

NATIONAL AUSTRALIA BANK LTD
Form 6-K
May 12, 2004

FILE NO 1-9945

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON DC 20549

FORM 6-K

REPORT OF FOREIGN ISSUER

Pursuant to Rule 13a-16 or 15d-16 of
the Securities Exchange Act of 1934

For the month of May 2004

National Australia Bank Limited

ACN 004 044 937

(Registrant's Name)

Level 24

500 Bourke Street

MELBOURNE VICTORIA 3000

AUSTRALIA

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

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Form 20-F Form 40-F

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes No

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82

6 Months Ended 31 March 2004

National Australia Bank Limited

Half Year Results 2004

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**Media Release
12 May 2004**

NATIONAL S CASH EARNINGS DOWN 8.7%

NET PROFIT UP 19%

INTERIM DIVIDEND STEADY AT 83 CENTS

FINANCIAL HIGHLIGHTS (March 04/March 03 Comparison)

Cash earnings before significant items of \$1.85 billion, down 8.7%

Net profit after significant items up 19% to \$2.23 billion

Interim dividend of 83 cents (fully franked).

Retail banking cash earnings:

Australia - up 10.5%

New Zealand steady (up 2.9% in local currency)

Europe - down 37.1% (down 27.5% in local currency)

INTERIM DIVIDEND STEADY AT 83 CENTS

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Corporate & Institutional Banking cash earnings before significant items down 12.8% (down 6.5% excluding currency movements)

Wealth Management operating profit after tax up 37.3%

Asset quality sound: gross non-accrual loans to total loans improved from 0.65% to 0.46%

Return on equity before significant items of 18.8% up from 16.8%.

Economic Value Added (EVA[®]) down 11.5% to \$978 million*.

Total capital at 9.35%, Tier 1 at 7.47% and Adjusted Common Equity ratio of 5.36% after the buy back of 5.5 million ordinary shares.

*EVA[®] is a registered trademark of Stern Stewart & Co. It measures the economic profit earned in excess of the Group's cost of capital.

CHIEF EXECUTIVE S REVIEW

This is a disappointing result but our New Zealand and Wealth Management businesses have made solid contributions.

Financial Services Australia increased cash earnings although the quality of the result was not ideal with total income up by only 4.8%. Both Financial Services Australia and Corporate and Institutional Banking have not surprisingly been adversely affected by the currency options trading issue.

We have started to work on and invest in our European businesses to address some of the major issues we have in those markets. Increased competition, compliance costs and adverse currency movements further affected the Financial Services Europe result.

Under these circumstances we have maintained our dividend payment.

DIVISIONAL PERFORMANCE

Financial Services Australia increased cash earnings by 10.5%. Strong growth in housing lending was partly offset by a fall in the overall net interest margin. Retail deposits increased by 9.7% since March 2003.

Agribusiness market share by lending volumes for the year to February increased from 21.7% to 28.9%. Business market share by lending volumes at 26.0% is down from 26.5% for the same period. (Source: Taylor Nelson Sofrais)

Financial Services Australia has opened 11 integrated financial services centres this half year and is on target to achieve the planned roll out of 42 centres by the end of the financial year. These centres are designed to meet customers' complete financial advice needs.

Financial Services Europe was adversely affected by a combination of higher pension fund expenses and currency movements. The large fall in cash earnings is disappointing but there are several developments underway to address this situation.

An extensive product renewal program has been completed, including the introduction of a new current account, savings accounts, mortgages, loans and insurance.

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The first four Financial Services Centres have been opened in Liverpool, Bristol, Reading and Southampton and generated £1.2 million in revenue in the half year. A further four centres are planned to open in Oxford, Milton Keynes, Maidstone and Guildford this year.

Financial Services New Zealand increased net interest income by 5.8% in local currency terms based on strong growth in business and personal lending as well as retail deposits.

Cash earnings were steady reflecting a fall in the net interest margin and a higher charge to provide for doubtful debts.

Highlights of the half year include the launch of the Campus Pack in conjunction with Student Card (a New Zealand student discount scheme) which increased the number of tertiary students banking with Bank of New Zealand by 60%.

