Unlocking Value in University Assets

The Balancing Act “Doing More with Less”
Agenda

Introduction
  Setting the Scene - Economic Factors
Capital Advisory
  Asset Finance
Structured Finance
  Key Contacts
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  Questions
Disclaimer
Introduction
Introduction & Setting the Scene

• The Australian University sector continues to grow and develop – a continuing journey
• Increasing foreign student numbers driving change, the sector more than ever is subject to global forces
• Reform agenda:
  – Competition – domestic and international
  – The student experience and expectation
• The funding spectrum: student accommodation and general infrastructure, fitout costs, R&D assets plus various technology (IT) & energy driven assets.
The long road from this ………………………………to this
Over the past 40 years, Higher Education has moved from periphery to the centre of Australian life. In the Mid-1970s, 3% of Australians had a Higher Ed qualification; by 2013/14, that proportion had increased to ~37%.

Students numbers (domestic and international) have doubled over the past 20 years, with higher proportions from international students and off-campus students.

Australia’s universities together have an enrolment of more than 1.3 million students.

The previous Federal Government had a target, by 2025, 40% of young Australian adults (aged 25 to 34) will hold a bachelor degree or above. To support this they removed enrolment caps in Jan 2012, increasing demand. This equated to an additional 50,000 students in 2013 which was planned to will grow to 217,000 additional students by 2025. With almost one in five students from overseas, Australia have one of the highest percentage international student populations in the OECD.

The 40 full universities in Australia comprised ~2% of Australia’s GDP in 2014.

Education is Australia’s 4th largest export after iron ore, coal and tourism (still ahead of agriculture), $16.3b (2013/14) supports ~130,000 jobs.

Australia is one of the world’s leading research nations on a per capita basis. Although it comprises less than 0.5% of the world’s population, it accounts for nearly 3% of the world’s research output.

With 15 Nobel Prizes to date, Australia is one of the worlds key research nations.
The Current Environment – Global Forces

The global economy is 7 years into a grinding, uneven expansion. This year has seen a tentative stabilization in China after a weak 2014, a return to stability in core Europe (albeit with a toxic Greek overlay), mixed outcomes in the US and Japan and modest 3-3½% growth overall.

Non-Asian emerging markets have struggled in the main, especially commodity exporters, while India is the positive outlier, being in recovery mode since Modi took office.

The advanced economies are in their best position since the Crisis, reflected in less stressed fiscal positions, while the EM are coming to the end of their ability to grow rapidly without external support.

• Major source markets for students will see improved growth outcomes in 2016, as well as moderate exchange rate appreciation against the AUD.

• The latter factor will likely characterise the rest of the decade, but emerging market growth rates will not replicate their 2000s performance in absolute terms.

• The Australian dollar itself should depreciate against the US dollar in coming months/quarters, before stabilizing in 2016. Recruitment of academic talent out of USD, GBP jurisdictions more difficult as home currency salaries become less competitive. Ranking impact?

• The Australian dollar will trend lower against a foreign student-weighted basket over the remainder of the decade.
International Students in higher education: growth

2003 - 2014

Sources: AEI.gov.au, Westpac Economics.
Higher education only.
International Student Commencements By State
2002 – 2014 (Higher education only)

Sources: AEI.gov.au, Westpac Economics

*2002 commencements = 100
QS ranking & USD tuition fees: $A decline helps


Source: IBIS World & Westpac Economics 2015
All forms of education

Source: IBIS World & Westpac Economics 2015
Reform Agenda

• Competition:
  • Domestic – always existed to some degree, however with the previous Federal Government’s changes to a “demand driven” system by removing caps process accelerated. What will be implemented out of the current Federal Governments reform package is uncertain, however what is certain is there will be some change!!!
  • International – by its nature the international student market is a competitive one and competition has only increased since the GFC.
  • Disrupters – University operating model v’s MOOC’s (Massive Open Online Courses)?

• Student Experience and Expectation:
  • Gen Y – give me what I want, when I want it and NOW
  • Students are more discerning consumers
  • With the increase in foreign student numbers, the sector more than ever is subject to global forces
Evolution of University Infrastructure Funding

University Funding

- Grant Funding and Philanthropy
- Surplus Cash Flow
- Bank Debt
- Debt Capital Markets
- Structure & Project Finance
- Asset Finance
Capital Advisory
Westpac's Capital Advisory team has been active in the Universities sector, assisting clients with thought leadership around:

- Capital Structure
- Credit Ratings
- Growth Funding Alternatives
- Financial Risk Management

The team focuses on developing solutions to suit clients’ strategic needs from a holistic perspective.

