



Moody's Investors Service

Credit Opinion: Macquarie Bank Limited

Global Credit Research - 07 Oct 2009

Sydney, New South Wales, Australia

Ratings

Category	Moody's Rating
Outlook	Negative
Bank Deposits	A1/P-1
Bkd Deposit Note/CD Program -Dom Curr	Aaa/--
Bank Financial Strength	C+
Issuer Rating	A1
Senior Unsecured	A1
Subordinate	A2
Commercial Paper	P-1
Other Short Term	P-1
Ult Parent: Macquarie Group Limited	
Outlook	Negative
Issuer Rating	A2
Senior Unsecured	A2
Subordinate MTN	A3
ST Issuer Rating	P-1
Other Short Term	P-1
Macquarie Capital Funding L.P.	
Outlook	Negative
Bkd Preferred Stock -Dom Curr	A3

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Key Indicators

Macquarie Bank Limited

	[1]2009	[2]2008	2007
Total Assets (USD Millions)	90,162	139,060	110,284
Total Assets (AUD Millions)	130,405	152,294	136,389
Shareholders' Equity (AUD Millions)	6,410	6,385	7,519
NPL/Shareholders' Equity & Loan Loss Reserves(%)	19.04	3.70	2.16
Overhead Ratio (%)	64.29	75.57	74.62
Shareholders' Equity/Total Assets (%)	4.92	4.19	5.51
Pre-provision Profit/Avg Total Assets (%)	0.76	0.62	--
Liquid Assets/Total Assets (%)	34.92	42.43	44.17
Total Risk-Weighted Ratio (CAR) (%)	14.40	17.73	--
"Non-Performing" Loans/Gross Loans (%)	2.85	0.49	0.35

[1] As of March 31. [2] Statement period in which the bank switched to Basel II accounting framework.

Opinion

SUMMARY RATING RATIONALE

Moody's continues to assign ratings to bank obligations independent of the Australian government's guarantee of certain deposits and debt instruments. The rationale for these non-guaranteed ratings is discussed in this research report. Individual bank obligations that are covered by the government guarantee are assigned "backed" ratings, on a case by case basis.

Moody's assigns a bank financial strength rating (BFSR) of C+ to Macquarie Bank (MBL), which translates into a baseline credit assessment of A2. MBL is a subsidiary of Macquarie Group Limited (MGL).

MBL's rating reflects its very strong liquidity position, solid capital base and strong risk management track record through the global financial crisis. Its business line diversity and cost flexibility continue to support its pre-provision performance, although provisioning costs have increased and funding costs increased as the business climate has weakened, driving the negative rating outlook. The bank has exited certain crisis-hit business lines, but its strong financial position is enabling it to take advantage of new business opportunities presented by the crisis.

MBL's BFSR considers the bank's stand-alone financial and business profile, but is nevertheless somewhat correlated to the rating of the broader Macquarie group. The bank is subject to regulatory ring-fencing, but its franchise and operations remain closely entwined with the group. In fact, inter-group coordination is a credit strength: the group has a strong track record of extracting value from opportunities via multiple business lines.

The bank's long-term global-scale local currency (GLC) deposit rating of A1 is based on the very high probability of systemic support, in case of need - which results in a 1 notch lift from the A2 baseline credit assessment. The short-term GLC deposit rating is Prime-1. Australia is considered a high support country and MBL is viewed as having high systemic importance, being an important player in Australia's financial market.

The bank's long- and short-term GLC issuer ratings - which address the risk of senior non-deposit obligations - and its senior debt ratings are also A1 / Prime-1, reflecting the same support considerations as the deposit ratings.

Thus the GLC deposit and debt ratings of MBL incorporate three main elements: (1) the bank's BFSR of C+, (2) Moody's assessment of a high probability of systemic support (a component of joint default analysis, referred to as JDA) and (3) the seniority of its deposits and debt.

The bank's foreign currency obligations are rated the same as its local currency obligations. Australia's sovereign ceilings for deposits and debt are at Aaa, and therefore do not constrain the bank's foreign currency ratings.