Bank of New Zealand increased home lending since March 2003 by 19% compared to market growth of 16%. Bank of New Zealand was the only bank to increase customer satisfaction according to Auckland University's customer survey for 2003.

Corporate & Institutional Banking has obviously faced a difficult half due to the impact of the foreign currency options trading situation and subsequent events. A higher charge for doubtful debts, adverse currency movements and reduced demand for debt market products, due to a low US interest rate environment, affected cash earnings.

Despite these challenging circumstances the focus on growing core relationships has continued and this has resulted in the maintenance of a solid base of underlying client income.

Corporate & Institutional Banking is actively contributing to the program to address the remedial actions required by APRA.

Wealth Management increased operating profit after tax by 37.3% reflecting strong growth in insurance business and the improvement in equity markets which led to growth in earnings from the investments business and investment earnings on capital.

The strong performance of equity markets from the March 2003 half has resulted in an 11.9% increase in average funds under management with fee revenue higher in all regions.

Wealth Management continues to be the number one provider of retail investment platforms in Australia with a market share of 18.8% and number two in retail funds under management as at December 2003. (Source: Assirt Market Share Report, December 2003)

Insurance earnings grew by 22.2% and Wealth Management retained the largest share of the total Australian retail life insurance market for both annual in-force premiums and new retail risk annual premiums. (Source: DEXX&R Research Reports, December 2003)

OUTLOOK

The National is focused on creating strong, sustainable growth in shareholder value.

As part of our response to the foreign currency options trading losses we are addressing the changes required by APRA as quickly as possible.

My future priorities are to lead the required cultural change, review our business strategies and our approach to risk management to make sure we have a sustainable platform for future growth. These are the first important steps in a recovery program that will take some time.

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RESULTS FOR THE HALF YEAR ENDED 31 MARCH 2004

FINANCIAL SUMMARY

REPORTING FORMAT

Reporting Structure

To assist with the interpretation of the Group's results, earnings have been reported under the following structure:

Retail Banking, which comprises:

Financial Services Australia (FSA)

Financial Services Europe (FSE)

Financial Services New Zealand (FSNZ);

Corporate & Institutional Banking (CIB);

Other (including Excess Capital, Group Funding & Corporate Centre); and

Wealth Management (WM).

Prior Period Comparatives

From 1 October 2003, there have been transfers of business units from Financial Services Europe to Corporate & Institutional Banking.

Reverse repurchase agreements and repurchase agreements have been reclassified from gross loans and advances and deposits and other borrowings to cash and other liquid assets and due from/to financial institutions respectively, depending on counterparty.

Transferable certificates of deposit have been reclassified from deposits and other borrowings to bonds, notes and subordinated debt .

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For comparability, the prior period balances have been reclassified from those included in the Profit Announcement released on 11 November 2003.

The nature of the restatements have been fully disclosed in the release to ASX dated 30 April 2004.

Please refer to the National's website at www.nabgroup.com for a copy of this announcement.

Cash Earnings

Cash earnings is a key performance measure and financial target used by the Group. Dividends paid by the Group are based on after-tax cash earnings (excluding significant items). Cash earnings is a key performance measure used by the investment community, as well as by those Australian peers of the Group with a similar business portfolio.

A reconciliation of cash earnings to net profit appears on page 7. Cash earnings is also explained in detail in the Non-GAAP financial measures section. Refer page 78 for further details.

Diluted Cash Earnings per Share

Management use growth in diluted cash EPS as a key indicator of performance as this takes full account of the impact of the exchangeable capital units (ExCaps) and provides a consistent basis for year on year comparison moving forward. The potential conversion of ExCaps has a dilutive impact on earnings per share (EPS), which varies from year to year depending on conversion.

Under the terms of the ExCaps the National has the option to require the exchange of all, but not part, of the ExCaps at any time for 7 7/8% convertible non-cumulative preference shares of the National. Holders of the ExCaps or the convertible non-cumulative preference shares have the option to exchange their holding for ordinary shares of the National (or at the National's option, cash) and the National also has the right to redeem, in part or full, under a special offer at any time after 19 March, 2007, with the prior consent of APRA.

