 billion - the bulk of which came from CBA's $3 billion PERLS VII issue.

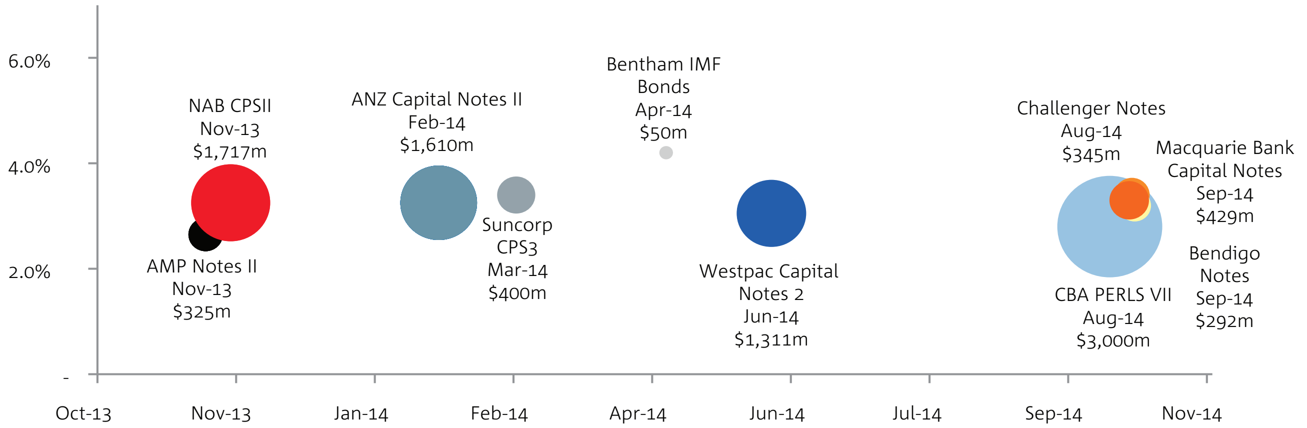
Over the course of the year, secondary trading spreads for listed capital issues tightened considerably as investors continued to hunt for yield in a market where returns on cash remain at extended lows and equity values are being exposed to higher volatility. Further, the continued growth seen in mandatory superannuation volumes continues to underpin growth in demand looking for investment in diversifying alternative asset classes.

Hybrid instruments experience sell-off on the back of reduced liquidity conditions

A trend of margin widening became apparent from the month of September as heightened market volatility was felt across various markets. This reflected emerging uncertainty and investor risk-aversion which saw a subsequent sell-off across multiple asset classes including listed Hybrid instruments. We saw this as primarily a liquidity issue as opposed to any real broader credit concerns. Consequently, we expect to see a return to a tightening bias in Secondary trading margins as we head to the end of the year and into 2015.

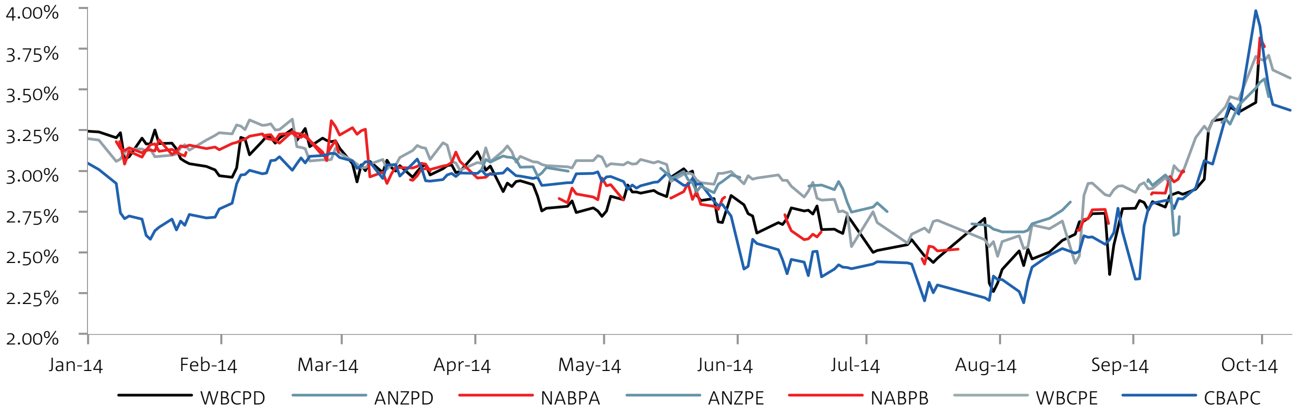
The large volume of issues in September led to a similar shortage of liquidity and 'indigestion' in the market that we saw in early 2012 when a similar amount of issuance ($4.2 billion) was announced within a week. Such a volume would seem to remain a broad maximum for the A$ listed market over a short period, although it is noted that normal liquidity returned to the market within 6 weeks in 2012, and that a similar period of recovery would seem likely in 2014.

Total ASX-Listed issuance for FY2014



Source: Bloomberg

Trading margin recovery begins



Source: Bloomberg

2015 outlook

Financial Issuance is expected to continue in 2015 with new money transactions the expected trend after a large capital refinancing year in 2014. The Australian market continues to display a broad appetite for Corporate issuance given the high concentration of Financial issuance and, consequently, the limited opportunities to diversify in the fixed income product space. We believe any new issuance will be met with supportive market conditions given spreads continue to remain low comparatively on a historic basis and the ongoing growth in demand for yield and diversification.

US High Yield Market

The US High Yield market offers Australian Corporates strength and flexibility

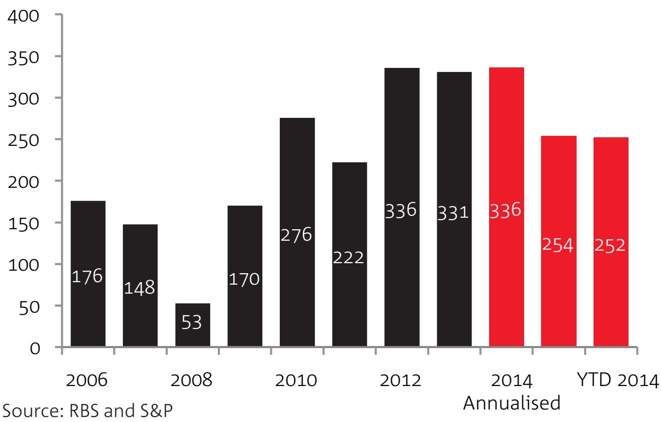
The US High Yield markets have had a phenomenal year and Australian corporates have accessed both the 144a High Yield and US Term Loan B markets throughout 2014. Both markets continue to offer attractively priced, highly flexible and long tenor financing solutions for a broad range of Australian corporates.

Demand outstrips supply

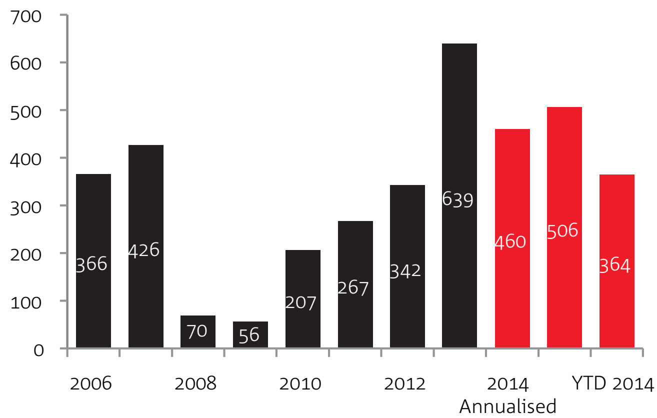
Both the US High Yield 144a bond market and US Term Loan B market spent the majority of the year with investor demand outstripping issuer supply yielding a mostly issuer friendly environment.

Whether you were an issuer or an investor, 2014 had something for everyone. Fund flows were strong in the first half of the year providing borrowers with strong support for transactions driving oversubscriptions and lower yields. July was however a turning point. Volumes weakened as we saw retail outflows driven by geopolitical concerns and potential for US rate increases. Yields increased for investors prepared to buy opportunistically.

US High Yield New Issue Volume (US$b)

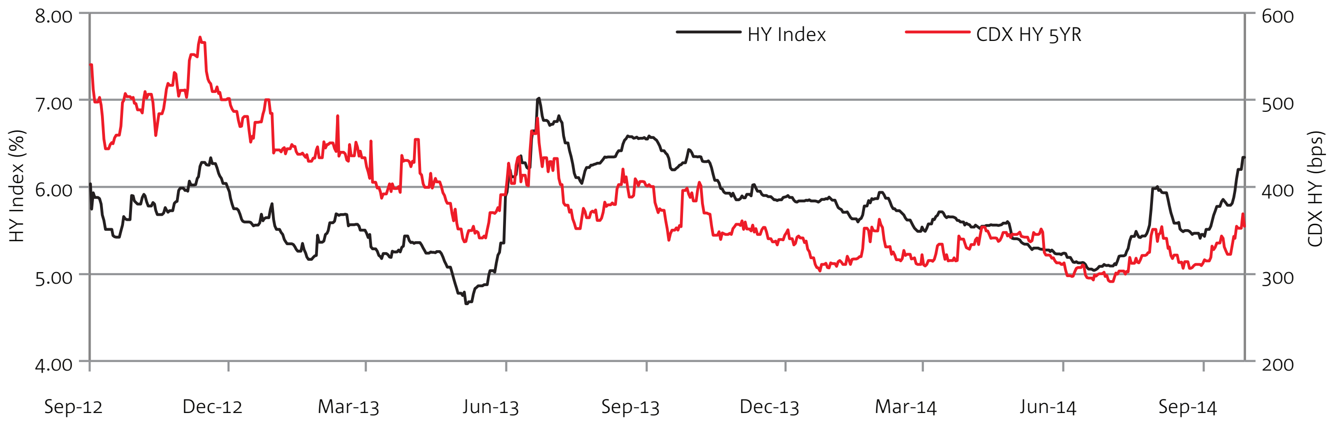


US Leveraged Loan Issue Volume (US$b)



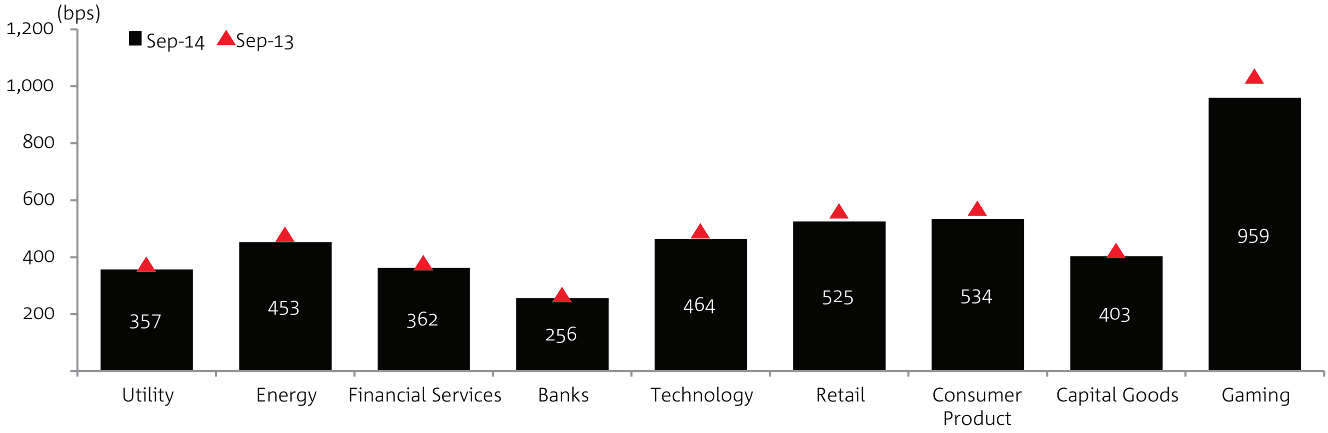
Source: RBS and S&P

Timing was of the essence to yield desired transaction levels



Source: Bloomberg

Average High Yield Spreads (by sector)



Source: Informa Global Markets via Bloomberg

We started the year recovering from the Fed's "Taper Tantrum" and fear over higher US rates in the summer of 2013 and ended the year with resurfacing US rate concerns, a tepid stock market and rising geopolitical tensions. Mid-year we entered a period of brief volatility spikes and "risk off" situations which helped keep spreads from declining significantly year on year.

