Management Discussion and Analysis

Macquarie Bank

Half-year ended 30 September 2019

NOTICE TO READERS

The purpose of this report is to provide information supplementary to the Macquarie Bank Limited Disclosure Report (U.S. Version) for the half-year ended 30 September 2019 and the Financial Report within the Macquarie Bank Limited Interim Report (the Financial Report) for the half-year ended 30 September 2019, including further detail in relation to key elements of Macquarie Bank Limited and its subsidiaries' (Macquarie Bank, the Consolidated Entity) financial performance and financial position. The report also outlines the funding and capital profile of the Consolidated Entity.

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

DATE OF THIS REPORT

Date of this report

This report has been prepared for the half-year ended 30 September 2019 and is current as at 1 November.

EXPLANATORY NOTES

Comparative information and conventions

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

References to the prior corresponding period (pcp) are to the six months ended 30 September 2018.

References to the prior period are to the six months ended 31 March 2019.

References to the current period and current half-year are to the six months ended 30 September 2019.

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

INDEPENDENT AUDITOR'S REVIEW REPORT

This document should be read in conjunction with the Financial Report for the half-year ended 30 September 2019, which was subject to independent review by PricewaterhouseCoopers.

PricewaterhouseCoopers' independent auditor's review report to the members of Macquarie Bank Limited dated 1 November 2019 was unqualified.

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

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Result overview

1.1 Executive summary

1H20 Net profit

$A992m

↑63% on pcp[1]

1H20 Net operating income

$A3,430m

↑20% on pcp[1]

1H20 Operating expenses

$A2,108m

↑6% on pcp[1]

1H20 Net profit contribution[2] by Operating Group

Banking and Financial Services

$A384m

↑2% on pcp

- Growth in BFS deposits, Australian loan portfolio and funds on platform average volumes
- Reduced average headcount mainly due to the realignment of the wealth advice business to focus on the high net worth segment.

Partially offset by:

- Lower wealth management fee income associated with realigning the wealth advice business to focus on the high net worth segment
- Increased costs associated with investment in technology to support business growth and to meet regulatory requirements
- Higher credit provisions in business banking loans and leasing.

Commodities and Global Markets

$A1,145m

↑42% on pcp

- Strong results across the commodities platform from increased client hedging activity particularly in Global Oil, North American Gas and Power and EMEA Gas and Power
- Timing of income recognition on storage and transport agreements
- Improved foreign exchange, interest rates and credit results driven by increased client activity across all regions
- Improved equity trading and retail results primarily in Asian markets.

Partially offset by:

- Increased operating expenses driven by expenditure on upgrading technology infrastructure and increased cost of regulatory compliance.

Operating Group updates

In the current period, CAF's businesses were aligned to other Operating Groups, where they have the greatest opportunities in terms of shared clients and complementary offerings:

- CAF Asset Finance moved to CGM, reflecting a longstanding, shared focus on innovative financing solutions for corporates, some of which are already shared clients.
- Certain fiduciary businesses, such as the infrastructure debt business (MIDIS), moved from CAF Asset Finance in the Bank Group to MAM in the Non-Bank Group.

In addition, the prior period included the transfer of Macquarie Bank's Australian vehicle finance business from CAF into BFS.

Comparatives have been reclassified to reflect the reorganisation of the CAF businesses.

DISCONTINUED OPERATIONS

On 10 December 2018, the economic risks and rewards of the CAF Principal Finance and Transportation Finance businesses were transferred at fair value to Macquarie Finance Holdings Pty Limited (MFHPL). The businesses were classified as discontinued operations which resulted in an operating profit of $A128 million in the prior corresponding period and $A321 million in the prior period being separately presented in the Income Statement together with a gain on disposal of $A507 million also being recognised in the prior period.

The financial information disclosed relates to the Consolidated Entity's continuing operations.

[1] From continuing operations only.
[2] Net profit contribution is management accounting profit before unallocated corporate costs, profit share and income tax.

1.1 Executive summary

Continued

Profit attributable to the ordinary equity holder

$A992m

35% on pcp

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	Sep 18	Mar 19	Sep-18
	$Am	$Am	$Am	%	%
Financial performance summary					
Net interest income	981	892	1,086	*10*	*(10)*
Fee and commission income	594	658	573	*(10)*	*4*
Net trading income	1,434	1,378	1,148	*4*	*25*
Net operating lease income	160	157	132	*2*	*21*
Share of net profits of associates and joint ventures	6	19	9	*(68)*	*(33)*
Credit impairment charges	(81)	(80)	(51)	*1*	*59*
Other impairment charges	(4)	(114)	(2)	*(96)*	*100*
Other operating income and charges	340	136	(30)	*150*	*
Net operating income	3,430	3,046	2,865	*13*	*20*
Employment expenses	(735)	(796)	(652)	*(8)*	*13*
Brokerage, commission and trading-related expenses	(307)	(386)	(391)	*(20)*	*(21)*
Occupancy expenses	(52)	(67)	(50)	*(22)*	*4*
Non-salary technology expenses	(85)	(86)	(81)	*(1)*	*5*
Other operating expenses	(929)	(1,109)	(814)	*(16)*	*14*
Total operating expenses	(2,108)	(2,444)	(1,988)	*(14)*	*6*
Operating profit from continuing operations before income tax	1,322	602	877	*120*	*51*
Income tax expense from continuing operations	(324)	(135)	(259)	*140*	*25*
Profit from continuing operations after income tax	998	467	618	*114*	*61*
Profit from discontinued operations after income tax	–	828	128	*(100)*	*(100)*
Profit from continuing and discontinued operations after income tax	998	1,295	746	*(23)*	*34*
Profit attributable to non-controlling interests	–	–	(4)	–	*(100)*
Profit attributable to equity holder of Macquarie Bank Limited	998	1,295	742	*(23)*	*35*
Distribution paid or provided for on Macquarie Income Securities	(6)	(8)	(7)	*(25)*	*(14)*
Profit attributable to the ordinary equity holder of Macquarie Bank Limited	992	1,287	735	*(23)*	*35*
From continuing operations	992	459	607	*116*	*63*
From discontinued operations	–	828	128	*(100)*	*(100)*
Key metrics					
Expense to income ratio (%)	61.5	80.2	69.4		
Effective tax rate from continuing operations (%)	24.5	22.4	29.7		

Net operating income

Net operating income of $A3,430 million for the half-year ended 30 September 2019 increased 20% from $A2,865 million in the prior corresponding period, mainly driven by higher Other operating income and charges as well as Net interest and trading income. This was partially offset by higher Credit and Other impairment charges.

Net interest and trading income

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
2,415	2,270	2,234

8% on prior corresponding period

- Strong results in CGM across the commodities platform from increased client hedging activity, particularly in Global Oil, North American Gas and Power and EMEA Gas and Power and timing of income recognition on storage and transport agreements. There was also a solid contribution from Agriculture, Metals and Mining
- Growth in BFS deposits and Australian loan portfolio average volumes in BFS.

Partially offset by:

- Reduced contributions from North American Gas Inventory management and trading following a strong prior corresponding period in CGM
- Accounting volatility from changes in the fair value on economic hedges and lower earnings on capital in Corporate
- The sale of an investment in Macquarie Pacific Funding (MPF) in BFS.

Fee and commission income

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
594	658	573

4% on prior corresponding period

- Increased fee contributions from Index products and retail products in the technology sector in CGM.

Partially offset by:

- Lower wealth management fee income associated with realigning the wealth advice business to focus on the high net worth segment in BFS

Net operating lease income

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
160	157	132

21% on prior corresponding period

- Higher secondary income from the Technology, Media and Telecoms (TMT) portfolios within CGM.

Share of net profits of associates and joint ventures

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
6	19	9

33% on prior corresponding period

- Decrease reflecting performance of underlying investments.

Credit and Other impairment charges

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
(85)	(194)	(53)

60% on prior corresponding period

- Higher credit provisions in business banking loans and leasing in BFS
- Write-downs on specific underperforming financing facilities and impairment charges related to a small number of commodity equity positions in CGM.

Other operating income and charges

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
340	136	(30)

significantly on prior corresponding period

- The recognition of a gain in Corporate on the sale of Macquarie Specialised Investment Solutions (MSIS) fiduciary businesses to Macquarie Asset Management Holdings Pty Limited (MAMHPL), a related party of MBL, owned 100% by MGL.

1.1 Executive summary
Continued

Operating expenses
Total operating expenses of $A2,108 million for the half-year ended 30 September 2019 increased 6% from $A1,988 million in the prior corresponding period mainly driven by higher Other operating expenses and Occupancy, and Employment expenses partially offset by a decrease in Brokerage, commission and trading-related expenses.

Key drivers included:

Employment expenses

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
735	796	652

↑13% on prior corresponding period

- Higher performance-related profit share mainly driven by the overall performance of the Operating Groups
- Higher share-based payments expense mainly driven by the accelerated amortisation of prior years' equity awards to retiring Key Management Personnel.

Brokerage, commission and trading-related expenses

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
307	386	391

↓21% on prior corresponding period

- Reductions in brokerage across equities markets in CGM
- The sale of an investment in Macquarie Pacific Funding in BFS.

Non-salary technology expenses

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
85	86	81

↑5% on prior corresponding period

- Higher technology expenses from investment and support of business growth.

Other operating expenses and Occupancy

HALF-YEAR TO		
30 Sep 19 $Am	31 Mar 19 $Am	30 Sep 18 $Am
981	1,176	864

↑14% on prior corresponding period

- Increased recoveries for support services received by the Bank Group due to higher business activity.

Income tax expense
Income tax expense for the half-year ended 30 September 2019 was $A324 million, a 25% increase from $A259 million from continuing operations in the prior corresponding period. The effective tax rate for the half-year ended 30 September 2019 was 24.5%, down from 29.7% in the prior corresponding period and up from 22.4% in the prior period.

The lower effective tax rate compared to the prior corresponding period was mainly driven by the geographic composition and nature of earnings.

Note on adoption of new Australian Accounting Standards
The September 2019 financial results reflect the adoption of AASB 16 *Leases* (AASB 16) on 1 April 2019. As permitted by AASB 16, the Consolidated Entity has not restated previously reported financial periods.

Refer to Note 1 *Summary of significant accounting policies* in the Financial Report for details regarding the Consolidated Entity's transition to AASB 16. No material transition adjustments arose following the adoption of AASB 16.

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02

Financial performance analysis

2.1 Net interest and trading income

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
Net interest income	**981**	892	1,086	*10*	*(10)*
Net trading income	**1,434**	1,378	1,148	*4*	*25*
Net interest and trading income	**2,415**	2,270	2,234	*6*	*8*

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

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

For businesses that predominantly earn income from lending activities, derivatives that hedge interest rate risk are required to be measured at fair value. The changes in fair value (volatility) is recognised in net trading income unless hedge accounting is applied by the Consolidated Entity, where either the hedged item is revalued for changes in fair value that are attributable to the hedged risk to remove the volatility, or the fair value volatility on the derivative is deferred until the hedged transaction is recognised in the income statement. For segment reporting, derivatives are accounted for on an accrual basis in the results of the applicable Operating Groups, with changes in fair value recognised within the Corporate segment and is managed via the application of hedge accounting.

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

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
BFS	**838**	845	834	*(1)*	*<1*
CGM					
Commodities	**1,013**	1,046	780	*(3)*	*30*
Foreign exchange, interest rates and credit	**333**	272	275	*22*	*21*
Equities	**143**	45	119	*218*	*20*
Specialised and Asset Finance	**78**	47	88	*66*	*(11)*
Corporate	**10**	15	138	*(33)*	*(93)*
Net interest and trading income	**2,415**	2,270	2,234	*6*	*8*

2.1 Net interest and trading income

Continued

Net interest and trading income of $A2,415 million for the half-year ended 30 September 2019 increased 8% from $A2,234 million in the prior corresponding period.

BFS

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

Net interest and trading income of $A838 million for the half-year ended 30 September 2019 was in line with $A834 million in the prior corresponding period. This was due to a 14% growth in the average BFS deposit balance and a 9% growth in average Australian loan and lease portfolio volumes, partially offset by the sale of an investment in MPF in the current period.