A complete reconciliation of the calculation of diluted cash earnings per share appears in note 16. Refer page 75 for further details.

DIVISIONAL PERFORMANCE SUMMARY

	Note	Mar 04 \$m	Half Year to Sep 03 \$m	Mar 03 \$m	Fav / (Unfav) Change on Sep 03 %	Mar 03 %
Cash earnings (1)						
Retail Banking						
Financial Services Australia	1	999	967	904	3.3	10.5
Financial Services Europe	1	308	407	490	(24.3)	(37.1)
Financial Services New Zealand	1	158	152	159	3.9	(0.6)
Retail Banking		1,465	1,526	1,553	(4.0)	(5.7)
Corporate & Institutional Banking (2)	1	375	447	430	(16.1)	(12.8)
Other (incl. Excess Capital, Group Funding and Corporate Centre) (2)	1	(117)	(54)	(23)	large	large
Total Banking		1,723	1,919	1,960	(10.2)	(12.1)
Wealth Management operating profit (2) (3)	1	221	213	161	3.8	37.3
Cash earnings before significant items and distributions		1,944	2,132	2,121	(8.8)	(8.3)
Distributions		(94)	(89)	(94)	(5.6)	
Cash earnings before significant items		1,850	2,043	2,027	(9.4)	(8.7)
Weighted av no. of ordinary shares (million)	16	1,505	1,508	1,524	0.2	1.2
Cash earnings per share before significant items (cents)	16	122.9	135.5	133.0	(9.3)	(7.6)
Diluted cash earnings per share before significant items (cents)	16	119.9	132.2	130.1	(9.3)	(7.8)
Reconciliation to net profit						
Cash earnings before significant items		1,850	2,043	2,027	(9.4)	(8.7)
Adjusted for:						
Significant items after tax	13	127			large	large
Cash earnings after significant items		1,977	2,043	2,027	(3.2)	(2.5)
Adjusted for:						
Net profit/(loss) attributable to outside equity interest		63	(18)	10	large	large
Distributions		94	89	94	(5.6)	
Wealth Management revaluation profit/(loss)		148	5	(205)	large	large
Goodwill amortisation		(53)	(49)	(49)	(8.2)	(8.2)
Net profit		2,229	2,070	1,877	7.7	18.8

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Net (profit)/loss attributable to outside equity interest	(63)	18	(10)	large	large
Net profit attributable to members of the Company	2,166	2,088	1,867	3.7	16.0
Distributions	(94)	(89)	(94)	(5.6)	
Earnings attributable to ordinary shareholders	2,072	1,999	1,773	3.7	16.9

(1) *Cash earnings is a performance measure used by the management of the Group. Refer to Non-GAAP financial measures on page 78 for a complete discussion of cash earnings.*

(2) *Cash earnings after outside equity interest.*

(3) *Refers to net profit generated through the Wealth Management operations. It excludes revaluation profit/(loss) after tax.*