We see this service as an enhancement to the relationships of our top clients.

Given the funding changes within the sector, we foresee many opportunities to assist our clients going forward.
Financing Trends

• The recently proposed reforms to Higher Education and uncertainty surrounding funding has resulted in Universities seeking more self-sufficient forms of funding

• As Universities deregulate and seek to more independently finance their operations, debt levels have been increasing and alternative forms of financing are becoming more attractive

• The number of rated Australian Universities has been increasing, with University of Sydney (Aa1) being the most recently rated by Moody’s in March 2014

• The University of Sydney and The University of Melbourne both used their credit ratings to access the domestic bond market in 2014

• Victoria University and Monash University used their high implied credit ratings to access the USPP market

<table>
<thead>
<tr>
<th>Recent Issuance (2014)</th>
<th>University of Sydney</th>
<th>University of Melbourne</th>
<th>Victoria University</th>
<th>Monash University</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date of Issuance</td>
<td>April 2014</td>
<td>June 2014</td>
<td>October 2014</td>
<td>November 2014</td>
</tr>
<tr>
<td>Volume</td>
<td>A$200m</td>
<td>A$250m</td>
<td>US$143.5m</td>
<td>US$79m</td>
</tr>
<tr>
<td>Tenor</td>
<td>7 years</td>
<td>7 years</td>
<td>17.5 years</td>
<td>25 years</td>
</tr>
<tr>
<td>Margin</td>
<td>ASW + 88bps</td>
<td>ASW + 80bps</td>
<td>Undisclosed</td>
<td>UST17.5 + 120bps</td>
</tr>
</tbody>
</table>

• The current dynamic regulatory environment provides opportunities for Universities and the banking sector to work more closely together to find new financing solutions to suit unique funding needs
Australian Universities are strongly rated by Moody’s and S&P

- All Australian universities are currently rated in the Aa / AA range. Government support provides a strong A grade floor across the sector.

- This is a result of the high / moderately high likelihood of government support, and strong international and domestic demand:
  - The Australian Government contributes an important and stable component of Universities’ revenues
  - Universities play a very important role for the Australian Government in fulfilling public policy
  - Universities in Australia have a high academic reputation in international league tables, receiving a higher rating benefit than many international peers
  - In 2014, the Australian Government provided research block grant funding of $1.7b to Australian Universities
  - Overseas students represented circa 23.1% of all enrolled students in 2014.

- In the Higher Education sector, S&P focuses on the following key qualitative factors:
  1) Government Support and the Regulatory Framework
  2) The Universities’ competitive position as measured by its academic reputation, course range and research base
  3) Student Demand
  4) The University’s operational performance and estates management program
  5) The University’s management quality, business strategy and governance
Rating Agencies Views on Reforms to Higher Education

Credit neutral for Rated Australian Universities

• The Australian Government has proposed in fiscal 2015 to implement the following significant reforms:
  1) Reduce Commonwealth funding for some Commonwealth supported places
  2) Deregulate tuition fees by removing the maximum cap students can pay for a Commonwealth supported place

• The rating agencies perceive that these reforms are likely to be credit neutral for the rated Australian Universities

• S&P believes the universities will likely alter their business models and tuition fees to compensate for the expected loss in Commonwealth funding by:
  – Removing the student contribution cap provides greater leeway for some Universities to raise revenues
  – Higher education demand remains robust, and larger Universities are likely to benefit the most
  – The rated Universities are best placed to take on a greater increase in student numbers
  – Staff salaries and infrastructure costs will likely be reduced

• Smaller to medium sized universities may find it difficult to grow student numbers significantly without spending on new infrastructure
### Publically Rated Australian Peer Group

- There are currently 6 publically rated Australian Universities (with La Trobe being withdrawn in June 2014)