Credit Strengths

- [1] Very strong liquidity profile and a small but swiftly-building deposit franchise
- [2] Diverse revenue streams, strong risk management and a historically restrained appetite for credit/market risk have contributed to stable earnings relative to wholesale banking peers
- [3] Sound capitalization and access to support from MGL - which has a track record of maintaining substantial capital buffers
- [4] Strong brand value in home market, founded on management strength and advisory capabilities
- [5] Nimbleness & expertise allows the firm to avail itself of niche business opportunities - and have underpinned its continual evolution

Credit Challenges

- [1] Earnings exposure to global financial markets slowdown - in particular equity markets
- [2] High single-name concentration exposures
- [3] Increasingly complex and diversified operations will require ongoing risk-management vigilance. The close operational integration of Macquarie Group companies inevitably results in some correlation between the risk profile of the bank and its affiliates, despite regulatory ring-fencing

Rating Outlook

The rating outlook is negative, in line with the broader Macquarie Group - with which the bank is closely integrated - and reflecting asset quality and earnings pressures that are likely to persist into calendar 2010.

The global financial crisis has led to some significant restructuring of MBL's business lines, having exited low margin, wholesale funding-intensive businesses such as residential mortgage securitization and margin lending. Whilst fairly substantial in asset size, these businesses were relatively low contributors from a return on assets perspective, and their sale / winding down do not have a major rating impact, given that, with its strong liquidity and capital, the Bank is well positioned to take advantage of new opportunities as they arise. MBL has also demonstrated the value of its retail franchise, doubling its retail deposit market share in the 12 months to June 2009.

What Could Change the Rating - Up

As the negative outlook indicates, we do not anticipate an upgrade in the near term. To move the rating back to a stable outlook, we would probably require:

- [1] increased comfort with regards to the likely operating environment trend in 2010
- [2] evidence that MBL can (re-)build earnings via its traditional fee-driven model, without taking on significant proprietary positions
- [3] reduction in single-name exposure concentrations
- [4] a stable rating outlook on other Macquarie group companies

What Could Change the Rating - Down

[1] Weaker earnings, asset impairments or capital/liquidity transfers to support the rest of the Group's operations, such that MBL's financial metrics fall below the expected range for its rating.

[2] A rapid reduction from the currently very strong level of liquid assets relative to short-term purchased funds

[3] An increase in retained risk positions relative to capital and earnings, such as through higher balance sheet exposures or an increased contribution from proprietary trading or principal investments

Recent Results and Developments

FY2009 net operating income at was down 26% to A\$3.069bn at March 2009 as a result of the global financial crisis. However, the bank's flexible expense base, driven substantially by its profit share arrangements, kept the decline in operating profit before tax and profit from discontinued operations to only 12%. FY2009 net profit was down very considerably on the prior year, which had included the gain on sale of operations as part of the bank's re-organisation into a holding company structure.

Although the bank does not engage primarily in lending, with non-securitised loans at only 17% assets, loan-loss provisioning increased sharply, with impaired & 90 days past due loans climbing to 2.9% at March 2009. However, relative to the bank's strong capital base, this remains within the expected range for the bank's rating.

DETAILED RATING CONSIDERATIONS

Detailed rating considerations for MBL's currently assigned ratings are as follows:

Bank Financial Strength Rating

MBL carries a BFSR of C+, with a negative outlook. As a point of reference, the output of Moody's BFSR scorecard is one notch higher at B-, which is almost exclusively driven by the high liquidity management subscore. However we emphasise that the scorecard is not well suited to wholesale banking institutions, being primarily designed to accommodate commercial banks. We view a high liquidity score as being wholly appropriate for a wholesale funded institution with a complex (and therefore inevitably less transparent) business mix, which may be more confidence-sensitive during times of market stress.

Qualitative Rating Factors (50%)

Factor 1: Franchise Value

Trend: Neutral

There is limited meaning to discussing MBL's franchise value on a stand-alone basis. The bank is very closely integrated with the rest of the Macquarie Group.