GROUP PERFORMANCE SUMMARY

	Note	Mar 04 \$m	Half Year to Sep 03 \$m	Mar 03 \$m	Fav / (Unfav) Change on Sep 03 %	Mar 03 %
Banking (1)						
Net interest income	2	3,519	3,610	3,692	(2.5)	(4.7)
Other operating income (1) (2)	7	2,044	2,211	2,066	(7.6)	(1.1)
Banking net operating income (1)		5,563	5,821	5,758	(4.4)	(3.4)
Wealth Management						
Net interest income	2	66	63	54	4.8	22.2
Net life insurance income (3)	6	455	363	81	25.3	large
Other operating income (2)	7	412	367	366	12.3	12.6
Net operating income		6,496	6,614	6,259	(1.8)	3.8
Banking operating expenses (1)	8	(2,800)	(2,856)	(2,692)	2.0	(4.0)
Wealth Management operating expenses (4)	8	(436)	(412)	(394)	(5.8)	(10.7)
Charge to provide for doubtful debts	10	(305)	(311)	(322)	1.9	5.3
Cash earnings before tax		2,955	3,035	2,851	(2.6)	3.6
Banking income tax expense (1)	12	(730)	(731)	(781)	0.1	6.5
Wealth Management income tax benefit/(expense)	12	(218)	(190)	61	(14.7)	large
Cash earnings before significant items, distributions and outside equity interest		2,007	2,114	2,131	(5.1)	(5.8)
Wealth Management revaluation profit/(loss) after tax	1	148	5	(205)	large	large
Goodwill amortisation		(53)	(49)	(49)	(8.2)	(8.2)
Net profit before significant items		2,102	2,070	1,877	1.5	12.0
Significant items after tax	13	127			large	large
Net profit		2,229	2,070	1,877	7.7	18.8
Net (profit)/loss attributable to outside equity interest						
Wealth Management		(58)	22	(6)	large	large
Corporate & Institutional Banking		(5)	(5)	(4)		(25.0)
Other			1		large	large
Net profit attributable to members of the Company		2,166	2,088	1,867	3.7	16.0
Distributions		(94)	(89)	(94)	(5.6)	
Earnings attributable to ordinary shareholders		2,072	1,999	1,773	3.7	16.9

(1) Banking refers to Total Banking adjusted for eliminations. Refer to note 1 for further details.

- (2) *Other operating income excludes net interest income, net life insurance income and revaluation profit/(loss).*
- (3) *Net life insurance income is the profit before tax excluding net interest income of the statutory funds of the life insurance companies of the Group.*
- (4) *Operating expenses excludes life insurance expenses incorporated within net life insurance income.*

REGIONAL PERFORMANCE SUMMARY

	Mar 04	Half Year to Sep 03	Mar 03	Fav / (Unfav) Change on Sep 03	Mar 03
	\$m	\$m	\$m	%	%
Cash earnings					
Australia					
Retail Banking (1)	991	959	895	3.3	10.7
Corporate & Institutional Banking	199	188	202	5.9	(1.5)
Wealth Management	190	190	137		38.7
Other (incl. Excess Capital, Group Funding & Corporate Centre) (2)	(181)	(82)	(64)	large	large
Total Australia	1,199	1,255	1,170	(4.5)	2.5
Europe					
Retail Banking (1)	309	408	491	(24.3)	(37.1)
Corporate & Institutional Banking	82	149	104	(45.0)	(21.2)
Wealth Management	14	14	12		16.7
Other (incl. Group Funding & Corporate Centre)	(11)	(58)	(46)	81.0	76.1
Total Europe	394	513	561	(23.2)	(29.8)
New Zealand					
Retail Banking (1)	165	159	167	3.8	(1.2)
Corporate & Institutional Banking	59	68	74	(13.2)	(20.3)
Wealth Management	5	(4)	6	large	(16.7)
Other (incl. Group Funding & Corporate Centre)	(11)	(3)	(8)	large	(37.5)
Total New Zealand	218	220	239	(0.9)	(8.8)
United States					
Corporate & Institutional Banking	17	22	26	(22.7)	(34.6)
Other (incl. Group Funding & Corporate Centre)	77	76	89	1.3	(13.5)
Total United States	94	98	115	(4.1)	(18.3)
Asia					
Corporate & Institutional Banking	18	20	24	(10.0)	(25.0)
Wealth Management	12	13	6	(7.7)	large
Other (incl. Group Funding & Corporate Centre)	9	13	6	(30.8)	50.0
Total Asia	39	46	36	(15.2)	8.3
Cash earnings before significant items and distributions	1,944	2,132	2,121	(8.8)	(8.3)

(1) Regional Retail Banking results differ from Financial Services Australia, Europe and New Zealand primarily due to the inclusion of the global fleet management business units within Financial Services Australia.

(2) Earnings on excess capital is wholly attributed to Australia.

Refer to the Division Performance Summary on page 7 for a reconciliation of cash earnings before significant items and distributions to net profit.

