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Commonwealth Bank of Australia ACN 123 123 124

CBA Risk Management Briefing

8 December 2006

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Agenda

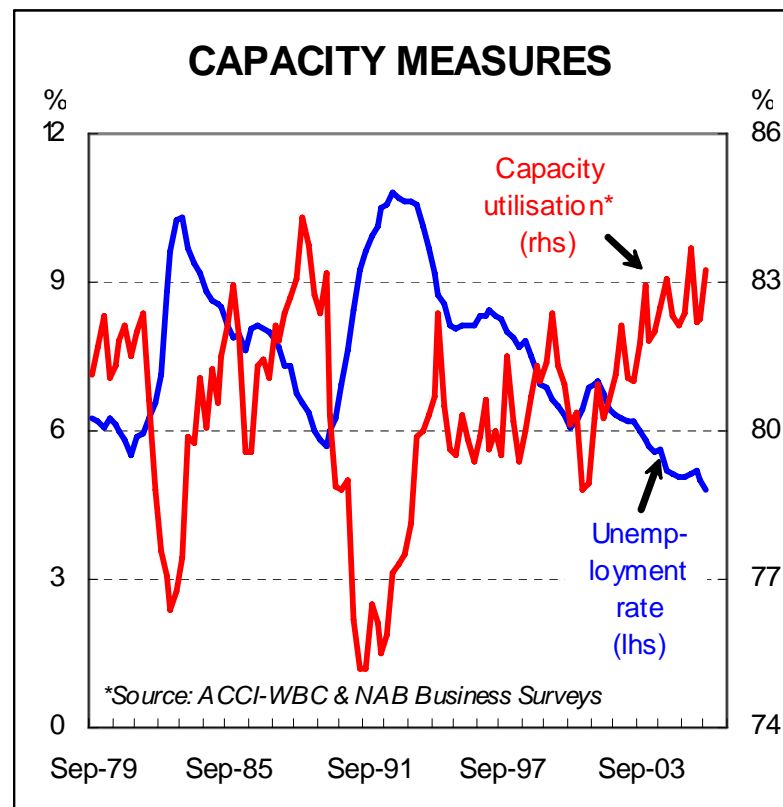
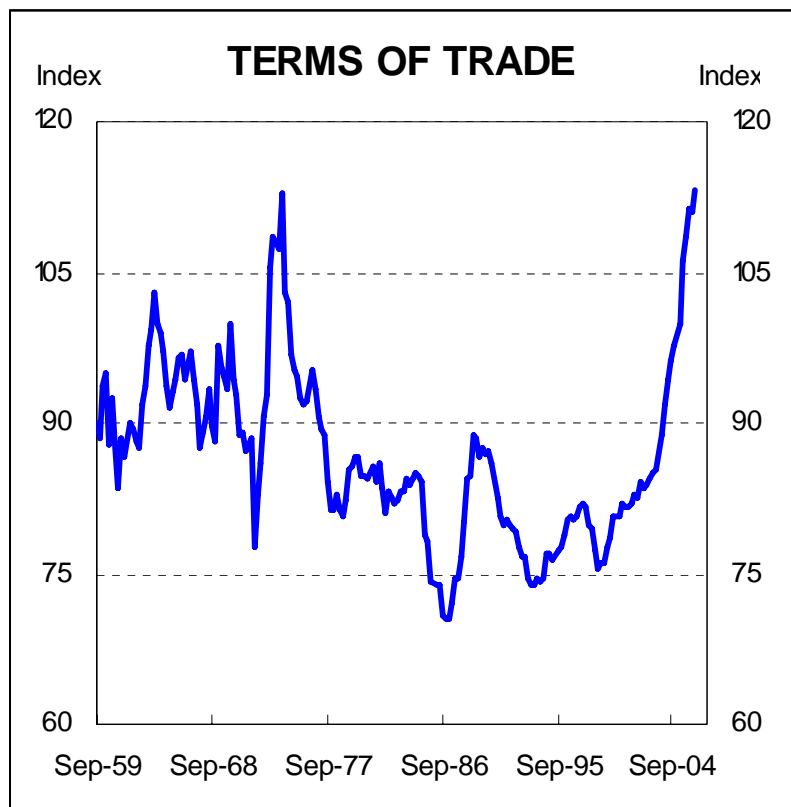
- **Introduction – Mick Leonard**
- **Economic Update – Michael Blythe**
- **Overview – Mick Leonard**
- **Insurance Risk – Jim Evans**
- **Retail Credit Risk – David Grafton**
- **Market Risk – Paul Riordan**
- **Panel Questions**



Michael Blythe
Chief Economist



Key Drivers: Strong Income & Spending



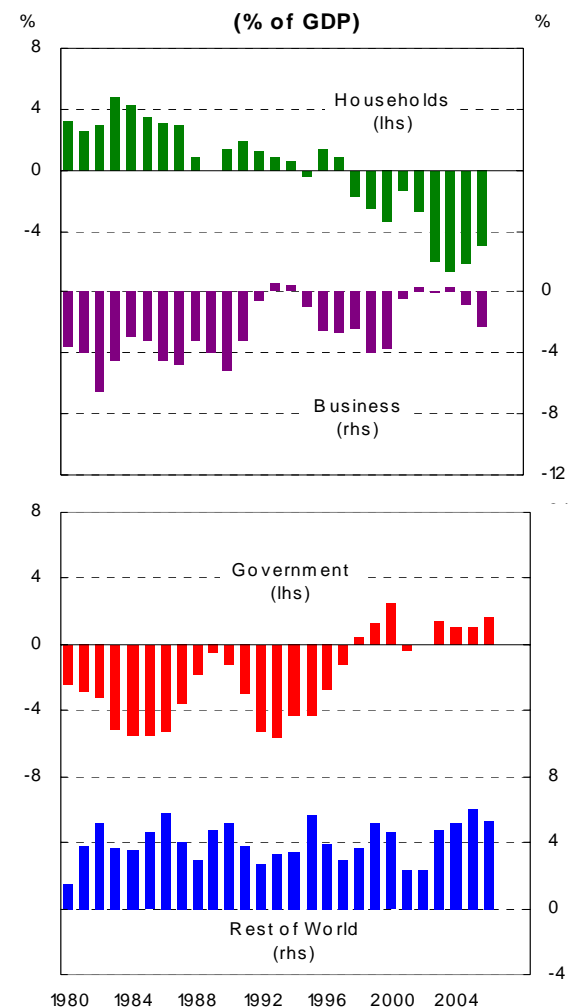
- Rising terms of trade are providing a substantial income boost.
- Lengthy period of uninterrupted growth means little slack in the economy.

Key Outcomes

Squaring the circle

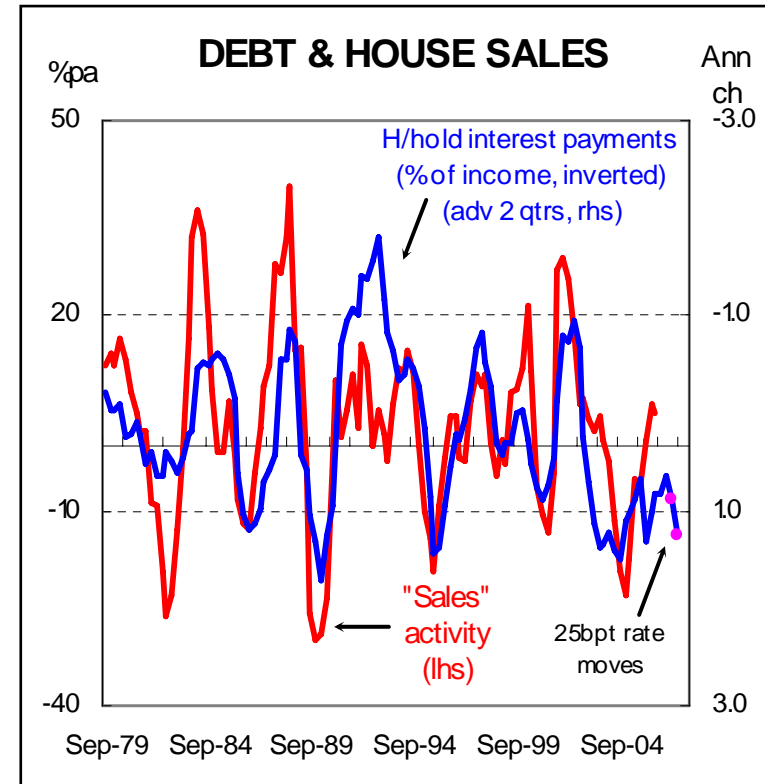
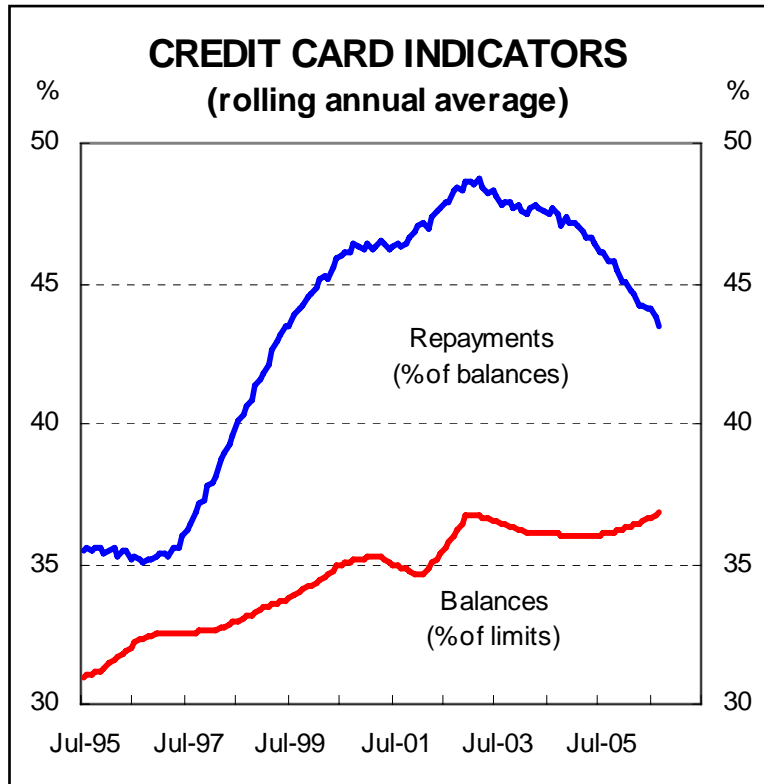
- From a savings-investment perspective, the terms of trade boom encouraged global investors to lend us more and allowed government to become a net lender as well.
- The flip side is that businesses and, especially, households were encouraged to increase their borrowings.
- Implications:
 - leveraged to the global economy like never before;
 - the household sector is most exposed.

AUSTRALIA: NET LENDING BY SECTOR



Household Strain – Debt

Paying the piper



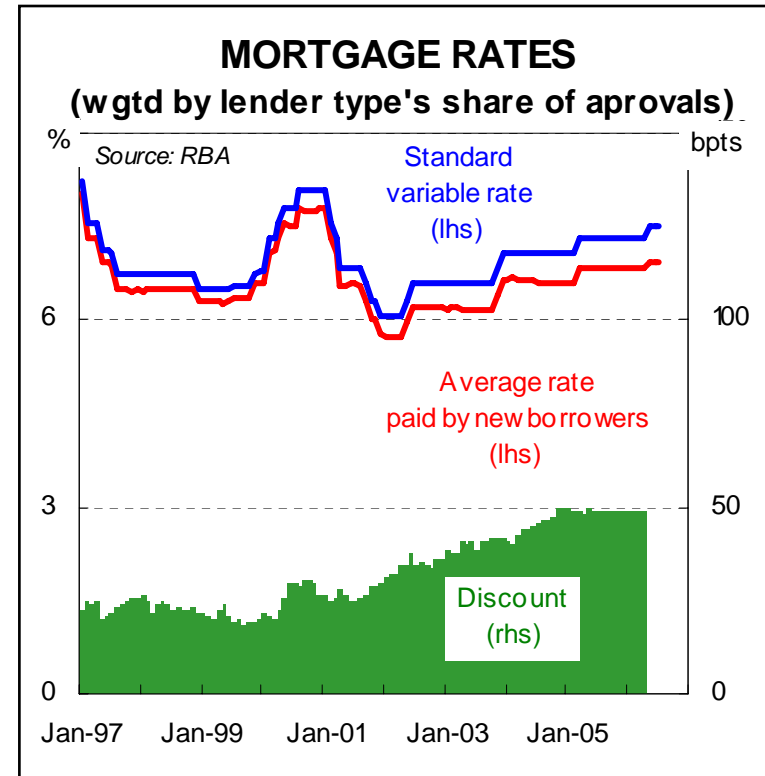
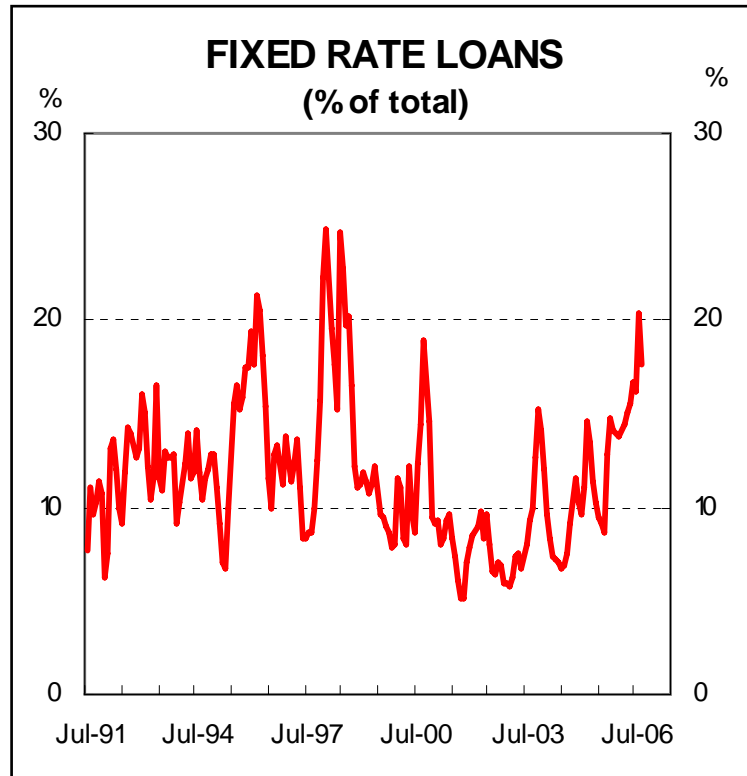
- Adverse trends in credit card indicators an indication of h/hold budget strain.
- Rising debt servicing implies risks lie with slower spending.