Australian borrowers

US High Yield Bonds and TLBs offer Australian non-investment grade corporates an alternative to the traditional Australian bank loan market, allowing borrowers to tap the largest and deepest global debt market in the world, offering competitive pricing, looser covenant packages, lower amortisation and longer debt tenors.

There continues to be strong investor appetite, specifically for Australian leveraged issuances because:

- Australia offers a mature legal system within direct exposure to China and other emerging economies
- Australian debt provides geographic diversification for debt investor portfolios

The strength and flexibility of this market for Australian borrowers has been clearly illustrated in the Australian US high yield discussion paper released by Moody's in August 2014, in which the agency noted that the number of Australian HY rated issuers has increased tenfold since 2011. Similarly the portfolio of Australian USD HY debt has likewise increased tenfold to USD$20.5 billion over the same three year period.

NAB/RBS alliance

Recognising the need to provide an efficient product offering to our Australian clients, in 2014 NAB and RBS entered into an alliance in 2014. This alliance covers US Dollar Leveraged Finance products to combine strong relationships with high quality execution in US dollar markets.

The Alliance leverages RBS' product expertise and distribution capabilities to bring a strong product offering to NAB's Australian corporate clients. The Alliance presents practical financing for borrowers looking to access long term flexible USD capital. We believe this is a valuable additional channel for borrowers providing:

- Access to a broader product spectrum without the need to expand the number of banks
- Retain NAB as a trusted relationship bank – gain RBS as a trusted advisor
- No incremental cost compared to transacting with a third party
- Combined RBS and NAB client and product knowledge ensures best in class execution

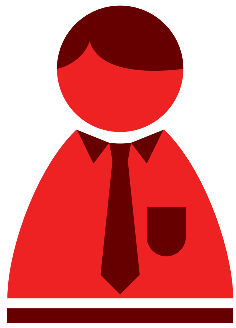
2015 outlook

Despite the periods of market turbulence and the constant threat of higher US yields, credit market fundamentals continue to provide underlying support for range bound spread levels in general. Corporate earnings have been strong including earnings reported so far through September 2014.

Outlook remains for a stronger US economy in 2015 coupled with low default rates and corporate earnings that continue to grow by approximately 10%. The wild cards in the near term will be the impact on the US markets from continued sub-par global growth and whether a consistently cautious (dovish) Fed turns into a more aggressive (hawkish) one.

Bringing customers to customers

2014 sees NAB focus on connecting issuers and investors through product innovation



A large focus for NAB has always been to consider how we could meet issuer requirements within the Basel III borrowing environment. We have also had to recognise that though the term deposit suite has developed into an asset class in its own right there hasn't been enough diversity in lower risk investment opportunities. Therefore we need to create investments that could meet with the investor desire for lower volatility – higher ranked fixed income alternatives.

Customers to customers

At NAB we have characterised this development as bringing Customers to Customers. The understanding to have longevity for our issuers means NAB needs a robust investor wealth pool investing in fixed income. In January 2014, Bendigo and Adelaide Bank launched a subordinate note offering. As part of the origination process we approached the client about the prospect of engaging our substantial sub-institutional investor base. The positive response from the client was based on the premise that as an issuer, the customer was unlocking potential new investors and those investors could become long term supporters of the organisation. The result was that when the issue was closed, our sub institutional investors represented 36% of the total investment.

Over the next few months we continued to work on our education message and worked with our investors to understand the possibilities of the Over The Counter (OTC) fixed income market in Australia. The education narrative covered different bond structures, covenants, issuer communication, and credit research. This education didn't just include investors and issuers, but our bankers as well.

Product innovation

In June NAB launched the first unrated senior unsecured OTC Bond on behalf of NEXTDC. This bond was a ground breaking initiative bringing together investors, NAB asset financing experts, and risk managers all working to create a total capital solution for a new to NAB client and an appropriate investment to add to our customers portfolios. The issue was a Senior Unsecured, 5 year non call 2.5 years with an 8.00% coupon and a 1% per annum make whole. The sub-institutional investor base responded to the opportunity by accounting for 82.5% of the A$60 million issued.

Our Debt Market Origination team were able in part to leverage off our expanded client base when they went to Members Equity Bank to discuss the possibility of a new subordinated debt offering. Members Equity Bank, like Bendigo and Adelaide Bank, was able to recognise the value of our differentiated investor base as a benefit to growing a new tier of investors. Members Equity Bank issued a 10 year non call 5 at BBSW +2.70% and the sub-institutional investor base represented 60% of the A$300 million issued which was a huge increase on the 36% derived from the Bendigo and Adelaide Bank issue.

2015 outlook

Though there could be some claims that the growth in investor numbers was based on the chase for yield, the strongest driver in our opinion was the benefit of educating clients prior to any issuance. The growth in investor engagement in subordinate notes and unrated covenant protected bonds has been as a result of consistent education commitment with our distribution partners. Volumes in the OTC market for NAB doubled last year and we expect the similar amount of growth again in 2015.

With 2015 looking like a volatile year we will expect to see this growth accelerate as customers continue to look for investments that meet the investor demands for low volatility to diversify portfolios.

A new funding model for local government

Changes recently made to the financial sector's Basel III rules are making it increasingly expensive for councils to borrow from banks

Historically, local councils in Victoria have accessed bank loans for their financing needs. As no Australian council has ever defaulted on a loan, banks have considered lending to local councils as being particularly low risk. However, as Director of Institutional Product Development at NAB, James Waddell explains, this became a problem.

Given the safe nature of these borrowers, banks have previously provided very long dated loans to councils. But under new Basel III rules, banks are now required to 'match fund', that is match a long term loan to a council by borrowing for a similar period themselves, which has made borrowing from banks more expensive for councils.

The Municipal Association of Victoria (MAV) approached NAB to work on delivering a solution that would provide an optimal outcome for their members – and from this, the Local Government Funding Vehicle (LGFV) was created.

A simple concept

The LGFV is a trust that makes loans for councils while issuing bonds for investors that finance them. The bonds are provided on equivalent terms to the loans, such as having the same maturity dates, and while the loans are not rated, the bonds carry a credit rating of Aa2 from Moody's investor services. That's a better rating than those of major Australian banks, so Victoria's local councils can now borrow debt at a lower cost than before.

This new borrowing model will create efficiencies, reduce the borrowing costs of local councils and, as it has in other jurisdictions, open up new avenues for local government finance. The money saved by councils will create an opportunity for councils to reduce their council rates and/or free up cash flow to reallocate to community services.

But it seems the biggest mystery about the LGFV so far is why it's taken so long for the concept to be applied in Australia. This type of funding structure already exists overseas in countries such as New Zealand, Canada, the UK and Scandinavia. Lenders such as Kommunalbanken in Norway have a public policy mandate from the central government, so they've been providing low cost finance to the Norwegian local government sector since 1926. While in New Zealand, the Local Government Funding Agency has been lending to councils since incorporation in 2011.

Working side by side with the Commonwealth Bank (CBA), the Municipal Association of Victoria (MAV) and Ernst & Young, NAB and its related entities acted as arranger, lead manager, Trust Manager and Trustee in establishing the LGFV program. And while Victorian local councils have taken the first step with the LGFV, the door's now open for other states to establish similar programs. Through their Treasury Corporations, state Governments in Queensland and Western Australia have acted as a lender to the local government sector in their respective states, but this approach comes with its own issues. We look forward to discussing the brave new world with them.

The LGFV issued 5 and 7 year bonds at pricing which was 10 basis points inside that of the major banks borrowing curve. This was evidenced by ANZ borrowing at Swap plus 85 the same week, the LGFV borrowed at swap plus 75 two days later.

The investor reception was very strong with many accounts spending considerable time understanding the bond documentation. In the end fifteen accounts participated and we expect that many more will join them as the program grows in size.

As a leading lender to the local government sector as well as a market leading debt capital markets house in Australia, NAB has a team of specialists that can develop funding and investment solutions for businesses and investors.

The higher education sector emerges as a new borrower in the market

Low nominal interest rates and strong credit ratings combined with Basel III rules are making it attractive for Universities to borrow from capital markets

Historically, the Australian higher education institutions have relied on funding from government to provide new facilities. However, recently, government funding for new infrastructure has dried up. As a result, a number of universities have accessed capital markets and bank loans for their infrastructure financing needs. And in recent times, NAB has been arranger of three of the last four public debt issues to Australian universities including Universities of Wollongong, Sydney and Melbourne.

Simultaneously, the higher education sector is experiencing a period of substantial change, increased competition and a desire by vice chancellors to ensure their institutions prosper by offering the facilities and experiences expected by students now and in the future.

Some aspects of the federal budget supported by the sector, including fee deregulation, will have an untested impact on the sector; while the demise of the Higher Education Endowment Fund has withdrawn A$500 million (annually) of funding for capital expenditure from the sector has had an immediate negative impact on funding available for capital works.

An educational arms race

In this environment universities are engaged in an educational arms race with the primary weapon being new and improved buildings and facilities. The arsenal includes specialised research facilities used to attract world renowned academics, the best students, research funding and philanthropic contributions. Universities are also building student accommodation facilities to provide students with “a first year experience” on campus as a cornerstone of their offering.

Universities are also progressing “self funded debt” opportunities – these include building and letting buildings to external tenants, creating business parks and other commercial precincts.

Universities are generally lowly geared and highly rated, benefitting from support and strong links to government making them attractive candidates for lenders.

Opportunities exist in the market

Given the growing funding opportunities combined with low credit risk, a significant opportunity exists for debt providers to the sector.

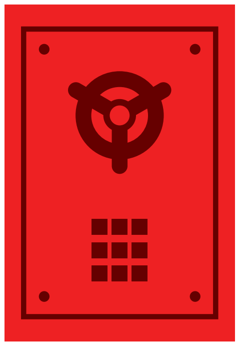
Sydney University (Aa1 Moody’s) approached the market in April and priced a debut $200 million seven year transaction at swap plus 88 basis points. Demand for the issue was strong and the book built to over $600 million in the space of three hours.

Melbourne University (AA+ S&P) followed in June and priced a debut $250 million seven year transaction at swap plus 80 basis points. Demand for the issue exceeded expectations at $750 million despite the tight pricing.

Monash University (NAIC-1) has earned the distinction of being the first Australian University to borrow in the offshore markets. In November Monash priced a debut A$150 million (equivalent) twenty-five year US private placement at UST plus 120 basis points. The placement was heavily oversubscribed by investors with bids received in excess of 3 times the volume sought (at the clearing spread).

As a leading lender to the higher education sector as well as a market leading debt capital markets house in Australia, NAB has a team of specialists that can develop funding and investment solutions for businesses and investors.

Securitisation in 2014, with NAB making it a hat trick for House of the Year

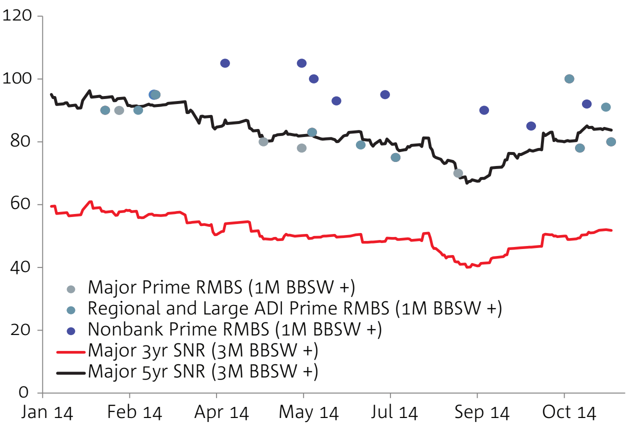


NAB leads a buoyant Securitisation Market with strong investment demand a driving theme throughout the year

Mirroring last year, investment demand for Australian securitised debt opened strongly in 2014 with domestic and offshore interest driving strong issuance volumes and spread contraction during calendar Q1 across a range of Bank and ADI RMBS issues.

