

Macquarie Group Ltd.

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Macquarie Group Ltd.

Major Rating Factors

Strengths:

- Strong market positions in key business lines in its Australian home market
- Diverse revenue streams relative to size
- Very good risk-management capabilities

Counterparty Credit Rating

A-/Stable/A-2

Weaknesses:

- Dependence on non-deposit sources of funding
- Sensitive to franchise and investor-confidence risks
- Exposed to reputational and operational risks, and risks associated with its entrepreneurial culture, in addition to typical credit and market risks

Rationale

The ratings on Macquarie Group Ltd. (MQG, A-/Stable/A-2), and its subsidiaries [Macquarie Bank Ltd. (A/Stable/A-1), Macquarie Financial Holdings Ltd. (A-/Stable/A-2), Macquarie International Finance Ltd. (A-/Stable/A-2), and Macquarie Life Ltd. (A/Stable/--)] are supported by the group's strong market positions in the key business lines in its Australian home market, including retail and institutional broking; investment banking; funds management; and fixed income, commodities, and currency (FICC). Home-market activities are supported internationally by a targeted range of investment banking products and services. MQG is the non-operating holding company for the Macquarie group, which is an Australian-based banking and diversified financial services company.

We consider that MQG group's very good risk-management capabilities offset the risks inherent in the group's business model, to an extent. In our view, the group's business model is sensitive to risks related to franchise and investor confidence, potential reputational and operational risks, and risks related to MQG group's entrepreneurial culture, as well as typical credit and market risks. Further, MQG has a liking for complex, innovative and sometimes highly structured transactions. These activities add layers of complexity routinely requiring strong risk management and systems. Traditionally, MQG has managed its broad range of risks well, and is considered to have a sound, proven risk management framework. Should any risk management weaknesses emerge in the future, however, negative rating consequences are likely to result.

We expect that MQG's risk appetite will not increase significantly, and that business expansion will be broadly in areas where MQG group has expertise. MQG has a track record of putting relatively small amounts of capital at risk in new ventures, and has a good track record in strategic partnering. That said, MQG has embarked upon a number of acquisitions in the post-global financial crisis (GFC) environment, in particular in the equities, advisory and funds management fields, and we will monitor value derived from acquisition activities to ensure continuing congruence with our current rating. The total amount of capital at risk related to these acquisitions is considered manageable, at the current rating level.

Still of relatively modest size by global investment banking standards, MQG's revenue-drivers are relatively diverse relative to its size. MQG has a broad range of business lines underneath its five main operating divisions, and its

earnings profile is becoming more geographically diverse. Further, some of its businesses, such as asset management and advisory, do not entail large amounts of capital at risk. Overall, we expect the MQG's earnings to remain supportive of the ratings. While markets, in particular equities markets, remain difficult and choppy, MQG is expected to generate profits for fiscal 2011 broadly in line with 2010. The quality of MQG's reported earnings is expected to be good, less affected by asset impairments, equity-accounted gains and losses, and one-off profit or loss items that featured in fiscal 2009 and 2010 accounts.

Traditionally orientated toward wholesale rather than retail markets, and not supported by a broad-based branch network, funding is expected to be an ongoing challenge. We believe this to be a sensitivity that impacts the rating. The GFC presented MQG with significant funding challenges, although it responded to these challenges, aided by the Commonwealth of Australia guarantee scheme, by reducing its dependence on short-term wholesale debt and lengthening its maturity profile and exiting funding-intensive businesses such as residential mortgages and margin lending. Further, MQG strengthened on-balance sheet funding by converting a large portion of funds held off-balance sheet in money market accounts to on-balance sheet deposit accounts.

Related to its reliance on non-deposit sources of funds is that MQG's business is expected to continue to be sensitive to investor confidence. MQG group's investor-sentiment metrics, such as credit-default-swap (CDS) spreads and the equity price, showed significant volatility during the GFC and its share price remains well below highs prior to the GFC. While this is a potential negative factor impacting MQG's capital flexibility, it presently gives us few concerns at the current rating level. Overall, capital is considered neutral to the rating. MQG's risk-adjusted capital (RAC) ratio for its fiscal half year ended Sept. 30, 2010, was 8.3%, which places MQG at the lower end of the second quartile of 75 of the largest financial institutions that we rate globally.

Short-term credit factors

The short-term rating on MQG is 'A-2'. Standard & Poor's considers that funding is a rating weakness for MQG group. This is primarily because, in our opinion, compared with the major commercial banks, MQG group has a weaker franchise in the wholesale and retail funding markets. Further, we consider that by the nature of MQG group's profile, it is more exposed to franchise and investor sentiment risks than are the major commercial banks. Nonetheless, while the Australian government's withdrawal of its guarantee scheme for large deposits and wholesale borrowings put more pressure on MQG group's funding, it has to-date contended satisfactorily with this pressure.