SUMMARY OF FINANCIAL POSITION

	Note	As at Mar 04 \$m	Sep 03 \$m	Mar 03 \$m	Change on Sep 03 %	Mar 03 %
Assets						
Cash and other liquid assets (1)		11,641	8,405	9,999	38.5	16.4
Due from other financial institutions (1)		20,200	29,234	34,233	(30.9)	(41.0)
Due from customers on acceptances		14,988	19,562	20,677	(23.4)	(27.5)
Trading securities		25,691	23,724	21,414	8.3	20.0
Trading derivatives		24,352	23,644	25,228	3.0	(3.5)
Available for sale securities		2,794	6,513	5,005	(57.1)	(44.2)
Investment securities		7,099	8,647	10,925	(17.9)	(35.0)
Investments relating to life ins. business		37,982	35,846	30,278	6.0	25.4
Loans and advances (1)		233,987	225,735	218,200	3.7	7.2
Shares in entities and other securities		867	1,445	1,186	(40.0)	(26.9)
Regulatory deposits		436	225	180	93.8	large
Property, plant and equipment		2,483	2,498	2,493	(0.6)	(0.4)
Income tax assets		1,248	1,203	1,213	3.7	2.9
Goodwill		682	740	787	(7.8)	(13.3)
Other assets		11,130	10,050	12,378	10.7	(10.1)
Total assets		395,580	397,471	394,196	(0.5)	0.4
Liabilities						
Due to other financial institutions (2)		43,968	52,530	58,125	(16.3)	(24.4)
Liability on acceptances		14,988	19,562	20,677	(23.4)	(27.5)
Life insurance policy liabilities		34,059	32,457	30,206	4.9	12.8
Trading derivatives		21,046	21,479	24,821	(2.0)	(15.2)
Deposits and other borrowings (2) (3)		210,624	201,194	196,260	4.7	7.3
Income tax liabilities		1,238	1,537	1,255	(19.5)	(1.4)
Provisions		1,143	1,262	1,251	(9.4)	(8.6)
Bonds, notes and subordinated debt (3)		25,204	24,257	21,310	3.9	18.3
Other debt issues		1,693	1,743	1,808	(2.9)	(6.4)
Other liabilities		13,707	14,239	14,668	(3.7)	(6.6)
Net assets		27,910	27,211	23,815	2.6	17.2
Equity						
Ordinary shares		6,029	6,078	6,377	(0.8)	(5.5)
Preference shares (4)			730	730	large	large
National Income Securities		1,945	1,945	1,945		
Trust Preferred Securities		975	975			large
Contributed equity	15	8,949	9,728	9,052	(8.0)	(1.1)
Reserves	15	784	893	1,254	(12.2)	(37.5)
Retained profits	15	14,619	13,786	13,224	6.0	10.5
Total equity parent entity interest		24,352	24,407	23,530	(0.2)	3.5

Outside equity interest in controlled entities	15				
Wealth Management (5)	3,385	2,614	70	29.5	large
Corporate & Institutional Banking	173	190	215	(8.9)	(19.5)
Total equity	27,910	27,211	23,815	2.6	17.2

(1) *Comparatives have been restated to reflect the reclassification of reverse repurchase agreements. Refer page 6 for further details.*

(2) *Comparatives have been restated to reflect the reclassification of repurchase agreements. Refer page 6 for further details.*

(3) *Comparatives have been restated to reflect the reclassification of transferrable certificates of deposits. Refer page 6 for further details.*

(4) *On 22 January 2004, the National bought back the preference shares issued in connection with the issue of TrUEPrSM.*

(5) *Increase primarily relates to consolidation of certain Wealth Management registered schemes.*