Notes



Household Strain – Interest Rates

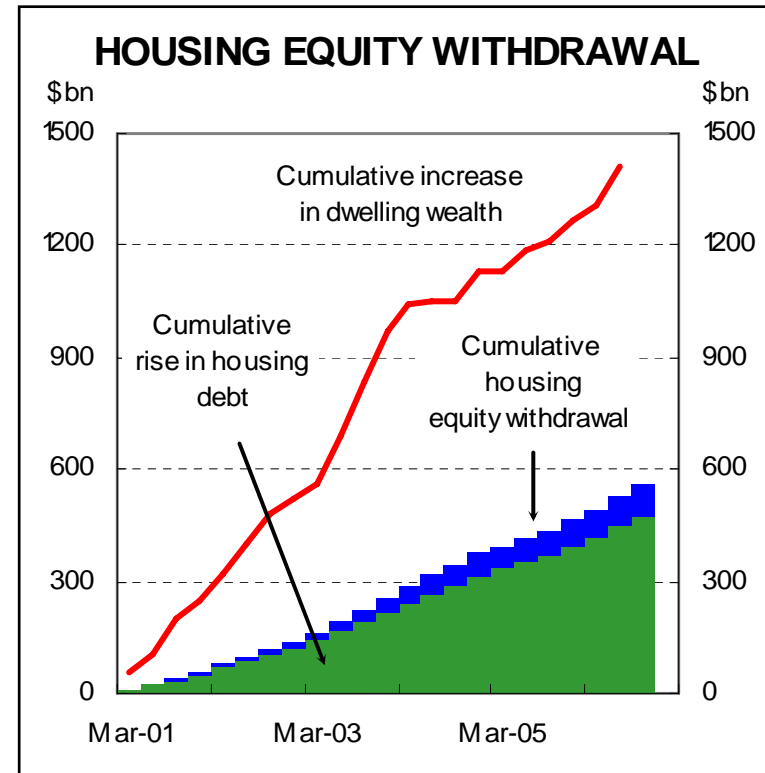
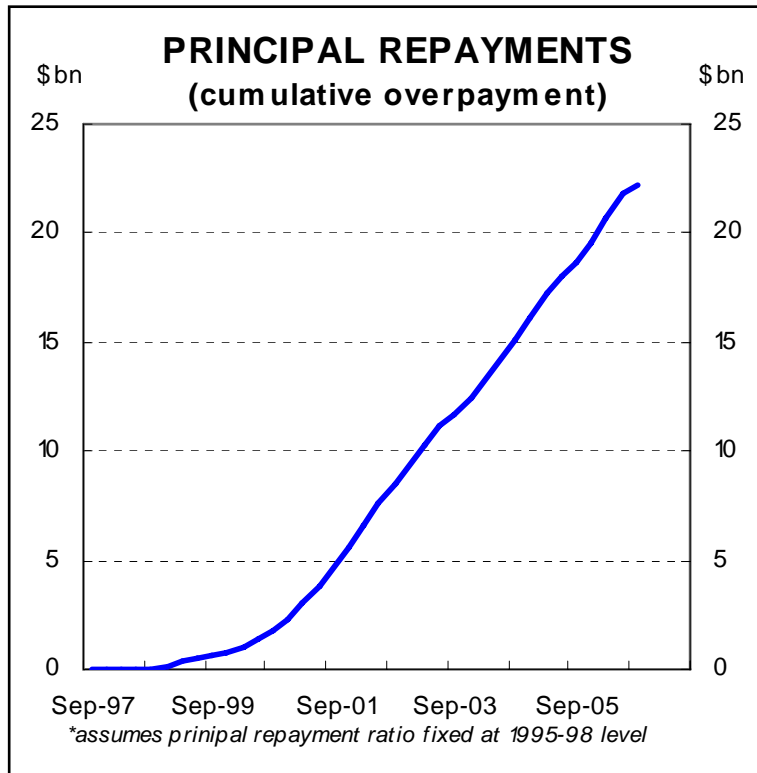
Consumer Insurance - Part 1



- Fixed rate lending running at high levels.
- Competition limiting flow through of RBA actions to lending rates.

Household Strain – Interest Rates

Consumer Insurance - Part 2

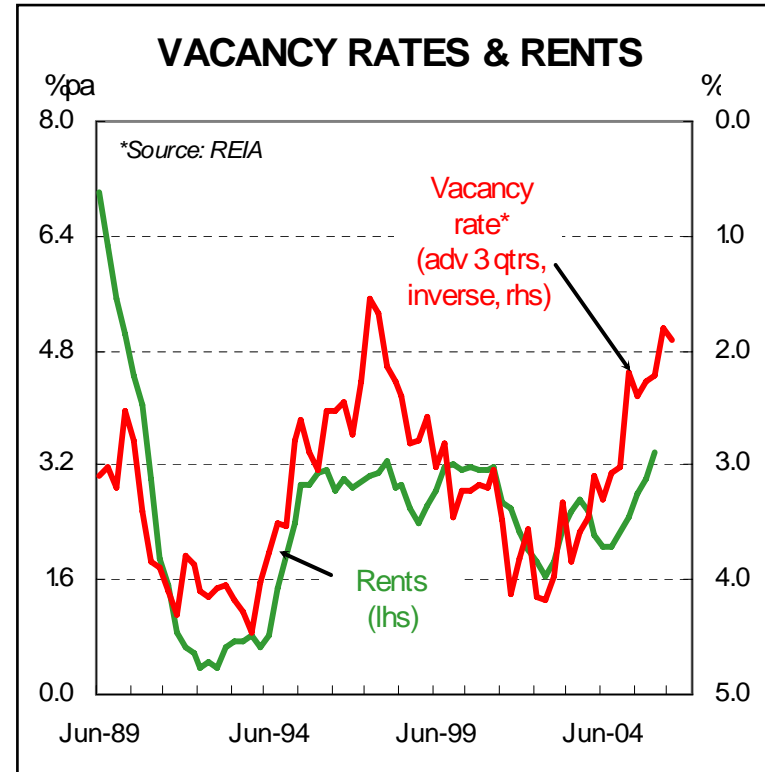
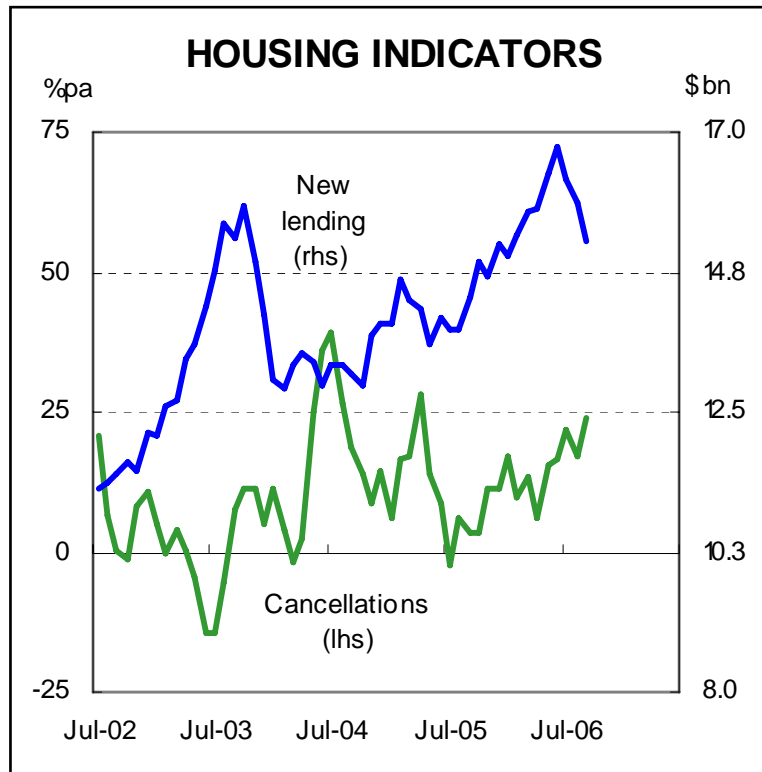


- Borrowers continue to repay loans at a rate in excess of contractual commitments.
- Accumulated housing wealth is a significant untapped financing source.

Notes

Housing

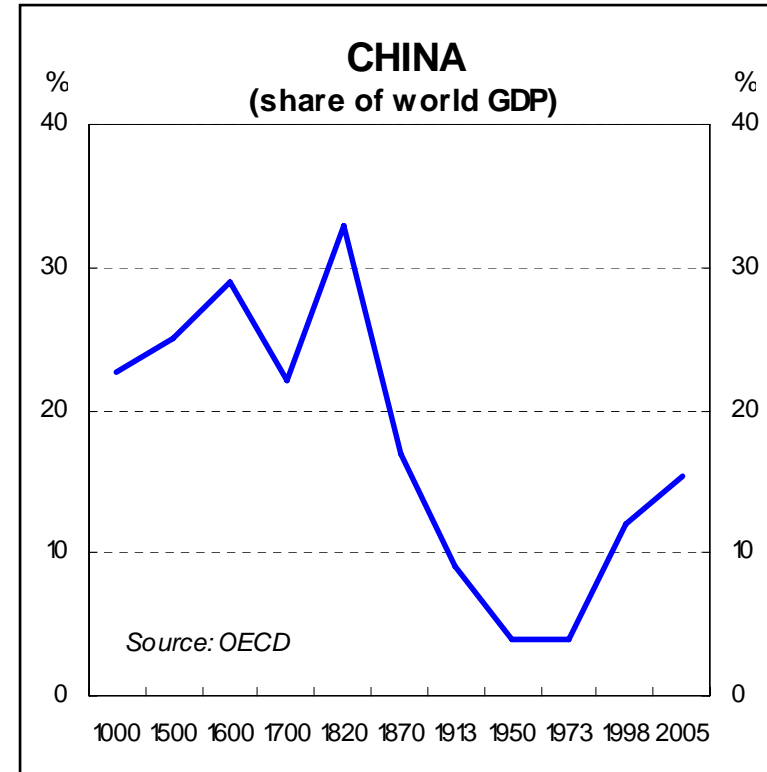
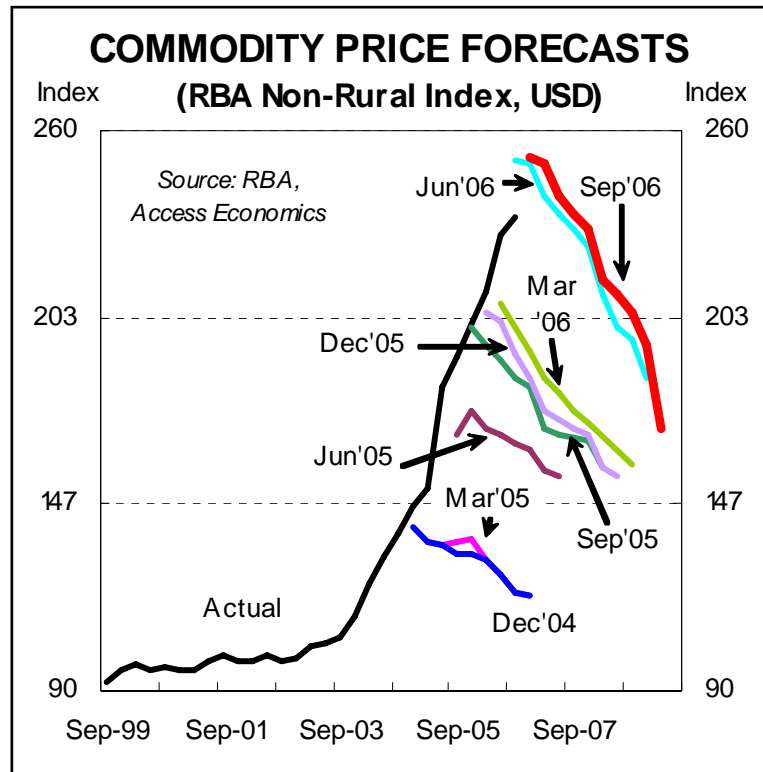
Demography is Destiny



- Housing activity has slowed in response to higher interest rates.
- Demographic drivers favour a lift in residential construction.

Commodity Price Bust?

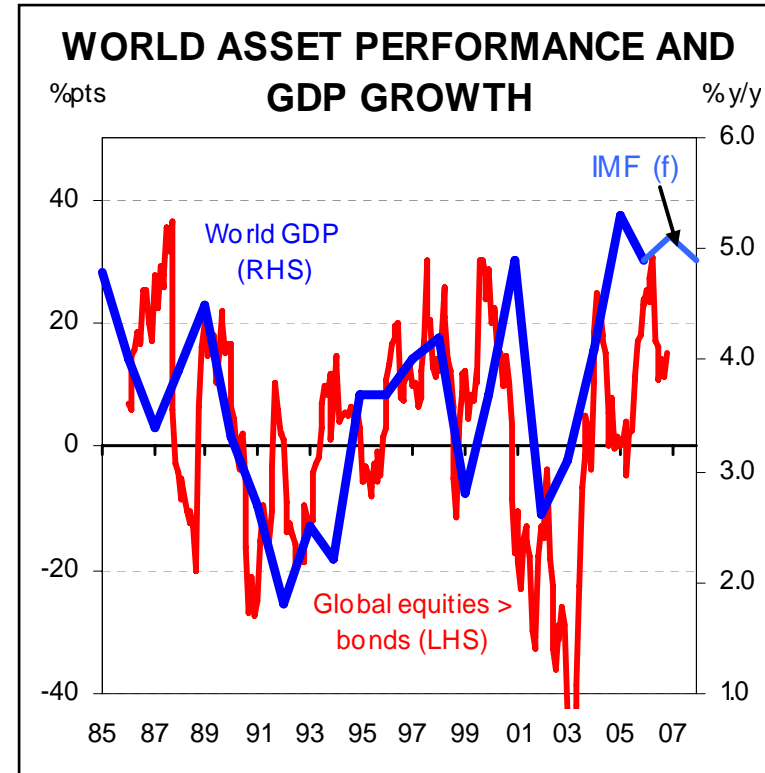
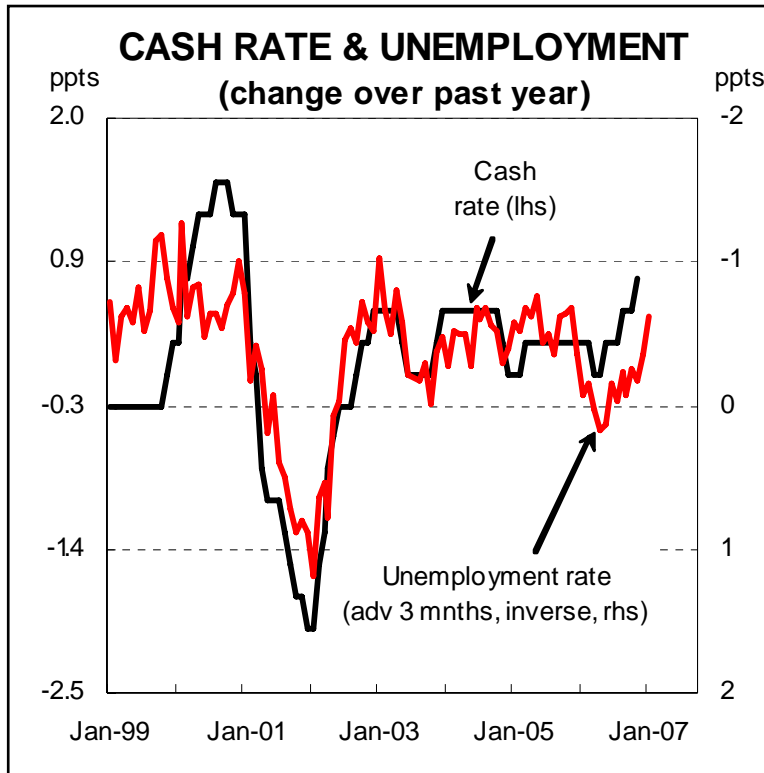
What Goes Up Must Come Down?