As at 30 September 2019 the deposit and Australian loan and lease portfolios included:

- BFS deposits of $A56.2 billion, up 5% from $A53.4 billion as at 31 March 2019;
- Australian mortgage volumes of $A43.6 billion, up 13% from $A38.5 billion as at 31 March 2019;
- Australian vehicle finance volumes of $A14.7 billion, down 3% from $A15.2 billion as at 31 March 2019; and
- Business banking loan volumes of $A8.5 billion, up 4% from $A8.2 billion as at 31 March 2019.

CGM

Commodities

Net interest and trading income from commodity related activities is generated from the provision of hedging and risk management services and loans and working capital finance to clients across a range of commodity sectors including metals, energy and agriculture.

Risk management products income is mainly driven by client volumes, which are influenced by the level of price volatility in the markets in which those clients operate. CGM enters into financial and physical contracts including exchange traded derivatives, over-the-counter (OTC) derivatives, storage contracts and transportation agreements as part of its commodities platform. These arrangements enable CGM to facilitate client transactions and provide CGM with trading opportunities where there is an imbalance between the supply and demand for commodities.

Revenue is dependent on a number of factors including the volume of transactions, the level of risk assumed and the volatility of price movements across commodity markets and products. Storage contracts and transportation agreements, which are managed on a fair value basis for financial and risk management purposes, are required to be accounted for on an accruals basis for statutory reporting purposes, which may result in some variability in the timing of reported income.

Net interest and trading income from commodities of $A1,013 million for the half-year ended 30 September 2019 increased 30% from $A780 million in the prior corresponding period. The current period included strong results across the commodities platform from increased client hedging activity in energy markets including Global Oil, North American Gas and Power, and EMEA Gas and Power in comparison with the prior corresponding period primarily driven by increased commodity price volatility. There was also a solid contribution from Agriculture, Metals and Mining.

Lending and Financing income decreased mainly due to a reduction in agricultural loans and reduced activity in the gas and power sectors.

The current period result was also driven by the timing of income recognition on storage and transport for oil and gas contract agreements, partially offset by reduced contributions from North American Gas, which benefited from supply and demand imbalances across specific American regions in the prior corresponding period.

Foreign exchange, interest rates and credit

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

Net interest and trading income from foreign exchange, interest rates and credit related activities of $A333 million for the half-year ended 30 September 2019 increased 21% from $A275 million in the prior corresponding period, mainly driven by increased client activity across all regions in a variety of structured interest rate and foreign exchange products.

Equities

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

Equities net interest and trading income of $A143 million for the half-year ended 30 September 2019 increased 20% from $A119 million in the prior corresponding period, reflecting increased opportunities in China and an improved performance from retail products across Asia.

Specialised and Asset Finance (SAF)

Net interest and trading income in Specialised and Asset Finance predominately relates to net income from the loan and finance lease portfolios (including ship finance, equipment and technology financing) and the funding costs associated with the operating lease portfolios (including energy, telecommunication and mining assets).

Net interest and trading income of $A78 million for the half-year ended 30 September 2019 decreased 11% from $A88 million in the prior corresponding period. The decrease was largely driven by lower secondary income from equipment finance lease portfolio within TMT, increased funding costs from growth in the TMT operating lease portfolio and a decline in the non-core legacy retail portfolio which was partially offset by favourable foreign exchange movements.

The loan and finance lease portfolio was $A5.5 billion as at 30 September 2019, an increase of 2% from $A5.4 billion as at 31 March 2019. The increase was largely due to the growth in the funds products, partially offset by the legacy and equipment finance portfolio.

Corporate

Net interest and trading income in the Corporate segment includes the net result of managing Macquarie Bank's liquidity and funding requirements, earnings on capital, funding costs associated with non-core investments held centrally and accounting volatility arising from movements in underlying rates relating to economically hedged positions where hedge accounting in terms of AASB 9 is unable to be achieved.

Net interest and trading income of $A10 million for the half-year ended 30 September 2019 decreased 93% from $A138 million in the prior corresponding period primarily due to accounting volatility from the changes in the fair value on economic hedges and lower earnings on capital.

2.2 Fee and commission income

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
Brokerage and other trading-related income	**237**	259	273	*(8)*	*(13)*
Other fee and commission income[1]	**357**	399	300	*(11)*	*19*
Total fee and commission income	**594**	658	573	*(10)*	*4*

Fee and commission income comprises of Brokerage and other trading-related income and Other fee and commission income. Brokerage and other trading-related income primarily includes brokerage income from the Equities and Futures businesses in CGM and brokerage income from the BFS Wrap and Visions platforms. Other fee and commission income includes fees earned on a range of BFS' products and services including provision of wealth services, mortgages, vehicle finance, credit cards, business loans and deposits, while CGM includes income from structured, index and retail products.

Total fee and commission income of $A594 million for the half-year ended 30 September 2019 increased 4% from $A573 million in the prior corresponding period primarily due to increased fee contributions from Index products and retail products in the technology sector in CGM, partially offset by a reduction in BFS primarily due to the realignment of the wealth advice business to focus on the high net worth segment.

[1] Other fee and commission income includes Portfolio administration fees, Lending fees and Other fee and commission income as disclosed in Note 2 *Operating profit from continuing operations before income tax* of the Financial Report.

2.3 Net operating lease income

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	*Sep 18*	*Mar 19*	*Sep 18*
	$Am	$Am	*$Am*	*%*	*%*
Rental income	**614**	604	515	*2*	*19*
Depreciation on operating lease assets	**(454)**	(447)	(383)	*2*	*19*
Net operating lease income	**160**	157	132	*2*	*21*

Net operating lease income of $A160 million for the half-year ended 30 September 2019 increased 21% from $A132 million in the prior corresponding period, primarily driven by higher secondary income from the TMT portfolio within CGM.

The total operating lease portfolio was $A2.3 billion as at 30 September 2019, broadly in line with $A2.4 billion as at 31 March 2019.

2.4 Share of net profits of associates and joint ventures

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	*Sep 18*	*Mar 19*	*Sep 18*
	$Am	$Am	*$Am*	*%*	*%*
Share of net profits of associates and joint ventures	**6**	19	9	*(68)*	*(33)*

Share of net profits of associates and joint ventures of $A6 million for the half-year ended 30 September 2019 decreased 33% compared to $A9 million in the prior corresponding period, reflecting the performance of underlying investments.

2.5 Credit and Other impairment charges

	HALF-YEAR TO			*MOVEMENT*	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
Credit impairment (charges)/reversal					
Loan assets	**(94)**	(73)	(64)	*29*	*47*
Financial investments, other assets, undrawn commitments and financial guarantees	**(1)**	(11)	3	*(91)*	*
Recovery of exposures previously written off	**14**	4	10	*250*	*40*
Total credit impairment charges	**(81)**	(80)	(51)	*1*	*59*
Other impairment charges					
Interests in associates and joint ventures	**–**	(102)	–	*(100)*	–
Intangible assets and other non-financial assets	**(4)**	(12)	(2)	*(67)*	*100*
Total other impairment charges	**(4)**	(114)	(2)	*(96)*	*100*
Total credit and other impairment charges	**(85)**	(194)	(53)	*(56)*	*60*

Total credit and other impairment charges of $A85 million for the half-year ended 30 September 2019 increased 60% from $A53 million in the prior corresponding period.

Credit impairment charges

Credit impairment charges of $A81 million for the half-year ended 30 September 2019 increased 59% from $A51 million in the prior corresponding period due to higher credit provisions in business banking loans and leasing in BFS and write-downs on specific underperforming financing facilities in CGM.

Other impairment charges

Other impairment charges of $A4 million for the half-year ended 30 September 2019 increased 100% from $A2 million in the prior corresponding period and decreased 96% from $A114 million in the prior period. The prior period included impairments on certain commodity-related equity positions in CGM.

2.6 Other operating income and charges

	HALF-YEAR TO			*MOVEMENT*	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
Investment income					
Net gain on equity and debt investments	**11**	29	26	*(62)*	*(58)*
Net gain on interests in associates and joint ventures	**9**	62	–	*(85)*	*
Net gain on sale of businesses and subsidiaries held for sale	**242**	(3)	3	*	*
Net gain on change of control, joint control and/or significant influence	**–**	10	–	*(100)*	–
Total investment income	**262**	98	29	*167*	*
Other income	**78**	38	(59)	*105*	*
Total other operating income and charges	**340**	136	(30)	*150*	*

Total other operating income of $A340 million for the half-year ended 30 September 2019 compared to charges of $A30 million in the prior corresponding period, mainly driven by higher investment income in Corporate.

Investment income

Investment income of $A262 million for the half-year ended 30 September 2019, a significant increase from $A29 million in the prior corresponding period mainly due to the recognition of a gain in Corporate on the sale of MSIS fiduciary businesses to MAMHPL, a related party of MBL, owned 100% by MGL.

Other income

Other income of $A78 million for the half-year ended 30 September 2019 compared to charges of $A59 million in the prior corresponding period, primarily driven by Corporate which included consolidation adjustments recognised in the current period. The prior corresponding period included the impact of a structural change in funding between the Bank and Non-Bank Groups in Corporate.

2.7 Operating expenses

	HALF-YEAR TO			*MOVEMENT*	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
Employment expenses					
Salary and related costs including commissions, superannuation and performance-related profit share	**(622)**	(722)	(583)	*(14)*	*7*
Share-based payments	**(111)**	(78)	(66)	*42*	*68*
(Provision)/reversal for long service leave and annual leave	**(2)**	4	(3)	*	*(33)*
Total employment expenses	**(735)**	(796)	(652)	*(8)*	*13*
Brokerage, commission and trading-related expenses	**(307)**	(386)	(391)	*(20)*	*(21)*
Occupancy expenses	**(52)**	(67)	(50)	*(22)*	*4*
Non-salary technology expenses	**(85)**	(86)	(81)	*(1)*	*5*
Other operating expenses					
Service cost recoveries from related entities	**(717)**	(705)	(614)	*2*	*17*
Professional fees	**(69)**	(75)	(59)	*(8)*	*17*
Travel and entertainment expenses	**(22)**	(24)	(23)	*(8)*	*(4)*
Advertising and communication expenses	**(15)**	(15)	(16)	–	*(6)*
Amortisation of intangibles assets	**(9)**	(9)	(10)	–	*(10)*
Auditor's remuneration	**(10)**	(15)	(9)	*(33)*	*11*
Other expenses	**(87)**	(266)	(83)	*(67)*	*5*
Total other operating expenses	**(929)**	(1,109)	(814)	*(16)*	*14*
Total operating expenses	**(2,108)**	(2,444)	(1,988)	*(14)*	*6*

Total operating expenses of $A2,108 million for the half-year ended 30 September 2019 increased 6% from $A1,988 million in the prior corresponding period mainly due to increased recoveries for support services received by the Bank Group and higher performance-related profit share and share-based payments expense. This was partially offset by a decrease in Brokerage, commission and trading-related expenses.

Key drivers of the movement included:

- Total employment expenses of $A735 million for the half-year ended 30 September 2019 increased 13% from $A652 million in the prior corresponding period due to higher performance-related profit share mainly driven by the overall performance of the Operating Groups and higher share-based payments expense mainly driven by the accelerated amortisation of prior years' equity awards for retiring Key Management Personnel. This was partially offset by a decrease in salary and related costs driven by lower headcount in BFS due to the realignment of the wealth advice business to focus on the high net worth segment.
- Brokerage, commission and trading-related expenses of $A307 million for the half-year ended 30 September 2019 decreased 21% from $A391 million in the prior corresponding period primarily due to reductions in brokerage across equities markets in CGM and the sale of an investment in MPF in the current period in BFS.
- Total other operating expenses of $A929 million for the half-year ended 30 September 2019 increased 14% from $A814 million in the prior corresponding period, primarily due to increased recoveries for support services received by the Bank Group due to higher business activity. The prior period included the recognition of certain legacy-related expenses in Corporate.