<table>
<thead>
<tr>
<th>Financial Ratios</th>
<th>University of Melbourne FY13</th>
<th>University of Sydney FY14</th>
<th>Australian National University FY13</th>
<th>Macquarie University FY13</th>
<th>University of Newcastle FY13</th>
<th>University of Wollongong FY13</th>
<th>La Trobe University FY12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rating (Moody’s / S&amp;P)</td>
<td>AA+</td>
<td>Aa1</td>
<td>AA+</td>
<td>Aa2</td>
<td>Aa2</td>
<td>AA</td>
<td>AA- (withdrawn)</td>
</tr>
<tr>
<td>Total Enrolments (EFTSL)</td>
<td>40,454³</td>
<td>43,613</td>
<td>14,802</td>
<td>27,945³</td>
<td>26,195</td>
<td>22,661³</td>
<td>26,158³</td>
</tr>
<tr>
<td>Int’l Student / Total enrolment (%)</td>
<td>29%³</td>
<td>25%</td>
<td>30%</td>
<td>27%</td>
<td>19%</td>
<td>38%³</td>
<td>23%³</td>
</tr>
<tr>
<td>Revenue³</td>
<td>$1,883m</td>
<td>$1,766m</td>
<td>$974m</td>
<td>$862m</td>
<td>$676m</td>
<td>$574m</td>
<td>$614m</td>
</tr>
<tr>
<td>Int’l Student Fees / Revenue (%)</td>
<td>20%</td>
<td>22%³</td>
<td>11%</td>
<td>24%³</td>
<td>12%³</td>
<td>26%</td>
<td>16%</td>
</tr>
<tr>
<td>Australian Gov’t Funding⁴ / Revenue (%)</td>
<td>52%³</td>
<td>55%</td>
<td>62%³</td>
<td>45%</td>
<td>69%</td>
<td>55%³</td>
<td>60%³</td>
</tr>
<tr>
<td>Debt³</td>
<td>$168m</td>
<td>$438m</td>
<td>$292m</td>
<td>$357m</td>
<td>$85m</td>
<td>$132m</td>
<td>$135m</td>
</tr>
<tr>
<td>Debt / Capital⁵ (%)</td>
<td>4%</td>
<td>11%³</td>
<td>12%</td>
<td>23%³</td>
<td>8%³</td>
<td>14%</td>
<td>13%</td>
</tr>
</tbody>
</table>

Notes: 1 – Information from Moody’s. 2 – Information from S&P. 3 – From individual Universities’ Annual Reports. 4 – Includes up front student loans (HECS grants). 5 - Calculated by Debt / Total Equity.
University Debt Funding – Bank Debt Market

The bank debt market continues to be an attractive funding option for Universities

- Bank debt funding has the following key advantages as a source of funding:
  - Competitively priced
  - Revolving facilities provide flexibility
  - Simple documentation and quick to put in place
  - No penalties for early cancellation or prepayment

- Westpac has seen a large number of universities access the bank debt market in 2014 and we have seen the following trends:
  - **Tenor**: Universities are putting in place facilities with a range of tenors from 5 – 10 years and in some instances, longer dated facilities out to 15 years.
  - **Pricing**: Margins have come in over the course of 2014 and like other borrowers, universities are coming to market to take advantage of these favourable conditions.
  - **Structure**: Where there is a large funding requirement, universities are moving away from traditional bilateral facility structures to the capital markets where longer term funding at attractive pricing is available.
Asset Finance
Introduction

The Westpac Asset Finance team manages the capital & operating expenditure needs of Westpac’s Public Sector (State and Federal Government) clients, including the University & Education sector. Financing solutions structured around operating expenditure, asset procurement/upgrades, managing technical and/or asset obsolescence, essentially creating an environment to deliver more (asset growth) with less (capital expenditure budgets). Cash can be redeployed to other projects.

Example asset classes:

<table>
<thead>
<tr>
<th>Computer and Technology</th>
<th>Fit Out / Accommodation</th>
<th>Research and Medical Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Infrastructure Assets (i.e. power generators, solar, car parking systems)</td>
<td>Fleet Vehicles (passenger and light commercial)</td>
<td>Energy Efficient Assets (e.g. Power Metres, lighting, solar, HVAC)</td>
</tr>
<tr>
<td>Energy Savings Agreements</td>
<td>Information Technology</td>
<td>Data Centres / Disaster Recovery</td>
</tr>
</tbody>
</table>
Benefits for Universities

Equipment Risk
- Equipment risk transfers to financier protecting customer against movement in equipment values.
- Equipment may be returned without penalty at contract expiry providing flexibility.
- Allows customer to utilise “long-life” equipment to meet short term needs.
- Security typically limited to specific assets.