- History says commodity booms are followed by busts.
- But the demand-supply balance still looks favourable.

Interest Rates

One and Done [again?]



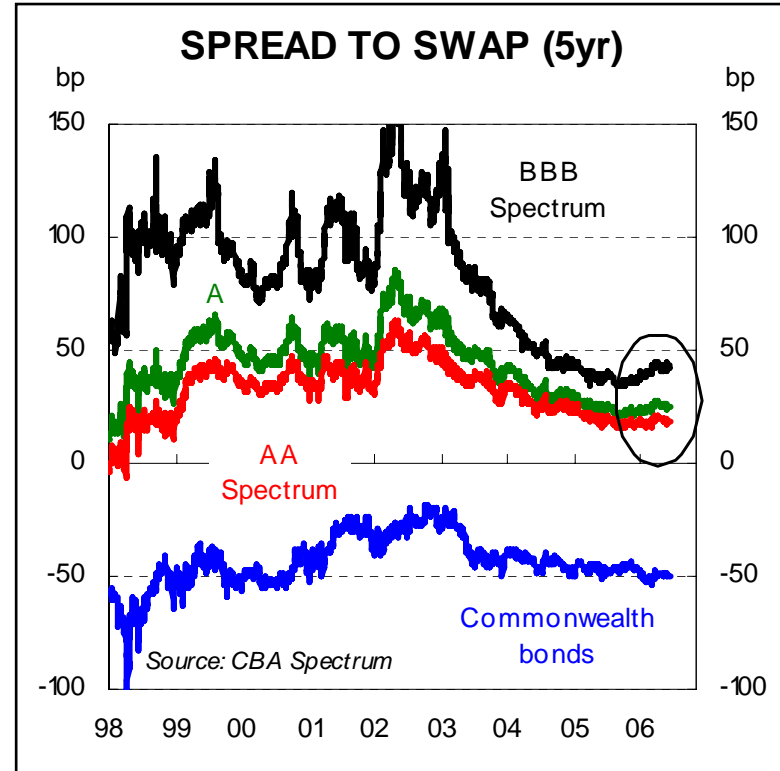
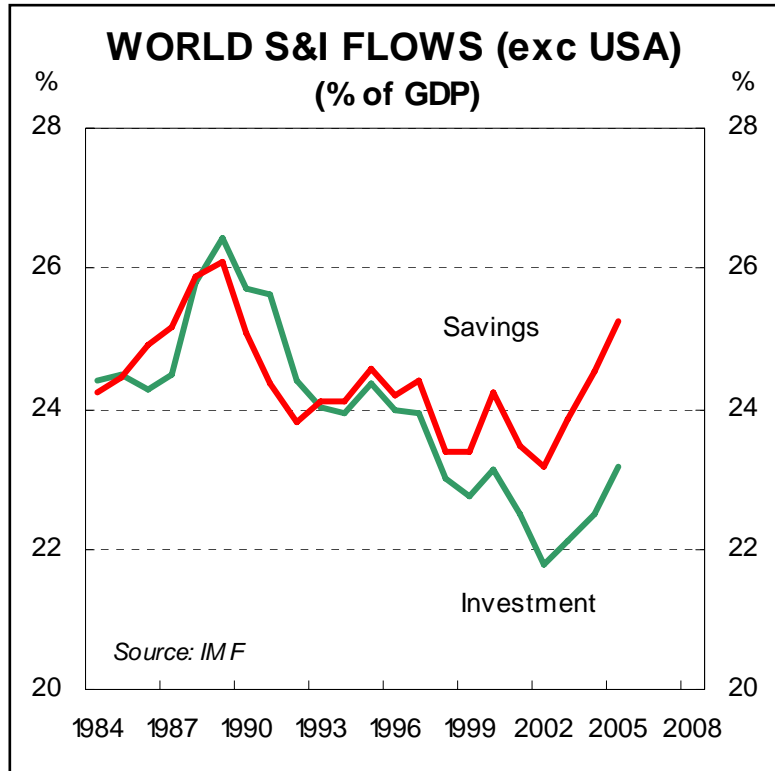
- Tightening bias remains – but tough test for getting a 6½% cash rate over the line.
- Global economic backdrop favours growth assets over yield.

Notes



Credit Markets

As Good as it Gets?



- Background conditions favour a lift in M&A activity.

Notes



Our View

Global growth momentum to continue

- US is slowing but Japan and Asia to absorb any slack;
- Underlying commodity price outlook still favourable;
- Period of low interest rates and excess global liquidity over;
- Background conditions favour a repricing of risk.

Australia retains momentum and inflation risks remain

- Business capex and prospective export lift are rebalancing growth;
- High petrol prices and rate rises exposing highly leveraged households;
- Rising terms-of-trade to keep spending pushing against capacity;
- Inflation risks to the high side but fundamental drivers relatively favourable;
- Drought a significant drag.

Economic policy and markets

- RBA to maintain a tightening bias;
- Bonds still vulnerable to higher risk premia;
- AUD to the high side of the range.



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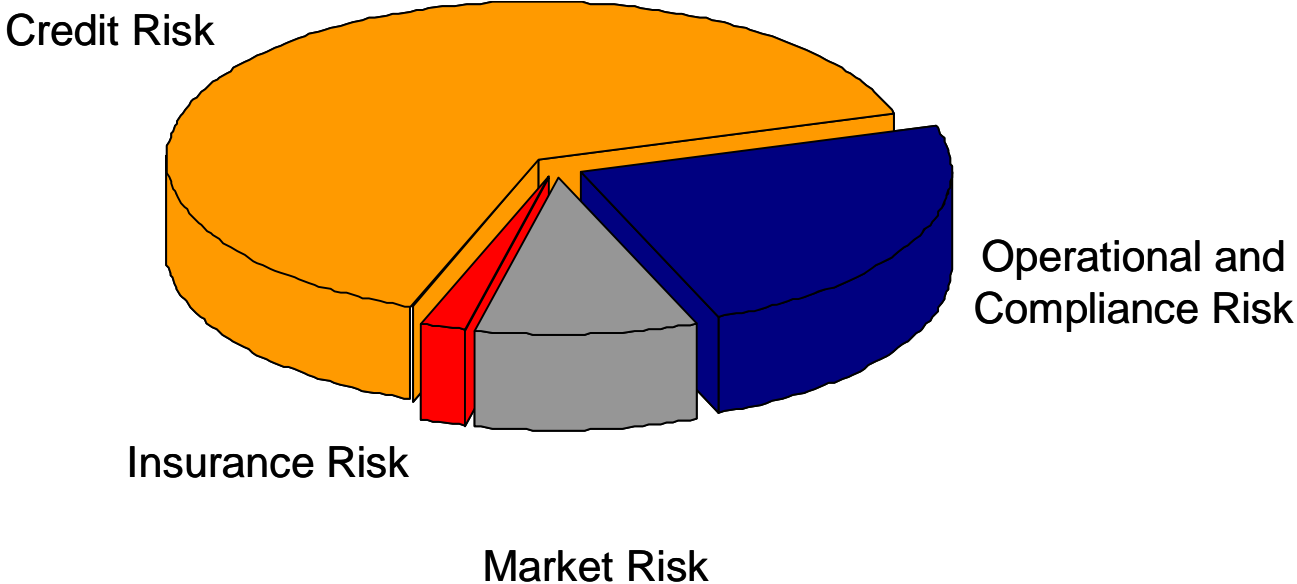
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Mick Leonard
Chief Risk Officer



Our Risks



Economic Capital - 30 June 2006

Notes

Today

- Risk Management as a strategic and operational advantage
- Looking forward
- Maximising investment in Risk Management



A Strategic and Operational Advantage

Our strengths:

- People
- Identification & Measurement
- Pricing for risk
- Tools
- Processes



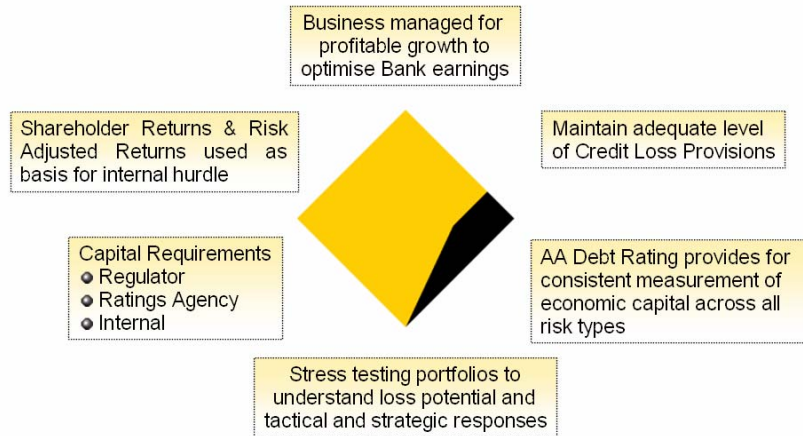
Our philosophy:

Together we deliver optimal customer outcomes



Notes

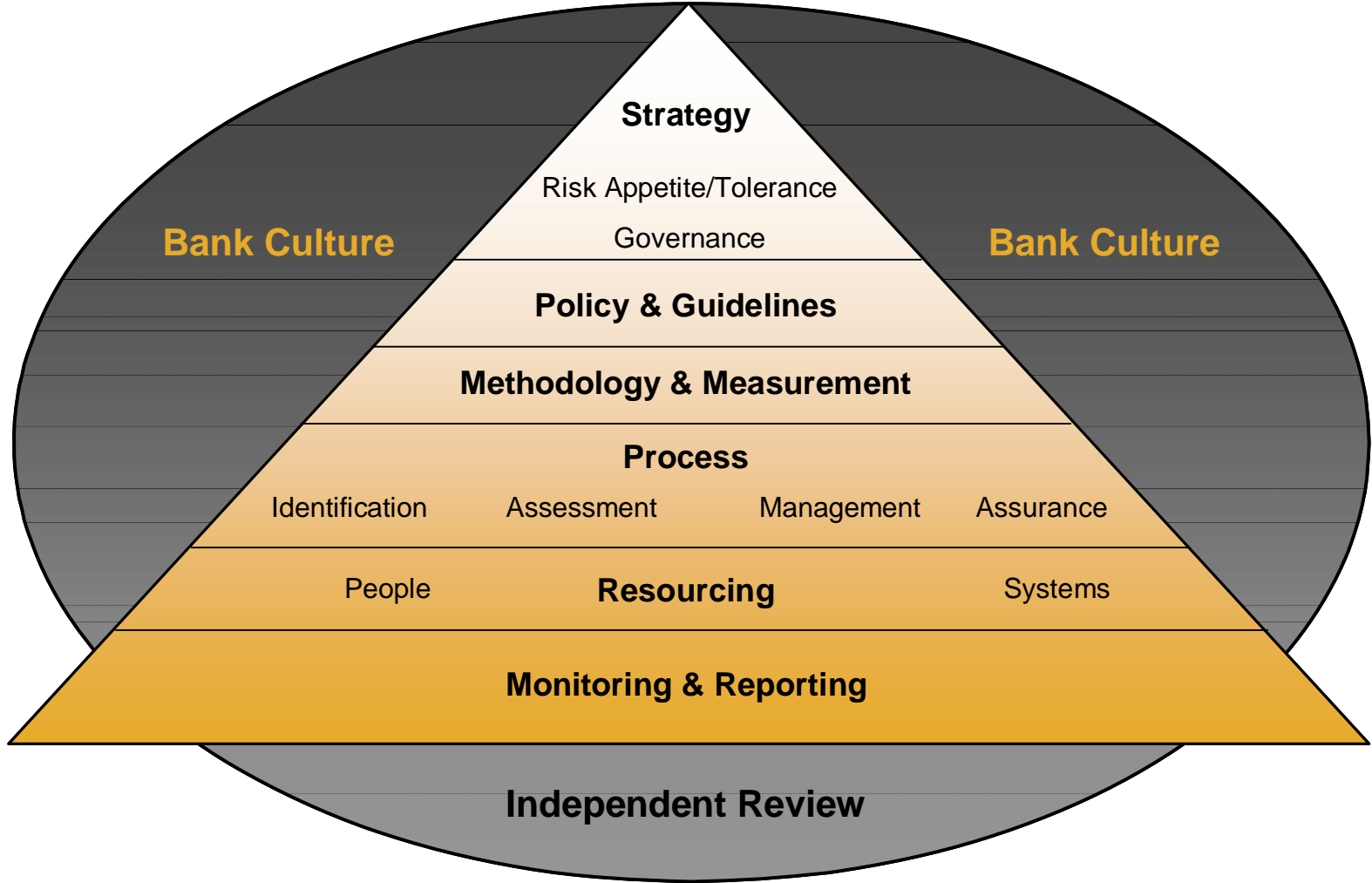
Clear Risk Appetite



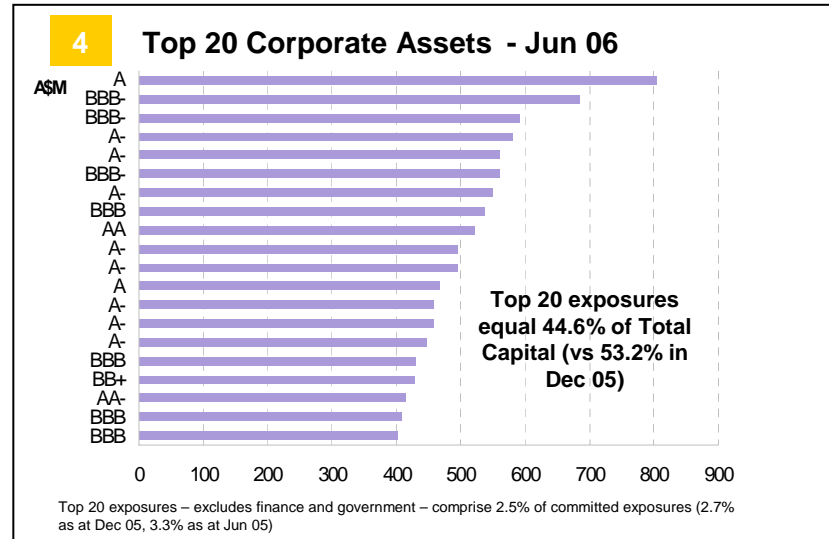
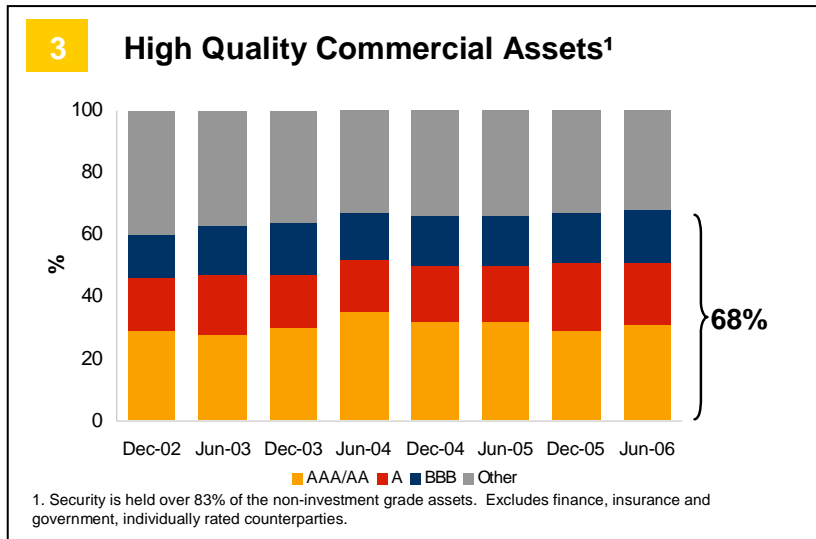
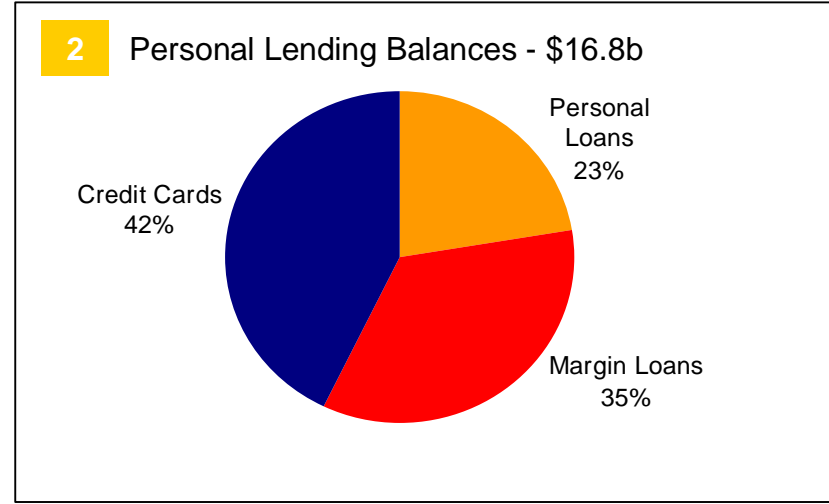
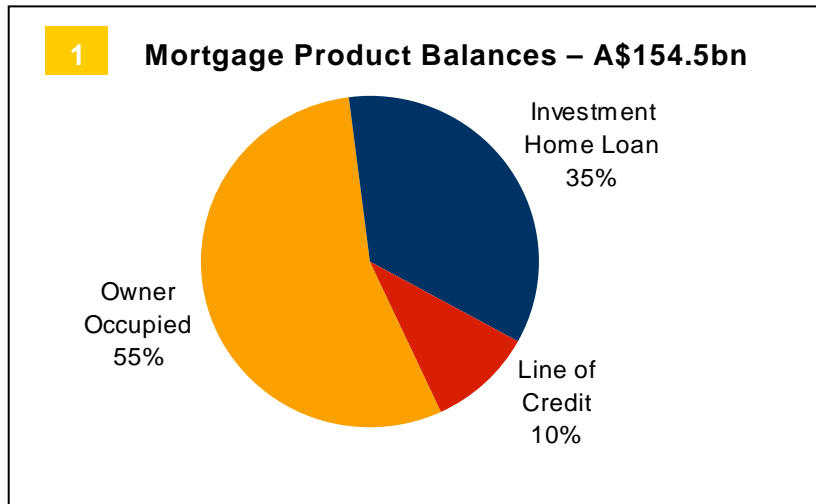
Single Accountability, Shared Oversight



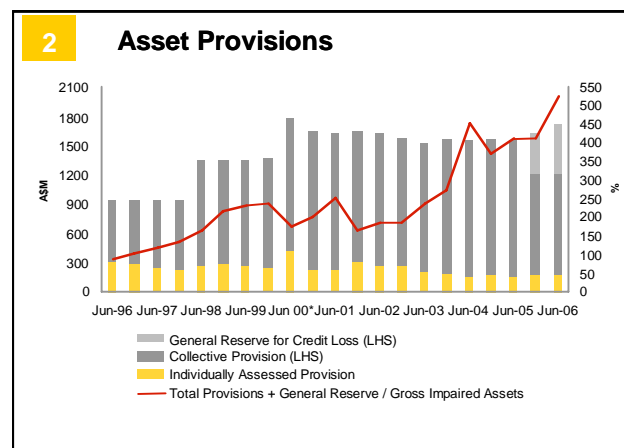
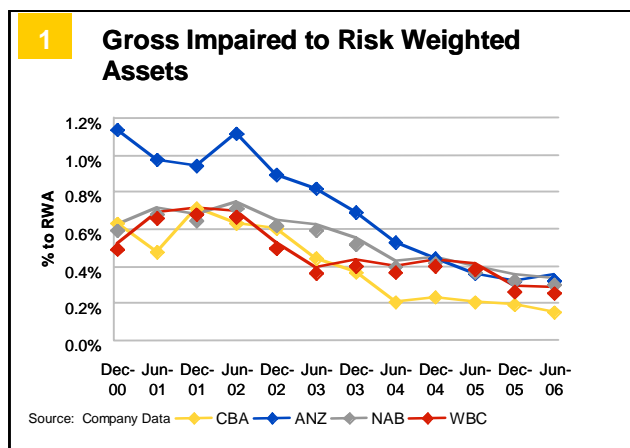
How We Manage Risk Bank-Wide



Looking Forward



Low Bad Debts and Well Provisioned



AIFRS Adjustment as at 1 July 2005

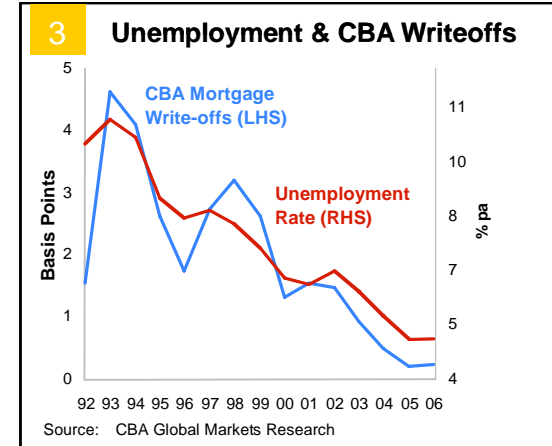
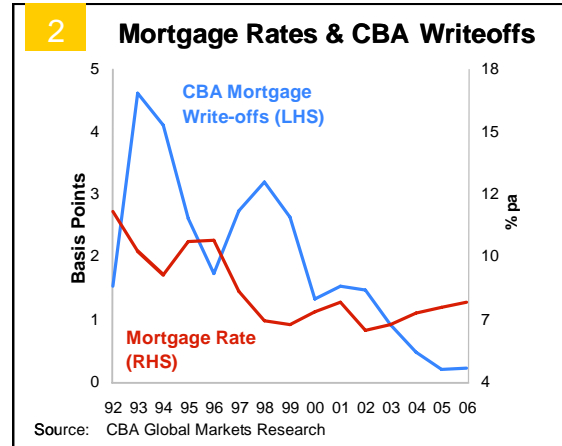
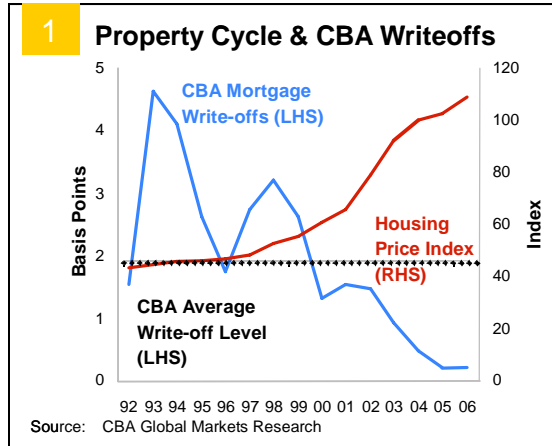
	AIFRS \$m	AGAAP \$m	Variance \$m
Collective / General Provision	1,021	1,390	(369) ³
Other Balance Sheet Items ¹	75	-	75
Sub-Total	1,096	1,390	(294)
Individually Significant / Specific Provision ²	191	176	15
	1,287	1,566	(279)

1. This amount was previously included within the Australian GAAP General Provision, and under AIFRS must now be reclassified within "Assets at fair value through profit and loss", "Available-for-sale assets" and "Other Liabilities" 2. Includes interest reserved of \$19 million 3. This adjustment will be largely offset by the creation of a General Reserve for Credit Loss.

Notes

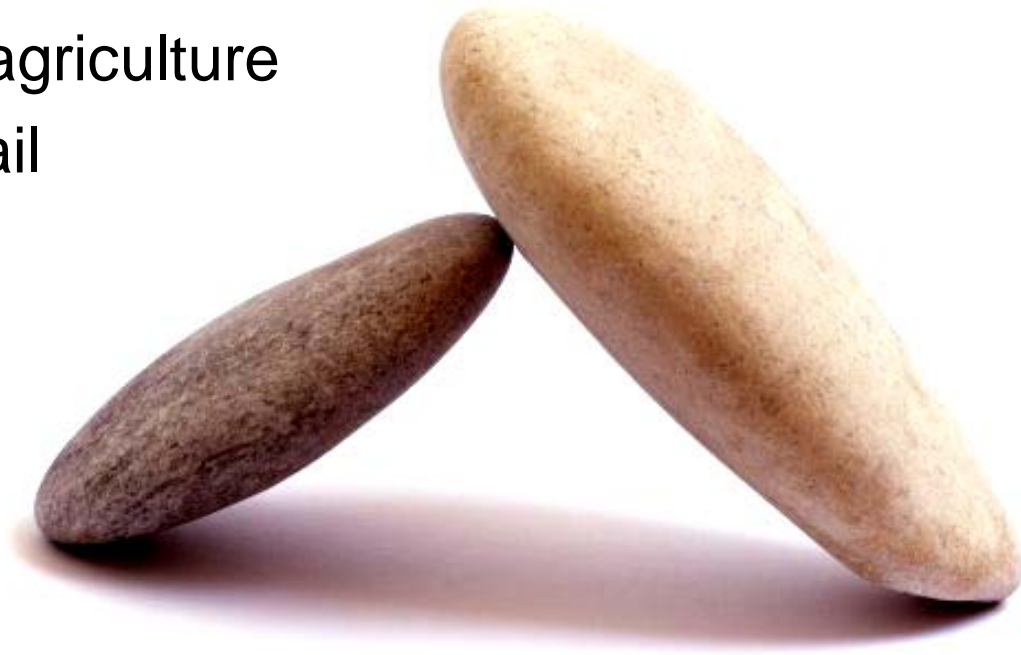


Key Indicators



Monitoring Sensitivities

- Retail unsecured
- Automobile Industry, including Auto parts
- Grape growing
- Property developers
- Some aspects of agriculture
- Discretionary Retail



Managing Sensitivities

- Stress Test the Portfolio
 - Internal
 - an event driven approach i.e. a worst case economic downturn, to assess the impact on the portfolio of exceptional but plausible large loss events
 - specific parameters based on a hybrid between historical experience and a hypothetical future case
 - External
 - APRA Panama
 - IMF Financial System Stability Assessment
- Contingency Planning
- Diversification
- Recovery Workout Group
- Opportunities



Reduced Volatility = Predictable Earnings

Regulatory Developments

Sarbanes Oxley

- A review of the design and operating effectiveness of SOX internal controls over financial reporting was conducted and independently tested for the 2006 Financial Year.
- This was undertaken to support an internal SOX compliance management assessment across the Bank.
- It concluded that there were no material weaknesses identified as at June 30th 2006 and that the Bank's internal controls over financial reporting were effective as at that date.
- The benefits from SOX include improved controls and testing regimes, with improved visibility and clarification of control ownership. Management's external Certification is on track for June 30th 2007.
- Significant announcements are expected from the PCAOB and US SEC about December 2006.

AIFRS

- The Bank adopted the Australian equivalent to International Financial Reporting Standards (AIFRS) from 1 July 2005.
- Ongoing convergence project between the International Accounting Standards Board and FASB (US Accounting Standards setters).

Basel II

- The Bank is targeting Advanced accreditation for Basel II for both credit risk and operational risk
- The Basel II project has assisted in the elevation of risk management culture throughout the Bank. The implementation of improved risk management awareness, processes and systems mean that we can:
 - Package and price our products more competitively
 - Making better decisions, taking risk into consideration
 - Optimise our regulatory capital position
 - Support our objectives of excelling in customer service
- The Bank awaits advice from the regulator for standards related to Pillar II & III. We are on target for 1 January 2008, with the parallel run for 2007.