This theme gained pace during Q2 with a large number of deals coming to market, 38% up on Q2-2013, and a milestone break-through the 80 basis point level from a major bank RMBS issuer. Investment appetite was strong both across asset class and capital structures with continuing support by domestic and offshore investors searching for diversification and yield. For senior RMBS tranches books were underpinned by a strong balance sheet bid as domestic banks sought to stockpile eligible collateral in readiness for the January 2015 commencement of APRA's Liquidity Coverage Ratio and the associated RBA Committed Liquidity Facility.

Spread relativity: Prime RMBS to three and five year Bank Senior Unsecured



Source: Bloomberg and NAB

Q3 conditions saw no signs of change with books remaining well oversubscribed and pricing contracting to post-GFC lows across names. The frequent question, "how much tighter can prices go", soon being answered by a spike in volatility with global growth concerns and Ebola headlines weighing on markets. The Australian itraxx index pushed out from high 70's to 106-107 during October but towards the back end of the month with primary issuance recommencing.

NAB has arranged and led the majority of securitisation deals to market. We continue to be recognised by our clients as being the leading house in the Securitisation market with the strongest rankings in overall quality of service. Our team is recognised as being the most proactive with new ideas with the strongest product specialists across a broad client base (Peter Lee Associates, 2014) and for the third year in a row has been recognised by industry participants as the Securitisation House of the Year (KangaNews).

2014 AU securitisation league table

Bookrunner	A$m	No. deals	Rank
National Australia Bank	**4,626**	**21**	**1**
ANZ	2,919	11	2
JP Morgan	2,462	9	3
Westpac	1,188	6	4
Macquarie Bank	1,041	4	5
Deutsche Bank	919	5	6
Commonwealth Bank	562	7	7
Morgan Stanley	250	1	8
RBS Australia	249	2	9
Jefferies	206	2	10

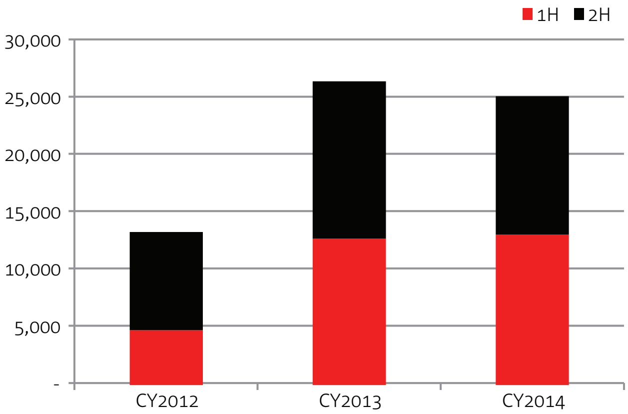
Source: KangaNews, 2014 AU Securitisation League Table, (including AUD and foreign currency tranches – Excl. self-led deals) – 15 Oct 2014 + Pepper Prime 2012-1 AR-u

RMBS

RMBS continues to represent the bulk of the Australian securitisation market, with over A$25 billion (equivalent) in public issuance across a total of 31 deals as at the end of November.

With a handful of further deals anticipated to close prior to calendar year end, total public RMBS issuance is expected to exceed that of 2013 (A$26.35 billion equivalent).

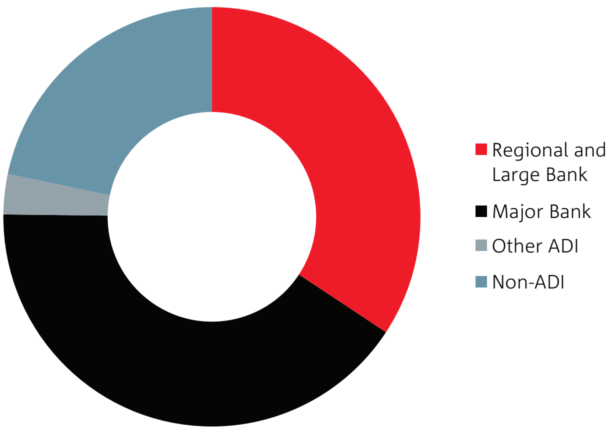
Public RMBS issuance volumes



Source: NAB as at 31 October 2014

All RMBS issuer classifications have been active during the course of the year with the exception of the Credit Union sector although issuance is anticipated during Q4 and during the first half of 2015. While year on year issuance is expected to be slightly up, half on half year comparisons show reasonably comparative issuance volumes across 2013 and 2014.

2014 YTD issuance volume by issuer type

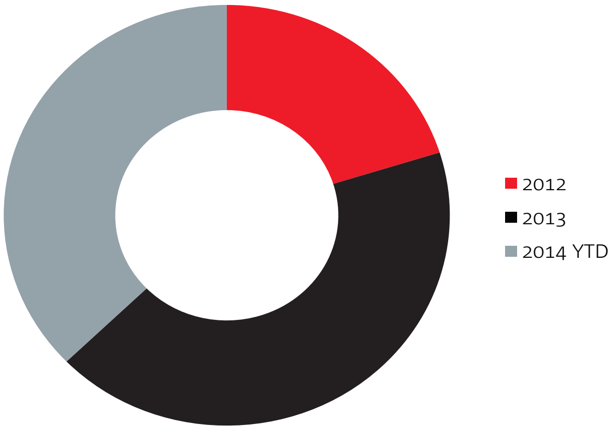


Source: NAB

Spreads tightened throughout the year and of note, the pricing relativity between Major Bank RMBS and Regional and Other Large Banks narrowed, with other ADI and non-ADI issues also experiencing contraction.

The proportion of prime and nonconforming RMBS public issuance as at the end of November has been consistent with 2013 at around 7% respectively, with outright volume slightly up at just over A$2 billion. Further nonconforming issuance is not expected until early 2015. We anticipate 2015 will see a year on year increase in issuance volume.

Public nonconforming issuance



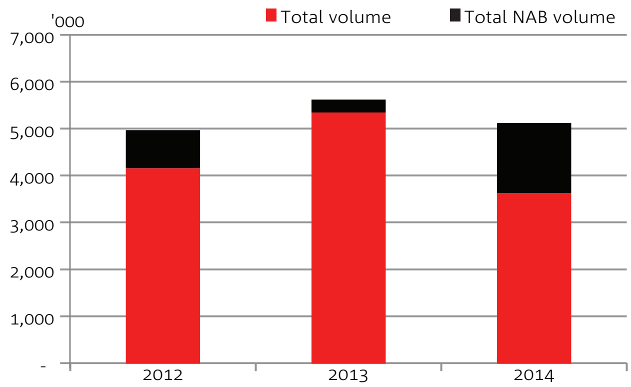
Source: NAB

Another consistent year on year theme is the issuance by well-known non-ADI names in USD 144a format providing for greater diversification across their investor base. We expect issuers will continue to invest in diversification with opportunistic transactions during the course of 2015.

ABS

A smaller subset of the total securitisation market, Australian ABS transactions are typically strongly supported by local and offshore investors seeking asset diversification. Regular auto issuers including Macquarie-SMART and Bank of Queensland-REDS EHP along with consumer finance issuer Flexigroup-Certegy returned to the market during 2014, multiple times in the case of Macquarie-SMART, including issuance in USD and EUR.

Australian ABS issuance A$ equivalent



Source: NAB

2014 also saw FleetPartners return to market with it's late November launch of FP Turbo Series 2014-1, being the first Australian ABS deal to include operating leases. The transaction upsized to A$277 million from a A$200 million launch, pricing on 27th November.

Total year to date issuance for Australian ABS, including FP Turbo Series 2014-1, stands at just over A$5 billion equivalent across 7 deals, slightly below 2013 levels.

Structural innovation

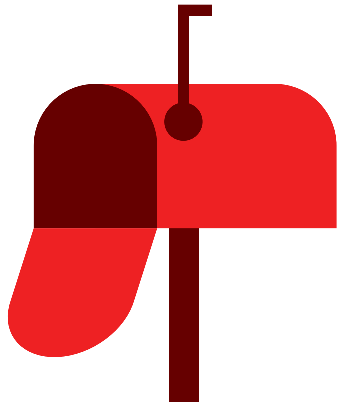
While simplicity in structure is a key objective for issuers it is broadly recognised that the ongoing need for diversification and sustainability is dependent on continued innovation in structuring techniques. In the absence of master trust programs, the inclusion of non-AUD soft or hard bullets (supported by a committed redemption facility) can be used to achieve a number of objectives including: enhancing investor diversification via USD, EUR and GBP offerings, reducing balance guarantee swap costs, preserving domestic investor issuer limits; structuring to desired WALs, creating price tension, and mitigating extension risk. Controlled amortisation tranches have also been included to achieve like objectives, most recently via non-ADI issuer RESIMAC's Premier 2014-1 issue which included a USD200 million 2.9 year WAL controlled amortisation tranche.

Research

NAB provides a weekly research offering titled Securitisation Insights, semi-annual review and outlook publications and special articles to ensure our issuer and investor clients remain informed about the Australian Securitisation market.

Agency and Trustee Services

Evolution in the market leads to Agency teams taking on a dynamic role within the relationship



This past year, we have continued to witness the development of market dynamics that have led to factors such as mixed funding structures including tranched senior debt, capital markets issues, Condition Precedent reliant co-funding arrangements from JV equity, trust structures, and Export Credit Agency lenders. In addition, we are seeing continual structural change from the lender side, including new offshore bank participants mainly out of Asia; and high grade buy and hold fund investors, such as superannuation funds looking for longer term cashflows in the senior parts of the capital structure.

The number of distressed transactions has fallen away, reflective of banks' provision levels, and as result we are seeing a reduction short-term special situation fund investors. We are also seeing these changes play out in both the primary and secondary markets. One of the benefits of this evolution is that we are seeing greater levels of liquidity, at least based on volumes of substitutions, although we note that certain lenders are less relationship focussed than others, potentially leading to stress at the times its needed the least.

In addition to the above, we are seeing client demand for expanded service levels to include full transaction management covering traditional agency, but also integrating with trustees, transactional banking providers and actively providing cash management solutions to minimise negative carry, but most importantly to reduce operational risk.

For instance, in 2014 we closed real estate construction transactions where our role commenced from financial close, involves management of escrow moneys, construction drawdowns (including relationships with expert third parties), all the way through completion and management of settlements of pre-sales. We also closed a project finance transaction which involved us acting as agent, security trustee and account bank during construction, but more importantly operational cash bank post construction, enabling the client to seamlessly move between pre and post operational phases without having to change banking systems, thereby minimising the associated operational risks.

Benefits of a strong agent

The above dynamics mean that the Agency function can no longer be a passive one. The role demands that agents have a deep understanding of client strategic imperatives, the fundamentals of deals, as well as the characteristics of a syndicate, in particular the motivations of relationship vs investor lenders. Our approach to the business is to use our experience and knowledge of market participants to act as a trusted advisor to our clients, in particular during times of stress or change in strategic direction. In our experience this leads to more efficient outcomes in terms of speed, but also cost savings whenever the advice can lead to better structuring of protocols in documentation, necessitating less re-work later on. We find that our strongest agent/client relationships tend to be at Group Treasurer or CFO level evidencing the importance of the role when done well.

The future

NAB's Agency and Trustee business has taken on a decidedly front foot position. We have continued to invest in our people, but also continue to develop our service offering in a way which complements our clients' needs.

We are harnessing the bank's capabilities, allowing us to morph into a full service transaction manager and are regularly closing and are actively engaged in intercreditor and corporate trustee roles for highly complex transactions, seamlessly facilitating arrangements between borrowers and funders across the capital structure.

Capital management trends within the AREIT sector

The AREIT sector has come a long way in terms of refining their respective capital management structures

Australian Real Estate Investment Trust (AREITs) have led the charge in creating capital management structures characterised by competitive Weighted Average Costs of Debt (WACD) and a strategic approach to establishing extended tenor without incurring a material overall increase to a vehicle's WACD.