Structural
- Can allow options to purchase (subject to accounting treatment).
- Mid-term variations allow equipment to be upgraded / replaced during the term.
- Construction funding plus leasing provides a “one stop shop” solution.
- Master facilities allow easy to execute repeat financings for a variety of assets / tenors.

Tax and Accounting
- Off-balance sheet funding may change financial profile (debt, opex, capex, cash)
- Operating Lease typically excluded from debt covenants
- Treated as operating expense so preserves capex limits
Operating Lease Features

Value Proposition

Universities own a substantial number of assets which require significant replacement capital expenditure each year. Westpac can provide a value for money solution to fund existing and new assets which meet your specific objectives, which include:

- Flexibility
- Rental with purchase option
- Releasing capital for other expenditure tasks/projects
- Value for money
- Sale and leaseback
- Project specific solutions
- Operating expense / balance sheet / P&L Drivers
- Deliver capability / solution vs just a funding outcome
Benefits to Universities

Financing assets via operating leases will provide you with a number of benefits which include, but are not limited to:

- A cost effective financing solution for unfunded assets due to expenditure constraints.
- Increases diversification through alternate funding structures and tenors.
- Aligns the funding tenor to the useful life of the assets.
- Provides flexibility in line with cash flow, operating and capital expenditure and the fund mix/objectives of the each University.
- Asset risk is transferred to Westpac to facilitate operating lease treatment.
- Provides fixed rate funding to mitigate interest rate/inflation risk (floating rate can be provided).
- Provides the ability to fund assets pursuant to opex budget without seeking Treasury approval for capital expenditure.
- Provides end of term flexibility via asset returns, purchase or re-finance at maturity.
4

Structured Finance
Student Rental Receivables

Providing funding diversification and tenor benefits

Rental receivables can be packaged into bonds, providing funding for development of student accommodation or other assets.

Why?

- **Tenor:** Can provide up to [30] years funding (via issuance to debt investors), delivering a better assets / liability tenor match for the University.

- **Funding diversification:** Ability to fund via bank and investor markets both locally and off-shore (including in the US PP market).

- **Retain property ownership:** Does not require sale of the rental property.

- **Balance sheet presentation:** Potential to book funding as “unearned revenue” rather than a “debt liability”.

Considerations

- Funding amount determined by discounting the receivables at the required funding costs.

- A rental guarantee (or other security) may be required to be provided by the University.

- Investors typically prefer rated instruments, therefore a transaction credit rating (as opposed to a University credit rating) may facilitate tighter pricing. This can be arranged by Westpac.

- Westpac can repackage the transaction and on-sell to investors, thereby avoiding the University directly facing investors.

- Structures may also be available to fund both the construction and completion phases of student accommodation.
NRAS Funding Solution

Exceptionally cheap funding

A University with National Rental Affordability Scheme ("NRAS") incentives can unlock cost efficient funding via selling those incentives to Westpac.

Why?

✓ **Lower Pricing:** Lower than other bank debt facilities, delivered by unlocking the tax benefits embedded in federal NRAS incentives.

✓ **Tenor:** Up to 10 years of incentives can be funded, extending out the debt maturity profile of the university.

✓ **Fixed rate finance:** Allows the University to take advantage of the current low interest rate environment.

✓ **No-refinance risk:** Transaction fully amortises during the life of the deal.

Structure

Mechanics

- The University agrees to transfers NRAS incentives to Westpac in return for an upfront payment.

- Westpac funds the purchase of the incentives by becoming an "Approved Participant". The bank is repaid over 10 years via claiming a refundable tax offset in its annual tax return.

- The University acts as Agent for Westpac, managing all reporting obligations under the NRAS incentives.

- No change to the University’s existing tenancy managements arrangements.
NRAS Funding Solution

Key Considerations

Amount Advanced

• The advance amount is calculated by determining the present value of the remaining incentives.
• Discount rate used is based on the bank’s cost of funds.
• Other inputs include: assumed occupancy rates, rental indexation rate, company tax rate and timing for the bank to claim the incentive.

University obligations

• The University will typically be required to repay amounts not received by the bank as a result of occupancy rates, rental indexation and the company tax rate not matching assumptions used to calculate the advance amount.
• Transaction does not typically require additional security to be provided to the bank.