Anti Money Laundering & Counter Terrorism Financing

- The proposed new legislation for AM/CTF signals a move to a risk based system. The Bank continues to work with the regulator (AUSTRAC) and industry bodies to finalise the rules. The Bank is also updating its AML risk assessment and will complete a scoping study following the passage of the Bill.
- Our approach will be to implement a program with minimal disruption to our customer relationships, while leveraging our technology investment in CommSee and the Group Data Warehouse

Maximising Investment in Risk

Approach: Anti Money Laundering

Optimise business outcomes versus compliance

Benefits:

- Package & price our products more competitively
- Optimise capital
- Improved processes & systems
- Better decisions that reflects risk
- Improved risk awareness
- Support our objectives of excelling in customer service

Sarbanes Oxley

Investment = Delivering Business Growth



Key Messages

- Strategic & Operational Advantage → Bank-wide
- Reduced Volatility → Predictable Earnings
- Investment → Delivering Business Growth

Together we deliver optimal customer outcomes





Jim Evans

Executive General Manager
Risk Management & Compliance
Wealth Management



Notes

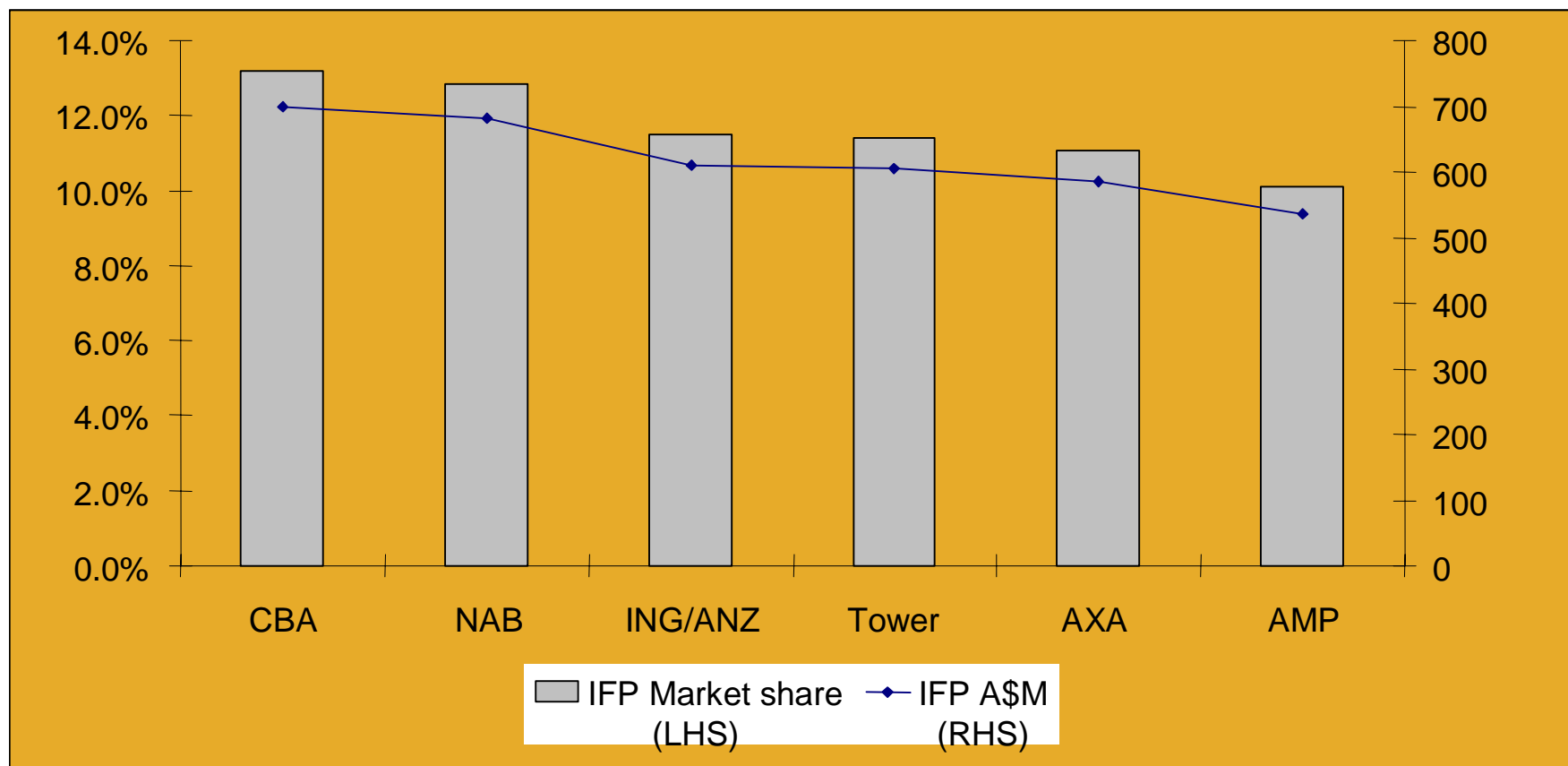
Today

- About our business
- What we do
- How we manage risk
- Risk Management cycle
- How we complement the Bank's products and services



About Our Business

Life insurance – in force premium market share



Source: Data per Plan For Life as at 30 June 2006.

CMLA Life assets as at Oct 06 \$22.6 bn

CMLA Life net assets as at Oct 06 \$1.2 bn

What We Do

- Insurance businesses offer products that are promises to pay
- The promise is either event based or time based
- Examples are losses that arise from accident, weather, earthquakes
- For people these can be sickness, disability, temporary loss of income or time based, being superannuation.



How We Manage Risk

- Governance processes
- Risk management cycle
 - Specifying the problem
 - Developing the solution
 - Monitoring the experience



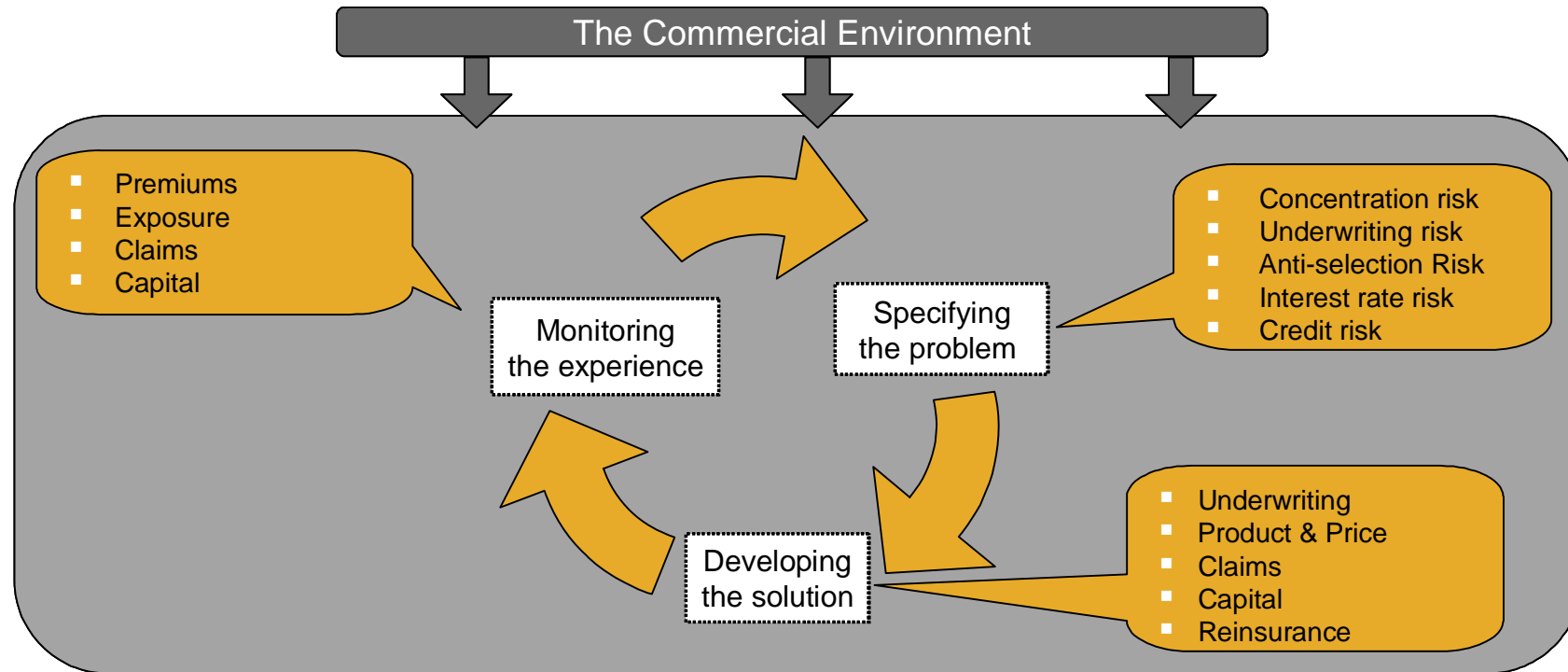
Governance Process

- Majority of Independent Directors
- Appropriate committee structures and members superannuation trustees – majority of independents
- Board and committee charters create agenda completeness.



Risk Management Cycle

- Insurers pool risks to consistently achieve required return on capital.
- A three stage risk management process is adopted where risks are constantly monitored (and new ones identified) with future assumptions revised in light of past experience.



Take risk opportunities to satisfy customer needs that are profitable to the shareholder

Notes

Developing the Solution

Example: Home & Content Insurance

- Underwriting risk
- Anti-selection risk
- Concentration risk
- Interest rate risk
- Reinsurance credit risk



Monitoring the Experience

Example: Home & Content Insurance

Regular monitoring identifies where & why actual experience differs from expected:

- New Business Sales
- Sales Conversion & Retention
- Exposure
- Claims
- Capital



Refine solutions (products) to enhance growth & market share



How we Complement the Bank's Products and Services

- What is different about insurance?
 - Evolution of time (Create wealth)
 - Event risk (Protect wealth)
- Products are designed to enhance people's lifestyles through either:
 - Wealth creation (Superannuation)
 - Wealth protection (Insuring assets)
- Complementary to Banking products

Risks are seen as an opportunity to help a customer in a way that is profitable to our shareholders

Create and Protect People's Wealth

Key Messages

Insurance businesses offer products that are promises

- Governance processes are critical
- Quality risk management is vital
- So that we can create and protect people's wealth

The resulting benefits are

- Quality products
 - Competitive pricing
 - Risk adjusted returns
- Reduce volatility of financial results
 - Competent and reliable management

Optimal Shareholder Returns





David Grafton

Executive General Manager
Credit Risk Management and Analytics
Retail Banking Services



Today

- What is happening in:
 - Retail Credit Risk Management
 - Retail Credit Portfolios
- What are the improvements driving performance?
- The benefits



What is Happening in Retail Credit Risk Management?

- Considerable investment in improving capability
- Talented team of scale and capability
- All credit scorecards rebuilt and range of new ones implemented
- New parameterised credit risk management software systems

Notes



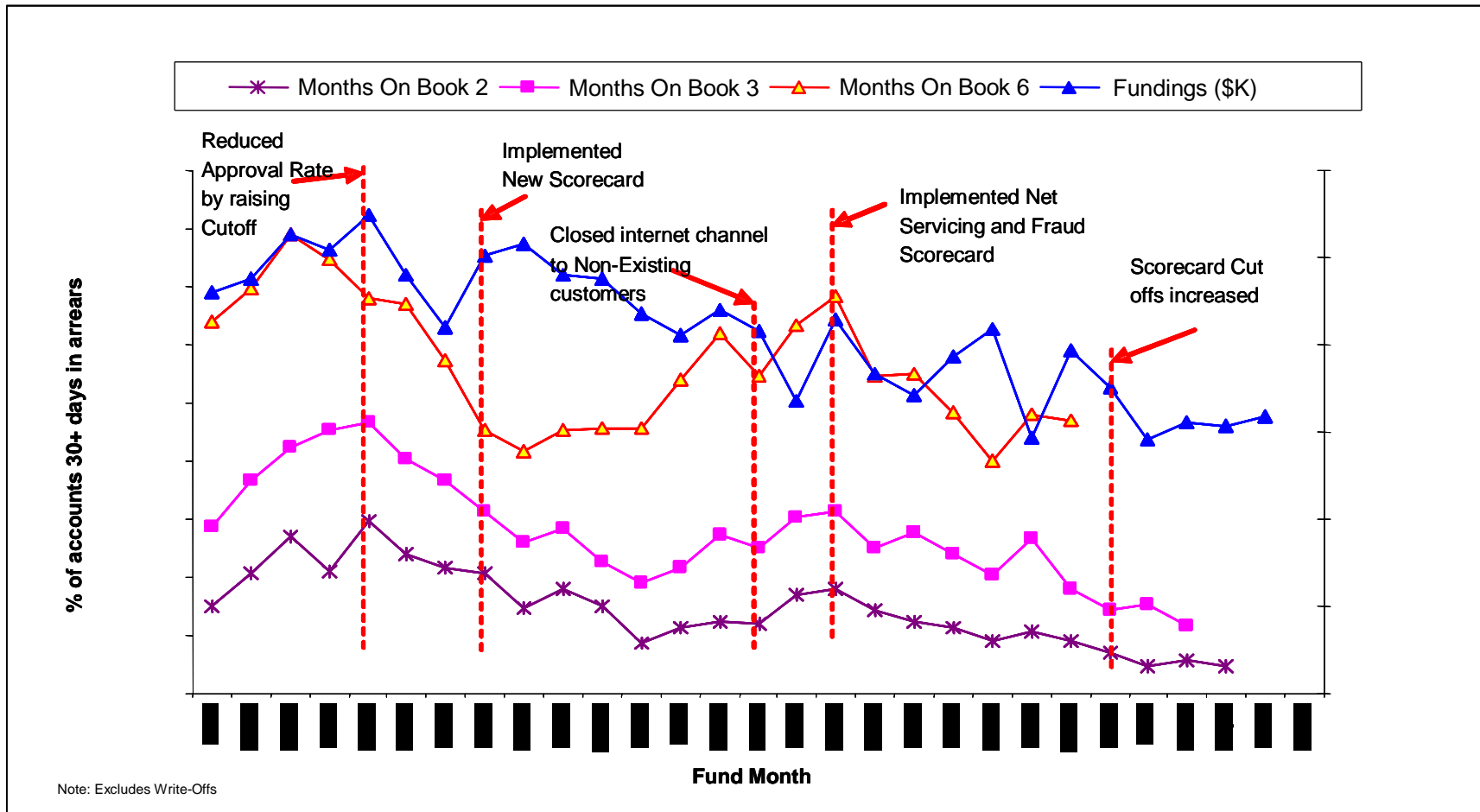
Centre of Excellence

- Small Business Automation
- International [NZ, China, Indonesia]
- Group Security [fraud]
- Group Risk Management [Basel models]