Offsetting funding and liquidity risks, to an extent, is that MQG is holding a reasonably high level of cash and liquid assets. Excluding self-funded trading assets and other accounting gross-ups (where MQG may not have unrestricted access), MQG retains liquid assets coverage for a reasonable portion of its group borrowings.

In our opinion, MQG's funding is reasonably well-diversified by counterparty, term, and currency, although funding is predominantly from semi-professional or professional markets. This is despite the group's higher level of deposits generated in fiscal 2011 by converting a large portion of funds held off-balance sheet in money market accounts to on-balance sheet deposit accounts. We view this increase in deposit levels as a one-off structural shift in liabilities, with our ongoing focus being on the extent to which MQG can retain these customer accounts while at the same time attracting new deposit customers. Further, we note that through conversion of these accounts MQG has now fully utilized a source of financial flexibility that was previously embedded within its business operations.

The ratings on MQG factor in Standard & Poor's expectation that MQG will be able to access funding and capital markets as required. Any dislocation affecting MQG in its ability to roll over the short-term borrowings in an orderly manner is likely to cause negative ratings momentum, noting that we believe that Macquarie has sufficient

flexibility to meet refinancing requirements in the normal course of events. Likewise, any problems encountered refinancing Government guaranteed borrowings will be viewed negatively.

Outlook

The stable outlook reflects our expectation that MQG will continue to evidence very good risk-management capabilities given the range and complexity of risks it manages in relation to its size and, increasingly, its geographical spread of businesses. In our opinion, failure to do so could result in immediate negative rating consequences. We also expect that the group's risk appetite will not increase significantly, and any significant business expansion will be broadly in areas where MQG group has expertise, with acquisitions well-conceptualized and funded at a level that gives us comfort at the current rating.

To maintain our view that the outlook is stable we expect that MQG will maintain supportive liquidity and capital as well as a satisfactory earnings outlook. We expect that MQG will maintain a RAC ratio at or about its current levels to giving us increasing confidence to counterbalance potential sensitivities concerning funding and investor sentiment. We note that MQG's RAC ratio deteriorated between 2010 and 2011, mainly because of strong asset growth, although did not decrease to an extent that presently gives us concern at the current rating.

Upward rating sentiment is not expected in the short-to-medium term. Rather, we see MQG's key challenge as solidifying its credit-standing at the current rating level.

Table 1

Macquarie Group Ltd. Asset Quality, Funding, And Liquidity Ratios					
	--Year-ended March 31--				
(%)	2010*	2009	2008	2007	2006
Gross nonperforming assets/customer loans plus other real estate owned	1.7	2.8	3.8	0.9	0.7
Net nonperforming assets/customer loans plus other real estate owned	0.6	1.7	2.5	0.5	0.3
Loan loss reserves/gross nonperforming assets	63.8	41.3	34.4	46.6	50.6
Loan loss reserves/customer loans	1.1	1.2	1.3	0.4	0.3
New loan loss provisions/average customer loans	0.3	0.4	0.9	0.2	N/A
Net charge-offs/average customer loans	0.1	0.3	0.1	(0.0)	N/A
Customer deposits/funding base	35.9	25.3	23.1	15.0	14.8
Total loans/customer deposits	161.9	225.4	242.8	377.7	386.6
Total loans/customer deposits plus long-term funds	61.1	60.8	60.0	65.1	60.3
Customer loans (net)/assets (adjusted)	37.0	35.0	34.3	34.7	36.6

*Data as of Sept. 30.

N/A--Not applicable.

Table 2

Macquarie Group Ltd. Profitability Ratios					
	--Year-ended March 31--				
(%)	2010*	2009	2008	2007	2006
Net interest income/average earning assets	1.2	1.2	0.9	0.8	1.0
Net interest income/revenues	16.2	17.0	15.6	9.8	10.1
Fee income/revenues	52.1	57.7	66.2	55.2	48.6

Table 2

Macquarie Group Ltd. Profitability Ratios (cont.)					
Market-sensitive income/revenues	18.9	20.7	16.5	22.0	16.6
Personnel expense/revenues	50.7	48.7	39.1	50.0	51.7
Noninterest expenses/revenues	84.7	83.9	75.3	72.3	72.7
New loan loss provisions/revenues	2.1	3.4	8.3	1.3	0.6
Net operating income before loan loss provisions/loan loss provisions	744.2	475.5	297.4	2,141.7	4,920.0
Net operating income after loan loss provisions/revenues	13.3	12.7	16.4	26.4	26.7
Pretax profit/revenues	13.3	20.3	16.4	26.4	26.7
Tax/pretax profit	17.1	15.5	1.5	14.4	19.6
Core earnings/revenues	10.6	10.3	14.9	21.6	20.3
Core earnings/average adjusted assets	0.5	0.5	0.5	1.2	1.3
Noninterest expenses/average adjusted assets	4.3	3.7	2.7	3.9	4.5
Core earnings/average adjusted common equity	8.6	7.7	11.8	27.9	26.8
Pretax profit/average common equity (%)	9.0	13.2	11.5	29.5	N/A

*Data as of Sept. 30.