A second element to the AREIT capital management agenda sits with interest rate hedging and the structures AREITs deploy to protect themselves against adverse interest rate movements. The motives for AREITs to construct, implement and refine their capital management structures is in part a recognition of two key issues unique to AREITs. First, the nature of AREIT earnings sees revenue

2010-2011

AREIT	Weighted average debt maturity	Average hedge maturity	Average borrowing costs	Hedged percentage	Balance sheet gearing
CFS Retail	3.6	5.3	6.90%	99%	26.70%
Charter Hall	3.5	5.5	7.00%	73%	38.70%
Dexus	3.4	6.1	6.70%	85%	29.10%
GPT	5.1	5.0	6.80%	90%	23.30%
Goodman	3.3	4.6	3.14%	86%	24.50%
ING Office	3.2	3.7	5.10%	75%	13.80%
Mirvac	4.2	5.0	7.40%	64%	27.30%
Stockland	6.2	4.5	5.30%	51%	20.00%

2013-2014

AREIT	Weighted average debt maturity	Average hedge maturity	Average borrowing costs	Hedged percentage	Balance sheet gearing
CFS Retail	3.5yrs	3.7yrs	5.40%	84%	30.90%
Charter Hall	3.7yrs	2.0yrs	4.50%	76%	33.20%
Dexus	5.2yrs	5.7yrs	5.40%	60%	33.70%
GPT	6.0yrs	5.2yrs	4.80%	76%	27.30%
Goodman	5.4yrs	4.8yrs	4.27%	94%	32.00%
Investa Office	5.8yrs	2.4yrs	4.70%	35%	31.50%
Mirvac	4.3yrs	4.3yrs	5.60%	58%	28.50%
Stockland	5.2yrs	4.2yrs	6.20%	59%	25.00%

Source: NAB , Company Reports

and revenue growth having a comparatively high level of predictability given the predominantly fixed nature of rent increases plus the comparatively consistent levels of portfolio occupancy (90%-95%). Secondly, movements in interest rate costs or more broadly financing costs are the one key material element of an AREIT's P&L over which it has the least operational control.

AREITs have in previous periods used Commercial Mortgage Backed Securities (CMBS) and various hybrid instruments as alternative funding sources in addition to bank debt as a means of diversifying the debt profile although in a pre GFC world the motive for diversification was less pronounced. The hybrid instruments were structured and priced to appeal to retail investors but overtime have been liquidated with only a couple still remaining on issue. The CMBS product required a pool of assets to be "ring fenced" and revaluations of these assets did not play through to either reduce or increase the CMBS LVR, hence, not an instrument post launch that allowed issuers to book a gain/loss from the MTM impacts of asset valuation movements.

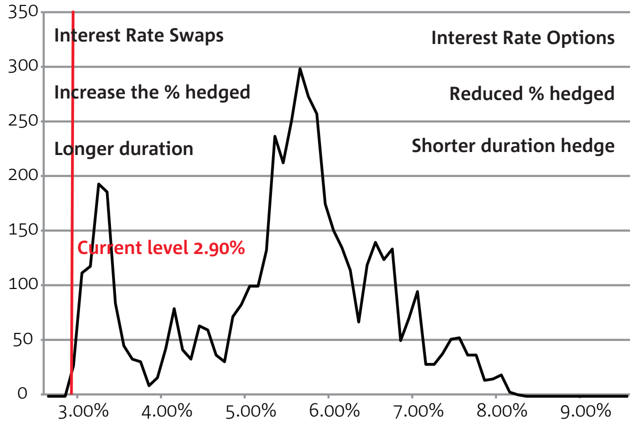
The GFC experience has resulted in AREITs moving beyond CMBS and hybrid debt instruments in order to (a) dilute bank debt funding exposure and (b) secure other forms of real estate debt that better aligned with the assets/liabilities nature of real estate investing.

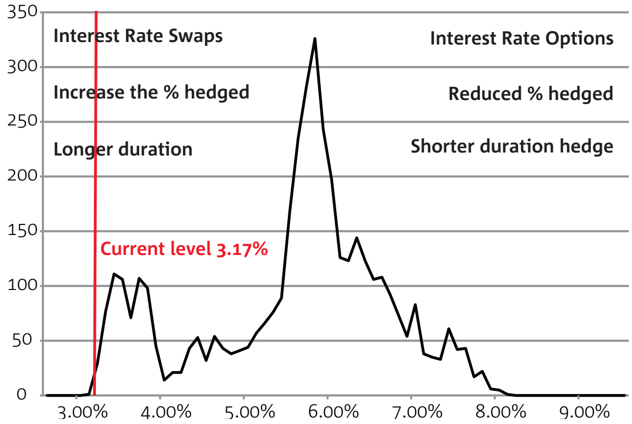
To illustrate the shift in key capital management metrics since 2010-2011 to 2013-2014, we have set out below the headline comparative metrics of a selected group of AREITs which shows the comparative hedging/average borrowing costs between the two reporting periods. In broad terms gearing (net debt/net assets) has upticked since 2010, a period in which AREITs were emerging from the GFC yet generally sit within the mid-point of stated target gearing ranges.

In response to the three and five year swap rate curve over the intervening period plus some AREITs resetting hedge books through paying out out-of-the-money hedge books and resetting hedges at the prevailing rates AREITs have constructed a lower average borrowing rate than that reported in 2010.

The charts, right, show the three and five year swap curves on a semi-rolling basis and plots where current pricing sits versus historical averages. Both on a three year and five year basis, the current pricing is at historical lows with both the swap curves hitting all-time lows in October 2014. The expectation by some AREIT Treasurers is for this trend to continue well into 2015, therefore the motivation to increase current hedging levels is weighed up against having a higher proportion of floating rate debt in order to take advantage of the three strategies and structures

Credit spreads





Source: NAB and five year swap curve profile.

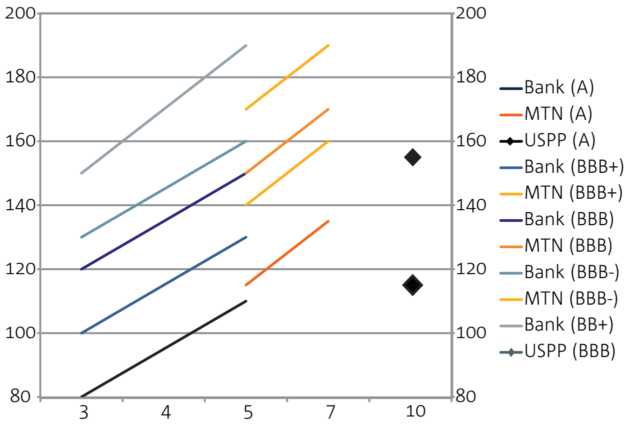
of interest rate hedge books across the AREIT sector do differ and with AREITs such as Mirvac and Stockland having a material portion of their financing costs held in capitalised interest linked with their respective residential development workbooks, their approach to interest rate hedging can be expected to differ from those AREITs which receive a higher portion of their revenue from rental income.

A further mitigating factor in how AREITs approach interest rate hedging is, in addition to a house view on the direction of rates better matching or at best aligning the weighted average hedge maturity with an AREIT's weighted average lease expiry profile (WALE) in order that there is a relationship between the duration of contracted earnings (WALE) and an AREIT's hedge book in order that so as not be over-hedged.

The 2014 AREIT debt funding model sees the majority of the AREIT sector (by market capitalisation) hold bank debt, Medium Term Notes (MTNs) and US Private Placement (USPP) and potentially 144A Notes inside its debt funding facility pool. Whilst there is no fixed weighting ratio between the various debt funding sources, the general consensus has seen a broad 1/3/1/3/1/3 approach adopted although that mix is expected to shift over time in line where pricing/tenor trade-offs hold the marginal funding value. More recently we saw Stockland issue the first green bond offshore raising €300 million with funding raised from this issue deployed to green-based projects including residential community development projects.

The following table plots the relative costs of the various debt instruments and the tenor on offer which in part could be described as an "efficiency frontier" across a suite of debt instruments utilised by the AREITs. One key factor in the decision to issue longer-dated funding such as a USPP is the probability over the life of the issue that the AREIT issuer could look to "make whole" that instrument well in advance of its maturity date. Given that USPP investors enter these deals in the expectation that the issue will remain on foot until maturity, early termination even if done in accordance with the loan deed does make re-issuance in that same market by the same AREIT more challenging.

Credit spreads



Source: NAB

Having longer dated debt does bring with it an AREIT taking a view on the outlook for rates and whether the duration risk in holding longer term debt is being sufficiently compensated in the pricing.

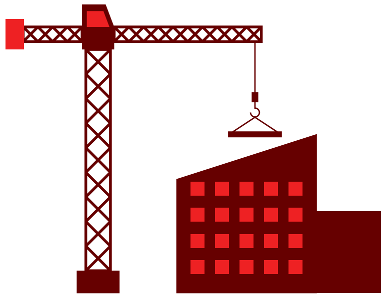
Whilst the bulk of the larger market cap AREITs have substantially refined and constructed their respective capital management profiles, we now expect that mid-cap names will also look to either debut in the MTN or USPP market with others looking to build out their current modest exposure to the DCM sector.

Summary

The AREIT sector has come a long way in terms of refining their respective capital management structures from a debt composition and pricing standpoint. In large part, this was a response to the GFC and the clear message that material exposure to single debt sources reduces refinancing options that can ultimately adversely impact shareholders as we saw with the multiple equity raisings undertaken by the AREIT sector ($13bn) during the GFC in order to de-leverage vehicles. The capital management agenda undertaken by the larger cap AREITs is expected to be mirrored by mid-cap AREITs in order to reduce bank debt exposure and build out debt tenor.

Interest hedging strategies remain a less consensual issue amongst AREIT Treasurers with some viewing the lower rates environment as opportune to taken on hedges whilst others view a lower hedging profile opportune in order to take advantage of historical low floating rates.

Funding Australia's infrastructure future



The dialogue around the provision of infrastructure to sustain the Australian way of life and further development of our modern society going forward is undeniably an important one

Fostering debate and informed consideration on how to provide sustainable infrastructure funding for society's future prosperity is a commendable activity taken on by members of government, industry and the community.

The task is significant. We know the Infrastructure Partnerships Australia estimate that is regularly referred to, that there is a $700 billion funding need over the next decade. There are other, larger estimates. Few would deny that there is much work to be done in order to finance the long term infrastructure investments – the nation building – we need to secure our future.

Yet, as always, it raises that inevitable question about how to fund this infrastructure need. And beyond the roads, bridges, and ports, what about the social infrastructure that should go with this – those essential elements of any prosperous society?

Funding infrastructure in new ways

At NAB, we see that the financing of large scale, long-term infrastructure projects will need to come from a variety of public and private sector sources. Given the need for banks to diversify their loan portfolios, to avoid excessive maturity mismatches between assets and deposits, and to not have excessive exposure to one borrower or project – this makes particular sense.

Of course, there is no one, easy solution, which is why ongoing engagement between industry, government, the community and regulators is essential. While laying the groundwork for greater accessibility to this market is a challenge, the other major task is in educating investors – and indeed the industry.

NAB believes education provides for a greater understanding of corporate bonds as an asset class – taking us a step closer towards building a deeper corporate bond market. A fully functioning retail corporate bond market will offer investors more choice and an opportunity to diversify their investments – broadening the range of assets available through superannuation funds.

The next step is making those retired savings available to fund essential infrastructure. We need to ensure our vital infrastructure projects are an appealing investment for large pools of super savings. What is now a virtual absence of corporate debt accessible by retail investors will change significantly in the near future. We are seeing the building blocks fall into place already.

Impact investing and social impact bonds

There is no doubt that the provision of built infrastructure into the future is essential to our growth and prosperity. However, the best and most useful infrastructure must take a holistic approach, and instinctively consider social impacts and uses. This should be an essential consideration in the provision of infrastructure.

The building of traditional infrastructure and the associated programs they deliver are relevant as a subset of the corporate bond market discussion. It goes to the importance of social infrastructure for our future prosperity, and the role that impact investing and social impact bonds can play in this. It was important enough to feature in the recent FSI Interim Report.