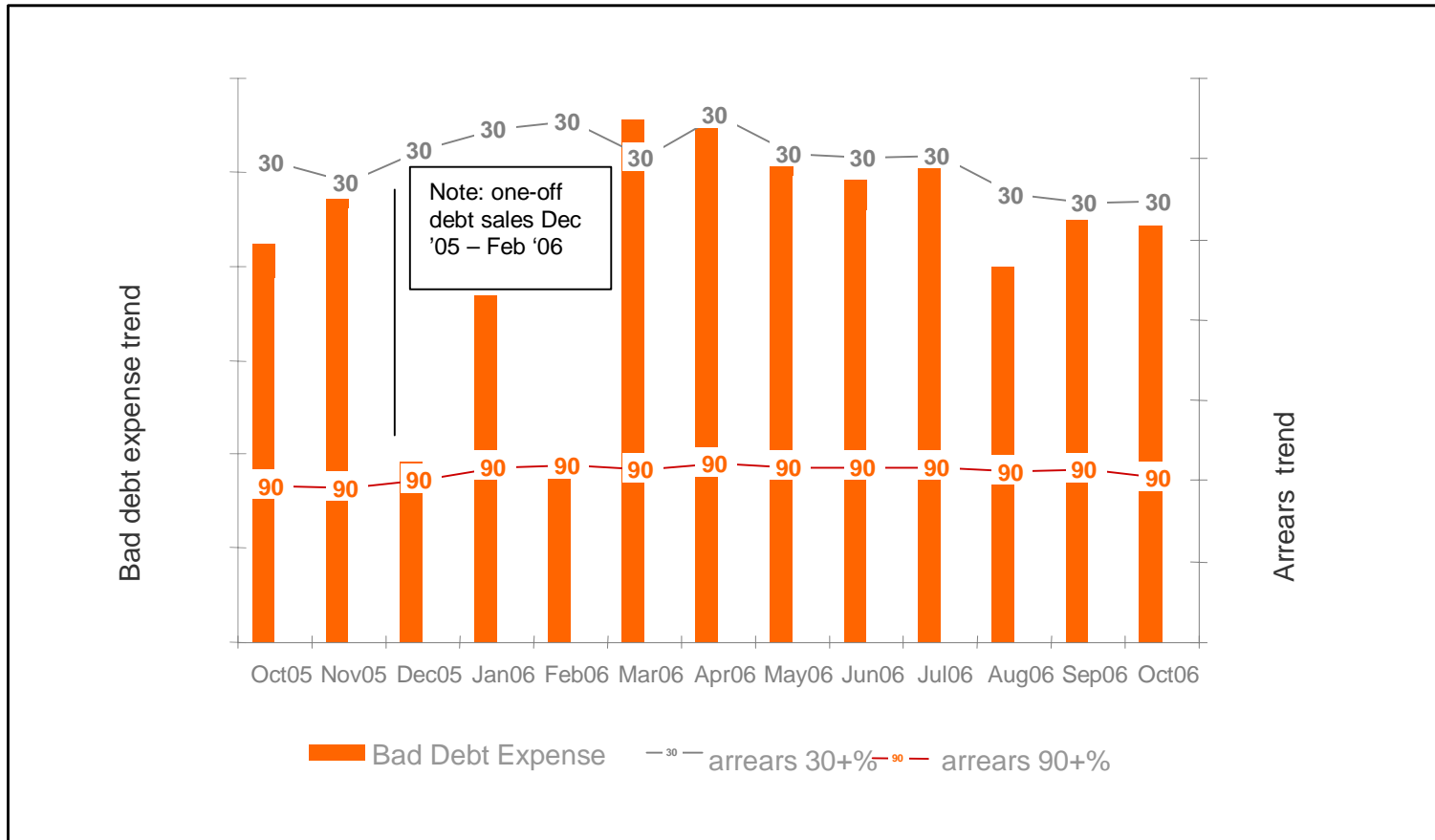
Leveraging capabilities across the Bank

Credit Portfolio: Results from Improved Capability – Personal Loans



Increased quality of new business

Credit Cards - Recent Improvements



Scorecards implemented plus new decisioning software driving arrears and loss performance

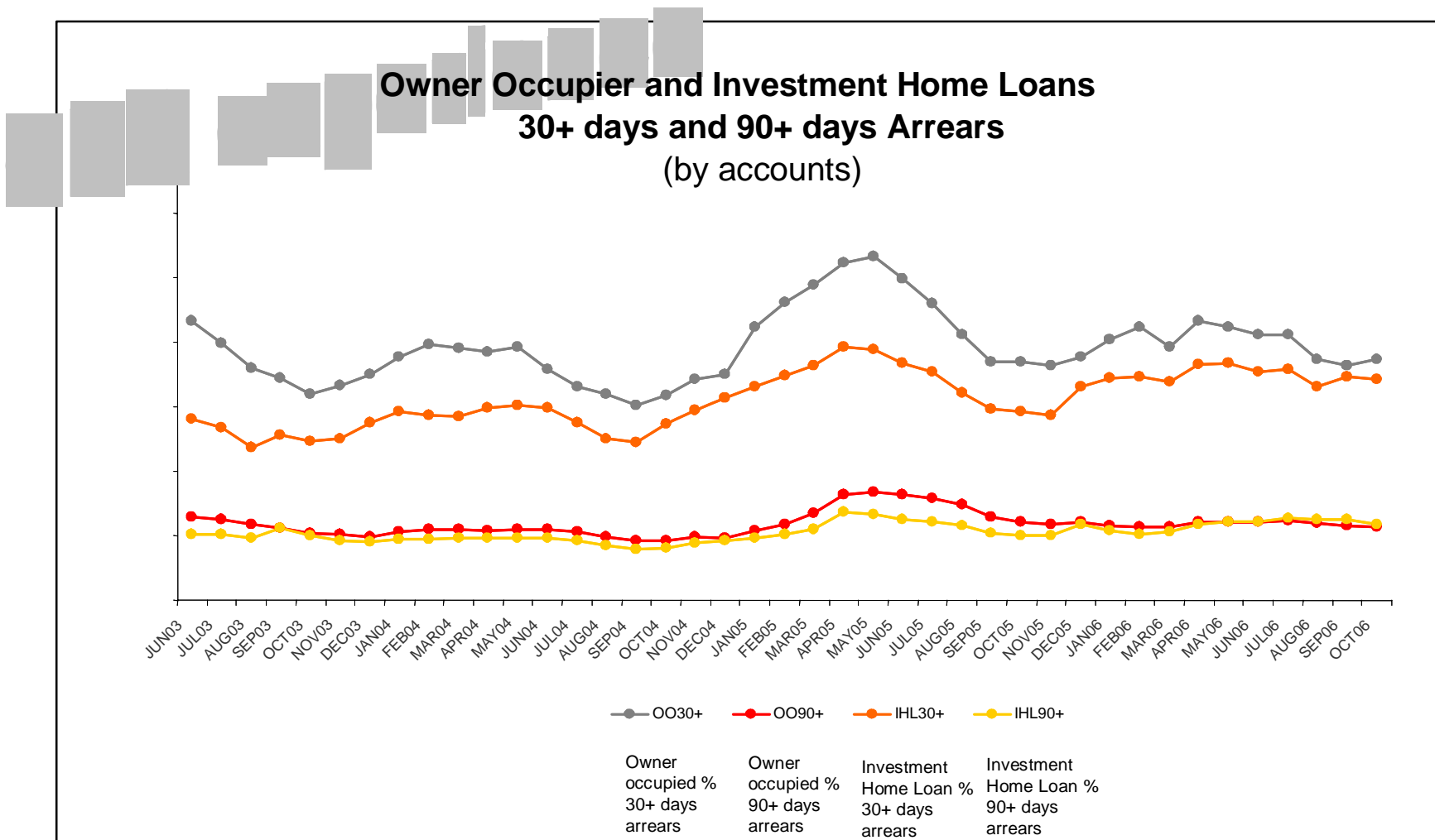
Home Loans - In Great Shape



Losses at historic lows, arrears flat

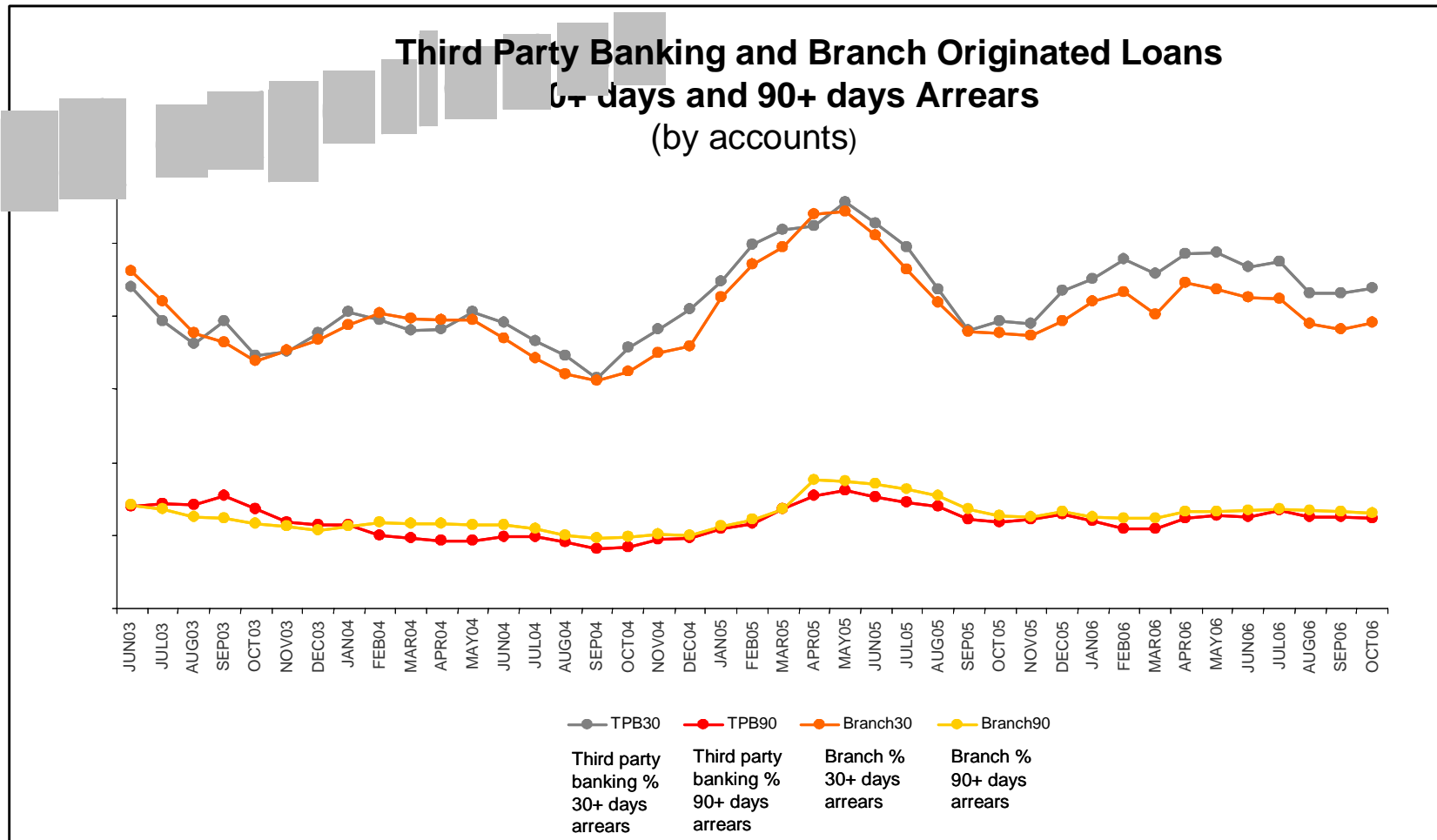
Home Loans - Dispelling Two Myths

(1) owner occupied loans perform much better than investment loans



Home Loans - Dispelling Two Myths

(2) third party introduced loans perform much worse than branch originated loans



Quality accreditation program working well

Home Loans – Low Doc

- Low doc loans less than 1% of portfolio
- Less than 4% of monthly new business written
- Arrears 2-3 times higher
- Risk of loss with insurer not with CBA
- Low doc loans capped at 80% LVR
- Customer pays for LMI 60-80% LVR
- Bank pays for insuring 0-60% LVR
- Pricing for insurance premium not for risk of loss

Notes



Home Loan Portfolio – Stress Tested

Market Value Stress

EL (\$m)	PD Stress Factor			
	1	2	4	6
0%	10.3	14.1	20.1	24.8
10%	27.3	38.4	56.7	70.6
20%	58.6	84.8	128.6	161.8
30%	103.6	153.1	236.4	299.4

Note:

PD = Probability of Default EL = expected loss (\$m)



- Under current conditions, 1 year HL expected loss at around \$10m
- \$299m loss = 3 months home loan net income
- Loss = 0.27% total value of loans, under most stressed conditions

What are the Improvements Driving Performance?