2.8 Headcount

	AS AT			MOVEMENT	
				Mar 19	*Sep 18*
	Sep 19	Mar 19	Sep 18	*%*	*%*
Headcount by Operating Group[1]					
BFS	**2,643**	2,768	2,948	*(5)*	*(10)*
CGM	**1,662**	1,676	1,667	*(1)*	*(<1)*
Total headcount – Operating Groups	**4,305**	4,444	4,615	*(3)*	*(7)*
Total headcount – Discontinued Operations[2,3]	**–**	49	267	*(100)*	*(100)*
Total headcount – Corporate[4]	**8**	62	70	*(87)*	*(89)*
Total headcount	**4,313**	4,555	4,952	*(5)*	*(13)*
Headcount by region					
Australia[5]	**2,962**	3,106	3,348	*(5)*	*(12)*
International:					
Americas	**451**	494	540	*(9)*	*(16)*
Asia	**222**	242	306	*(8)*	*(27)*
Europe, Middle East and Africa	**678**	713	758	*(5)*	*(11)*
Total headcount – International	**1,351**	1,449	1,604	*(7)*	*(16)*
Total headcount	**4,313**	4,555	4,952	*(5)*	*(13)*
International headcount ratio (%)	**31**	32	32		

Total headcount decreased 13% to 4,313 as at 30 September 2019 from 4,952 as at 30 September 2018 due to the realignment of the wealth advice business to focus on the high net worth segment in BFS and the transfer of CAF Principal Finance and Transportation Finance businesses to MFHPL. In addition, certain fiduciary businesses, such as the infrastructure debt business (MIDIS), transferred from CAF Asset Finance to MAM.

[1] Headcount numbers in this document includes certain staff employed in operationally segregated subsidiaries (OSS).
[2] The prior corresponding period included 42 headcount relating to the Macquarie Investment Management (MIM) business within MAM which was sold to MFHPL and its subsidiaries on 15 April 2015. These employees were subsequently transferred to MFHPL in December 2018.
[3] The prior corresponding period and prior period included headcount relating to the Principal Finance and Transportation Finance businesses within CAF which were sold to MFHPL and its subsidiaries on 10 December 2018. These employees were subsequently transferred to MFHPL in May 2019.
[4] The prior corresponding period and prior period headcount numbers include the headcount of the MSIS (MIDIS) Fiduciary businesses transferred from CAF to MAM.
[5] Includes New Zealand.

2.9 Income tax expense

	HALF-YEAR TO		
	Sep 19	Mar 19	Sep 18
	$Am	$Am	$Am
Operating profit before income tax	**1,322**	602	877
Prima facie tax @ 30%	**397**	181	263
Income tax permanent differences	**(73)**	(46)	(4)
Income tax expense	**324**	135	259
Effective tax rate[1]	**24.5%**	22.4%	29.7%

Income tax expense for the half-year ended 30 September 2019 of $A324 million increased 25% from $A259 million from continuing operations in the prior corresponding period. The effective tax rate for the half-year ended 30 September 2019 was 24.5%, down from 29.7% in the prior corresponding period and up from 22.4% in the prior period.

The lower effective tax rate compared to the prior corresponding period was mainly driven by the geographic composition and nature of earnings.

[1] The effective tax rate is calculated on Operating profit before income tax and after non-controlling interests. Non-controlling interests reduced operating profit before income tax by Nil for the half-year ended 30 September 2019 (31 March 2019: Nil; 30 September 2018: $A4 million).

03

Segment analysis

3.1 Basis of preparation

Operating Segments

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

For internal reporting, performance measurement and risk management purposes, the Consolidated Entity is divided into Operating Groups and a Corporate segment.

The prior period included the transfer of Macquarie Bank's Australian vehicle finance business from CAF into BFS. During the current period, CAF's core business in the Bank Group was aligned to CGM, reflecting a longstanding, shared focus on innovative financing solutions for corporates, some of which are already shared clients. In addition, certain fiduciary businesses, such as the infrastructure debt business (MIDIS), moved from CAF Asset Finance in the Bank Group to MAM in the Non-Bank Group. Comparatives have been reclassified to reflect this reorganisation between the Operating Groups.

These segments have been set up based on the different core products and services offered. Segment information has been prepared in accordance with the basis of preparation described below.

Following the reorganisation described above, the Operating Groups comprise:

– **BFS** provides a diverse range of personal banking, wealth management, business banking and vehicle finance products and services to retail clients, advisers, brokers and business clients
– **CGM** provides integrated, end-to-end offering across global markets including equities, fixed income, foreign exchange, commodities and technology, media and telecoms as well as providing clients with risk and capital solutions across physical and financial markets. CGM also delivers a diverse range of tailored finance solutions globally across a variety of industries and asset classes.

The financial information disclosed relates to the Consolidated Entity's continuing operations.

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

Items of income and expense within the Corporate segment include the net result of managing Macquarie Bank's liquidity and funding requirements, earnings on capital and the residual accounting volatility relating to economically hedged positions where hedge accounting is applied as well as accounting volatility for other economically hedged positions where hedge accounting is not applicable. Other items of income and expenses include earnings from investments, central credit and asset related impairments, unallocated head office costs and costs of central service groups, the Consolidated Entity's performance-related profit share and share-based payments expense, income tax expense and certain distributions attributable to certain non-controlling interests and holders of Macquarie Income Securities (MIS).

Below is a selection of key policies applied in determining Operating Segment results.

Internal funding arrangements

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

Generally, Operating Groups may only source funding directly from external sources where the funding is secured by the Operating Group's assets. In such cases the Operating Group bears the funding costs directly and Group Treasury may levy additional charges where appropriate.

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

Transactions between Operating Segments

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

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

Accounting for derivatives that hedge interest rate risk

For businesses that predominantly earn income from lending activities, derivatives that hedge interest rate risk are required to be measured at fair value. The changes in fair value (volatility) is recognised in net trading income unless hedge accounting is applied by the Consolidated Entity, where either the hedged item is revalued for changes in fair value that is attributable to hedged risk to remove the volatility, or the fair value volatility on the derivative is deferred until the hedged transaction is recognised in the income statement. For segment reporting, derivatives are accounted for on an accrual basis in the results of the applicable Operating Groups, with changes in fair value recognised within the Corporate segment and managed via the application of hedge accounting.

Central service groups

The central service groups provide a range of functions supporting Macquarie Bank's Operating Groups, ensuring they have the appropriate workplace support and systems to operate effectively and the necessary resources to meet their regulatory, compliance, financial reporting, legal and risk management requirements.

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

Performance-related profit share and share-based payments expense

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

Income tax

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

Presentation of segment income statements

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

3.1 Basis of preparation

Continued

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	BFS $Am	CGM $Am	Corporate $Am	Total $Am
Half-year ended 30 September 2019				
Net interest and trading income	838	1,567	10	**2,415**
Fee and commission income	224	363	7	**594**
Net operating lease income	–	157	3	**160**
Share of net (losses)/profits of associates and joint ventures	(3)	9	–	**6**
Other operating income and charges				
Credit and Other impairment charges	(41)	(31)	(13)	**(85)**
Other operating income and charges	–	44	296	**340**
Internal management revenue/(charge)	2	2	(4)	**–**
Net operating income	1,020	2,111	299	**3,430**
Total operating expenses	(636)	(966)	(506)	**(2,108)**
Operating profit/(loss) before income tax	384	1,145	(207)	**1,322**
Income tax expense	-	-	(324)	**(324)**
Profit/(loss) after income tax	384	1,145	(531)	**998**
Profit attributable to non-controlling interests	-	-	-	**-**
Profit/(loss) attributable to equity holder	384	1,145	(531)	**998**
Distributions paid or provided for on MIS	-	-	(6)	**(6)**
Net profit/(loss) contribution from continuing operations	**384**	**1,145**	**(537)**	**992**
Half-year ended 31 March 2019				
Net interest and trading income	845	1,410	15	**2,270**
Fee and commission income	231	383	44	**658**
Net operating lease income	–	153	4	**157**
Share of net profits/(losses) of associates and joint ventures	9	11	(1)	**19**
Other operating income and charges				
Credit and Other impairment charges	(54)	(137)	(3)	**(194)**
Other operating income and charges	19	84	33	**136**
Internal management revenue/(charge)	–	8	(8)	**–**
Net operating income	1,050	1,912	84	**3,046**
Total operating expenses	(673)	(1,033)	(738)	**(2,444)**
Operating profit/(loss) before income tax	377	879	(654)	**602**
Income tax expense	–	–	(135)	**(135)**
Profit/(loss) after income tax	377	879	(789)	**467**
(Profit)/loss attributable to non-controlling interests	–	(1)	1	**–**
Profit/(loss) attributable to equity holder	377	878	(788)	**467**
Distributions paid or provided for on MIS	–	–	(8)	**(8)**
Net profit/(loss) contribution from continuing operations	**377**	**878**	**(796)**	**459**
Half-year ended 30 September 2018				
Net interest and trading income	834	1,262	138	**2,234**
Fee and commission income	242	322	9	**573**
Net operating lease income	–	132	–	**132**
Share of net (losses)/profits of associates and joint ventures	(1)	10	–	**9**
Other operating income and charges				
Credit and Other impairment charges	(28)	(20)	(5)	**(53)**
Other operating income and charges	–	44	(74)	**(30)**
Internal management revenue/(charge)	2	6	(8)	**–**
Net operating income	1,049	1,756	60	**2,865**
Total operating expenses	(673)	(948)	(367)	**(1,988)**
Operating profit/(loss) before income tax	376	808	(307)	**877**
Income tax expense	–	–	(259)	**(259)**
Profit/(loss) after income tax	376	808	(566)	**618**
Profit attributable to non-controlling interests	–	(1)	(3)	**(4)**
Profit/(loss) attributable to equity holder	376	807	(569)	**614**
Distributions paid or provided for on MIS	–	–	(7)	**(7)**
Net profit/(loss) contribution from continuing operations	**376**	**807**	**(576)**	**607**

3.2 BFS

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	%	%
Net interest and trading income	**838**	845	834	*(1)*	*<1*
Fee and commission income					
Wealth management fee income	**142**	146	166	*(3)*	*(14)*
Banking and leasing fee income	**82**	85	76	*(4)*	*8*
Total fee and commission income	**224**	231	242	*(3)*	*(7)*
Share of net (losses)/profits of associates and joint ventures	**(3)**	9	(1)	*	*200*
Other operating income and charges					
Credit impairment charges	**(41)**	(39)	(28)	*5*	*46*
Other impairment charges	**–**	(15)	–	*(100)*	–
Other income	**–**	19	–	*(100)*	–
Total other operating income and charges	**(41)**	(35)	(28)	*17*	*46*
Internal management revenue	**2**	–	2	*	-
Net operating income	**1,020**	1,050	1,049	*(3)*	*(3)*
Operating expenses					
Employment expenses	**(183)**	(203)	(218)	*(10)*	*(16)*
Brokerage, commission and trading-related expenses	**(87)**	(108)	(108)	*(19)*	*(19)*
Technology expenses[1]	**(191)**	(181)	(181)	*6*	*6*
Other operating expenses	**(175)**	(181)	(166)	*(3)*	*5*
Total operating expenses	**(636)**	(673)	(673)	*(5)*	*(5)*
Net profit contribution	**384**	377	376	*2*	*2*
Non-GAAP metrics					
Funds on platform[2] ($Ab)	**91.5**	86.0	88.1	*6*	*4*
Australian loan and lease portfolio[3] ($Ab)	**67.4**	62.5	60.0	*8*	*12*
BFS deposits[4] ($Ab)	**56.2**	53.4	49.4	*5*	*14*
Headcount	**2,643**	2,768	2,948	*(5)*	*(10)*

Net profit contribution of $A384 million for the half-year ended 30 September 2019, up 2% from the prior corresponding period:

- growth in BFS deposits, Australian loan portfolio and funds on platform average volumes
- reduced average headcount mainly due to the realignment of the wealth advice business to focus on the high net worth segment.

Partially offset by:

- lower wealth management fee income associated with realigning the wealth advice business to focus on the high net worth segment
- increased costs associated with investment in technology to support business growth and to meet regulatory requirements
- higher credit provisions in business banking loans and leasing.