GROUP KEY PERFORMANCE MEASURES

	Note	Mar 04	Half Year to Sep 03	Mar 03
Shareholder measures				
EVA [®] (\$ million) (1)		978	1,154	1,105
Earnings per share (cents)				
Cash earnings per ordinary share before significant items (2)	16	122.9	135.5	133.0
Diluted cash earnings per share before significant items (2)	16	119.9	132.2	130.1
Cash earnings per ordinary share after significant items (2)		131.4	135.5	133.0
Earnings per ordinary share before significant items		129.2	132.6	116.3
Earnings per ordinary share after significant items		137.7	132.6	116.3
Weighted average ordinary shares (no. million)	16	1,505	1,508	1,524
Weighted average diluted shares (no. million)	16	1,574	1,577	1,595
Dividends per share (cents)		83	83	80
Performance (after non-cash items) (3)				
Return on average equity before significant items		18.8%	19.8%	16.8%
Return on average equity after significant items		20.0%	19.8%	16.8%
Return on average assets before significant items		0.96%	1.03%	0.94%
Net interest income				
Net interest spread	3	1.95%	2.16%	2.22%
Net interest margin	3	2.40%	2.50%	2.56%
Profitability (before significant items)				
Cash earnings per average FTE (\$ 000)		86	95	95
Banking cost to income ratio (4)		50.9%	49.6%	47.3%

		Mar 04	As at Sep 03	Mar 03
Capital				
Tier 1 ratio	15	7.47%	7.82%	7.47%
Tier 2 ratio	15	2.94%	3.30%	3.02%
Deductions	15	(1.06%)	(1.42%)	(1.33%)
Total capital ratio	15	9.35%	9.70%	9.16%
Adjusted common equity ratio	15	5.36%	4.95%	5.09%
Assets (\$ bn)				
Gross loans and acceptances		253	249	243
Risk-weighted assets	15	277	252	254
Off-balance sheet assets (\$ bn)				
Funds under management and administration		77	73	65
Assets under custody and administration		397	311	343
Asset quality				
Gross non-accrual loans to gross loans and acceptances	11	0.46%	0.55%	0.65%
Net impaired assets to total equity (parent entity interest)	11	3.0%	3.9%	4.5%
General provision to risk-weighted assets	11	0.64%	0.71%	0.75%
Specific provision to gross impaired assets	11	41.0%	33.5%	36.1%

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General and specific provisions to gross impaired assets	11	193.3%	163.4%	155.7%
Other information				
Full-time equivalent employees (no.)	9	43,282	42,540	43,002

(1) *Economic Value Added (EVA®) is a registered trademark of Stern Stewart & Co. Refer pages 23 and 79 for further details.*

(2) *Cash earnings attributable to ordinary shareholders excludes revaluation profits/(losses) after tax and goodwill amortisation.*

(3) *Includes non-cash items, ie. revaluation profits/(losses) after tax and goodwill amortisation.*

(4) *Total Banking cost to income ratio is before eliminations (refer note 1). Costs include total expenses excluding significant items, goodwill amortisation, the charge to provide for doubtful debts and interest expense. Income includes total revenue excluding significant items and net of interest expense. Refer to Non-GAAP financial measures for a complete discussion of the cost to income ratio on page 79.*

RESULTS FOR THE HALF YEAR ENDED 31 MARCH 2004

MANAGEMENT DISCUSSION & ANALYSIS

Management Discussion & Analysis Overview

OVERVIEW (1)

Economic conditions

The recovery in the global economy gathered pace during the half year to March 2004, and appears set to continue during the balance of 2004. Driven by stimulatory policy, the United States grew strongly. There was a pick-up in demand and strong investment in emerging economies (notably China). Japan began to recover and European activity stabilised. Against this backdrop, business conditions in the economies that contain the bulk of the Group's assets – namely Australia, the UK and New Zealand have been relatively favourable.

Australia

Reflecting a recovery from possibly Australia's worst drought in 100 years and an improvement in the global economy, Australian activity has picked up significantly since mid 2003. Looking ahead, Australian growth is expected to be quite strong at around 4% in 2004. Exports are expected to continue a gradual recovery, while domestic demand is forecast to moderate significantly. Higher interest rates and reduced wealth gains are expected to see dwelling investment contract moderately and consumption growth soften during 2004. Also underpinning economic forecasts are an easing in business investment growth and ongoing strength in public spending. After reaching a 15 year high in late 2003, we expect credit expansion to moderate to a still solid pace in 2004, reflecting largely an easing in household demand. Subsequent to increasing the cash rate by 50 bps, the Reserve Bank of Australia has kept the cash rate unchanged at 5.25% in early 2004, due to tentative signs of cooling in property markets and the marked strengthening of the \$A to a 7 year high in early 2004. The Group expects the Reserve Bank of Australia to increase the cash rate moderately further during 2004, as the global recovery continues, housing activity cools and the \$A eases.