This is an issue close to NAB, and represents an extension of our fair value agenda. Indeed at the heart of our organisation is the belief, the ethos, to do the right thing. NAB is a leading advocate for Impact Investment and we believe the next stage in Impact Investment is the development of an active Social Finance market in Australia.

Global trends and market forces such as an ageing population and a declining tax base support the forecast that impact investment will be a $32 billion market in Australia by 2022 according to IMPACT-Australia, of which NAB is a founding partner.

In line with our values system, we believe we have a responsibility to deliver holistic and innovative financial solutions that help our customers address social and environmental problems through impact investment. Impact Investment makes sense as a commercial business opportunity and can play a vital role in building successful communities and future proofing our nation.

It provides an opportunity for a collaborative approach to addressing the significant growing social issues facing the Australian population. The gap between demand for welfare services and what government can provide is growing and we believe accepting no change to the current arrangement would disadvantage the Australian economy and our prosperity in the future.

Government can play an active role here. Other countries have shown how timely government action can catalyse impact investment market development. The United Kingdom has been a leader in this. A 2010 social impact bond – the first of its kind – was launched in the UK to fund a program to reduce recidivism rates at Peterborough Prison in Cambridgeshire, with promising results. Just this year, the United States Government announced the launch of a social impact bond to reduce teen pregnancy and improve education, while our neighbours in New Zealand are currently exploring a social impact pilot, potentially around reducing recidivism, increasing employment, and improving management of chronic health condition.

Australia should not be left behind

The NSW Government has released two social bonds, one to support families to facilitate their child's return from foster care and another to fund the Resilient Families service that provides support to families and children post-crisis.

Meanwhile South Australia has released a tender to deliver a series of workshops to deliver classroom training workshops and online training materials to build capacity amongst service providers and government staff.

NAB is focused on delivering innovative models for the social sector to access capital, developing investments that are designed with the intent to create a positive social impact beyond financial return, including identifying new ways to fund affordable housing programs, creating a private fund to invest in social enterprises, and working with several not-for-profit organisations to structure deals to bring to the Australian Bond market.

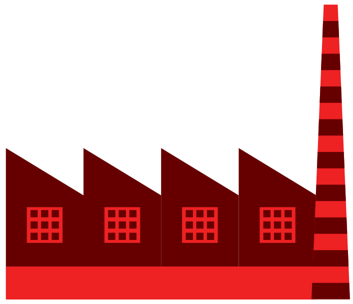
Working together in the national interest

The solutions are there, but the work is ahead of us, and involves collaboration between governments at all levels, industry, and community. We need a funding model that can ensure we have the infrastructure we need to power the growth and competitiveness of our nation well into the future.

And we need to consider not just the tangible, built infrastructure – that will only get us so far. We must factor in the vital social infrastructure needs of our nation as well. With our strong financial system, ready investors, and that growing pool of super savings, we must grasp this opportunity.

NAB is certainly committed for the long term and sees the opportunity to leverage Australia's leading role in infrastructure across the globe.

2014 was a big year for infrastructure in Australia



With the launch of some of the largest Projects ever seen in the Australian Infrastructure market, combined with an influx of new international players and an expanding pipeline, FY14 was quite a year within the Infrastructure Finance sector, and NAB Specialised Finance was at the heart of it

To keep up with the country's economic and population growth, Australia has a significant infrastructure expenditure pipeline, which is putting the Federation at the centre of the world infrastructure market.

Within the social infrastructure space, for example, a significant number of Public Private Partnership or PPP transactions were closed here in Australia during the year. Projects were procured across NSW, Victoria, Queensland and WA with one further financing completed in our sister market of New Zealand. Combined Project values across the deals were just over A$7 billion, representing a significant long term investment in infrastructure by the respective Government authorities. The Projects were predominantly funded by private sector capital, but state grants and the ongoing service payments required to fund operations are all costs of Government. Incidentally, NAB performed well arranging finance for clients on all but one of the seven PPP deals that closed in NAB's FY14, which is a terrific result. These Projects are now delivering new road, rail, schooling and custodial assets along with a large modern convention centre and a 60,000 seat stadium, each providing significant benefits to communities across Australia.

The A$7 billion of Projects closed in FY14 appears to be a small tip on an ever expanding iceberg. During FY14 a further three PPPs were bid and are still either live or have closed since 30th September. Other major Projects such as the WestConnex and NorthConnex road and tunnel Projects in Sydney were also launched during the year. Anyone who has travelled along the Parramatta road in West Sydney at rush hour, or indeed tried to head north on a Friday evening towards Newcastle, knows all too well how important these Projects are for alleviating congestion and improving connectivity across the Sydney road network. Both Projects represent significant construction tasks, including as they do intra-urban tunnel boring and surface road building. In total these two Projects alone are expected to cost around A$20 billion to procure and will be delivered over the next five

The Social Infrastructure Project Pipeline

2014

Perth Stadium WA

Ravenhall Prison East West Link VIC

North West Rail Link NSW

Northern Beaches Hospital NSW

Sydney Light Rail NSW

2015

WA Schools WA

WestConnex NSW

North Connex NSW

Moorebank Inermodal NSW

2nd Harbour Crossing NSW

2016

Perth Light Rail WA

Parramatta Light Rail NSW

NSW Prison PPP NSW

Melbourne Airport Link VIC

Bus and Train Project (2016+) QLD

Cross River Crossing (2016+) QLD

years or so. On top of this the Mike Baird Government is also prioritising a second harbour rail crossing, further Light Rail developments and even talking about a second Sydney airport and related transport Infrastructure. It's a similar story in both Melbourne and Brisbane with the respective East West Link road tunnel and soon to launch Underground Bus and Train tunnel coming with price tags in the A$5 billion+ bracket.

Given the dollar values involved and the clear benefit to society when infrastructure is delivered effectively, the sector is also currently a hot topic dominating the debate and party manifestoes in relation to the upcoming state elections in Victoria, New South Wales and Queensland. The further modernisation of Australian infrastructure will of course cost the state and federal Governments significant amounts of money over the long term, and by making their choices at the ballot box the electorates in the Country's three largest states by population will shortly decide on key elements of how best to deliver the spend.

The tiered nature of the Australian Government structures, places the primary funding responsibility for most public infrastructure on the states. The global economic slowdown has had a material impact on the fiscal performance of all states, with Western Australia and Queensland most affected as both these states relied on the continuation of the resources boom to sustain their budgetary positions. South Australia, Western Australia and Queensland lost their AAA credit ratings in the aftermath of the global financial crisis and have been pursuing various measures to regain these ratings. A strong credit rating has also been a particular priority of both Victoria and New South Wales. With these states also looking to control expenditure, improve revenue and return to sustainable budget surpluses. This strategy naturally makes the states less likely to initiate large-scale infrastructure programmes without substantial funding support. So how will the states fund the infrastructure pipeline?

The answer, at least for most, is capital recycling. This just means selling established brownfield infrastructure to help fund necessary new expenditure. The New South Wales Government started the recent trend with the sale of the Sydney Desalination Plant in 2012, followed by the sale of Port Botany and Port Kembla in 2013 and the Port of Newcastle earlier this year. Given the perceived benefits to the wider economy of the capital recycling process continuing, the Commonwealth Treasurer recently announced an agreement with the states to provide an additional subsidy of 15% of the assessed business value of a sale, where the proceeds of an asset sale are marked for re-investment in infrastructure. This initiative encourages asset sale processes and the direction of the proceeds into needed infrastructure development.

The most recent privatisation of sorts saw the Queensland state defined benefit pension scheme sell Queensland Motorways for A$7 billion, well ahead of early sale value estimates. On that deal NAB supported the successful bidder and important client Transurban. The major set of asset sales on the horizon though are the 'Poles and Wires' sale processes in New South Wales and Queensland, which if they go ahead will see those two state Governments privatise assets with a regulatory value of around A$50 billion. The decision on whether to go ahead with the sales is a key point of contention within the upcoming New South Wales and Queensland elections, with incumbent Governments pledging to start the sale processes as soon as possible if they are returned to office next year.

Like the rest of the market we are waiting with bated breath. FY14 was a big year for Infrastructure, and it could just be the start of things.

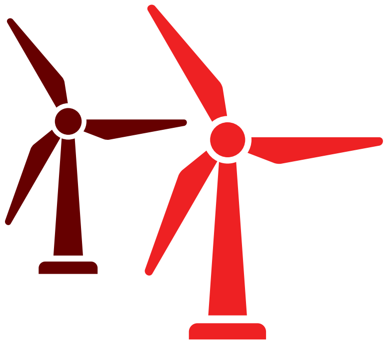
Other notable trends

The infrastructure asset pipeline has put Australia on the map in terms of asset development opportunities for building contractors. The multi-billion dollar proposals have caught the attention of the world's largest builders, many of whom have recently established offices in Australia to ensure they are well positioned to chase these opportunities hard. The likes of ACS Group, Ferrovial, Acciona, Bouygues, Samsung, MTR, Ghella, McConnell Dowell, Salini Impregilo, OHL, Keolis and Alstom have all bid on large Australian infrastructure projects this year, meaning the large end construction market is a genuinely international one here in Australia. During the year ACS Group took control of Australia's largest construction Group, Leighton Holdings, leaving Lend Lease as the only major Australian owned contractor in the large scale market.

Given NAB's presence within the infrastructure finance markets of the United Kingdom, Asia and North America, and the fact that many of these Groups have been active previously in Australia, the Bank already has established relationships with a lot of these companies. The weight they are all putting behind their push into the Australian market however is close to unprecedented, and with our support we are hopefully it will be a successful push which aids Australia's infrastructure development over the short, medium and ultimately long term.

Global renewables market

There is a global shift toward reducing our environmental footprint



In 2013, new renewable energy capacity globally grew at its fastest pace to date with an estimated investment of US$250 billion. NAB recognises the tremendous opportunity this presents our customers to participate in the growth of this sector. We are proud to be the No.1 Renewables Project Financier in our core Australian and New Zealand markets, which has positioned NAB to support this growth through the provision of a range of debt solutions and ancillary products to our customers. We are also a leading Renewable Energy Financier in the UK market.

Renewable generation

Globally, renewable generation accounted for almost 22% of power generation (76% hydro, 12.5% wind) and was on par with that of natural gas, whose generation declined slightly in 2013, but remained well behind coal. The International Energy Agency ('IEA') estimated that in 2013 global renewable energy net capacity additions reached 123GW which is its highest level to date. Investment totalled US$250 billion which was 60% of the estimated US$400 billion invested in new power generation in 2013. Going forward, the IEA estimates an average annual investment in renewable energy of US$230 billion (in 2013 real terms) through to 2020.

Global growth in renewable power generating capacity is driven principally by two factors:

1. Desire to de-carbonise the electricity sector. De-carbonisation is deemed important as the electricity generation sector is a major emitter of carbon which has been linked to climate change
2. Improve security of supply. Renewable energy plants such as wind and solar farms rely on naturally occurring resources such as wind and irradiation and therefore reduce reliance on importing fossil fuels, prices and supply of which can be volatile

The renewable energy country attractiveness index ("RECAI") - which is a methodology created by EY to rank 40 countries on the attractiveness of their renewable energy investment and deployment opportunities - ranks China, US and Germany as the top three most attractive countries to invest in the renewable sector.

Australia

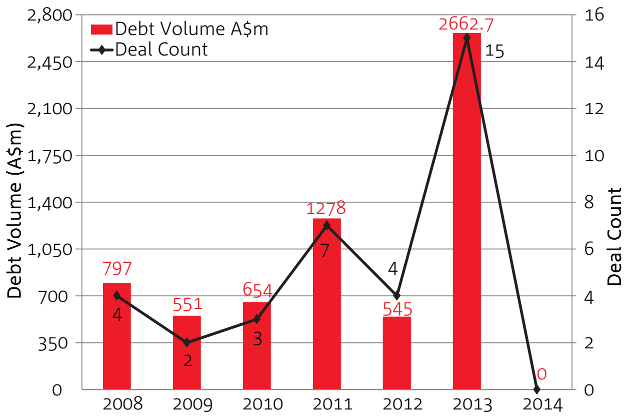
To date, Australia has been committed to a renewable energy target of 41,000 GWh by 2020 to encourage additional generation and reduce its greenhouse gas emissions ("RET Policy"). Since the last federal election, the prior bi-partisan support for the RET Policy has been questioned and the Federal Government is yet to finalise its decision to provide certainty to current and potential investors in the sector.