[1] Technology expenses include technology staff expenses, depreciation of technology assets, amortisation of capitalised software and maintenance costs.
[2] Funds on platform includes Macquarie Wrap and Vision.
[3] The Australian loan and lease portfolio comprises residential mortgages, loans to Australian businesses, vehicle finance, insurance premium funding and credit cards.
[4] BFS deposits excludes corporate/wholesale deposits.

Net interest and trading income

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

Net interest and trading income of $A838 million for the half-year ended 30 September 2019 was in line with $A834 million in the prior corresponding period. This was due to a 14% growth in the average BFS deposit balance and a 9% growth in average Australian loan and lease portfolio volumes, partially offset by the sale of an investment in MPF in the current period.

As at 30 September 2019 the deposit and Australian loan and lease portfolios included:

– BFS deposits of $A56.2 billion, up 5% from $A53.4 billion as at 31 March 2019;
– Australian mortgage volumes of $A43.6 billion, up 13% from $A38.5 billion as at 31 March 2019;
– Australian vehicle finance volumes of $A14.7 billion, down 3% from $A15.2 billion as at 31 March 2019; and
– Business banking loan volumes of $A8.5 billion, up 4% from $A8.2 billion as at 31 March 2019.

Wealth management fee income

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

Funds on platform closed at $A91.5 billion as at 30 September 2019, an increase of 6% from $A86.0 billion as at 31 March 2019 largely due to net positive client inflows and market movements.

Wealth management fee income of $A142 million for the half-year ended 30 September 2019 decreased 14% from $A166 million in the prior corresponding period due to the realignment of the wealth advice business to focus on the high net worth segment.

Banking and leasing fee income

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

Banking and leasing fee income of $A82 million for the half-year ended 30 September 2019 increased 8% from $A76 million in the prior corresponding period largely driven by increased lending and payment transaction volumes.

Credit impairment charges

Credit impairment charges of $A41 million for the half-year ended 30 September 2019 increased 46% from $A28 million in prior corresponding period largely due to higher provisions in business banking loans and leasing.

Operating expenses

Total operating expenses of $A636 million for the half-year ended 30 September 2019 decreased 5% from $A673 million in the prior corresponding period.

Employment expenses of $A183 million for the half-year ended 30 September 2019 decreased 16% from $A218 million in the prior corresponding period primarily from reduced headcount due to the realignment of the wealth advice business to focus on the high net worth segment.

Brokerage, commission and trading-related expenses of $A87 million for the half-year ended 30 September 2019 decreased 19% from $A108 million in the prior corresponding period, largely due to the sale of an investment in MPF in the current period.

Technology expenses of $A191 million for the half-year ended 30 September 2019 increased 6% from $A181 million in the prior corresponding period to support business growth.

Other operating expenses of $A175 million for the half-year ended 30 September 2019 increased 5% from $A166 million in the prior corresponding period driven by increased risk and regulatory costs.

3.3 CGM

	HALF-YEAR TO			MOVEMENT	
	Sep 19 $Am	Mar 19 $Am	Sep 18 $Am	*Mar 19 %*	*Sep 18 %*
Net interest and trading income					
Commodities	**1,013**	1,046	780	*(3)*	*30*
Foreign exchange, interest rates and credit	**333**	272	275	*22*	*21*
Equities	**143**	45	119	*218*	*20*
Specialised and Asset Finance	**78**	47	88	*66*	*(11)*
Net interest and trading income	**1,567**	1,410	1,262	*11*	*24*
Fee and commission income					
Brokerage and other trading-related income	**212**	230	234	*(8)*	*(9)*
Other fee and commission income	**151**	153	88	*(1)*	*72*
Total fee and commission income	**363**	383	322	*(5)*	*13*
Net operating lease income	**157**	153	132	*3*	*19*
Share of net profits of associates and joint ventures	**9**	11	10	*(18)*	*(10)*
Other operating income and charges					
Net income on equity and debt investments	**12**	68	4	*(82)*	*200*
Credit and Other impairment charges	**(31)**	(137)	(20)	*(77)*	*55*
Other income	**32**	16	40	*100*	*(20)*
Total other operating income and charges	**13**	(53)	24	*	*(46)*
Internal management revenue	**2**	8	6	*(75)*	*(67)*
Net operating income	**2,111**	1,912	1,756	*10*	*20*
Operating expenses					
Employment expenses	**(208)**	(240)	(203)	*(13)*	*2*
Brokerage, commission and trading-related expenses	**(220)**	(279)	(283)	*(21)*	*(22)*
Other operating expenses	**(538)**	(514)	(462)	*5*	*16*
Total operating expenses	**(966)**	(1,033)	(948)	*(6)*	*2*
Non-controlling interests[1]	**-**	(1)	(1)	*(100)*	*(100)*
Net profit contribution	**1,145**	878	807	*30*	*42*
Non-GAAP metrics					
Headcount	**1,662**	1,676	1,667	*(1)*	*(<1)*

Net profit contribution of $A1,145 million for the half-year ended 30 September 2019, up 42% from the prior corresponding period:

- strong results across the commodities platform from increased client hedging activity particularly in Global Oil, North American Gas and Power and EMEA Gas and Power
- timing of income recognition on storage and transport agreements
- improved foreign exchange, interest rates and credit result driven by increased client activity across all regions
- improved equity trading and retail results primarily in Asian markets.

Partially offset by:

- increased operating expenses driven by expenditure on upgrading technology infrastructure and increased cost of regulatory compliance.

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

Commodities net interest and trading income

Net interest and trading income from commodity related activities is generated from the provision of hedging and risk management services and loans and working capital finance to clients across a range of commodity sectors including metals, energy and agriculture.

Risk management products income is mainly driven by client volumes, which are influenced by the level of price volatility in the markets in which those clients operate. CGM enters into financial and physical contracts including exchange traded derivatives, OTC derivatives, storage contracts and transportation agreements as part of its commodities platform. These arrangements enable CGM to facilitate client transactions and provide CGM with trading opportunities where there is an imbalance between the supply and demand for commodities.

Revenue is dependent on a number of factors including the volume of transactions, the level of risk assumed and the volatility of price movements across commodity markets and products. Storage contracts and transportation agreements, which are managed on a fair value basis for financial and risk management purposes, are required to be accounted for on an accruals basis for statutory reporting purposes, which may result in some variability in the timing of reported income.

Net interest and trading income from commodities of $A1,013 million for the half-year ended 30 September 2019 increased 30% from $A780 million in the prior corresponding period. The current period included strong results across the commodities platform from increased client hedging activity in energy markets including Global Oil, North American Gas and Power, and EMEA Gas and Power in comparison with the prior corresponding period primarily driven by increased commodity price volatility. There was also a solid contribution from Agriculture, Metals and Mining.

Lending and financing income decreased mainly due to a reduction in agricultural loans and reduced activity in the gas and power sectors.

The current period result was also driven by the timing of income recognition on storage and transport for oil and gas contract agreements, partially offset by reduced contributions from North American Gas, which benefited from supply and demand imbalances across specific American regions in the prior corresponding period.

Foreign exchange, interest rates and credit net interest and trading income

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

Net interest and trading income from foreign exchange, interest rates and credit related activities of $A333 million for the half-year ended 30 September 2019 increased 21% from $A275 million in the prior corresponding period, mainly driven by increased client activity across all regions in a variety of structured interest rate and foreign exchange products.

Equities net interest and trading income

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

Equities net interest and trading income of $A143 million for the half-year ended 30 September 2019 increased 20% from $A119 million in the prior corresponding period, reflecting increased opportunities in China and an improved performance from retail products across Asia.

Specialised and Asset Finance net interest and trading income

Net interest and trading income in Specialised and Asset Finance predominately relates to net income from the loan and finance lease portfolios (including ship finance, equipment and technology financing) and the funding costs associated with the operating lease portfolios (including energy, telecommunication and mining assets).

Net interest and trading income of $A78 million for the half-year ended 30 September 2019 decreased 11% from $A88 million in the prior corresponding period. The decrease was largely driven by lower secondary income from equipment finance lease portfolio within TMT, increased funding costs from growth in the TMT operating lease portfolio and a decline in the non-core legacy retail portfolio which was partially offset by favourable foreign exchange movements.

The loan and finance lease portfolio was $A5.5 billion as at 30 September 2019, an increase of 2% from $A5.4 billion as at 31 March 2019. The increase was largely due to the growth in the funds products, partially offset by the legacy and equipment finance portfolio.

Fee and commission income

Fee and commission income of $A363 million for the half-year ended 30 September 2019 increased 13% from $A322 million in the prior corresponding period.

The current period included increased fee contributions from Index products and retail products in the technology sector.

Net operating lease income

Net operating lease income of $A157 million for the half-year ended 30 September 2019 was up 19% from $A132 million in the prior corresponding period with the movement driven by higher secondary income from the TMT portfolio. The Energy portfolio contributes the majority of operating lease income and was stable over the period.

The operating lease portfolio was $A2.3 billion as at 30 September 2019, broadly in line with $A2.4 billion as at 31 March 2019.

Net income on equity and debt investments

Net income on equity and debt investments of $A12 million for the half-year ended 30 September 2019 increased significantly from $A4 million in the prior corresponding period. The increase was driven by the equity realisation on a specific holding in the metals sector.

Credit and Other impairment charges

Credit and Other impairment charges of $A31 million for the half-year ended 30 September 2019 increased 55% from $A20 million in the prior corresponding period, and a decrease of 77% from $A137 million in the prior period which included higher levels of impairments on specific underperforming financing facilities and a small number of commodity equity positions.

Operating expenses

Total operating expenses of $A966 million for the half-year ended 30 September 2019 increased 2% from $A948 million in the prior corresponding period.

Employment expenses of $A208 million for the half-year ended 30 September 2019 increased 2% from $A203 million in the prior corresponding period mainly due to the impact of foreign exchange movements.

Brokerage, commission and trading-related expenses include fees paid in relation to trading-related activities. Brokerage, commission and trading-related expenses of $A220 million for the half-year ended 30 September 2019 decreased 22% from $A283 million in the prior corresponding period due to reductions in brokerage across equities markets.

Other operating expenses of $A538 million for the half-year ended 30 September 2019 increased 16% from $A462 million in the prior corresponding period, reflecting the impact of upgrading technology infrastructure as well as increased regulatory compliance costs.

3.4 Corporate

	HALF-YEAR TO			MOVEMENT	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Am	$Am	$Am	*%*	*%*
Net interest and trading income	**10**	15	138	*(33)*	*(93)*
Fee and commission income	**7**	44	9	*(84)*	*(22)*
Net operating lease income	**3**	4	–	*(25)*	*
Share of net losses of associates and joint ventures	**–**	(1)	–	*(100)*	–
Other operating income and charges					
Net income on equity and debt investments	**242**	5	–	*	*
Credit and Other impairment charges	**(13)**	(3)	(5)	*	*160*
Other income and charges	**54**	28	(74)	*93*	*
Total other operating income and charges	**283**	30	(79)	*	*
Internal management charge	**(4)**	(8)	(8)	*(50)*	*(50)*
Net operating income	**299**	84	60	*256*	*
Operating expenses					
Employment expenses	**(344)**	(353)	(231)	*(3)*	*49*
Brokerage, commission and trading-related expenses	**–**	1	–	*(100)*	–
Other operating expenses	**(162)**	(386)	(136)	*(58)*	*19*
Total operating expenses	**(506)**	(738)	(367)	*(31)*	*38*
Income tax expense	**(324)**	(135)	(259)	*140*	*25*
Macquarie Income Securities	**(6)**	(8)	(7)	*(25)*	*(14)*
Non-controlling interests[1]	**–**	1	(3)	*(100)*	*(100)*
Net loss contribution	**(537)**	(796)	(576)	*(33)*	*(7)*
Non-GAAP metrics					
Headcount[2]	**8**	62	70	*(87)*	*(89)*

The Corporate segment comprises head office and central service groups including Group Treasury, and certain investments that are neither core for strategic reasons nor aligned to an Operating Group. The Corporate segment also includes costs that are not allocated to the Operating Groups, including performance-related profit share and share-based payments expense, income tax expense and the net result of managing Macquarie Bank's liquidity and funding requirements.

