MARKET PRESSURES AND OUR CUSTOMERS

The collapse of the US sub-prime mortgage market over the past 12 months triggered fundamental change in financial markets globally.

Investor confidence in financial institutions and the market in general has been shaken, resulting in sharp declines in share prices across multiple sectors and countries. Total global losses from the resulting financial crisis could run into the trillions and few commentators are willing to speculate when the uncertainty and market volatility will end.

The tightening of the global credit markets has made doing business more difficult for us.

Banks are cautious about lending to each other for fear of the other party's exposure to sub-prime 'assets'. This has made credit sourced from global markets harder to find and much more expensive.

"Our focus in this environment is continuing to run a strong and profitable business, mindful of the impact our decisions have on our customers, especially those who are struggling with increased living expenses," says Peter Marriott, Chief Financial Officer and Chair of the ANZ Corporate Responsibility Council.

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— PETER MARRIOTT, CHIEF FINANCIAL OFFICER AND CHAIR OF THE ANZ CORPORATE RESPONSIBILITY COUNCIL

MANAGING THE RISING COSTS OF CREDIT

The dramatic change in the financial and economic landscape over the past 12 months has required careful analysis and strategic decision-making to ensure our business is strongly positioned and continues to deliver sustainable performance over the long term. Specifically, we have monitored, and when required, adjusted our capital levels, improved 'stress testing' of our various customer portfolios, tightened credit risk management and ensured our risk management team is involved in business decisions even earlier than usual.

We acted swiftly to increase our provision for 'bad' debts to provide a strong position against the deteriorating credit market and softening economic conditions.

The situation has also required us to manage the impact of the market turmoil on the cost of funding for our lending activities, and this has involved some tough decisions which inevitably affect our customers.

Australian lenders drew criticism this year for increasing home loan interest rates independently of an increase to the official cash rate by the Reserve Bank of Australia (RBA).

ANZ increased the interest rates on most mortgage products on three occasions this year outside 'official' RBA interest rate setting. Other lenders announced similar increases at the same time.

Many of our stakeholders were understandably concerned by this decision, questioning how we could justify increasing rates when the RBA had not increased the official cash rate. The inference was that banks were being opportunistic, taking advantage of the difficult and complex credit environment to increase their profit margins.

The decision to raise rates independently reflected that very little of our funding costs are tied solely to the RBA's official cash rate. The rates paid on customer deposits have moved in line with the official rate but this is only one source of funding for Australian banks; it is not sufficient to meet the demands of home loan borrowers.

We also rely on 'wholesale' funds sourced from international and domestic debt markets for the difference, funding which has become considerably more expensive since the global financial crisis began.

The interest rate changes recovered part of the increased costs we faced from 'wholesale' funding rather than customer sources. While this was explained publicly at the time of our announcement, we have identified a need to communicate how we arrive at pricing decisions like this more clearly to our customers in future.

We were also questioned about why we needed to recover costs from customers. Couldn't we draw on the profits we make to absorb these costs instead of passing them onto our customers?

An important message, but one that is difficult to deliver in an environment of financial uncertainty for our customers, is that these pricing decisions must be based on more than just breaking even.

Banks need to remain profitable, especially when global funding sources are scarce.

The failure of large banks in the US and Europe this year demonstrates how important this is, not just to bank shareholders, but also to customers. When a bank makes a profit, it adds to its capital reserves and therefore its capacity to continue to provide banking services, affordable credit to consumers and businesses, and a stable and secure place to deposit money.

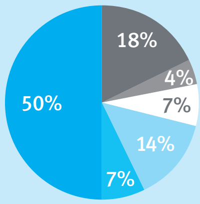
Profitable and well-capitalised banks also attract higher credit ratings, providing cheaper access to global market funds and keeping the costs of credit as low as possible for customers. At the time of printing, ANZ was one of only 15 AA rated banks in the world.

Our preference is to absorb as much of the costs of lending as we can. Increasing interest rates is always a difficult decision to make, and never popular with our customers. And we have made a public commitment to reduce our rates whenever economic conditions allow, including outside the RBA interest rate announcement cycle. We delivered on this commitment in mid October 2008 when we reduced interest rates on our mortgage products by 25 basis points.

"It's in no-one's interests to keep rates high," says John Harries, Managing Director Retail Products.

"It's not good for our competitiveness in the market and we know increases in a range of living expenses are stretching many household budgets."

ANZ'S SOURCES OF FUNDS GROUP FUNDING PROFILE* – SEPTEMBER 2008



- Total Customer Funding
- Short-term Wholesale Debt
- Commercial Bills
- Terms Debt Residual <1 yr
- Terms Debt Residual >1 yr
- SHE & hybrid debt

*percentage of net external assets (i.e All funded assets incl. non-core assets)

MARKET PRESSURES AND OUR CUSTOMERS

SUPPORTING OUR CUSTOMERS IN A CHANGING ECONOMY

The total number of ANZ retail customers behind in their repayments by 60 days or more (an industry measure of credit risk) has increased over the past 12 months, although the number (for example, only 0.39% of mortgage customers) is still very small as a proportion of our whole customer base.

This increase is forecast to continue over the next year as uncertainty in global markets impacts the 'real' economy.

Given the shift in economic conditions, we have tightened lending standards for some prospective borrowers, especially in areas where there is evidence of falling house prices.

Other measures have included, for example, increasing the use of SMS messages to mortgage, credit card and personal loan customers to provide them with reminders of upcoming due payments or to notify them when they have missed a repayment.