In 2013, the Australian market witnessed a total of A$2.6 billion debt funding raised for renewable power projects, the largest financing volume we have seen in any year and more than triple the average of the past 5 years. Impressively, there was:

- a total of 15 utility scale renewable projects successfully reached financial close
- 3 projects utilised turbines from manufacturers new to the Australian market
- the first utility scale solar farm was successfully project financed
- the entry of 8 new overseas investors and 8 new banks providing financing to renewables projects across Australia

In contrast, there has been no private sector project financing of renewables project in Australia in 2014 to date. The industry is at the cross roads and eagerly awaits energy policy certainty in relation to the RET Policy and bi-partisan support for the sector before it can again enjoy the successes of the past.

Australian Renewables - commercial bank involvement



Source: NAB

United Kingdom

The UK's commitment to renewable energy is enshrined in domestic and European legal undertakings. The UK is required to produce approximately 30% of its electricity from renewable power by 2020 from a level of 13.9% in 2013 in order to meet its binding renewable energy targets. Nearly £28 billion was invested during 2010-2013 in the UK renewables sector with an estimated additional £65 billion required up to 2020 to meet the UK's renewable energy targets.

A key attraction of the UK renewables market is the stable regulatory environment. Whilst renewable support mechanisms have rightfully evolved over time, the UK government has consistently grandfathered existing schemes which provides investors with confidence.

Rise of listed Yieldco's and the issuance of Green Bonds

In the UK alone, 6 Yieldco's which have a combined market capitalization of £1.4 billion have floated in the last 18 months. Yieldco's provide public access (and liquidity) to renewable projects and are seen as an attractive investment due to their stable and inflation-linked dividend profile. Going forward, we expect this type of investment vehicle will remain popular with investors, however the management team and scale remain critical and as such we anticipate consolidation as industry leaders emerge.

Green bonds are debt securities issued by corporations such as utilities and banks to support their investment (either equity or debt) into renewable projects. Crucially for investors, the credit risk of a corporate green bond remains on the issuer's balance sheet. Bloomberg New Energy Finance estimates that the global market for Green Bonds totalled over US$16 billion in the first half of 2014, more than the US$14 billion in all of 2013. Whilst global Green Bonds issuance was only circa 1% of the value of the US corporate bond issuance (US$1.4 trillion) in 2013 we expect Green Bond issuance to grow. Green Bonds should appeal to investors who incorporate and adopt socially responsible and environmentally sustainable investments. From an issuer's perspective, Green Bonds provide an alternate method of raising debt, access to a different investor base and with time, potential cost savings as investors might be willing to take a lower coupon given the green label.

Stable regulatory framework is paramount

Renewables often require quota or feed-in tariff schemes for projects to be economically viable - therefore a stable policy framework is crucial. Unanticipated changes to such regulatory framework is a risk that investors cannot manage well and can result in investment hiatus, as evidenced in the Australian market throughout this year.

At NAB, we appreciate that we need to ensure that the pressures of:

- rising retail electricity tariffs
- maintaining low wholesale electricity prices
- an ageing thermal generation fleet
- lower than expected overall energy demand

are appropriately balanced by the benefits of:

- minimising sovereign risk premiums
- lower emissions technologies
- increased fuel diversity and greater energy security

We believe some of these challenges will be, in part, dealt with through reduction of deployments costs, which we have already witnessed in the onshore wind and more markedly in the solar photovoltaic markets.

According to the IEA's latest World Energy Investment Outlook, almost US$10 trillion will be required to be invested globally in power generation to 2035. Of that amount it is estimated that renewables will make up US$6 trillion of this investment. At NAB, we recognise the importance of renewable power. We believe that when the pressures of renewable power are appropriately balanced against the benefits, renewables should play an important role in the energy landscape. Critical to the success of such investment opportunities, whether through traditional project financing structures or innovative solutions such as Yieldco's or Green Bonds, is a regulatory framework that is consistent and has the confidence of all key stakeholders.

NAB's commitment to the environment

At NAB, we have recognised the importance of the environment for our long-term sustainability and the wellbeing and prosperity of our economy and communities. As a result of this, our environmental agenda is strategically focused on three key areas:

- climate change
- resource efficiency
- natural value

NAB is a leading provider of project finance and has arranged non-recourse funding for approximately 4.2GW of renewable energy projects globally. In Australia, NAB is the leading arranger of project finance for utility scale renewable energy projects, having arranged over A$1.8 billion of transactions over the last 8 years. Our renewable capability also extends globally, including the UK, where NAB has been active for 8 years and has arranged £2.1 billion for renewable energy projects.

In 2014, NAB continued to support the infrastructure demands of a lower carbon economy by financing two key renewable energy transactions, which include:

1. Sarulla Geothermal plant in Indonesia - upon completion, this will be the country's largest single-contract geothermal power project. It has a nominal installed capacity of 330MW
2. Infinis' operational wind farm refinancing - this transaction was awarded Project Finance Magazine's 'European Onshore Wind Deal of the Year 2013' and involved NAB leading the structuring and refinancing of a portfolio of 16 onshore operational wind farms in the UK, representing an installed capacity of 274MW

For the full year 2013, NAB was the No.1 Australian domestic bank, ranked 10th globally as Lead Arranger, Asset Finance in the Bloomberg Clean Energy and Energy Smart Technologies League Tables. During that year, NAB became one of the first banks to arrange project financing for a utility scale solar power station in Australia.

We have also achieved some milestones that demonstrate our commitment to energy efficiency:

1. NAB was Australia's first carbon neutral bank: Our carbon neutrality is underpinned by a focus on energy efficiency, the use of cleaner energy sources, and where possible, support for local carbon abatement
2. We are leaders in the development of Environmental Upgrade Agreements, having arranged four of the five privately financed Environmental Upgrade Agreements, providing innovative new funding sources for environmental retrofits of commercial buildings

Asset Finance and Leasing trends in 2014

The global aircraft finance market continued to evolve in 2014

Asset Finance & Leasing continued to expand in global aircraft finance markets in 2014. The year was characterised by numerous new product launches for AF&L for airline and aircraft leasing customers of NAB.

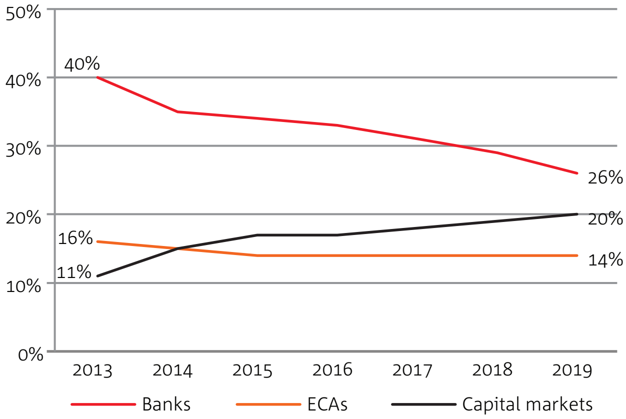
From a liquidity perspective, strong demand from lenders and the continued overall low interest rate environment has led to a global aircraft finance market that is extremely robust. The strong bid across all parts of the market has been fuelled by the accommodative policies of central banks in the US, Japan and Europe and a drive from various banks to return to the aircraft sector following their withdrawal from the market in the global financial crisis. Tighter spreads benefitted airlines and aircraft lessors in 2014 and saw financiers expand into new areas of the aircraft finance market in search of yield, a positive for the market which has resulted in broader participation from financiers.

Aircraft finance has been provided throughout 2014 as aircraft manufacturers work to respond to global customer demand for new, fuel-efficient aircraft driven by continued air travel growth and an accelerated aircraft replacement cycle in response to higher fuel prices. The industry continues to demand significant resources; Boeing estimates a global aircraft funding requirement of over US$110 billion for 2014, which is expected to increase steadily to US$140 billion by 2018.

Structural changes in the funding mix

Despite the bank debt market being awash with liquidity in 2014, the aircraft finance market continues to be one of realignment. The mix of new delivery funding sources is expected to evolve over the near-term. Historically, export credit agencies and commercial bank debt have been the dominant sources of aircraft finance. Going forward there is expected to be a proportional reduction in the supply of export credit support and commercial debt and an offsetting increase in share of funding coming from capital markets.

Forecast mix for aircraft funding share: three largest sources



Source: Avolon. Note that the balance of the funding requirement is met via lessors' self-funding and OEMs.

Although the bank debt market has been strong, airlines and aircraft lessors have been keen to diversify funding sources. They have been lured into capital markets, where - particularly in the US high yield space - institutional investors have developed a strong appetite for aircraft assets. The attraction for capital markets participants is that aircraft offer returns for tangible assets with long-term lives that often exceed the returns from competing fixed income investments with similar credit ratings. Bonds (EETCs and ABS in particular) backed by high quality collateral (young aircraft) with sound credits (airlines and lessors) have resonated strongly with institutional investors in pursuit of an attractive relative return.

The future

NAB's AF&L business seeks to take a front foot position to capitalise on these trends. In partnership with debt markets businesses, AF&L will continue to develop its product range by opening a bond investment platform to complement our existing market activity. As we expand offshore, we plan to develop a full-service product suite for airline and aircraft leasing customers, allowing NAB to grow and compete in this dynamic market.

Spotlight on North America

The US markets continue to provide opportunities for Australian issuers

US Private Placement Market – an issuer's market in 2014

The US Private Placement market had another strong year in 2014, with over US$50 billion of volume priced across more than 200 transactions. Investors started the year with increased budgets, however struggled to find enough new deal flow to meet their investment targets. This was particularly evident in the NAB US Private Placement 1H14 Investor Survey, with the majority of investors responding that their allocation on bids was between 26-40%.

The supply/demand imbalance resulted in an 'issuer's' market in 2014, with US Private Placement investors increasingly aggressive on transactions in order to improve their allocation outcome. Investors demonstrated increased appetite to accommodate flexible issuance structures, providing foreign currency, delayed funding and non-benchmark tenors. Transactions continued to be multiple times oversubscribed, with significant price tightening through the marketing process.

Australian and New Zealand issuers were met with strong demand, with over 30 transactions completed from the region in 2014, accounting for ~15% of total market volume. The strength of investor demand was evident on a number of NAB led transactions including Port of Brisbane's A$175 million US Private Placement (which received over A$700 million in A$ interest from US based investors) and Auckland Airport's US$250 million US Private Placement (which had an order book in excess of US$2 billion).

NAB was again recognized as the market leader in bringing Australasian issuers to the US Private Placement market, ranking as the #1 Agent in both the Private Placement Monitor and Thomson Reuters H1 2014 League tables. This came on the back of the June 2014 Peter Lee Survey results where NAB took four out of seven #1 spots for US Private Placements, including the overall metric of "#1 Overall Lead Provider for US Private Placement Issues" among all banks globally.

2014 Australasian issuance in the US Private Placement Market

Property
CFS Retail *US$200m*
GAIF *US$222m**
SCA Property *US$197m**
GPT *US$175m*
IOF *US$200m*
Dexus *US$250m*
Stockland *US$125m*
Precinct Properties *US$75m*

Consumer/Industrials
Sonic Healthcare *€110m*
Boral *US$200m*
CSL *€350m*
Murray Goulburn *US$100m*
DuluxGroup *US$188m**
Cardno Holdings *US$160m*
Pratt Finance *US$190m*
Ansell *US$200m*
Fonterra *US$500m*
Monash University *A$150m**

Infrastructure/Utilities
Powercor *US$300m*
Brisbane Airport *US$250m**
Sydney Airport *A$380m*
Finders Ports *US$282m*
Port of Brisbane *A$175m*
SA Power *US$370m*
Brookfield Rail *US$485m*
Adani Abbot Point Terminal *US$150m*
Auckland Airport *US$250m*
Meridian Energy *US$140m*
PowerCo *NZ$100m*
Todd *US$250m*
Genesis Energy *US$150m*
Multinet Gas *A$170m**

*Equivalent. NAB led transactions highlighted in red.