[1] "Non-controlling interests" adjusts reported consolidated profit or loss for the share that is attributable to non-controlling interests, such that the net profit contribution represents the net profit attributable to the ordinary equity holder.
[2] The prior corresponding period and prior period headcount numbers include the headcount of the MSIS (MIDIS) Fiduciary businesses transferred from CAF to MAM.

Net interest and trading income

Net interest and trading income in the Corporate segment includes the net result of managing Macquarie Bank's liquidity and funding requirements, earnings on capital, funding costs associated with non-core investments held centrally and accounting volatility arising from movements in underlying rates relating to economically hedged positions where hedge accounting in terms of AASB 9 is unable to be achieved.

Net interest and trading income of $A10 million for the half-year ended 30 September 2019 decreased 93% from $A138 million in the prior corresponding period primarily due to accounting volatility from the changes in the fair value on economic hedges and lower earnings on capital.

Net income on equity and debt investments

Net income on equity and debt investments was $A242 million for the half-year ended 30 September 2019, driven by a gain on the sale of MSIS fiduciary businesses to MAMHPL, a related party of MBL, owned 100% by MGL.

Credit and Other impairment charges

Credit and Other impairment charges of $A13 million for the half-year ended 30 September 2019, increased significantly from $A5 million in the prior corresponding period.

Other income and charges

Other income of $A54 million for the half-year ended 30 September 2019, compared to charges of $A74 million in the prior corresponding period due to consolidation adjustments recognised in the current period. The prior corresponding period included the impact of a structural change in funding between the Bank and Non-Bank Groups.

Employment expenses

Employment expenses relate to the Consolidated Entity's central service groups including COG, FMG, RMG, Legal and Governance, and Central Executive, as well as expenses associated with the Consolidated Entity's profit share and retention plans.

Employment expenses of $A344 million for the half-year ended 30 September 2019 increased 49% from $A231 million in the prior corresponding period as a result of higher performance-related profit share mainly driven by the overall performance of the Operating Groups and higher share-based payments expense mainly driven by the accelerated amortisation of prior years' equity awards to retiring Key Management Personnel.

Other operating expenses

Other operating expenses in the Corporate segment includes non-employment related operating costs of central service groups, and certain transactions between the Bank and Non-Bank Groups.

Other operating expenses of $A162 million for the half-year ended 30 September 2019 increased 19% from $A136 million in the prior corresponding period, and decreased 58% from $A386 million in the prior period which included the recognition of certain legacy-related expenses.

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04

Balance sheet

4.1 Statement of financial position

	AS AT			MOVEMENT	
	Sep 19[1] $Am	Mar 19 $Am	Sep 18 $Am	*Mar 19 %*	*Sep 18 %*
Assets					
Cash and bank balances	**7,773**	7,693	7,361	*1*	*6*
Cash collateral on securities borrowed and reverse repurchase agreements	**29,910**	29,148	27,580	*3*	*8*
Trading assets	**22,311**	17,502	19,514	*27*	*14*
Margin money and settlement assets	**15,098**	14,496	15,076	*4*	*<1*
Derivative assets	**17,606**	14,090	17,901	*25*	*(2)*
Financial investments	**6,030**	5,470	5,160	*10*	*17*
Other assets	**1,856**	2,105	3,410	*(12)*	*(46)*
Loan assets	**80,290**	73,821	75,365	*9*	*7*
Due from related body corporate entities	**1,216**	1,522	1,414	*(20)*	*(14)*
Property, plant and equipment	**2,668**	2,738	10,917	*(3)*	*(76)*
Interests in associates and joint ventures	**219**	219	752	*-*	*(71)*
Intangible assets	**179**	177	198	*1*	*(10)*
Deferred tax assets	**460**	441	231	*4*	*99*
Total assets	**185,616**	169,422	184,879	*10*	*<1*
Liabilities					
Cash collateral on securities lent and repurchase agreements	**5,494**	4,216	6,668	*30*	*(18)*
Trading liabilities	**7,678**	7,757	7,019	*(1)*	*9*
Margin money and settlement liabilities	**21,458**	17,901	19,575	*20*	*10*
Derivative liabilities	**14,057**	12,523	18,046	*12*	*(22)*
Deposits	**58,965**	56,120	52,576	*5*	*12*
Other liabilities	**2,636**	3,043	4,124	*(13)*	*(36)*
Borrowings	**2,611**	1,560	7,020	*67*	*(63)*
Due to related body corporate entities	**16,295**	16,791	15,243	*(3)*	*7*
Debt issued	**39,247**	33,587	36,703	*17*	*7*
Deferred tax liabilities	**10**	134	492	*(93)*	*(98)*
Total liabilities excluding loan capital	**168,451**	153,632	167,466	*10*	*1*
Loan capital	**4,828**	4,550	4,366	*6*	*11*
Total liabilities	**173,279**	158,182	171,832	*10*	*1*
Net assets	**12,337**	11,240	13,047	*10*	*(5)*
Equity					
Contributed equity	**7,900**	7,898	9,937	*<1*	*(20)*
Reserves	**637**	516	757	*23*	*(16)*
Retained earnings	**3,799**	2,824	2,345	*35*	*62*
Total capital and reserves attributable to the ordinary equity holder of Macquarie Bank Limited	**12,336**	11,238	13,039	*10*	*(5)*
Non-controlling interests	**1**	2	8	*(50)*	*(88)*
Total equity	**12,337**	11,240	13,047	*10*	*(5)*

[1] The September 2019 financial position reflects the adoption of AASB 16 *Leases* (AASB 16) on 1 April 2019. As permitted by the standard, the Consolidated Entity has not restated the comparative financial reporting periods. Refer to Note 1 *Summary of significant accounting policies* of the Financial Report for further details.

Assets

Total assets of $A185.6 billion as at 30 September 2019 increased 10% from $A169.4 billion as at 31 March 2019 primarily as a result of an increase in Loan assets, Trading assets and Derivative assets.

- Loan assets of $A80.3 billion as at 30 September 2019 increased 9% from $A73.8 billion as at 31 March 2019 as a result of net new mortgage and business banking-related loans, partially offset by net repayments in vehicle finance products in BFS
- Trading assets of $A22.3 billion as at 30 September 2019 increased 27% from $A17.5 billion as at 31 March 2019 following an increase in long equity positions and government bonds, together with an increase in oil inventory, partially offset by the sale of Corporate bonds in CGM
- Derivative assets of $A17.6 billion as at 30 September 2019 increased 25% from $A14.1 billion as at 31 March 2019 primarily as result of mark-to-market movements and an increase in client trades in commodity markets, interest rate products and foreign exchange derivatives in CGM.

Liabilities

Total liabilities of $A173.3 billion as at 30 September 2019 increased 10% from $A158.2 billion as at 31 March 2019 primarily as a result of an increase in Debt issued, Margin money and settlement liabilities, Deposits and Derivative liabilities.

- Debt issued of $A39.2 billion as at 30 September 2019 increased 17% from $A33.6 billion at 31 March 2019 primarily as a result of Treasury's funding and liquidity management activities that included the issuance of long and short-term debt and a new BFS securitisation
- Margin money and settlement liabilities of $A21.5 billion as at 30 September 2019 increased 20% from $A17.9 billion as at 31 March 2019 primarily as a result of an increase in call margin placed by financial institutions as a result of increased client flows and derivative volumes, and outstanding commodity trade settlements in CGM
- Increase in business and retail-related deposits contributed to the 5% increase in the Deposits from $A56.1 billion as at 31 March 2019 to $A59.0 billion recorded as at 30 September 2019
- Derivative liabilities of $A14.1 billion as at 30 September 2019 increased 12% from $A12.5 billion as at 31 March 2019 primarily as a result of mark-to-market movements and an increase in client traded energy products in CGM.

Equity

Total equity increased 10% to $A12.3 billion as at 30 September 2019 from $A11.2 billion as at 31 March 2019.

The increase in the Consolidated Entity's total equity was attributable to the earnings of $A1.0 billion generated during the period and an increase in the foreign currency and net investment hedge reserve of $A0.2 billion primarily as a result of depreciation of the Australian dollar against the United States dollar, partially offset by a reduction in the cash flow hedge reserve as a result of mark-to-market changes in the related hedging instruments.

4.2 Loan assets

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

	AS AT			MOVEMENT	
	Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	$Ab	$Ab	$Ab	*%*	*%*
Loan assets per the statement of financial position	**80.3**	73.8	75.4	*9*	*6*
Operating lease assets	**2.3**	2.3	10.6	*–*	*(78)*
Other reclassifications[1]	**0.6**	0.5	0.5	*20*	*20*
Less: loans held by consolidated SPEs which are available as security to noteholders and debt providers[2]	**(8.6)**	(7.2)	(7.5)	*19*	*15*
Total loan assets including operating lease assets per the funded balance sheet[3]	**74.6**	69.4	79.0	*7*	*(6)*

[1] Reclassification between loan assets and other funded balance sheet categories.
[2] Excludes notes held by Macquarie in consolidated Special Purpose Entities (SPE).
[3] Total loan assets including operating lease assets per the funded balance sheet includes self-securitised assets.

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

		AS AT			MOVEMENT	
		Sep 19	Mar 19	Sep 18	*Mar 19*	*Sep 18*
	Notes	**$Ab**	$Ab	$Ab	*%*	*%*
BFS						
Retail mortgages	1	**38.8**	35.6	32.7	*9*	*19*
Business banking	2	**9.0**	8.7	8.4	*3*	*7*
Vehicle finance	3	**11.9**	11.5	12.0	*3*	*(1)*
Total BFS		**59.7**	55.8	53.1	*7*	*12*
CGM						
Asset Finance:	4	**7.8**	7.8	7.3	–	*7*
Finance lease assets		**5.5**	5.5	5.1	–	*8*
Operating lease assets		**2.3**	2.3	2.2	–	*5*
Resources and commodities	5	**4.5**	3.3	3.3	*36*	*36*
Other	6	**2.6**	2.5	2.5	*4*	*4*
Total CGM		**14.9**	13.6	13.1	*10*	*14*
Corporate[2]						
Principal finance loans	7	**–**	–	8.4	–	*(100)*
Operating lease assets	8	**–**	–	4.4	–	*(100)*
Total Corporate		**–**	–	12.8	–	*(100)*
Total		**74.6**	69.4	79.0	*7*	*(6)*

[1] Total loan assets including operating lease assets per the funded balance sheet includes self-securitised assets.
[2] Effective 10 December 2018, CAF's Principal Finance and Transportation Finance businesses were transferred from the Bank Group to the Non-Bank Group. Corporate includes balances related to the Principal Finance and Transportation Finance businesses which were transferred to the Non-Bank group in the prior period as these do not relate to an ongoing Operating Group in MBL.

4.2 Loan assets
Continued

Explanatory notes concerning asset security of funded loan asset portfolio

1. Retail mortgages
Secured by Australian residential property.

2. Business banking
Secured relationship managed loan portfolio secured largely by working capital, business cash flows and real property.

3. Vehicle finance
Secured by Australian motor vehicles.

4. Asset Finance
Predominantly secured by underlying financed assets.

5. Resources and commodities
Diversified loan portfolio primarily to the resources sector that are secured by the underlying assets.

6. CGM Other
Predominantly relates to recourse loans to financial institutions, as well as financing for other sectors.

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

8. Operating lease assets
Secured by underlying financed assets including transportation assets.

4.3 Equity investments

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

– Financial investments; and
– Interests in associates and joint ventures.

Equity investments reconciliation

	AS AT			MOVEMENT	
	Sep 19 $Ab	Mar 19 $Ab	Sep 18 $Ab	*Mar 19 %*	*Sep 18 %*
Equity investments					
Statement of financial position					
Equity investments at fair value	**0.2**	0.3	0.3	*(33)*	*(33)*
Interests in associates and joint ventures	**0.2**	0.2	0.7	–	*(71)*
Total equity investments per statement of financial position	**0.4**	0.5	1.0	*(20)*	*(60)*
Adjustment for funded balance sheet					
Equity hedge positions[1]	**–**	(0.1)	(0.2)	*(100)*	*(100)*
Total funded equity investments	**0.4**	0.4	0.8	–	*(50)*

[1] These relate to assets held for the purposes of economically hedging Macquarie Bank's fair valued liabilities to external parties arising from various equity-linked instruments except investment in associates. Consequently, these have been excluded from the analysis of equity investment exposures.