Tighter economic conditions will also test how effectively we support those customers finding it difficult to meet repayments on their home loan, credit card or other loan. We have made a substantial investment in this area over the last 18 months in response to feedback from financial counsellors and consumer organisations.

Customer Connect, for example, is a new customer hardship program, developed with the support of Kildonan Uniting Care, a community-based organisation with expertise in consumer hardship. The program gives our staff in Australia skills to provide more effective support to customers in temporary financial difficulty. It promotes respectful, honest and transparent discussions between the Bank and our customers about what they can afford to pay and the assistance they need to stabilise their situation and get back on track with their finances.

Training to deliver the program was provided to all staff in our mortgages, credit cards, personal loans and small business areas who, as part of their job, regularly speak to customers falling behind on their repayments.

Briget Stuart works in ANZ's personal loan inbound call centre team and finds our new approach encourages more constructive conversations with customers about debt.

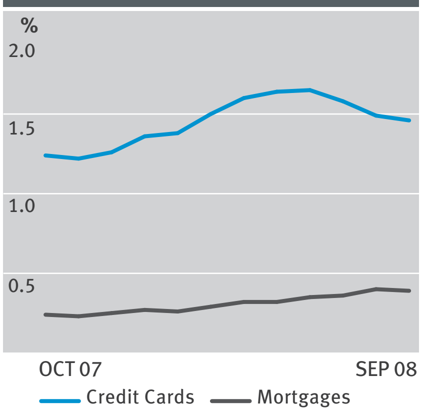
"Customers who call me have usually just received a letter or call about their overdue account so they are already on edge – often they are petrified. The last thing they need is to be judged on whether they 'deserve' our help."

Staff are encouraged to, where possible, offer temporary repayment arrangements based on what the customer can afford and without regard to the reason for their hardship.

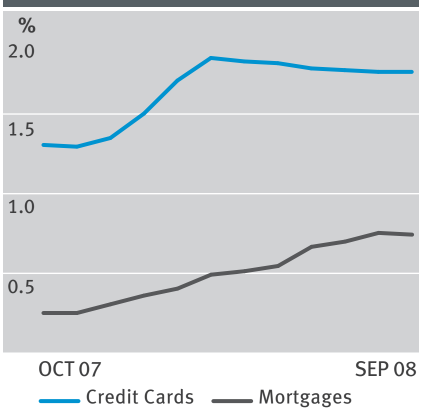
"I find customers relax as soon as they realise we are not going to grill them about their hardship – we are only interested in how much they can afford. If we trust them, they will trust and be honest with us about their repayments," says Briget.

Where a temporary arrangement can be agreed on with a customer, staff will check back after three months to see whether the arrangement needs to be extended or whether they can resume normal repayments.

RETAIL CUSTOMERS OVERDUE 60+ DAYS AUSTRALIA



RETAIL CUSTOMERS OVERDUE 60+ DAYS NEW ZEALAND



"I find customers relax as soon as they realise we are not going to grill them about their hardship – we are only interested in how much they can afford. If we trust them, they will trust and be honest with us about their repayments,"

— BRIGET STUART, COLLECTIONS CONSULTANT, PERSONAL LOANS

MORE ABOUT ANZ'S APPROACH:

- 2008 Customer Charter Report
  www.anz.com/charter
- 2008 Customer Advocate Report
  www.anz.com/advocate
- Responsible lending at ANZ
  www.anz.com/rlending
- Products and services
  www.anz.com/products

We are monitoring the immediate and long-term repayment behaviour of Customer Connect customers to determine whether the relief arrangements we are setting are reasonable, how many customers return to normal repayments and how long this typically takes. Early signs are that the program will be most successful in cases where a customer's financial difficulty is only short term.

A similar program has been established in New Zealand. 'Financial Wellbeing' provides branch and business banking staff training to help them better understand the current financial climate and the financial stress some of our customers are experiencing as well as guidance and information on supporting customers who may be struggling with credit card debt, personal loans or mortgage repayments.

KEEPING OUR PRODUCTS SIMPLE

The lending practices which contributed to the US sub-prime crisis remind us that we must ensure our products are responsibly sold and easy to understand. This means defining as clearly as possible the financial choices people can make.

Customers are also demanding simplicity. In addition to our bi-annual study of adult financial literacy in Australia conducted this year, we completed detailed customer research to more deeply understand what people value in their bank.

The consistent feedback across all ages, incomes and geographies was that customers value simple, uncomplicated products and services that respond to their individual needs.

We continue to reshape our products in response to this feedback. This year, for example, we simplified our mortgages offering, creating four products with clear differences between each. Our goal was to make it easier for our customers to select the right home loan. The new range of products includes ANZ Simplicity PLUS, a 'no frills' home loan with a lower rate and basic loan features.

We also added a new transaction product to help customers avoid fees charged when there are insufficient funds in a customer's account to cover a payment or withdrawal, known in Australia as 'exception fees'. ANZ Access Limited automatically blocks transactions that would cause the account to overdraw and is free of honour and dishonour fees.

According to CEO Australia, Brian Hartzer, a customer-focused approach to banking is never more important than in uncertain economic times.

"In times of turmoil, people seek out stability – somewhere they can manage their money with confidence.

"This is when we earn the trust of our customers, with outstanding customer service that meets their needs, simple products people can understand and most important of all, helpful advice and support for those who are in financial stress."

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