United Kingdom

Economic conditions in the UK economy remain quite favourable. Activity recorded above average growth in the second half of 2003 and most indicators suggest that the economy remained robust in the first three months of 2004, particularly on the domestic side. Manufacturing has emerged from its long, deep recession, supported by the domestic recovery and brighter export prospects. Services remains the main engine of growth for the economy, underpinned by strong consumer spending. Regional growth has converged, with high house price inflation and spending in the north contributing to the reduction in the north-south disparities. The buoyant public sector and booming construction has also helped to smooth the performance of the UK regions. Despite rising interest rates, personal debt continues to expand rapidly and the housing market is robust. Household income growth has also picked up, wealth has risen and unemployment has fallen. Though still strong, the rate of growth in lending to the non-financial corporate sector has eased from its recent highs. Sterling has been rising since the second half of 2003, threatening the emerging recovery in manufacturing. Activity looks set to be sustained during 2004.

New Zealand

New Zealand also recorded quite strong activity in the six months to March 2004. The high NZ\$ eroded farm incomes and caused falling prices for traded goods. At the same time, strong consumer spending fuelled by high domestic credit growth, a buoyant construction sector and robust net immigration boosted growth. A boom in house prices, and very low unemployment coupled with solid wage claims, led to strong inflationary pressures in the services industries. While the Reserve Bank of New Zealand raised the cash rate in January to curb these pressures, it subsequently left rates unchanged as signs of a slowing economy and a cooling housing market reduced overall price pressures. Looking ahead, activity is expected to ease during 2004 due to tighter financial conditions and lower immigration.

Group performance

Whilst economic conditions were reasonable in each of the National's markets, the Group result is disappointing.

The result has been impacted by a number of adverse factors:

The strength of the Australian dollar has reduced the contribution from offshore operations. This has particularly affected earnings in Australian dollar terms from Financial Services Europe and Corporate & Institutional Banking.

The loss of \$360 million relating to unauthorised foreign currency options trading. This has had a significant impact on Corporate & Institutional Banking earnings.

(1) The discussion on the following two pages relates to results before significant items. For a reconciliation to net profit refer page 7.

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Offsetting those factors was a significant net gain on the sale of the National's shareholdings in St George Bank Limited, and a net loss on the sale of shareholdings in AMP Limited and HHG PLC, and the writeback of provisions relating to SR Investments, Inc. (HomeSide).

Cash earnings after significant items of \$1,977 million for the half year were 2.5% lower than the March 2003 half.

Cash earnings per share decreased 1.6 cents (1.2%) to 131.4 cents. This result included significant items of \$127 million relating to foreign currency options losses, sale of shareholdings and the writeback of provisions relating to HomeSide (refer to page 22 for further details).

Cash earnings before significant items of \$1,850 million decreased 8.7% on the March 2003 half and 9.4% on the September 2003 half. At constant foreign exchange rates cash earnings before significant items decreased 3.7% and 7.6% respectively.

The key features of the result are the continued improvement in the credit quality of the banking book, growth in underlying earnings in both the Australian retail banking and the Wealth Management operations, and a slowdown in growth in New Zealand retail banking. European retail banking results declined significantly. This reflected lower income levels, increased pension fund charges and higher expenses due to the reinvestment program and compliance costs. Corporate & Institutional Banking results were depressed by increased expenses and higher specific provision charges, coupled with flat income levels. Cash earnings per share before significant items decreased 10.1 cents (7.6%) to 122.9 cents.

Diluted cash earnings per share before significant items also decreased 10.2 cents (7.8%) to 119.9 cents, after taking account of the impact of dilutive adjustments, primarily the exchangeable capital units.

Diluted cash earnings per share before significant items growth (cents)

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The interim dividend has increased by 3 cents to 83 cents per share compared with the prior corresponding period and will be 100% franked.