05

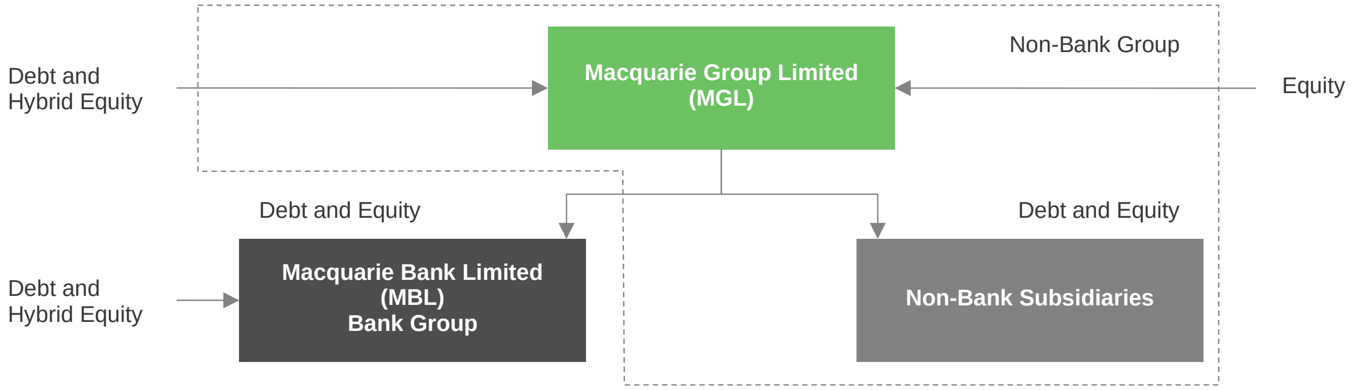
Funding and liquidity

5.1 Liquidity risk governance and management framework

Governance and oversight

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

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



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

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

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

Liquidity policy and risk appetite

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

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

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

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

5.1 Liquidity risk governance and management framework

Continued

Liquidity risk tolerance and principles

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

Risk tolerances

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

Liquidity management principles

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

Liquidity contingency plan

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

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

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

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

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

Funding strategy

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

5.2 Management of liquidity risk

Scenario analysis

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

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

The scenarios separately consider the requirements of the Bank Group, the Non-Bank Group and Macquarie Group. A range of assumptions Macquarie Group intends to be conservative are used regarding the level of access to capital markets, deposit outflows, contingent funding requirements and asset sales.

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

Liquid asset holdings

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

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

The cash and liquid asset portfolio is held in a range of currencies to ensure Macquarie Group's liquidity requirements are broadly matched by currency. Certain other business units also hold cash and liquid assets as part of their operations. The Bank Group had $A21.9 billion cash and liquid assets as at 30 September 2019 (31 March 2019: $A24.3 billion).

Funds transfer pricing

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

5.2 Management of liquidity risk

Continued

Credit ratings[1] at 30 September 2019

	MACQUARIE BANK LIMITED		
	Short-term rating	Long-term rating	Outlook
Moody's Investors Service	P-1	A2	Stable
Standard and Poor's[2]	A-1	A	Positive
Fitch Ratings	F-1	A	Stable

Regulatory developments

The Australian Prudential Regulation Authority's (APRA) liquidity standard (APS 210) details the local implementation of the Basel III liquidity framework for Australian banks. In addition to a range of qualitative requirements, the standard incorporates the Liquidity Coverage Ratio (LCR), and the Net Stable Funding Ratio (NSFR). The LCR and NSFR apply specifically to Macquarie Bank as the regulated ADI in Macquarie Group. Separate quantitative requirements are imposed internally by the ALCO and the Board.

Liquidity coverage ratio

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

Macquarie Bank's three month average LCR to 30 September 2019 was 172% (average based on daily observations). For a detailed breakdown of Macquarie Bank's LCR, please refer to Macquarie Bank's regulatory disclosures (available on Macquarie Group's website).

Net stable funding ratio

The NSFR is a twelve month structural funding metric, requiring that 'available stable funding' be sufficient to cover 'required stable funding', where 'stable' funding has an actual or assumed maturity of greater than twelve months. Macquarie Bank's NSFR as at 30 September 2019 was 111%. For a detailed breakdown of Macquarie Bank's NSFR, please refer to Macquarie Bank's regulatory disclosures (available on Macquarie Group's website).

[1] A security rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by an assigning rating agency and any rating should be evaluated independently of any other information.

[2] Standard and Poor's does not place outlook statements on short-term ratings.

5.3 Funded balance sheet

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

The table below reconciles the reported assets of the Bank Group to the net funded assets as at 30 September 2019.

		AS AT	
		Sep 19	Mar 19
	Notes	$Ab	$Ab
Total assets per the Bank Group's statement of financial position		**185.6**	169.4
Accounting deductions:			
Self-funded trading assets	1	**(18.3)**	(15.6)
Derivative revaluation accounting gross-ups	2	**(13.9)**	(12.4)
Segregated funds	3	**(11.2)**	(10.0)
Outstanding trade settlement balances	4	**(3.8)**	(3.1)
Short-term working capital assets	5	**(3.3)**	(3.7)
Intercompany gross-ups	6	**(16.3)**	(16.8)
Non-recourse funded assets:			
Securitised assets and other non-recourse funding	7	**(8.6)**	(7.2)
Net funded assets		**110.2**	100.6

Explanatory notes concerning net funded assets

1. Self-funded trading assets

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

2. Derivative revaluation accounting gross-ups

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

3. Segregated funds

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

4. Outstanding trade settlement balances

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

5. Short-term working capital assets

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

6. Intercompany gross-ups

These represent balances related to the net payable position between the Bank Group and Non-Bank Group arising out of intragroup transactions, loans and deposits. The majority of this is the Non-Bank Group deposit with MBL shown in the Bank Group funded balance sheet.

7. Securitised assets and other non-recourse funding

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

5.4 Funding profile

Funded balance sheet

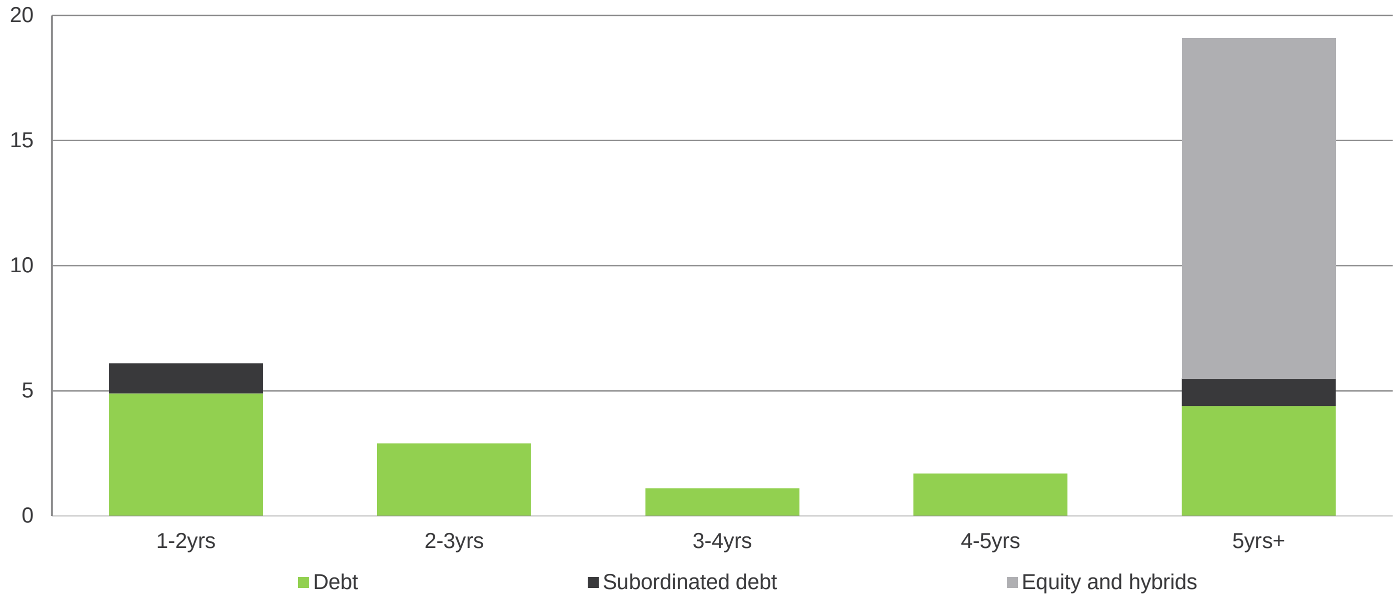
	Notes	AS AT Sep 19 $Ab	Mar 19 $Ab
Funding sources			
Wholesale issued paper:	1		
Certificates of deposit		**1.0**	1.0
Commercial paper		**7.8**	6.3
Net trade creditors	2	**1.1**	1.1
Structured notes	3	**2.0**	2.2
Secured funding	4	**2.5**	1.4
Bonds	5	**18.9**	16.1
Other loans	6	**1.0**	0.7
Syndicated loan facilities	7	**–**	–
Customer deposits	8	**58.8**	56.0
Subordinated debt	9	**3.1**	3.0
Equity and hybrids	10	**14.0**	12.8
Total		**110.2**	100.6
Funded assets			
Cash and liquid assets	11	**21.9**	24.3
Self-securitisation	12	**23.6**	21.1
Net trading assets	13	**25.8**	19.6
Loan assets including operating lease assets less than one year	14	**12.7**	13.0
Loan assets including operating lease assets greater than one year	14	**38.3**	35.3
Debt investment securities	15	**1.1**	1.1
Non-Bank Group deposit with MBL		**(14.2)**	(14.8)
Co-investment in Macquarie-managed funds and other equity investments	16	**0.4**	0.4
Property, plant and equipment and intangibles		**0.6**	0.6
Total		**110.2**	100.6

See section 5.5 for notes 1–16.

Term funding profile

Detail of drawn funding maturing beyond one year

$A billion



	AS AT SEP 19					
	1–2yrs $Ab	2–3yrs $Ab	3–4yrs $Ab	4–5yrs $Ab	5yrs+ $Ab	Total $Ab
Structured notes[1]	–	0.1	–	0.1	1.6	**1.8**
Secured funding	0.9	–	0.2	–	–	**1.1**
Bonds	4.0	2.8	0.9	1.6	2.7	**12.0**
Other loans	–	–	–	–	0.1	**0.1**
Total debt	**4.9**	**2.9**	**1.1**	**1.7**	**4.4**	**15.0**
Subordinated debt[2]	1.2	–	–	–	1.1	**2.3**
Equity and hybrids[2]	–	–	–	–	13.6	**13.6**
Total funding sources drawn	**6.1**	**2.9**	**1.1**	**1.7**	**19.1**	**30.9**
Undrawn	0.9	–	–	–	–	**0.9**
Total funding sources drawn and undrawn	**7.0**	**2.9**	**1.1**	**1.7**	**19.1**	**31.8**

Macquarie Bank has diversity of funding by both source and maturity. The weighted average term to maturity of term funding maturing beyond one year (excluding equity[3] which is a permanent source of funding, and securitisations) was 4.1 years as at 30 September 2019.

As at 30 September 2019, customer deposits represented $A58.8 billion, or 53% of the Bank Group's total funding, short-term (maturing in less than 12 months) wholesale issued paper represented $A8.8 billion, or 8% of total funding, and other debt funding maturing within 12 months and net trade creditors represented $A11.7 billion, or 11% of total funding.

[1] Structured notes are profiled using a behavioural maturity profile.

[2] Included in this balance are securities with conditional repayment obligations. These securities are disclosed using the earlier repricing dates instead of contractual maturity.

[3] Equity includes Macquarie Income Securities of $A0.4 billion which does not have a maturity date.