MBL is a relatively small player relative to Moody's rated wholesale bank peer group, however it has a strong position in its home market (despite competition from global wholesale banks) and also in a number of foreign markets, in its chosen business lines.

The bank has been restructuring its balance sheet, in line with the overall group, to refocus on businesses in which it has the greatest competitive advantage in the environment created by the global credit crisis. MBL has sold some capital-intensive, low margin businesses that are less attractive to a wholesale-funded institution like itself. These have notably included its margin lending business, its Italian mortgage book, and it has suspended its residential mortgage securitization business. At the same time, the bank, like the broader Group, has been looking to opportunities to employ its strong capital and liquidity. For example, MBL has indicated it is looking to lend to higher-rated corporate names at attractive risk-adjusted spreads, while the lending capacity of major international banks remains constrained. The October 2009 acquisition of an auto lease portfolio that compliments MBL's existing leasing book should be seen in this light.

With reference to the scorecard, the franchise score of C (baseline risk assessment of A2) somewhat understates the strength of the bank's position. The market share and sustainability subscore of C is driven by market share definitions. The earnings stability subscore of D is driven by scorecard assumptions that many of the types of wholesale business in which the bank is engaged have high volatility. Historically that has been the case, but due to the bank's diversity its performance has been very stable relative to the wholesale banking peer group, and it has not been until the current global financial crisis that there has been notable volatility at the bottom line. The geographic diversification score of B reflects the fact that MBL has the most geographically diversified revenue stream of all the rated banks in Australia, with offshore income accounting for over half of the total.

Factor 2: Risk Positioning

Trend: Neutral

MBL operates within the clearly defined risk appetite framework of the broader Macquarie Group, which measures risk relative to forward earnings and capital. It is supported by stress-testing based on a range of macro-economic linkages, whose predictive performance has held up well during the severe test of the global financial crisis. Moreover, MBL, like the Group, has exhibited negligible exposure to troubled asset classes and counterparties during the global credit crisis.

Relative to the global wholesale / investment banking peer group, MBL tends to run a low level of balance sheet risk, with notably little proprietary trading activity. The firm's high degree of diversification by business line and geography also sets it apart from the peer group. Nevertheless, it does retain some notable single-name exposure concentrations (concentration score of D), although these are somewhat mitigated by the Group's high capital allocation to higher loan-to-value ("equity") exposures.

Relative to commercial banks, loans constitute a relatively low proportion of MBL's asset base. The majority of the loan portfolio is retail focused - principally leases and residential mortgages - and granular. The majority of the mortgage book is securitized - and

we regard Australian securitizations as constituting relatively "clean" sales relative to other markets. The dollar value of residual non-securitised mortgage assets is not excessive relative to the Group's capital base and the assets of good quality. Probably greater credit risk is posed by MBL's financing of (i) selective commercial real estate projects, although the bank has an excellent track record of managing its asset quality in this sector, even through the sharp market correction of the early 1990's, and (ii) exposures relating to the Group's commodities (metals and mining) customers. Due to the Bank's healthy capital level, however, its current rating can withstand a reasonable level of asset quality deterioration.

As elsewhere, the crisis is affording MBL some unique opportunities: spreads have improved dramatically and it has the funding and capital to take selected lending opportunities. The nature of exposures taken, and the capital allocated against them may be significant from a rating perspective.

An important component of MBL's success - and that of the broader Macquarie Group - has been its ability to foster a highly entrepreneurial culture - in which individual business units are able to function with great autonomy, and where the firm is constantly expanding its business scope - while maintaining tight, central risk control. The Group's incentive structures reward behaviours geared towards long-term sustainability, with performance pay linked to risk-adjusted measures and deferred out as far as 10 years, in order to place responsibility for risk back with the business line. And the Group's business line expansion has generally proceeded at a measured pace, to products or geographies that are extensions of existing operations. MGL also often gains experience through joint ventures with local operators before committing greater resources, when it frequently acquires specialist teams to spearhead its efforts. Nevertheless, maintaining the balance between growth and control will become increasingly challenging, and at the same time important, as the Group becomes ever more diverse and international in its operations.