US Investment Grade Market – record issuance at attractive spreads

In the US Investment Grade market, supply eclipsed US$1 trillion in 2014, exceeding record totals achieved in 2013. Given the relative value offered in US high grade spreads and yields versus the rest of the world, investors piled into credit investments at an unabated pace, providing attractive funding for corporate and financial issuers alike.

Positive fund inflows for the year were directed across the maturity spectrum, as investors bought up front end, intermediate and long duration assets. With volume and duration available to issuers, issuance into the US continued to flow from all parts of the world. US pension and insurance funds continue to drive demand, along with asset managers, hedge funds, and a larger component of foreign investment out of central banks and sovereign wealth funds. Interest rates remain well bid as the Fed, while discontinuing Quantitative Easing, will reinvest proceeds from maturing debt. This, in conjunction with tight spreads made the journey into the US markets a worthwhile and rewarding proposition.

Corporate and Financial issuance was evenly split for the year. Fixed rate borrowing made up 88% of all issuance, and within those totals, 45% of funding was in 10 year or longer maturities.

US Frequent Issuers in the Australian market – more issuance and longer tenors

While North American issuers were largely absent from the Australian market during the first half of 2014, they came in droves during August and September. Many of these issuers such as Wells Fargo & Company, Bank of America Corporation and Morgan Stanley are regular issuers in this market and have established well-defined curves as a result of their issuance activity since the financial crisis. 2014 was the first time both Goldman Sachs Group Inc. and Metropolitan Life Global Funding printed two AUD transactions in the same calendar year.

In response to the low yield environment, investors sought to extend the duration of their portfolio. Historically, a five year tenor was the limit for financial issuers in the Australian debt market. However, AUD investors have become increasingly comfortable with participating in longer-dated senior unsecured transactions. The volume of financial supply with tenors greater than 5 years grew significantly year-on-year, with a total of eight financial transactions with seven and 10 year maturities.

Issuers in 2014 also looked to diversify away from the more traditional EUR secured market by visiting the Australian market to issue AUD covered bonds. Historically, European issuers have been a key feature in the Kangaroo covered bond space; however Canadian banks have become the most active Kangaroo issuers in this space. In 2014, both Royal Bank of Canada and Toronto Dominion Bank issued five year AUD Kangaroo covered bonds.

NAB was the only bank involved in every North American FI transaction in the Australian bond market in 2014, consolidating NAB's position as a proven partner in the Australian debt market.

Northern Hemisphere Asset Backed Market – duration and yield

2014 was a strong year of issuance in both ABS and RMBS. Australia once again proved to be a dominant nation of issuers, supporting almost A$30 billion in issuance and once again its issuance volumes surpassed some of the other major jurisdictions in this segment. Spread performance in 2014 was more pronounced as notes played catchup to the compression evidenced in other areas of the bond markets. As investors continued to seek out yield, issuers were more confident to issue in formats other than RMBS. Offshore, NAB supported seven deals, and led our first term 144a deal for an Australian nonbank issuer since the crisis. This step forward is a reminder that we have made positive inroads with investor awareness about the Australian product and underlying risks.

Looking to the year ahead, we expect more of the same: strong market liquidity, more deal variety and excellent client outcomes. We look forward to reporting back.

Spotlight on Europe

European markets attracted Australian issuers as the UK remained dominated by domestic issuers

Euro Market

The Euro market has had an outstanding year with volumes up on previous years and has provided a viable and very cost effective alternative to the US market. Issuance levels for 2014 as at end October are €864 billion vs €744 billion at the same point last year.

The primary driver of this performance has been demand side with investors looking to generate returns in the backdrop of a zero interest rate environment and the favourable basis for offshore issuers. The European Central Bank (ECB) has adopted an accommodative policy in the wake of continuing sluggish growth numbers and general economic activity throughout the Euro Zone. This policy has been through a number of different mechanisms: Zero interest rates, definitive statements by Mr Draghi (ECB president) that rates will be lower for longer, combined with proposals to revise eligible assets that the ECB will accept in its Targeted Long Term Refinancing Operation (TLTRO).

From an economic growth perspective it will be interesting which fiscal policy adjustments will be made (if any) in order to drive economic growth and address the competitive imbalances in the Euro Zone economies and, what this will do to issuance levels going forward. This could impact growth and subsequently capital expenditure plans leading to an increase in issuance.

Issuer	Amount (mn)	Coupon	Benchmark	Spread	Maturity	Moody's	S&P
Aurizon	500	2.00	mi-swaps	106	15 Aug 24	Baa1	BBB+
Scentre Management Ltd	600	1.5	mid-swaps	72	16 Jul 2020	A1	A
Scentre Management Ltd	600	2.25	mid-swaps	92	16 Jul 2024	A1	A
Scentre Management Ltd	400	3mE+65bp	3MO Euribor	67	16 Jul 2018	A1	A
Australia Pacific Airports (Melbourne)	350	1.75	mid-swaps	75	15 Oct 2024	A3	A-
Wesfarmers Ltd	600	1.25	mid-swaps	55	7 Oct 2021	A3	A-
Transurban Finance Co Pty Ltd	600	1.875	mid-swaps	82	16 Sep 2024	Baa1	A-
SPI Electricity & Gas Australia Holdings Pty Ltd	350	3.0	mid-swaps	110.2	13 Feb 2024	A3	A-
Aurizon Network Pty Ltd	500	2.0	mid-swaps	90	18 Sep 2024	Baa1	BBB+
SGSP (Australia) Assets Pty Ltd	500	2.0	mid-swaps	85	30 Jun 2022	Baa1	BBB+
Brambles Finance Limited	500	2.375	mid-swaps	90	12 Jun 2024	Baa1	BBB+
Sydney Airport Finance	700	2.75	mid-swaps	100	23 Apr 2024	Baa2	BBB

Source: Informa Global Markets via Bloomberg

The key theme that we are continuing to see is the ongoing attractiveness of issuance into the EUR market with spreads remaining at tight levels and basis swap markets moving in the right direction (for issuers) combining to make the market particularly attractive for non-EUR denominated issuers. Throughout the year issues have been launched at the tight end of new issue price guidance and any new issue premium remaining in the low single digits. This is applying across the spectrum of issuers from Corporates to Financials.

The attractiveness of the Euro markets for Australian issuers has been another theme for 2014 with a number of Australian companies coming to the market to take advantage of the tenor, volumes and funding diversification that the market brings to the issuers. Below is a table of the companies that have come to market and details of their trades.

As can be seen from the previous table the issuers have come from a variety of sectors with a domestic focus (ex Scentre), all issues saw very strong demand pointing to an increasing comfort level from European investors for Australian based companies.

Financial issuance has been slowing throughout the year as banks obtain funding from the ECB and run down balance sheets. There has also been a strong emphasis on sub-ordinated type products to ensure capital adequacy requirements are met in accordance with global regulators more stringent guidelines. These have seen strong prints with books significantly oversubscribed, as investors preferred the higher yielding option available from such issuance compared to senior unsecured. Interestingly, Origin Energy also issued a very successful deal in this space issuing €1.0 billion of a 60 Year Non Call 5 Year transaction.

Sterling Market

The Sterling market has had an interesting year with domestic issuers dominating the market as pricing has not lent itself to issuance from non-GBP denominated companies. In keeping with the tradition of the market longer tenors have been favoured and a focus on infrastructure issuers. However, with the announcements in this year's budget of non-compulsory buying of annuities in pension plans it could be expected that the market will open up more in the shorter end as the need for long tenor annuity duration matching by fund managers will be expected to decrease over time. This could have the unintended consequence of increasing issuance and competitiveness of the Sterling market as demand in the medium term tenors drives pricing in.

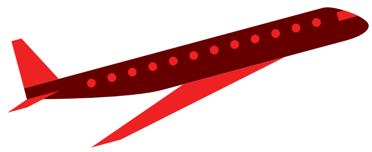
Australian issuance into the Sterling market was driven by financials with Scentre being the only corporate name to tap the market as can be seen from the table below.

The Institutional Term Loan market continues to go from strength to strength in the market as the reduced issuance has meant that Investors have had to look at alternative options to put their funds to work. The product allows investors to invest in similar tenors to the public market without the need for a full offering memorandum such as a prospectus plus, it has the added benefit of being executed in smaller tranche sizes off of existing bank facility platforms. This allows issuers more flexibility in their funding profile and allows them to diversify their funding mix and debt maturity profile.

Issuer	Amount (mn)	Coupon	Benchmark	Spread	Maturity	Moody's	S&P
Suncorp-Metway	250	3mL+60bp	3Mo Libor	60	6 Oct 2017	A1	A+
Scentre Management Limted	400	3.875	5% 2025 UKT	113	16 Jul 2026	A1	A
Commonwealth Bank of Australia	300	2.25	5% Mar-2018 UKT	90	7 Dec 2018	Aa2	AA-
Macquarie Bank Ltd	250	3.5	4.75% Mar-2020 UKT	145	18 Dec 2020	A2	A
Commonwealth Bank of Australia	350	3mL+30bp	3MO Libor	35	24 Jan 2018	Aaa	NR
Westpac Banking Corp	350	3mL+35	3MO Libor	35	28 Nov 2017	Aa2	AA-

Source: Informa Global Markets via Bloomberg

Spotlight on New Zealand

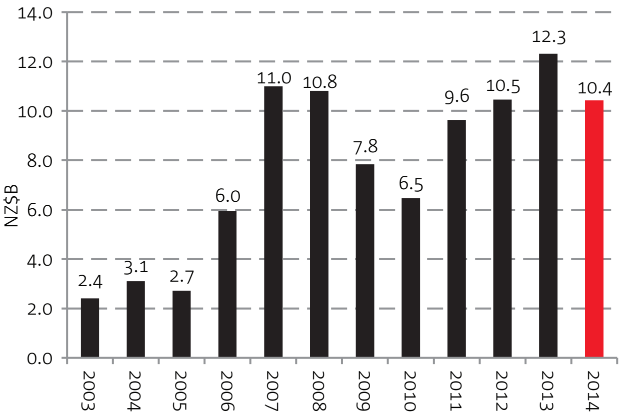


The New Zealand debt capital markets have had a strong year and continue to remain active and open for new issuance

2014 YTD has seen NZ$10.4 billion priced across 86 transactions, from a diverse range of corporates, bank, local authority and supranational and sovereign agency borrowers. This volume is on track to match the NZ$12.3 billion priced in 2013, and significantly above the volumes seen between 2009 and 2012.

We continue to see strong domestic demand from wholesale and retail investors for high quality, rated credits. Trading books are generally very low on inventory, while fund managers are accumulating a growing pool of cash as Kiwisaver funds increase. In addition, the market has seen a number of maturities in 2014 which have not been replaced by new issuance, further adding to demand conditions and providing an environment conducive for issuers looking to access the market.

Annual total market bond issuance

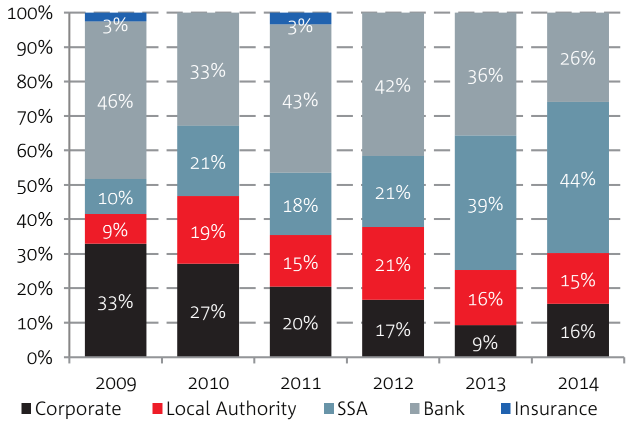


Source: BNZ

Strong demand for corporate credit, albeit low supply

Despite the strong total market volume, corporate issuance in 2014 has been very modest, with a total of NZ$1,615.5 million priced across nine transactions. Infratil, Fonterra (BNZ joint lead), Sky TV (BNZ joint lead), Contact Energy, Auckland International Airport, Mighty River Power, Kiwi Income Property Trust (BNZ joint lead), Toyota Finance NZ, and Fonterra (for a second time) have accessed the market, with a mix of retail and wholesale transactions, receiving strong support domestically.