5.4 Funding profile
Continued

Term funding initiatives

The Bank Group has a liability driven approach to balance sheet management, where funding is raised prior to assets being taken on to the balance sheet. Since 1 April 2019, the Bank Group has continued to raise term wholesale funding across various products and currencies.

Details of term funding raised between 1 April 2019 and 30 September 2019:

		Bank Group $Ab
Secured funding	Term securitisation and other secured finance	4.4
Issued paper	Senior unsecured	5.2
Total		9.6

From 1 April 2019 to 30 September 2019, the Bank Group raised $A9.6 billion of term funding including:

- $A5.2 billion of term wholesale issued paper comprising of $A3.0 billion of senior unsecured debt issuance, $A2.1 billion of private placements and $A0.1 billion of structured notes
- $A2.8 billion of PUMA RMBS securitisation issuances; and
- $A1.6 billion of secured trade finance facilities.

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

- $US25 billion Regulation S Debt Instrument Program, including Euro Commercial Paper, Euro Certificate of Deposit, Euro Medium-Term Notes, senior and subordinated fixed/floating rate notes, and Transferable Deposits. The Debt Instrument Program had $US9.0 billion debt securities outstanding as at 30 September 2019
- $US15 billion Commercial Paper Program under which $US5.2 billion of debt securities were outstanding as at 30 September 2019
- $US20 billion US Rule 144A/Regulation S Medium-Term Note Program under which $US6.0 billion of issuances were outstanding as at 30 September 2019
- $US1.1 billion Secured Trade Finance Facility of which $US0.5 billion was drawn as at 30 September 2019
- $US5 billion Structured Note Program under which $US1.3 billion of funding from structured notes was outstanding as at 30 September 2019; and
- $A5 billion Covered Bond Programme under which $A0.8 billion of debt securities were outstanding as at 30 September 2019.

Macquarie Bank accesses the Australian capital markets through the issuance of Negotiable Certificates of Deposit. As at 30 September 2019, Macquarie Bank had $A1.0 billion of these securities outstanding.

At 30 September 2019, Macquarie Bank had internally securitised $A23.6 billion of its own Australian assets (predominantly mortgages and motor vehicles).

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

Deposit strategy

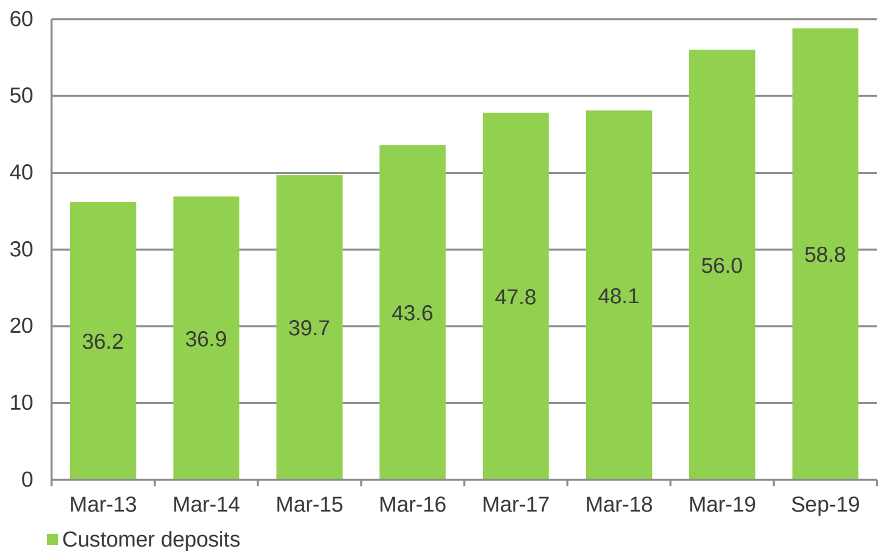
MBL continues to pursue a deposit strategy that is consistent with the core liquidity management tolerance of achieving diversity and stability of funding sources. The strategy is focused on growing the BFS deposit base, which represents a stable and reliable source of funding and reduces Macquarie Group's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

In particular, MBL is focused on the quality and composition of the deposit base, targeting transactional and relationship based deposits. The majority of MBL's deposits continue to be covered by the Financial Claims Scheme. The value cap on the deposits is set at $A250,000 per account holder.

The chart below illustrates the customer deposit growth since 31 March 2013.

Deposit trend

$A billion



5.5 Explanatory notes concerning funding sources and funded assets

1. Wholesale issued paper
Unsecured short-term wholesale funding comprised of both Certificates of Deposit and Commercial Paper.

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

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

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

5. Bonds
Unsecured long-term wholesale funding.

6. Other loans
Unsecured loans provided by financial institutions and other counterparties.

7. Syndicated loan facilities
Loan facilities provided by a syndicate of wholesale lenders.

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

9. Subordinated debt
Long-term subordinated debt.

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

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

12. Self-securitisation
This represents Australian assets which have been internally securitised and is a form of collateral on the RBA's list of eligible securities for repurchase agreements. Macquarie can utilise a portion of this as collateral in the Reserve Bank of Australia's Committed Liquidity Facility.

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

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

See section 4.2 for further information.

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

16. Co-investment in Macquarie-managed funds and other equity investments
These equity securities include co-investments in Macquarie-managed funds.

06

Capital

6.1 Overview

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

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

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

Eligible regulatory capital of Macquarie Group consists of ordinary share capital, retained earnings and certain reserves plus eligible hybrid instruments. Eligible hybrid instruments as at 30 September 2019 include the Macquarie Income Securities (MIS), Macquarie Bank Capital Notes (BCN), Macquarie Additional Capital Securities (MACS), Macquarie Group Capital Notes 2 (MCN2), Macquarie Group Capital Notes 3 (MCN3) and Macquarie Group Capital Notes 4 (MCN4).

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

Pillar 3

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

[1] Harmonised Basel III relates to the Basel III guidelines defined by the Basel Committee on Banking Supervision, documented in the following: 'Basel III: a global regulatory framework for more resilient banks and banking systems', published December 2010 (revised June 2011) by the Bank for International Settlements (BIS) and further updated by BCBS 279 'The standardised approach for measuring counterparty credit risk exposures'.
[2] APRA Basel III relates to the ADI Prudential Standards released by APRA for the period effective from 1 January 2013.

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

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

In July 2019, APRA implemented the standardised approach for measuring counterparty credit risk exposures (SA-CCR)[1].

Common Equity Tier 1 capital

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

Tier 1 capital

Tier 1 capital consists of Common Equity Tier 1 capital and Additional Tier 1 capital (hybrids). Additional Tier 1 capital as at 30 September 2019 consists of MIS, BCN and MACS. MBL periodically pays dividends to MGL and is recapitalised by MGL as required to support projected business growth.

MIS are a perpetual instrument with no ordinary equity conversion rights. MIS were listed for trading on the Australian Stock Exchange (now known as the Australian Securities Exchange) in 1999. MIS distributions are paid quarterly at a floating rate of BBSW plus 1.7% per annum and payment is subject to certain conditions including profitability of the Bank. MIS are included in Additional Tier 1 capital under Basel III transitional rules.

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

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

[1] Prudential Standard APS 180 Capital Adequacy: Counterparty Credit Risk.

6.2 Bank Group capital

Bank Group Basel III Tier 1 Capital

	AS AT SEP 19		AS AT MAR 19		*MOVEMENT*	
	Harmonised Basel III	**APRA Basel III**	Harmonised Basel III	APRA Basel III	*Harmonised Basel III*	*APRA Basel III*
	$Am	**$Am**	$Am	$Am	*%*	*%*
Common Equity Tier 1 capital						
Paid-up ordinary share capital	**7,507**	**7,507**	7,507	7,507	–	–
Retained earnings	**3,824**	**3,824**	2,852	2,852	*34*	*34*
Reserves	**637**	**637**	515	515	*24*	*24*
Gross Common Equity Tier 1 capital	**11,968**	**11,968**	10,874	10,874	*10*	*10*
Regulatory adjustments to Common Equity Tier 1 capital:						
Goodwill	**44**	**44**	42	42	*5*	*5*
Deferred tax assets	**67**	**437**	85	420	*(21)*	*4*
Net other fair value adjustments	**(131)**	**(131)**	(61)	(61)	*115*	*115*
Intangible component of investments in subsidiaries and other entities	**52**	**52**	50	50	*4*	*4*
Loan and lease origination fees and commissions paid to mortgage originators and brokers	**–**	**415**	–	411	–	*1*
Shortfall in provisions for credit losses	**315**	**350**	237	269	*33*	*30*
Equity exposures	**–**	**565**	–	678	–	*(17)*
Other Common Equity Tier 1 capital deductions	**161**	**201**	185	226	*(13)*	*(11)*
Total Common Equity Tier 1 capital deductions	**508**	**1,933**	538	2,035	*(6)*	*(5)*
Net Common Equity Tier 1 capital	**11,460**	**10,035**	10,336	8,839	*11*	*14*
Additional Tier 1 Capital						
Additional Tier 1 capital instruments	**1,681**	**1,681**	1,626	1,626	*3*	*3*
Gross Additional Tier 1 capital	**1,681**	**1,681**	1,626	1,626	*3*	*3*
Deduction from Additional Tier 1 capital	**–**	**–**	–	–	–	–
Net Additional Tier 1 capital	**1,681**	**1,681**	1,626	1,626	*3*	*3*
Total Net Tier 1 capital	**13,141**	**11,716**	11,962	10,465	*10*	*12*

Bank Group Basel III Risk-Weighted Assets (RWA)

	AS AT SEP 19		AS AT MAR 19		MOVEMENT	
	Harmonised Basel III $Am	**APRA Basel III $Am**	Harmonised Basel III $Am	APRA Basel III $Am	*Harmonised Basel III %*	*APRA Basel III %*
Credit risk						
Subject to IRB approach:						
Corporate	**24,927**	**24,927**	19,860	19,860	*26*	*26*
SME Corporate	**3,573**	**3,573**	3,573	3,573	–	–
Sovereign	**199**	**199**	211	211	*(6)*	*(6)*
Bank	**1,535**	**1,535**	1,424	1,424	*8*	*8*
Residential mortgage	**6,839**	**15,948**	5,918	13,890	*16*	*15*
Other retail	**4,373**	**4,373**	4,375	4,375	*(<1)*	*(<1)*
Retail SME	**3,584**	**3,591**	3,688	3,695	*(3)*	*(3)*
Total RWA subject to IRB approach	**45,030**	**54,146**	39,049	47,028	*15*	*15*
Specialised lending exposures subject to slotting criteria[1]	**6,079**	**6,079**	3,847	3,847	*58*	*58*
Subject to Standardised approach:						
Corporate	**320**	**320**	333	333	*(4)*	*(4)*
Residential mortgage	**762**	**762**	762	762	–	–
Other Retail	**2,240**	**2,240**	2,673	2,673	*(16)*	*(16)*
Total RWA subject to Standardised approach	**3,322**	**3,322**	3,768	3,768	*(12)*	*(12)*
Credit risk RWA for securitisation exposures	**740**	**740**	875	875	*(15)*	*(15)*
Credit Valuation Adjustment RWA	**5,343**	**5,343**	3,093	3,093	*73*	*73*
Exposures to Central Counterparties RWA	**716**	**716**	1,011	1,644	*(29)*	*(56)*
RWA for Other Assets	**3,766**	**2,426**	3,019	1,769	*25*	*37*
Total Credit risk RWA	**64,996**	**72,772**	54,662	62,024	*19*	*17*
Equity risk exposures RWA	**1,770**	**–**	2,191	–	*(19)*	–
Market risk RWA	**4,934**	**4,934**	5,382	5,382	*(8)*	*(8)*
Operational risk RWA	**10,386**	**10,386**	10,111	10,111	*3*	*3*
Interest rate risk in banking book RWA	**–**	**–**	–	–	–	–
Total Bank Group RWA	**82,086**	**88,092**	72,346	77,517	*13*	*14*
Capital ratios						
Bank Group Common Equity Tier 1 capital ratio (%)	**14.0**	**11.4**	14.3	11.4		
Bank Group Tier 1 capital ratio (%)	**16.0**	**13.3**	16.5	13.5		

[1] Specialised lending exposures subject to supervisory slotting criteria are measured using APRA determined risk weightings.