- Instant and better retail credit decisions via new decisioning software, new models and CommSee
- Completely rebuilt all retail credit decisioning models and implemented in last 2 years
- Using Basel II for business advantage
- Leveraged competitive advantage by using customer data in all scorecards
- New fraud scorecards (leading the market)



....making better credit decisions

The Benefits

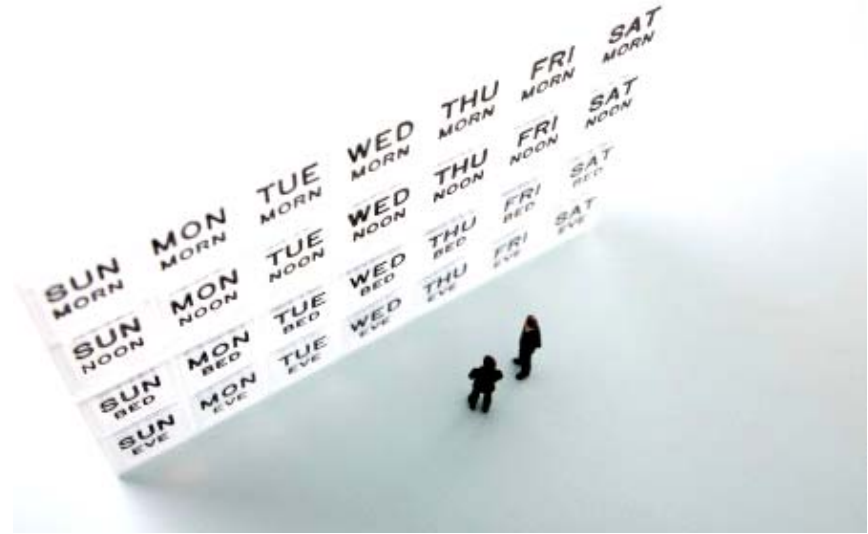
- Better credit models – mean better credit decisions
- Better credit decisions – mean reduced bad debt &/or increased business volumes
- Tools in place to optimise return for risk
- Financial benefits – currently well over \$100m over life of loans booked through new scorecards



Better customer & shareholder outcomes

Key Messages

- Created new capability for the Retail Bank
- Leveraging these capabilities across the CBA
- Improvements providing better consumer credit decisions
- Better customer & shareholder outcomes





Paul Riordan

Business Development & Risk Management

Premium Business Services

Market Risk

Today

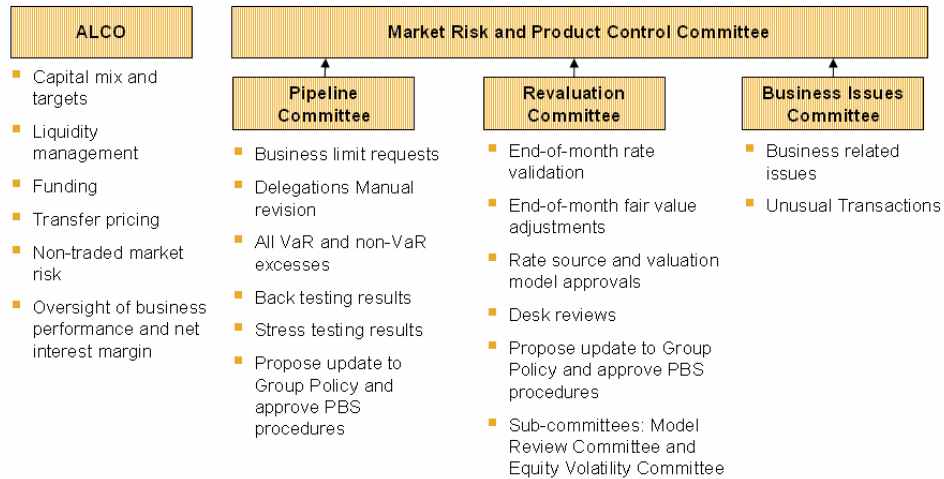
- Governance & Execution
- Poachers turned Gamekeepers
- Key Metrics



Other Key Information

Notes

Execution & Oversight



Governance Framework



Other Key Information

Notes

Key Principles

Clear Accountabilities & Authorities	<ul style="list-style-type: none">▪ Risk Policies, Limits & Trading Delegations▪ Committee structure governs changes▪ Group Risk Management oversight & governance
Segregation of Duties & Effective Limit Framework	<ul style="list-style-type: none">▪ Independent Market Risk Management (MRM)▪ MRM establishes/monitors risk limit framework▪ Independent Finance area
Transparency & Escalation	<ul style="list-style-type: none">▪ Daily risk reporting by MRM▪ Escalation as appropriate through PBS/FRM Committees, Group Executives & Risk Committee, and Finance
Control Culture & Resourcing	<ul style="list-style-type: none">▪ Front office training, accreditation & discipline▪ Specialist/experienced front office staff▪ Specialist/experienced market risk staff
Robust Risk Measurement	<ul style="list-style-type: none">▪ Specialist quantitative resources in MRM with risk measurement accountability▪ FRM oversight & model validation policy

Key Principles

- Clear Accountabilities & Authorities
- Segregation of Duties and Effective Limit Framework
- Transparency & Escalation
- Control Culture & Resourcing
- Robust Risk Measurement

Accountability, Transparency & No Surprises



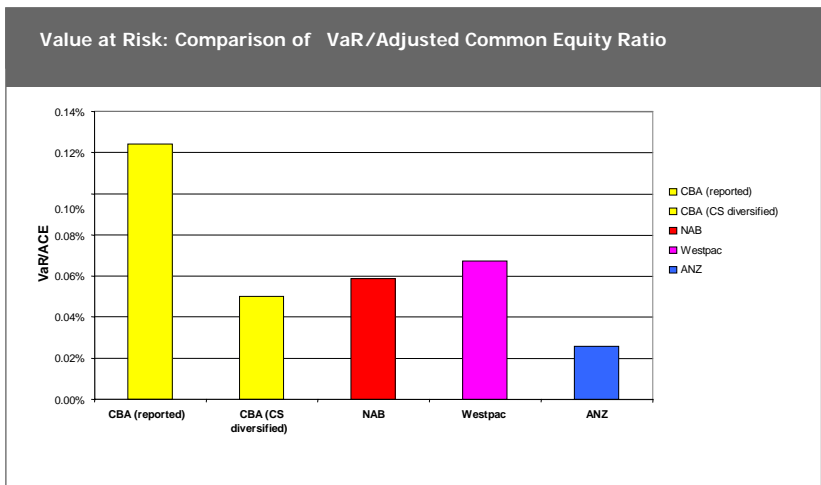
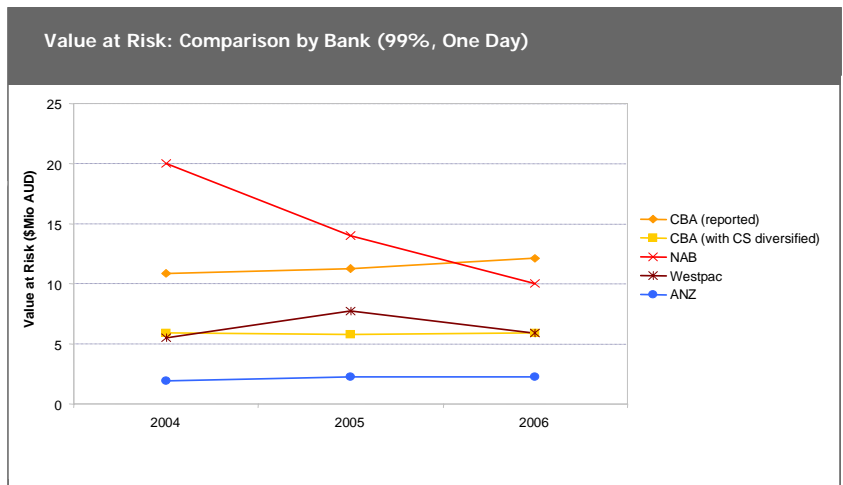
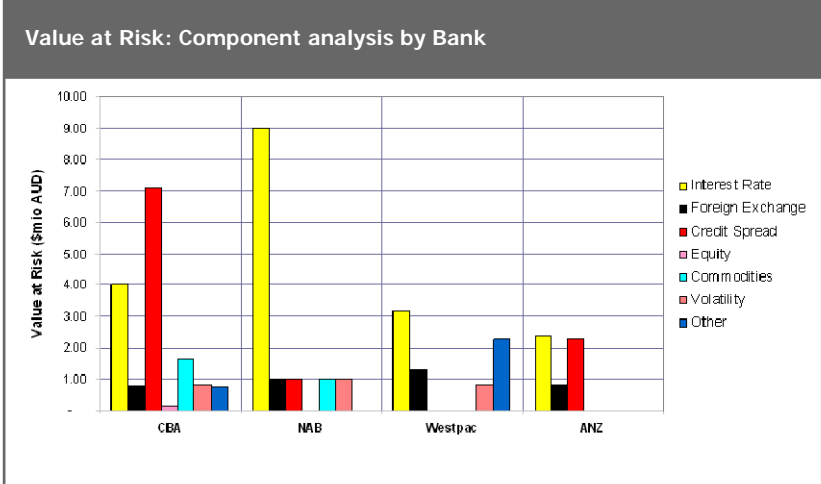
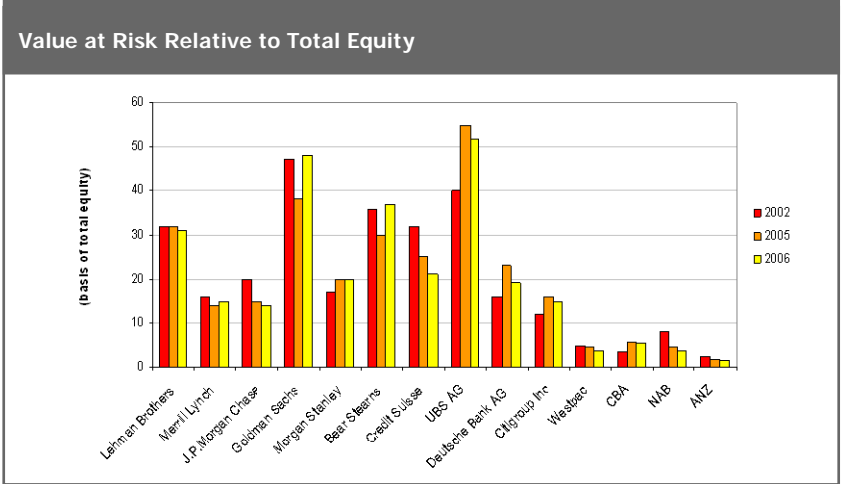
Poachers Turned Gamekeepers

- Market Risk team led by market-savvy former trading professionals
- A mix of skills and experience aligned with both current risk concentrations and growth opportunities
- Physical co-location of risk teams with the business
- Allows deep understanding of business strategies, market opportunities and culture
- Supported by a formalised committee structure including front office, risk, finance, operations and audit
- Detailed reviews of linkages between risk positions and resultant financial outcomes
- Regular stress testing and scenario analysis

Risk Optimisation, Not Risk Minimisation



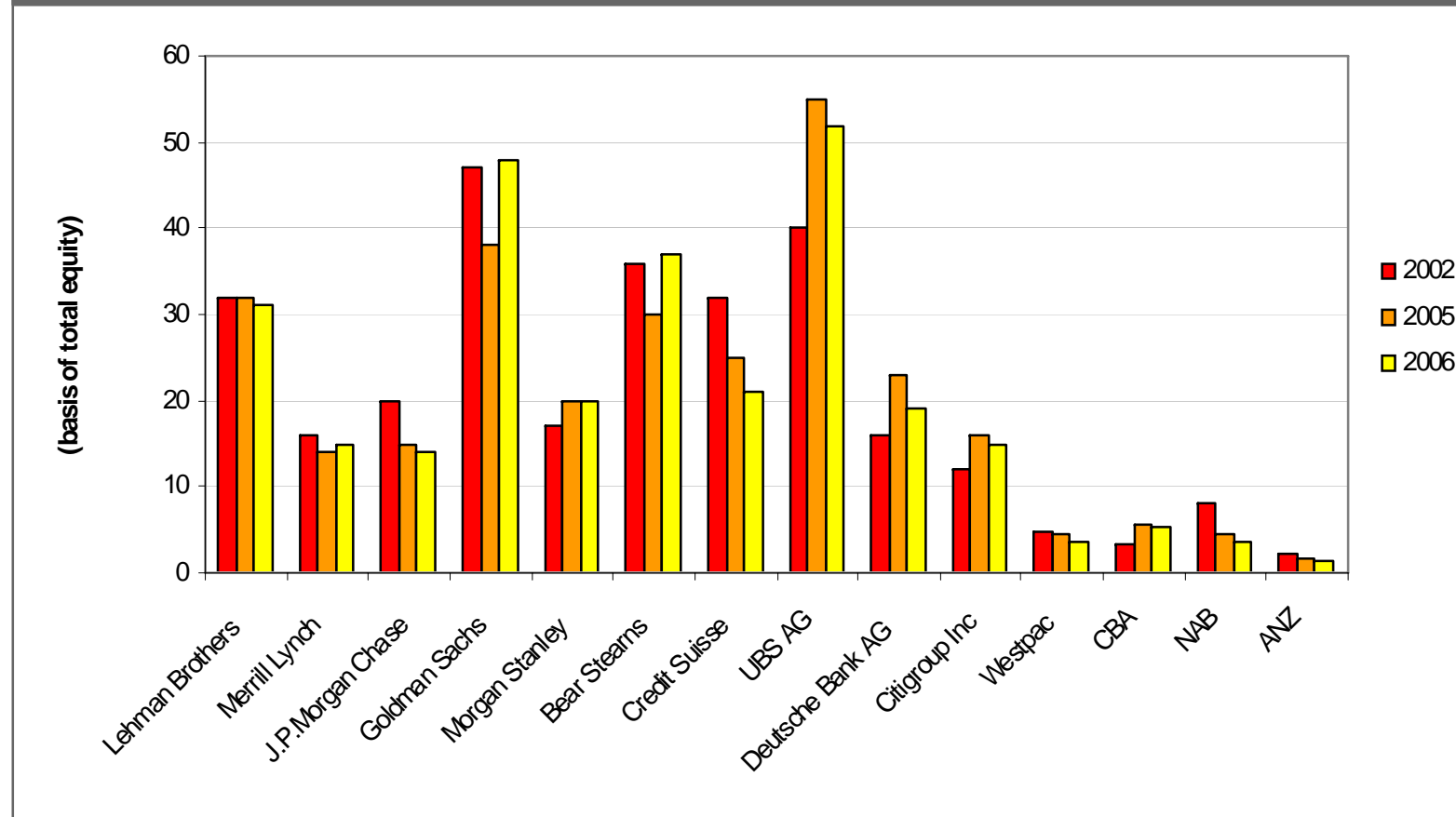
Snapshot - Key Market Risk Metrics



Sources:
 1. Derived from data in each bank's annual report.
 2. S&P report entitled 'Lifting the Lid on Traded Market Risk' published 31-Oct-2006