Factor 3: Regulatory Environment

Trend: Neutral

All Australian banks are subject to the same score on regulatory environment. This factor does not address bank specific issues; instead, it evaluates whether regulatory bodies are independent and credible, demonstrate enforcement powers and adhere to global standards of best practices for risk control. Moody's views the Australian regulatory environment as a positive factor that provides a strong underpinning to Australian bank ratings. Please refer to Moody's Banking System Outlook for Australia to obtain a detailed discussion on the Regulatory Environment.

Factor 4: Operating Environment

Trend: Neutral

This factor is also common to all Australian banks. Moody's assigns a B+ for the overall operating environment. Economic volatility is low - although not the lowest amongst developed countries - and the country has a strong legal system with good enforceability of creditor claims. We see these factors as supporting average bank asset quality and profitability over economic cycles. Please refer to Moody's Banking System Outlook for Australia to obtain a detailed discussion on the Operating Environment.

Quantitative Rating Factors (50%)

Factor 5: Profitability

Trend: Weakening

MBL has a high degree of geographic and business line diversification. While the performance of individual business lines has been volatile, this diversity has allowed the bank to maintain a high degree of earnings stability relative to its global wholesale banking peers over previous cycles.

In the current coordinated global downturn, operating revenue was down 26% at March 2009 and may remain constrained for some months yet, largely attributable to a decline in customer-flow driven trading revenues, in particular in equities. However, the bank's flexible compensation structure provides a major buffer: FY2009 staff costs were down 50% on FY2008. As a result, pre-provision earnings, which are a prime driver of ratings, actually improved 20% yoy.

Net income, (excluding extraordinary items) was down 12% on higher provisioning charges, but from a scorecard perspective, MBL continues to score in line with its rating. We again stress the limited applicability of a retail / commercial bank scorecard to a wholesale institution - although the fee-driven and diversified nature of MBL's income give it relatively more stable characteristics which are more suited to the scorecard's calibration than would be the case, say, for an institution with proportionately higher proprietary trading revenues.

Factor 6: Liquidity

Trend: Improving

MBL's liquidity and funding profile is very strong, having strengthened over the course of the global financial crisis as the bank took a pro-active approach to solidifying its position - and very considerably since 4Q08, as a result of increased access central bank repo funding in case of need (although it is worth noting that Australian financial institutions have not needed to use such facilities extensively during the crisis), and the Australian government's guarantee of bank debt and deposits.

Even pre-crisis, MBL traditionally maintained a conservative liquidity profile, in line with the overall Group - aiming to be able to cover one year's worth of wholesale obligations from internal sources. The bank's coverage of external wholesale maturities at March 2009 was 2 times, and almost completely covered the sum of its short-term external debt plus deposits. Adding net intergroup liabilities only reduces the coverage level fractionally.

We would see this as a cyclical high point and would expect liquidity levels to drop as wholesale funding market conditions improve and MBL, and the broader Macquarie Group, begins to exploit business opportunities opened up by the crisis.

MBL issued over A\$18 billion in 3-5 year government guaranteed debt from December 08 to July 09, more than doubling the stock of long-term debt and significantly lengthening the average tenor of its wholesale funding. The bank has also focused on deposit gathering, tapping its existing securities client base and assisted to some degree by the existence of the guarantee, raising A\$8bn of retail deposits from September 08 to February 09, and doubling its household deposit market share to 0.63% in the year to June 09.

MBL's liquidity management sub-score is A on the basis of its high holdings of liquid assets and decreased use of short-term wholesale funding. If the bank maintains its current long- / short-term funding mix, it would have to reduce its liquidity position by almost half for this subscore to fall to B. (As a matter of policy, we have not adjusted liquidity management sub-scores upwards during the crisis period because of the potential for access to systemic liquidity support, as the aim of the government is to pare back its liquidity support measures over the medium-term encompassed by Moody's ratings.)