Government Approval

• Approval is required from both State and Federal Governments for Westpac to become the “Approved Participant” of the incentives (this may take 4 – 6 weeks to complete).

Key Terms

• Standard corporate lending terms will apply including representations, warranties, undertakings and events of default.

Loan Execution Risk

• Westpac has already implemented this structure in the university structure, supported by state and federal governments, reducing execution risk for university participants.
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Appendices
Moody’s Global Education & Non-for Profit Ratings

- Moody’s rates over 800 rated Universities, philanthropic foundations, social service providers, membership organisations and cultural institutions. This includes ~470 Universities and community colleges. Trends have been:
  - Increased demand for higher education, growing participation rates
  - Heightened trans-national competition for students, faculty, research and philanthropy
  - Stagnant funding in developed countries leads to a more market oriented approach by universities
  - Capital renewal leads to alternative financing paths, including capital markets

- The Moody’s rated global Universe is outlined below. Currently there is over $225b of Rated Debt in the sector

United States
- Over 250 public & private universities
- More than 200 community colleges
- Over 100 NFP organisations
- Private K-12 Schools

Canada
- 10 Public Universities
- Ratings from Aa1 – A3

UK
- 4 Public Universities
- Ratings from Aaa – Aa2
- One philanthropic organisation

Australia
- 3 Public Universities
- Ratings from Aa1 – Aa2

Singapore and Mexico
- Singapore: 2 Public Universities (both Aaa)
- Mexico: 1 Public University: Baa3

Source: Moody’s Investor Service Higher Education Presentation March 2014
Key Moody’s Rating Factors

Moody’s ratings are a combination of credit strength and Government relationship

Source: AFR Moody’s Higher Education Reform Summit November 2014
Australian Contributions to Uni Revenues

2008 & 2013

Sources: Federal Government, Westpac Economics
Movements in USD exchange rate: 2012/13 vs 2014/15

Source: OECD, Westpac.
University Sector funding environment

The proportion of funding universities receive from the public sector under the Higher Education Funding Act 1988 has decreased significantly in recent years. In 1995, ~65% of funding came from public sources, however by 2011, this reduced to ~44%. The university sector has made a large shift towards private financing to bridge this deficit. International students attribute ~17% (IBIS World) of university revenue.

Debt levels have increased significantly (see right), as have the use of alternate modes of finance including joint ventures, asset finance and off-balance sheet development. Bank debt with long tenor (10 – 15 years) remains the preferred option due to the conservative stance of universities (and often first-time borrowing). Debt capital market issuance is moving from a “horizon” to option for refinancing, however most universities still prefer bank debt based on flexibility initially. Two universities have successfully raised funds via capital markets in 2014, namely UoMel $250m & UoSyd $200m.

In 2014 calendar year it was estimated that over $1.2b worth of debt finance will come to market within the University Sector.

Top 15 Universities Debt Levels

Source: 2012 Financial statements, based off Universities with the highest revenue. Incorporates drawn debt only.
For references in text, source: IBIS World
## Operating Features

### Operating Lease Features

<table>
<thead>
<tr>
<th>Feature</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asset Ownership</td>
<td>• Westpac retains legal title of assets.</td>
</tr>
<tr>
<td></td>
<td>• Renter has quiet enjoyment of the assets.</td>
</tr>
<tr>
<td>Asset Management</td>
<td>• Renter has control of the asset and has an obligation to maintain the asset and obtain insurances.</td>
</tr>
<tr>
<td>Residual Value Risk</td>
<td>• Westpac bares the Residual Value risk.</td>
</tr>
<tr>
<td></td>
<td>• Renter offsets technical/asset obsolescence.</td>
</tr>
<tr>
<td>Balance Sheet</td>
<td>• Transaction shown off balance sheet as a note to the accounts detailing the future rental obligations (excluding the Residual Value).</td>
</tr>
<tr>
<td>Depreciation</td>
<td>• Claimed by Westpac.</td>
</tr>
<tr>
<td>Rentals</td>
<td>•Rentals fully charged to the P&amp;L as an operating expense.</td>
</tr>
<tr>
<td>Sale &amp; Leaseback</td>
<td>• Profit is recognised upfront.</td>
</tr>
<tr>
<td>EBITDA Impact</td>
<td>• Rental reduces EBITDA (excluding any profit from a Sale &amp; Leaseback)</td>
</tr>
</tbody>
</table>
Questions?
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