07

Glossary

7.1 Glossary

1H19	The half-year ended 30 September 2018.
1H20	The half-year ended 30 September 2019.
AASB	Australian Accounting Standards Board.
ABS	Asset Backed Securities.
ADI	Authorised Deposit-taking Institution.
Additional Tier 1 Capital	A capital measure defined by APRA comprising high quality components of capital that satisfy the following essential characteristics: – provide a permanent and unrestricted commitment of funds; – are freely available to absorb losses; – rank behind the claims of depositors and other more senior creditors in the event of winding up of the issuer; and – provide for fully discretionary capital distributions.
Additional Tier 1 Deductions	An amount deducted in determining Additional Tier 1 Capital, as defined in Prudential Standard APS 111 *Capital Adequacy: Measurement of Capital*.
ALCO	The Asset and Liability Committee.
AMA	Advanced Measurement Approach (for determining operational risk).
ANZ	Australia and New Zealand.
APRA	Australian Prudential Regulation Authority.
Associates	Associates are entities over which Macquarie has significant influence, but not control. Investments in associates may be further classified as Held for Sale ('HFS') associates. HFS associates are those that have a high probability of being sold within 12 months to external parties. Associates that are not held for sale are carried at cost and equity-accounted. Macquarie Bank's share of the investment's post-acquisition profits and losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised within equity.
Bank Group	MBL and its subsidiaries.
Bank Group Capital	Level 2 regulatory group capital.
Banking Group	The Banking Group comprises BFS, and certain activities of CGM.
Basel III IRB Formula	A formula to calculate RWA, as defined in Prudential Standard APS 113 Capital Adequacy: *Internal Ratings-based Approach to Credit Risk*.
BCN	On 8 October 2014, MBL issued 4.3 million Macquarie Bank Capital Notes (BCN) at face value of $A100 each. BCN are subordinated, unsecured notes that pay discretionary, non-cumulative, semi-annual floating rate cash distributions and may be redeemed at face value on 24 March 2020, 24 September 2020 or 24 March 2021 (subject to certain conditions being satisfied) or earlier in specified circumstances. BCN can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 24 March 2023; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL or MBL); where MBL's common equity Tier 1 capital ratio falls below 5.125%, or where APRA determines MBL would be non-viable without an exchange or a public sector injection of capital (or equivalent support).
BBSW	Bank Bill Swap Rate.
BFS	Banking and Financial Services.
BFS deposits	BFS deposits are those placed with Banking and Financial Services and include products such as the Cash Management Account, Term Deposits and Relationship Banking deposits. Counterparties primarily consist of individuals, self-managed super funds and small-medium enterprises.
BIS	Bank for International Settlements.
CAF	Corporate and Asset Finance.
CCB	Capital Conservation Buffer.
Central Service Groups	The Central Service Groups consist of the Corporate Operations Group, Financial Management Group, Risk Management Group, Legal and Governance and Central Executive.
CGM	Commodities and Global Markets.
CLF	Committed Liquidity Facility.

7.1 Glossary

Continued

CMA	Cash Management Account.
Collective allowance for credit losses	The provision relating to losses inherent in a portfolio of loan assets or debt investment securities available for sale that have not yet been specifically identified.
Common Equity Tier 1 Capital	A capital measure defined by APRA, comprising the highest quality components of capital that fully satisfy all the following essential characteristics: – provide a permanent and unrestricted commitment of funds; – are freely available to absorb losses; – do not impose any unavoidable servicing charge against earnings; and – rank behind the claims of depositors and other creditors in the event of winding up. Common Equity Tier 1 Capital comprises paid up capital, Retained earnings, and certain reserves.
Common Equity Tier 1 Capital Ratio	Common Equity Tier 1 Capital net of Common Equity Tier 1 deductions expressed as a percentage of RWA.
Common Equity Tier 1 Deductions	An amount deducted in determining Common Equity Tier 1 Capital, as defined in Prudential Standard APS 111 *Capital Adequacy: Measurement of Capital*.
Consolidated Entity	Macquarie Bank Limited and its subsidiaries.
Directors' Profit Share (DPS)	The DPS plan comprises exposure to a notional portfolio of Macquarie-managed funds. Retained amounts for Executive Directors are notionally invested over the retention period. This investment is described as 'notional' because Executive Directors do not directly hold securities in relation to this investment. However, the value of the retained amounts will vary as if these amounts were directly invested in actual securities, giving the Executive Directors an effective economic exposure to the performance of the securities. If the notional investment results in a notional loss, this loss will be offset against any future notional income until the loss is completely offset.
Earnings on capital and certain corporate income items	Net operating income includes the income generated by Macquarie Bank's Operating Groups, income from the investment of Macquarie Bank's capital, and certain items of operating income not attributed to Macquarie Bank's Operating Groups. Earnings on capital and certain corporate income items is net operating income less the net operating income generated by Macquarie Bank's Operating Groups.
ECAM	Economic Capital Adequacy Model.
Effective tax rate	The income tax expense from continuing operations as a percentage of the profit from continuing operations before income tax, both adjusted for amounts attributable to non-controlling interests. The effective tax rate differs from the Australian company tax rate due to permanent differences arising from the income tax treatment of certain income and expenses as well as tax rate differentials on some of the income earned offshore.
Expense/Income ratio	Total operating expenses expressed as a percentage of Net operating income.
Financial Report	Macquarie Bank Limited Interim Financial Report.
FIRB	Foundation Internal Ratings Based Approach (for determining credit risk).
FVOCI	Fair value through other comprehensive income.
FVTPL	Fair value through profit or loss.
Headcount	Headcount represents Macquarie Bank's active permanent and variable workforce, and includes Macquarie Bank's employees (permanent and casual) and its contingent workers (contractors, agency workers and secondees). Macquarie Bank's non-executive directors are not included.
HQLA	High-quality liquid assets.
LGD	Loss given default is defined as the economic loss which arises upon default of the obligor.
Macquarie Bank, the Consolidated Entity	Macquarie Bank Limited and its subsidiaries.
Macquarie Group	MGL and its subsidiaries.
Macquarie Income Securities (MIS)	Macquarie Income Securities (MIS) are perpetual, subordinated instruments that have no conversion rights to ordinary shares. Discretionary distributions are paid quarterly. They are treated as equity in the statement of financial position. There are four million $A100 face value MIS on issue.

MACS	On 8 March 2017, MBL, acting through its London Branch, issued $US750 million of Macquarie Additional Capital Securities (MACS). MACS are subordinated, unsecured notes that pay discretionary, non-cumulative, semi-annual fixed rate cash distributions. Subject to certain conditions the MACS may be redeemed on 8 March 2027, or every 5th anniversary thereafter. MACS can be exchanged for a variable number of fully paid MGL ordinary shares on an acquisition event (where a person acquires control of MBL or MGL), where MBL's common equity Tier 1 capital ratio falls below 5.125%, or where APRA determines MBL would be non-viable without an exchange or a public sector injection of capital (or equivalent support).
MAM	Macquarie Asset Management.
MAMHPL	Macquarie Asset Management Holdings Pty Limited.
MBL	Macquarie Bank Limited ABN 46 008 583 542.
MCN	On 7 June 2013, MGL issued six million Macquarie Group Capital Notes (MCN) at a face value of $A100 each. MCN were subordinated, non-cumulative, unsecured notes that paid discretionary, non-cumulative, semi-annual floating rate cash distributions. MCN were redeemed on 7 June 2018.
MCN2	On 18 December 2015, MGL issued 5.3 million Macquarie Group Capital Notes 2 (MCN2) at a face value of $A100 each. MCN2 are subordinated, non-cumulative, unsecured notes that pay discretionary, non-cumulative, semi-annual floating rate cash distributions and may be redeemed at face value on 17 March 2021, 17 September 2021 or 17 March 2022 (subject to certain conditions being satisfied) or earlier in specified circumstances. MCN2 can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 18 March 2024; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL); or where APRA determines MGL would be non-viable without an exchange or a public sector injection of capital (or equivalent support).
MCN3	On 7 June 2018, MGL issued 10 million Macquarie Group Capital Notes 3 (MCN3) at a face value of $A100 each. MCN3 are subordinated, non-cumulative, unsecured notes that pay discretionary, non-cumulative, quarterly floating rate cash distributions and may be redeemed at face value on 16 December 2024, 16 June 2025 or 15 December 2025 (subject to certain conditions being satisfied) or earlier in specified circumstances. MCN3 can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 15 December 2027; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL); or where APRA determines MGL would be non-viable without an exchange or a public sector injection of capital (or equivalent support).
MCN4	On 27 March 2019, MGL issued 9.1 million Macquarie Group Capital Notes 4 (MCN4) at a face value of $A100 each. MCN4 are subordinated, non-cumulative, unsecured notes that pay discretionary, non-cumulative, quarterly floating rate cash distributions and may be redeemed at face value on 10 September 2026, 10 March 2027 or 10 September 2027 (subject to certain conditions being satisfied) or earlier in specified circumstances. MCN4 can be converted into a variable number of MGL ordinary shares (subject to certain conditions being satisfied) on these redemption dates; mandatorily exchanged on 10 September 2029; exchanged earlier upon an acquisition event (with the acquirer gaining control of MGL); or where APRA determines MGL would be nonviable without an exchange or a public sector injection of capital (or equivalent support).
MEREP	Macquarie Group Employee Retained Equity Plan.
MFHPL	Macquarie Financial Holdings Pty Limited.
MGL, the Company	Macquarie Group Limited ABN 94 122 169 279.
Net loan losses	The impact on the income statement of loan amounts provided for or written-off during the period, net of the recovery of any such amounts which were previously written-off or provided for in the income statement.
Net tangible assets per ordinary share	(Total equity less Macquarie Income Securities less Non-controlling interest less the Future Income Tax Benefit plus the Deferred Tax Liability less Intangible assets) divided by the number of ordinary shares on issue at the end of the period.
Net Trading Income	Income that comprises gains and losses related to trading assets and liabilities and includes all realised and unrealised fair value changes and foreign exchange differences.
Non-Bank Group	MGL, MFHPL and its subsidiaries.
Non-Banking Group	The Non-Banking Group comprises Macquarie Capital, MAM, and some business activities of CGM that use certain offshore regulated entities of the Non-Banking Group.

7.1 Glossary
Continued

Non-GAAP metrics	Non-GAAP metrics include financial measures, ratios and other information that are neither required nor defined under Australian Accounting Standards.
Operating Groups	The Operating Groups consist of BFS and CGM.
RBA	Reserve Bank of Australia.
Risk-weighted assets (RWA)	A risk-based measure of an entity's exposures, which is used in assessing its overall capital adequacy.
RMBS	Residential Mortgage-Backed Securities.
Specialised and Asset Finance (SAF)	SAF is a global provider of specialist finance and asset management solutions across: Technology, Media & Telecoms; Energy, Renewables & Sustainability; Fund Finance; Resources; Structured Lending; and Shipping & Export Credit Agencies.
SPEs	Special purpose entities.
Subordinated debt	Debt issued by Macquarie Bank for which agreements between Macquarie Bank and the lenders provide, in the event of liquidation, that the entitlement of such lenders to repayment of the principal sum and interest thereon is and shall at all times be and remain subordinated to the rights of all other present and future creditors of Macquarie Bank. Subordinated debt is classified as liabilities in the Macquarie Bank's financial statements and may be included in Tier 2 Capital.
Tier 1 Capital	Tier 1 Capital comprises of (i) Common Equity Tier 1 Capital; and (ii) Additional Tier 1 Capital.
Tier 1 Capital Deductions	Tier 1 Capital Deductions comprises of (i) Common Equity Tier 1 Capital Deductions; and (ii) Additional Tier 1 Capital Deductions.
Tier 1 Capital Ratio	Tier 1 Capital net of Tier 1 Capital Deductions expressed as a percentage of RWA.
True Index products	True Index products deliver clients pre-tax index returns (before buy/sell spreads on transactions). Any under-performance is compensated by Macquarie Bank and conversely, any out-performance is retained by Macquarie Bank.
UK	The United Kingdom.
US	The United States of America.

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