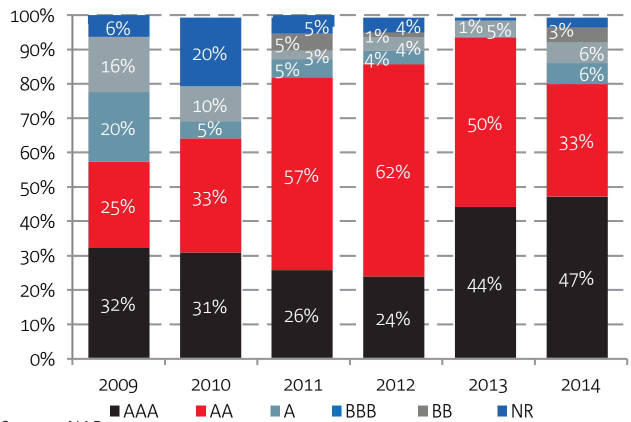
Historical issuance by sector



Source: BNZ

Corporate issuance has remained low comprising only 17% of total NZD volume in 2014 in comparison with its peak of 33% in 2009. This however is an increase from 2013 where corporate issuances only represented 9% of all issuances. The sustained low volumes have been driven by a lack of supply rather than demand, with investors continuing to display strong appetite for corporate credit.

Historical issuance by rating



Source: NAB

In addition, 'BBB' band and below, as well as unrated credits remain underrepresented in the market, declining from 22% in 2009 to 15% in 2014.

Rise in Kauri Issuance

Consistent with 2013 but distinct from previous years, 2014 issuance has again been dominated by 'AAA' rated and SSA Kauris, with supportive basis swap levels and attractive swap spreads in the first part of the year providing a compelling environment for primary activity for both issuers and investors.

Issuance from the sector in 2014 stands at NZ$4.575 billion, with largest prints from Nordic Investment Bank ($425 million, BNZ JLM), World Bank ($550 million) and Rentenbank ($400 million, BNZ Sole Lead Manager).

Activity in the Kauri market has been subdued since August 2014 due in large part to unfavourable movements in swap spreads. We expect to see issuers continuing to access this market as windows of opportunity arise. Surprisingly the Kauri market has been in the top 3-4 currencies for World Bank, Rentenbank and KBN this year.

Growth of the LGFA

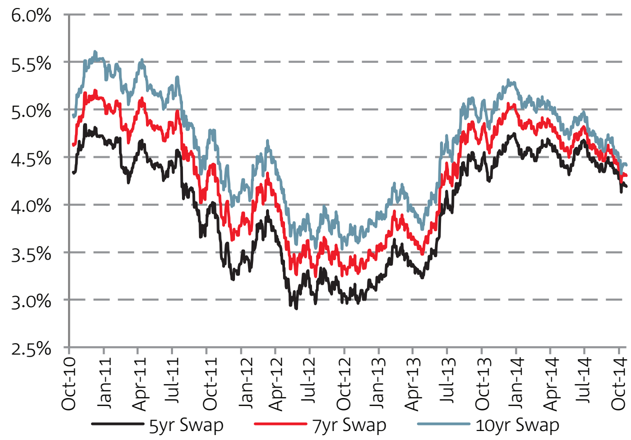
The Local Government Funding Authority (LGFA) was established at the end of 2011 and is owned by 30 New Zealand councils and the Crown. The primary purpose of the LGFA is to provide more efficient funding costs and diversified funding sources for New Zealand local authorities, which prior to the LGFA issued solely in their own names.

The LGFA has successfully completed 13 tenders in 2014 year to date (for a total of $705 million), and has now placed a total of $3.755 billion across multiple transactions.

NZD swap rates

The NZD swap curve has continued to flatten during the year. At current levels, the 7 year tenor is proving to be the most attractive tenor as issuers' spread expectations and yield driven retail investors' coupon aspirations move in to line.

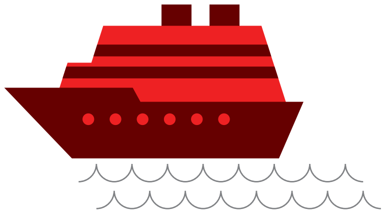
Historical NZD Swap Rates



Source: NAB

Spotlight on Asia

The Asian debt capital market has continued to develop at breakneck speed in 2014



A combination of deregulation of the financial system (predominantly in China), a strong appetite for risk assets and a conducive market environment has been supporting Asian borrowers funding requirements. Issuance windows have remained open for long periods that have given confidence to dealers to push new issuers into the capital market. Liquidity has remained very strong, supporting large issue sizes and record pricing outcomes.

Chinese corporates look to offshore markets for funding

A large and growing list of Chinese corporates have issued debut transactions in the USD Regulation S market this year. Yield has been the key driver for investors, with lower rated issuers and subordinated debt structures receiving the broadest investor support.

In some weeks, the volume of Chinese corporate supply has dominated the Asian debt capital market, leaving little residual room in the pipeline for other more traditional higher grade borrowers.

An increasing proportion of investor allocation has come from Europe, suggesting European investors are becoming more comfortable with Chinese credits.

US market still the primary destination for high grade Asian financials

The large banks of Japan, Singapore and South Korea are well accustomed to global bond markets, having been regular issuers for a number of years now. The US market remains the primary source of wholesale funding for the higher grade 'global' banks residing in Asia.

This extends not just to senior unsecured but to subordinated debt as well. As an example, Oversea-Chinese Banking Corporation has issued two Benchmark sized Tier-2 transactions in USD this year already, as it looks to strengthen its capital position after the acquisition of Hong Kong based, Wing Hang Bank Ltd for ~US$5 billion earlier in the year. The Japanese lender, SMFG and Korean banks, Hana and Woori also issued successful USD Tier 2 transactions in 2014.

Lack of Covered Bond issuance

2014 is notable for what it didn't produce as much as what it did. Despite a long history in Europe, and much anticipation, the first covered bond under the recent Singaporean or South Korean legislation has not eventuated.

It is expected that DBS Bank, Oversea-Chinese Banking Corp and United Overseas Bank may issue more than S$10 billion combined during the next three years. Covered bonds are already popular in Europe and Australia and institutional demand should be strong, given the stable and strong credit ratings of the banks in question.

CNH Bond market emerged as a major alternative to the US dollar market for Chinese issuers

The CNH market continues to deepen and broaden in 2014 despite the recent increase in FX volatility. Throughout 2014, we saw more cross-border CNH bond issuance by both international and Chinese issuers, offering longer-tenor deals and achieving larger average deal sizes.

An increasingly volatile Chinese currency (as opposed to steady appreciation for RMB in the past few years) has also spurred growth in the CNH derivatives markets, including RMB futures, cross currency swap (CCS) , deliverable forwards and other hedging instruments. Notably, we saw daily trading volume of CCS more than doubled from last year. These moves continue to be favourable for the country's FX reform.

Another key theme in 2014 is that more RMB offshore centres emerged and clearing banks assigned, including

Paris, Frankfurt, Luxembourg, Sydney and Toronto. As a result of this, we have seen sovereigns, SSAs and policy banks tapping CNH bonds in various jurisdictions:

- IFC issued the first London-listed CNH bond in March 2014
- BOC Sydney issued the first ASX-listed CNH bond in April 2014
- The UK sovereign issued the first CNH bond in London in October 2014

The establishment of new offshore centres will continue to drive fast growth in the offshore RMB liquidity pool and hence the offshore RMB market.

Opening of the Taiwanese Formosa market

The market in Asia continues to see buoyant demand for private placement trades as investors seek to gain access to names in bespoke issuance currencies and tenors unavailable in public benchmark offerings. Private placements are a cheaper source of funding for issuers given the bespoke nature, smaller size and illiquidity of a secondary market. They are a significant contributor to overall issuance volumes across Asia.

One of the most interesting developments in the Asian private placement market in 2014 was the opening of the domestic Taiwanese market to foreign issuers. Known as “Formosa” bonds, this market allows domestic institutional buyers to invest in foreign issuers by wavering certain restrictions on foreign currency and credit investments in this Formosa bond format.

Taiwan institutional investors (generally Life Insurance companies) are large buyers of a structured product called Zero Coupon or Fixed Rate Callable bonds. These trades are traditionally denominated in USD, have a long legal tenor (i.e. 30 years) but also have the ability to be cancelled (“called”) earlier by the Issuer on specific periodic dates. This optional callability enhances the yield of the bond versus the risk of early redemption (i.e. re-investment risk for the investor). The size of the market for this product in Taiwan from 1 October 2013 to 30 September 2014 was approximately US$4.5 billion of which NAB was an active participant as both an Issuer and dealer. The typical size of a callable bond pre-Formosa was around US$40 million per issue.

By comparison, the Formosa market opened on 30 May 2014 and for the four months ending 30 September 2014 accounted for an additional US$9 billion in callable bond issuance on an average issue size of US$400 million per deal (effectively 10 times the average issuance size pre-Formosa). We expect the Formosa market to continue to grow in 2015 and have estimated total issuance volume at US$17-20 billion over the next 12 months.

The Formosa market has now become an alternative and stable source of long dated (callable) funding in public benchmark size for both frequent financial issuers and sophisticated corporate issuers.

Awards

National Australia Bank has developed and distributed some of the largest finance deals around the world. As such we are consistently ranked as a pre-eminent financial services provider by local and international surveys and publications

KangaNews	Australian Securitisation House of the Year (2012, 2013, 2014)	National Australia Bank
	Australian Domestic Financial Institution Bond Deal of the Year	Bendigo & Adelaide Bank
	Australian Domestic Corporate Bond Deal of the Year	AGL Energy
	Kangaroo Credit Bond Deal of the Year	Fonterra Co-operative Group
	Australian Syndicated Loan Deal of the Year	Telstra Corporation
	Offshore Financial Institution Bond Deal of the Year	National Australia Bank
	US Private Placement Bond Deal of the Year	ETSA Utilities Finance (SA Power Networks)
IJGlobal	#1 MLA Project Finance in Australian PPP's (Aus) 3Q14	National Australia Bank
Project Finance Deals of the Year 2013	APAC PPP Deal of the Year	Sydney Convention Centre
	APAC Ports Deal of the Year	NSW Ports
	APAC Water Deal of the Year	Aquasure
	APAC Healthcare Deal of the Year	New Bendigo Hospital
Project Finance International (PFI) Awards 2013	APAC Deal of the Year	Sydney Convention Centre
	APAC Social Infrastructure of the Year	New Bendigo Hospital
	APAC Transport Deal of the Year	NSW Ports
Infrastructure Partnerships Australia	National Infrastructure Awards Project of the Year 2013	Sydney Desalination Plant
Infrastructure Investor Awards 2013	APAC Infrastructure Deal of the Year	Ports Botany & Kembla
	APAC Transaction of the Year	New Bendigo Hospital
	European Infrastructure of the Year	Stansted Airport

Bloomberg New Energy Finance	#1 Australian Domestic Bank Asset Finance, Clean Energy & Energy Smart Technologies Online League Tables FY 2013	National Australia Bank
Peter Lee Associates Debt Securities Originations Survey Australia 2014 (Ranking against the four major domestic banks)	#1 Strongest Private Placement/'Tap' Capability in the US Market #1 Quality of Insight on Issuance Opportunities and Timing. #1 for Creative Debt Raising Ideas #1 Strongest Domestic Distribution Capability for Hybrid Securities to Retail and Institutional Investors	National Australia Bank
Peter Lee Associates Debt Securities Originations Survey Australia 2014 (Ranking against the four major domestic banks. Financial institution respondents only)	#1 Best Overall advice on Debt Issuance Strategy - Financial Institution Issuers.	National Australia Bank
Peter Lee Associates Debt Securities Originations Survey Australia 2014 (Ranking against all banks)	#1 for Best Structuring Capability for Medium Term Asset/ Mortgage Backed Securities	National Australia Bank

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