N/A--Not applicable.

Table 3

Macquarie Group Ltd. Capital Ratios					
	--Year-ended March 31--				
(%)	2010*	2009	2008	2007	2006
Adjusted total equity/adjusted assets	N/A	N/A	5.9	5.4	5.1
Adjusted total equity/managed assets	N/A	N/A	5.7	5.2	4.9
Adjusted total equity plus loan loss reserves (specific)/customer loans (gross)	N/A	N/A	18.4	16.0	14.3
Common dividend payout ratio	89.2	40.1	121.3	51.2	43.7

*Data as of Sept. 30.

N/A--Not applicable.

Table 4

Macquarie Group Ltd. Summary Balance Sheet					
	--Year-ended March 31--				
(Mil. A\$)	2010*	2009	2008	2007	2006
Assets					
Cash and money market instruments	19,032	14,193	14,474	29,507	32,032
Securities	34,514	34,911	30,631	32,945	22,367
Trading securities (marked to market)	15,938	12,138	9,260	15,807	15,518
Nontrading securities	18,576	22,773	21,371	17,138	6,849
Loans to banks (net)	N/A	1,207	3,034	3,516	-
Customer loans (gross)	56,757	49,468	50,069	56,093	47,948
Loan loss reserves	602	581	656	239	162
Customer loans (net)	56,155	48,887	49,413	55,854	47,786
Earning assets	110,294	96,207	94,840	118,918	99,737
Equity interests/participations (nonfinancial)	2,719	3,927	6,123	5,500	4,071
Intangibles (nonservicing)	1,180	1,225	602	494	100

Table 4

Macquarie Group Ltd. Summary Balance Sheet (cont.)					
Fixed assets	708	605	605	375	378
Derivatives credit amount	23,430	21,561	27,428	21,136	11,913
All other assets	20,322	19,424	16,834	17,923	17,742
Total assets	158,060	145,940	149,144	167,250	136,389
Intangibles (nonservicing)	1,180	1,225	602	494	100
Minus insurance statutory funds	(5,047)	(4,846)	(4,314)	(5,699)	(5,847)
Adjusted assets	151,833	139,869	144,228	161,057	130,442
Liabilities					
Total deposits	45,028	32,411	33,726	25,824	16,530
Noncore deposits	9,981	9,927	11,858	10,041	4,127
Core/customer deposits	35,047	22,484	21,868	15,783	12,403
Repurchase agreements	6,482	7,490	3,953	13,781	7,489
Other borrowings	46,228	49,035	57,011	65,753	59,588
Other other borrowings	593	593	591	-	-
Other liabilities	48,729	45,235	44,894	51,831	45,263
Total liabilities	146,467	134,171	139,584	157,189	128,870
Total equity	11,593	11,769	9,560	10,061	7,519
Minority interest-equity	75	79	107	83	10
Common shareholders' equity (reported)	10,932	11,095	8,548	8,696	6,271
Share capital and surplus	6,344	6,547	4,904	4,522	3,096
Revaluation reserve	228	87	(220)	257	238
Retained profits	4,325	4,268	3,627	3,718	2,795
Total liabilities and equity	158,060	145,940	149,144	167,250	136,389

*Data as of Sept. 30.

Table 5

Macquarie Group Ltd. Equity Reconciliation Table					
--Year-ended March 31--					
(Mil. A\$)	2010*	2009	2008	2007	2006
Common shareholders' equity (reported)	10,932	11,095	8,548	8,696	6,271
Plus minority interest (equity)	75	79	107	83	10
Minus dividends (not yet distributed)	(297)	(347)	(114)	(552)	(482)
Minus revaluation reserves	(228)	(87)	220	(257)	(238)
Minus nonservicing intangibles	(1,180)	(1,225)	(602)	(494)	(100)
Minus tax loss carryforwards	(222)	(222)	(511)	0	0
Adjusted common equity	9,080	9,293	7,648	7,476	5,461
Plus admissible preferred and hybrids	N/A	N/A	905	1,282	1,238
Total Adjusted Capital	N/A	N/A	8,553	8,758	6,699
Adjusted total equity	N/A	N/A	8,553	8,758	6,699

*Data as of Sept. 30.