The other scorecard liquidity ratio of (Market Funds - Liquid Assets) / Total Assets, which comes out at D on an unadjusted basis, considerably understates the true liquidity picture of the bank. Firstly, it does not take into account the maturity profile of wholesale debt, and due to IFRS accounting includes non-recourse securitization funding. If we make adjustments for these factors (but not other IFRS gross-ups that overstate the actual volume of assets to be funded by the bank) by measuring liquid assets to recourse short-term wholesale funding, the ratio score rises to a B.

Factor 7: Capital Adequacy

Trend: Neutral

MBL's scores well within the range expected for a BFSR of A, even though its Tier 1 ratio at FY1H09 was down to 11.4% from 12.4%. More significantly from a rating perspective, the bank's Tangible Common Equity / Risk-Weighted Assets ratio improved to 15.0% from 14.0%.

Like its peers, MBL is maintaining a higher than normal capital ratio during the crisis period. The ratio may be expected to be run down as conditions improve, and as the bank takes advantage of opportunities presented by the crisis. Following a group restructure in 2007, and before the global financial crisis, MGL had indicated that it was likely to maintain a Tier 1 ratio in the high single digit range at MBL. Such a level would be down from the pre-restructure range, but - dependent upon the lending activities in which MBL engages henceforth - might be matched by a similar decrease in concentration risks as a result of transferring the specialist funds business to Macquarie Financial Holdings Limited.

It is still somewhat early to judge whether post-crisis conditions will allow for capital to be run at such a level without any rating impact on the bank, or what the risk concentrations of the bank will be going forward. From a pure scorecard perspective, a high single digit Tier 1 ratio would be in the B range, but as discussed, the scorecard has somewhat limited applicability to wholesale banks.

Factor 8: Efficiency

Trend: Improving

Efficiency is weak relative to a large commercial bank, but MBL's cost base is highly flexible, due to the high discretionary bonus component of total costs. This factor allows the bank a high degree of short-term flexibility to cope with earnings shocks. (Of course mid-term flexibility is likely to be more limited, for if bonus levels are persistently below market, talent loss may result). Accordingly the bank's cost to income ratio improved to 64% from 76% during FY2009.

Factor 9: Asset Quality

Trend: Weakening

Lending is not a core activity for MBL in the way that it is for a commercial bank - but asset quality is weakening in line with the overall environment.

Almost half of the bank's loans are consolidated securitization trusts, notably RMBS. Australian mortgage-backed structures employ lenders mortgage insurance (LMI) for credit enhancement, and as such the originator does not retain a first loss position. Australian LMI providers have not suffered the same degree of weakness as in other Western markets and remain highly rated.

Non-securitised loans, on which the bank bears the credit risk, composed only 17% of assets at March 2009, but loan-loss provisioning increased sharply, with impaired & 90 days past due loans climbing to 2.9%. Asset quality weakness was principally in the areas of US/UK commercial real estate and lending to the bank's traditional commodities firm customers. However, MBL allocates comparatively high levels of capital against higher loan-to-value lending, which acts as an important shock absorber.

As a result, MBL's problem loans remain within the expected range for the bank's rating at 19% of capital & loan loss reserves. And increased lending activity (to higher-rated borrowers) in 2009 is likely to dilute the problem loan percentage.

Global Local Currency Deposit Rating (Joint Default Analysis)

Moody's assigns a global-scale local currency (GLC) deposit rating of A1 to MBL. The GLC deposit rating is supported by the bank's Baseline Credit Assessment of A2 as well as by our systemic support assumption of Aaa for Australia. The bank receives a 1 notch uplift from its Baseline Credit Assessment, bringing the GLC deposit rating to A1.

Moody's joint default analysis (JDA) approach is used to assess the potential for systemic support during normal market conditions. Moody's continues to incorporate this approach into its ratings of bank obligations that are not covered by the Australian government's Guarantee Scheme for Large Deposits and Wholesale Funding. MBL's government-guaranteed obligations are assigned separate "backed" ratings, on a case by case basis.

Parental Support Considerations

MBL's ratings do not include any uplift from the potential for support from its parent, MGL, under our JDA approach because (i) it is rated lower at A2 as a result of being structurally subordinated to its operating subsidiaries, and (ii) MGL's and MBL's performance are likely to be highly correlated.

