Group Corporate Affairs

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ASX Announcement

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National on track to meet earnings targets

National Australia Bank today re-confirmed it is on track to deliver full year cash earnings per share growth at the bottom of its 8 to 11 per cent range for the 2003 financial year after absorbing adverse exchange rate movements and higher pension costs in Europe.

The strength of the Australian dollar is expected to reduce full year cash earnings per share growth by approximately 1.5 per cent against the prior year. Higher pension expenses in the United Kingdom compared with last year will reduce cash earnings per share growth by approximately 1.4 per cent.

Commenting on the full year performance, the National's Managing Director and Chief Executive Officer, Mr Frank Cicutto said: "The Group has continued to perform well in the second half."

"We expect to comfortably achieve double digit underlying profit growth in our retail banking operations in Australia and New Zealand, which reflects the strength of our franchises in these countries," he said.

"Transforming our United Kingdom and Irish businesses through organic growth is a key part of our strategic agenda. This will take time to achieve but we now have a new management team that is making good progress towards this goal.

"I am pleased with the success of Corporate & Institutional Banking in building our client-based activities and the resulting improvement in the quality of income.

"Wealth Management has made good progress in the insurance and investment businesses in Australia and we will continue to invest in Wealth Management's capabilities in Australia and the United Kingdom."

European Pension Schemes

As flagged earlier this year, the Group commissioned an unscheduled interim actuarial review of its European defined benefit schemes as at 30 June 2003 in response to worldwide equity market falls and reductions in interest rates to historically low levels.

Based on this partial interim review, the actuaries have confirmed that each fund exceeds the minimum funding requirements test set by legislation in the United Kingdom. In addition, the actuaries have advised that based on their best estimate assumptions in relation to investment earning and discount rates, the funds have an aggregate surplus position of approximately £0.3 billion. This provides comfort that in the long term the funds are expected to meet their obligations.

Under the relevant accounting standards certain actuarial assumptions are prescribed. The principal difference relates to the use of the yield on high quality corporate bonds as the discount factor for the future liabilities of the fund (notwithstanding that a majority of the funds are invested in equities). Using these conservative assumptions shows an accounting deficit position of approximately £0.5 billion for the funds at 30 June 2003.

From a profit and loss perspective, actuarial gains and losses are taken into account over the average remaining employment period of fund members, generally between 10 and 15 years. In line with advice provided to the market in April this year, a full year pension charge (pre-tax) of approximately £46 million is anticipated (prior year £16 million). This includes an increase in pension expense of approximately £10 million in the final quarter of the 2003 financial year reflecting the 30 June review. It is expected that higher pension charges will continue into the 2004 financial year.

As part of the review of our pension arrangements the Group has decided to close the existing pension schemes to new entrants in the United Kingdom from 1 January 2004. New employees joining the Group from this date onwards in the United Kingdom (with the exception of employees joining National Irish Bank) will be able to enter a new company sponsored defined contribution pension scheme.

Operational Performance

At the Group level, banking income has been driven by good performances in Australia and New Zealand. Loan growth has been strong, dominated by the mortgage market. The decline in net interest margin slowed in the second half. Other operating income is expected to show good growth driven by Australia and New Zealand retail banking and Corporate & Institutional Banking's strong client-based deal flow.

Expenses for the year are expected to be higher reflecting the impact of the increase in the European pension fund expense, higher compliance costs, salary increases and higher occupancy costs. The Group's expenses also reflect considerable investment expenditure on wealth management and our banking operations in the United Kingdom.

The Group's Positioning for Growth initiatives remain on track to deliver $370 million of cost savings by the end of the 2004 financial year.

Asset quality remains sound and we expect the full year charge to provide for doubtful debts to be in line with the prior year charge. This includes a further provision for King Brothers Bus Co in the second half of a similar size to the interim provision in March.

Financial Services Australia has continued to perform well reflecting its strong competitive position. Underlying profit growth is expected to be comfortably in double digits although net profit will be restrained by the King Brothers Bus Co provision. Market share gains were made in business and housing lending. Business volumes are expected to show growth of approximately 9 per cent and housing volumes approximately 20 per cent for the year.

Financial Services Europe is expected to produce a result comparable with last year in local currency terms – which is in line with expectations. Higher expenses, including pension costs, will be offset by lower charges to provide for doubtful debts resulting from improved asset quality. A stronger Australian dollar will mean a lower contribution to Group profit upon conversion.

Financial Services New Zealand is expected to record an excellent performance year on year with strong income growth, and modest expense growth. We expect double digit growth for the full year but due to additional charges to provide for doubtful debts the second half is expected to be flat on the first half in local currency. The business continues to perform solidly with market share gains in housing lending and solid business lending growth.

Corporate & Institutional Banking is expected to record modest profit growth over the previous year. Income flow from customer related business has helped to offset softer markets income. Asset quality remains sound.

Wealth Management is expected to show an improved operating result on last year driven by strong growth in investment earnings in the second half, and solid life company operating margins. The results accommodate continuing substantial investment in the strategic platform in Australia and the United Kingdom.

Mr Cicutto concluded: "We will continue to manage effectively the factors under our control. I am pleased with our performance and note that had it not been for higher pension costs and the movement in the Australian dollar we would be expecting a result at the top end of our forecast."

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