N/A--Not applicable.

Table 6

Macquarie Group Ltd. Profit And Loss					
	--Year-ended March 31--				
(Mil. A\$)	2010*	2009	2008	2007	2006
Net interest income	605	1,080	938	817	728
Interest income	2,637	4,591	6,420	6,698	4,632
Interest expense	2,032	3,511	5,482	5,881	3,904
Operating noninterest income	3,133	5,291	5,089	7,539	6,493
Fees and commissions	1,949	3,677	3,990	4,610	3,513
Trading gains	606	1,299	1,157	1,835	1,047
Other market-sensitive income	102	19	(163)	3	152
Net insurance income	46	44	55	35	27
Equity in earnings of unconsolidated subsidiaries	85	(230)	74	156	242
Other noninterest income	345	482	(24)	900	1,512
Operating revenues	3,738	6,371	6,027	8,356	7,221
Noninterest expenses	3,165	5,344	4,537	6,043	5,253
Personnel expenses	1,896	3,101	2,359	4,177	3,733
Other general and administrative expense	1,180	2,062	2,019	1,746	1,439
Preprovision operating income	573	1,027	1,490	2,313	1,968
Credit loss provisions (net new)	77	216	501	108	40
Operating income after loss provisions	496	811	989	2,205	1,928
Nonrecurring/special income	N/A	483	0	0	0
Pretax profit	496	1,294	989	2,205	1,928
Tax expense/credit	85	201	15	317	377
Net income (before minority interest)	411	1,093	974	1,888	1,551
Minority interest in consolidated subsidiaries	8	43	103	85	88
Net income before extraordinary	403	1,050	871	1,803	1,463
Net income after extraordinary	403	1,050	871	1,803	1,463

*Data as of Sept. 30.

Table 7

Macquarie Group Ltd. Core Earnings Reconciliation Table					
	--Year-ended March 31--				
(Mil. A\$)	2010*	2009	2008	2007	2006
Net income (before minority interest)	411	1,093	974	1,888	1,551
Minus nonrecurring/special income	0	(483)	0	0	0
Plus or minus tax impact of adjustments	N/A	75	0	0	0
Minus preferred dividends	(15)	(29)	(78)	(84)	(85)
Core earnings	396	656	896	1,804	1,466

*Data as of Sept. 30.

N/A--Not applicable.

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Ratings Detail (As Of March 31, 2011)*	
Macquarie Group Ltd.	
Counterparty Credit Rating	A-/Stable/A-2
Preferred Stock (1 Issue)	BBB
Senior Unsecured (9 Issues)	A-
Senior Unsecured (2 Issues)	A-2
<i>South African National Scale</i> (2 Issues)	zaA-1
<i>South African National Scale</i> (1 Issue)	zaAA+
Short-Term Debt (2 Issues)	A-2
Subordinated (2 Issues)	BBB+
Counterparty Credit Ratings History	
17-Feb-2010	A-/Stable/A-2
17-Sep-2008	A-/Negative/A-2
15-Nov-2007	A-/Stable/A-2
Sovereign Rating	
Australia (Commonwealth of) (Unsolicited Ratings)	AAA/Stable/A-1+
Related Entities	
Macquarie Bank Ltd.	
Issuer Credit Rating	A/Stable/A-1
Bank Fundamental Strength Rating	
<i>Local Currency</i>	B
Certificate Of Deposit	
<i>Foreign Currency</i>	A/A-1
<i>Local Currency</i>	A-1
Commercial Paper	
<i>Foreign Currency</i>	A/A-1
Preference Stock (1 Issue)	BBB+
Senior Unsecured (6 Issues)	A
Senior Unsecured (1 Issue)	A/NR
Short-Term Debt (2 Issues)	A-1
Subordinated (11 Issues)	A-
Subordinated (1 Issue)	A-/NR
Macquarie Capital Loans Management Ltd.	
Preference Stock (1 Issue)	BBB
Macquarie Finance Ltd.	
Junior Subordinated (1 Issue)	BBB+
Macquarie Financial Holdings Ltd.	
Issuer Credit Rating	A-/Stable/A-2
Macquarie International Finance Ltd.	
Issuer Credit Rating	A-/Stable/A-2
Macquarie Life Ltd.	
Financial Strength Rating	
<i>Local Currency</i>	A/Stable/--

Ratings Detail (As Of March 31, 2011)***(cont.)**

Issuer Credit Rating

Local Currency

A/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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