In practice there is some potential for MGL to provide additional capital support to MBL - but also for capital to flow the other way. MGL is the listed entity that would raise additional capital for the group if required. The regulator has also publicly indicated that so long as regulated entities - such as both MBL and MGL - individually meet minimum regulatory capital requirements, it is ambivalent where surplus capital is held within a group structure. Therefore, given that MBL operates at a relatively high level of capital, and in view of the close operational integration of MBL and the rest of the group, there is also a possibility that capital and dividends could flow from MBL up to MGL at certain times.

Systemic Support Considerations

With regards to the potential for systemic support, we view Australia as a high support country. The Australian regulator has a proactive approach to system management, favouring an open resolution approach to prevent problems arising at individual institutions, so as to safeguard financial system stability and safeguard depositor interests (and by extension, creditor interests). The Australian authorities have also demonstrated a pronounced willingness to provide liquidity support - directly from the central bank, or indirectly through supporting the liquidity of the country's major banks - on numerous occasions in recent decades. During the current crisis, a raft of measures has been taken, including broader eligibility for central bank repo funding and the Government's Guarantee Scheme.

The probability of systemic support in the event of a stress situation is judged to be high. This is based on MBL's significant position in the Australian financial market. Additionally, the regulator's own Probability And Impact Rating System - which measures the systemic impact of the failure of an individual institution - uses asset size as a major input. As one of Australia's larger banks, MBL scores well by this metric. It also plays a significant role in Australia's financial markets. Although the bank does not have a big presence in the retail deposit market at 0.63% of household deposits at June 2009 - another factor explicitly considered by the regulator - it is nevertheless comparable in size to many regional deposit gatherers.

A Financial Claims Scheme was introduced in November 2008, in conjunction with the Guarantee Scheme. The Financial Claims Scheme effectively provides retail depositors with an advance payout on expected recoveries from a bank liquidation, subject to a cap. Currently the cap is A\$1 million, but may it be revised in future.

Longer-term, once the current Guarantee Scheme has terminated, the creation of the Financial Claims Scheme offers Australian regulators some new policy options in dealing with troubled banks. It would provide a clear exit mechanism for troubled banks, by reducing the ramifications of a bank's closure for the vast majority of its retail depositors. Potentially this could decrease the likelihood of systemic support being provided and impact our JDA analysis. However, at this stage, such considerations are quite theoretical. Even after the Guarantee Scheme has ended, would expect that the Australian authorities' propensity to provide liquidity in an emergency will decrease only gradually as public expectations adapt. Furthermore, given the prominent role of Australia's banks in financing the country's persistent foreign funding requirement, we see a significant incentive for the authorities to maintain market confidence in the financial strength of the banks.

Foreign Currency Deposit Rating

The Foreign Currency Deposit ratings of MBL are unconstrained given that Australia has a country ceiling of Aaa.

Foreign Currency Debt Rating

The Foreign Currency Debt ratings of MBL are unconstrained given that Australia has a country ceiling of Aaa.

ABOUT MOODY'S BANK RATINGS

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. Bank Financial Strength Ratings do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honor its domestic or foreign currency obligations. Factors considered in the assignment of Bank Financial Strength Ratings include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although Bank Financial Strength Ratings exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the Bank Financial Strength Rating as well as Moody's opinion of any external support. Specifically, Moody's Bank Deposit Ratings are opinions of a bank's ability to repay punctually its deposit obligations. As such, Moody's Bank Deposit Ratings are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, and includes: intrinsic financial strength, sovereign transfer risk (in the case of foreign currency deposit ratings), and both implicit and explicit external support elements. Moody's Bank Deposit Ratings do not take into account the benefit of deposit insurance schemes which make payments to depositors, but they do recognize the potential support from schemes that may provide assistance to banks directly.