Banking

Total Banking includes Retail Banking, Corporate & Institutional Banking and Other (including Excess Capital, Group Funding & Corporate Centre). It excludes Wealth Management.

Banking operations generated \$1,723 million of total Group cash earnings, a decrease of 12.1% on the prior corresponding period, or 6.6% at constant foreign exchange rates. Income has been flat, while expenses have continued to grow in part reflecting continued investment in the business, compliance-related costs and growth in pension costs. The result includes flat provisioning charges reflecting the continued sound asset quality profile across all regions.

The 2004 efficiency targets established under Positioning for Growth (PFG) are set out below. Financial Services Australia has exceeded its target for the last three halves, but targets for Financial Services Europe and Corporate & Institutional Banking were not achieved.

	2004 Target	Mar 04 %	Half Year to Sep 03 %	Mar 03 %
Cost to income ratio by banking division				
Financial Services Australia	46.0	45.0	45.8	45.6
Financial Services Europe (excluding pension costs)	48.0	55.1	51.4	48.5
Financial Services Europe (including pension costs)		61.5	54.7	50.9
Financial Services New Zealand	48.0	49.6	49.7	50.8
Corporate & Institutional Banking	36.0	41.4	38.7	38.7
Total Banking (including pension fund expense)		50.9	49.6	47.3

As reported in September 2003, the Group achieved its PFG target of a net reduction in full time equivalent employees of 2,040. In addition, 85% of the original PFG targeted annual cost savings of \$370 million had been delivered. Since that time, there has been expense growth related to new initiatives and an increase in staffing levels to build the business. The National is currently undertaking a strategic review. This review will be completed during the second half and the outcomes advised to the market at that time.

Wealth Management

Wealth Management reported a solid result, with operating profit of \$221 million growing 37% from the March 2003 half and 4% from the September 2003 half. This result was underpinned by the strong performance of both the Insurance business up 22% and the Investments business up 33% (although the Investments business is down 8% on the September 2003 half). Average funds under management and administration (FUMA) grew \$3.6 billion, or 5% over the half year reflecting improved investment returns. In addition, the improved equity market performance contributed to higher earnings on shareholders' retained profits and capital.

The Group continues to invest for future growth, with \$16 million after tax of strategic investment expenditure included within the Wealth Management result.

	2004 Target	Mar 04	Half Year to Sep 03	Mar 03
Wealth Management efficiency targets				
Cost to premium income ratio (%) ⁽¹⁾	21.0	19.0	20.0	21.0
Cost to funds under management (basis points) ⁽²⁾	65	58	60	67

(1) Excludes volume-related expenses

(2) Excludes the NAFIM investor compensation and enforceable undertakings and volume-related expenses.

Asset Quality

The National's asset quality has remained sound, reflecting the Group's focus on acquiring and retaining quality business.

Gross non-accrual loans for the Group decreased from \$1,379 million at 30 September 2003 to \$1,171 million at 31 March 2004. This is an outcome of the current credit environment and the ongoing strategy to exit or return impaired assets to performing loans. The proportion of non-accrual loans to gross loans & acceptances has also reduced as a result of the active management of impaired assets.

Major indicators that demonstrate the strengthening credit quality of the Group's Balance sheet include:

Improvement in the security/collateral coverage across the business;

Favourable movement in the credit ratings across the portfolio; and

Changes in the Group's asset composition with an increasing proportion of housing lending and a lower proportion of business lending.

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The general provision for doubtful debts represents 0.64% of risk-weighted assets. This is based on the calculation of market risk in line with the Standard model, as required by APRA. If the impact of moving to the Standard Method is excluded, the ratio would have been 0.69%. The general provision is calculated via statistical based methodology, which takes account of risk through consideration of the credit rating of the borrower, term of the facility and level of security held against the facility.

The Group operates a strategic credit framework that is focused on asset quality with the objective to protect, manage and enhance the credit risk profile of the National. This approach involves implementing effective credit risk policies that seek to:

Promote independent credit reviews at the industry and account level to assess credit quality and determine retention/exit lending strategies;