According to Moody's joint default analysis (JDA) methodology, the global local currency deposit rating of a bank is determined by the incorporation of external elements of support into the bank's Baseline Credit Assessment. In calculating the GLC rating for a

bank, the JDA methodology also factors in the rating of the support provider, in the form of the local currency deposit ceiling for a country, Moody's assessment of the probability of government support for the bank in case a stress situation occurs and the degree of dependence between the issuer rating and the LCDC.

National Scale Rating

National scale ratings are intended primarily for use by domestic investors and are not comparable to Moody's globally applicable ratings; rather they address relative credit risk within a given country. An Aaa rating on Moody's National Scale indicates an issuer or issue with the strongest creditworthiness and the lowest likelihood of credit loss relative to other domestic issuers. National Scale Ratings, therefore, rank domestic issuers relative to each other and not relative to absolute default risks. National ratings isolate systemic risks; they do not address loss expectation associated with systemic events that could affect all issuers, even those that receive the highest ratings on the National Scale.

Foreign Currency Deposit Rating

Moody's ratings on foreign currency bank obligations derive from the bank's local currency rating for the same class of obligation. The implementation of JDA for banks can lead to a high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be reminded that foreign currency deposit ratings are in all cases constrained by the country ceiling for foreign currency bank deposits. This may result in the assignment of a different, and typically lower, rating for the foreign currency deposits relative to the bank's rating for local currency obligations.

Foreign Currency Debt Rating

Foreign currency debt ratings are derived from the bank's local currency debt rating. In a similar way to foreign currency deposit ratings, foreign currency debt obligations may also be constrained by the country ceiling for foreign currency bonds and notes, however, in some cases the ratings on foreign currency debt obligations may be allowed to pierce the foreign currency ceiling. A particular mix of rating factors are taken into consideration in order to assess whether a foreign currency bond rating pierces the country ceiling. They include the issuer's global local currency rating, the foreign currency government bond rating, the country ceiling for bonds and the debt's eligibility to pierce that ceiling.

About Moody's Bank Financial Strength Scorecard

Moody's bank financial strength model (see scorecard below) is a strategic input in the assessment of the financial strength of a bank, used as a key tool by Moody's analysts to ensure consistency of approach across banks and regions. The model output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating Factors

Macquarie Bank Limited

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
Qualitative Factors (50%)						C+	
Factor: Franchise Value						C	Improving
Market Share and Sustainability			x				
Geographical Diversification		x					
Earnings Stability				x			
Earnings Diversification [2]							
Factor: Risk Positioning						C+	Neutral
Corporate Governance [2]							
- Ownership and Organizational Complexity							
- Key Man Risk							
- Insider and Related-Party Risks							
Controls and Risk Management		x					
- Risk Management		x					
- Controls	x						
Financial Reporting Transparency			x				
- Global Comparability	x						
- Frequency and Timeliness			x				
- Quality of Financial Information			x				
Credit Risk Concentration	--	--	--	--	--		
- Borrower Concentration	--	--	--	--	--		
- Industry Concentration	--	--	--	--	--		
Liquidity Management		x					
Market Risk Appetite	x						
Factor: Operating Environment						B+	Neutral
Economic Stability		x					

Integrity and Corruption Legal System		x					
	x						
Financial Factors (50%)							B
Factor: Profitability							A
PPP % Avg RWA	6.13%						Neutral
Net Income % Avg RWA	4.47%						
Factor: Liquidity							C
(Mkt funds-Liquid Assets) % Total Assets					22.99%		
Liquidity Management			x				
Factor: Capital Adequacy							A
Tier 1 ratio (%)	13.93%						
Tangible Common Equity % RWA	14.72%						
Factor: Efficiency							D
Cost/income ratio					70.08%		Neutral
Factor: Asset Quality							A
Problem Loans % Gross Loans	0.41%						Weakening
Problem Loans % (Equity + LLR)	2.24%						
Lowest Combined Score (15%)							C
Economic Insolvency Override							Neutral
Aggregate Score							B-
Assigned BFSR							C+

[1] - Where dashes are shown for a particular factor (or sub-factor), the score is based on non public information [2] - A blank score under Earnings diversification or Corporate Governance indicates the risk is neutral



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