Key Market Risk Metrics

Value at Risk Relative to Total Equity



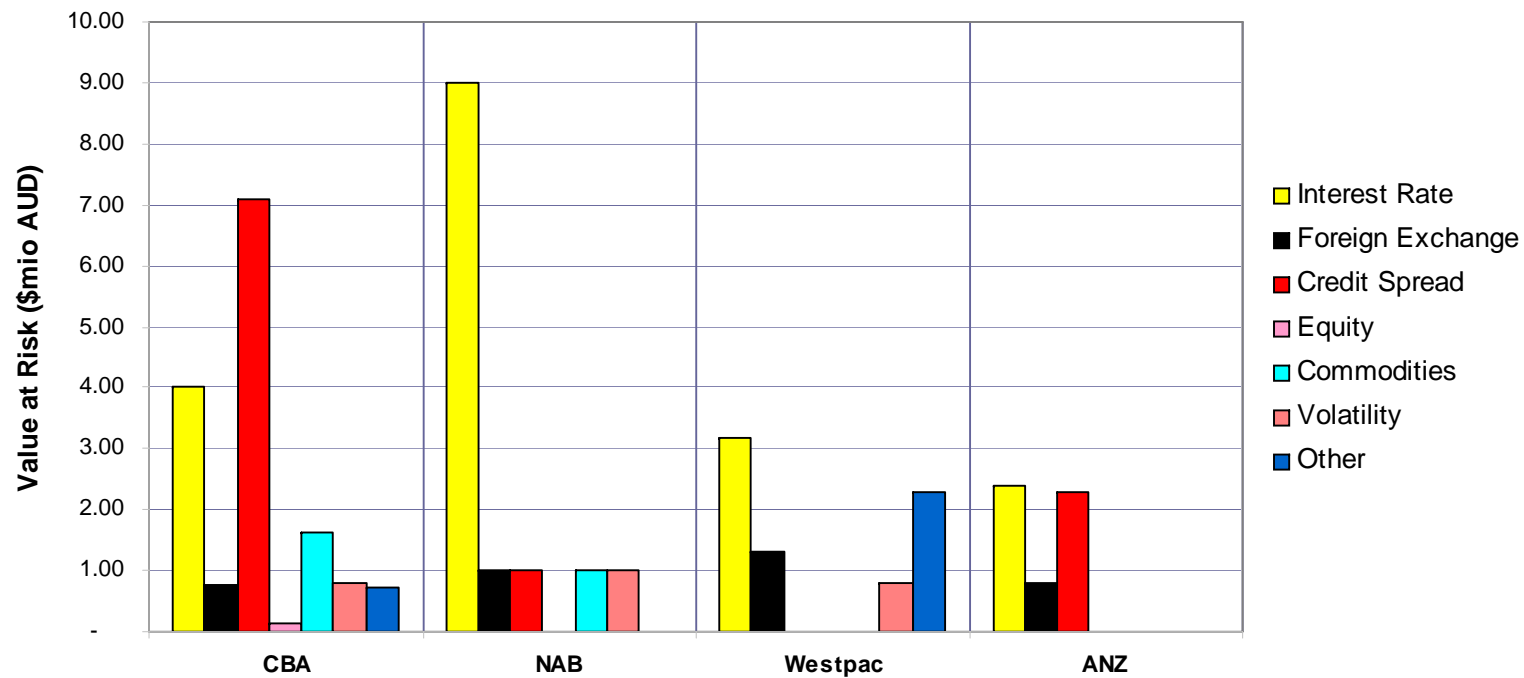
Sources:

1. S&P report entitled 'Lifting the Lid on Traded Market Risk' published 31-Oct-2006
2. Calculation for the four Australian Majors based on Total Equity (derived from data in each bank's annual report) and not 'adjusted total equity' as in the S&P report provided, as the study did not indicate what adjustments had been made



Key Market Risk Metrics

Value at Risk: Component analysis by Bank

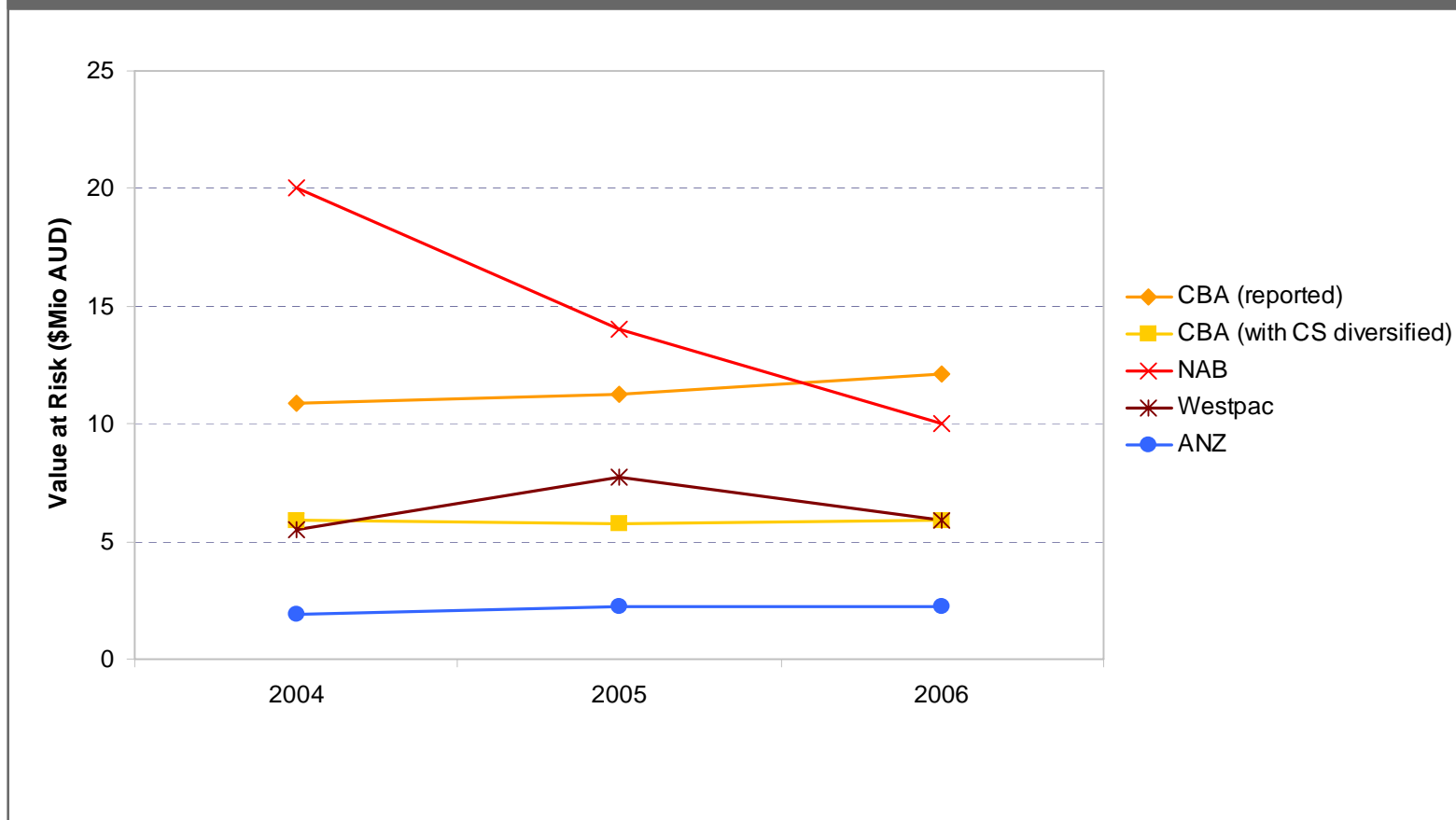


Source: Derived from data in each bank's annual report.



Key Market Risk Metrics

Value at Risk: Comparison by Bank (99%, One Day)



Source: Derived from data in each bank's annual report

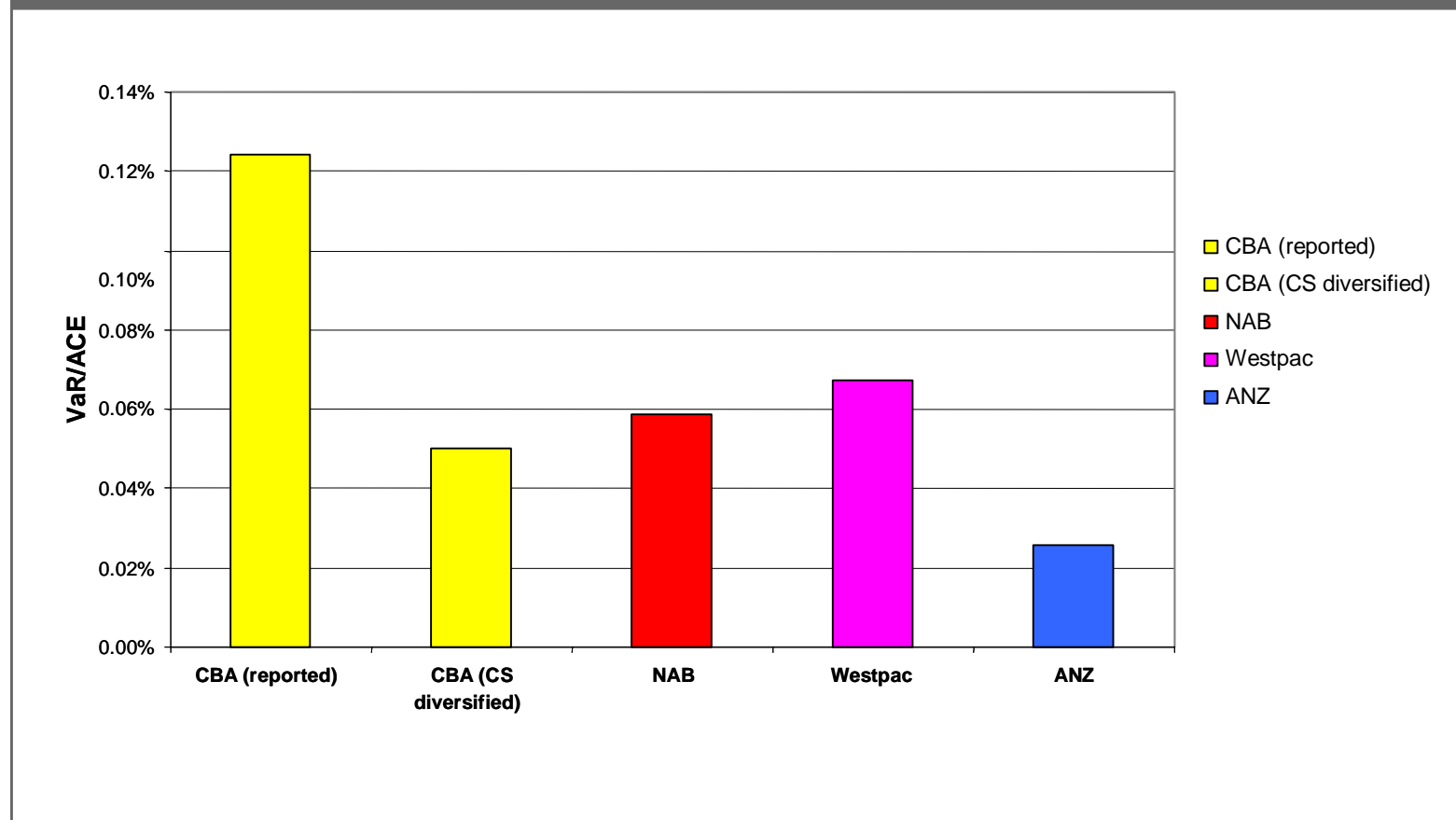
Note:

- CBA (reported) VaR is that published in the Annual Report. It comprises diversified IR, FX, Equity and Commodity VaR with a conservative Credit Spread add-on VaR.
- CBA (with CS diversified) VaR diversifies Credit Spread VaR along with IR, FX, Equity and Commodity VaR.



Key Market Risk Metrics

Value at Risk: Comparison of VaR/Adjusted Common Equity Ratio



Source: Derived from data in each bank's annual report

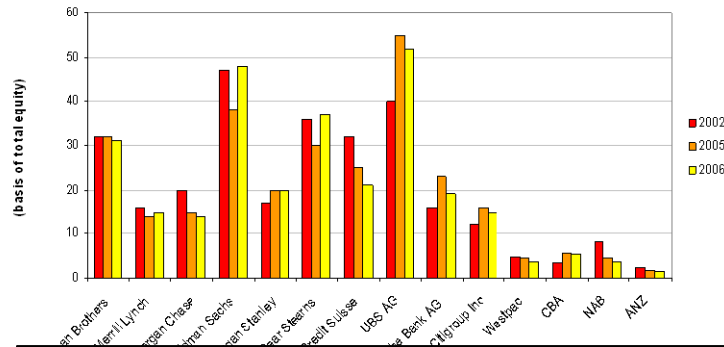
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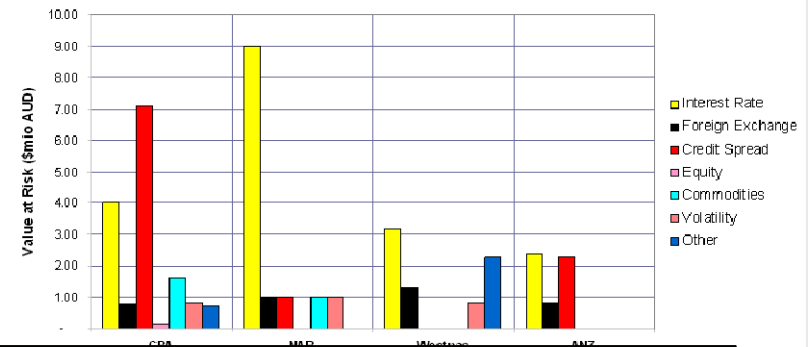


Snapshot - Key Market Risk Metrics

Value at Risk Relative to Total Equity

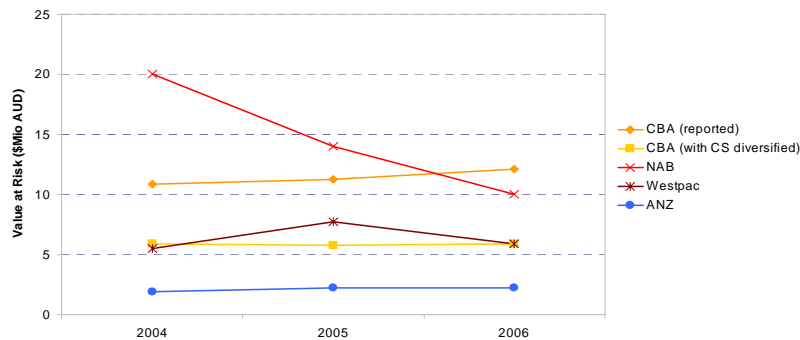


Value at Risk: Component analysis by Bank

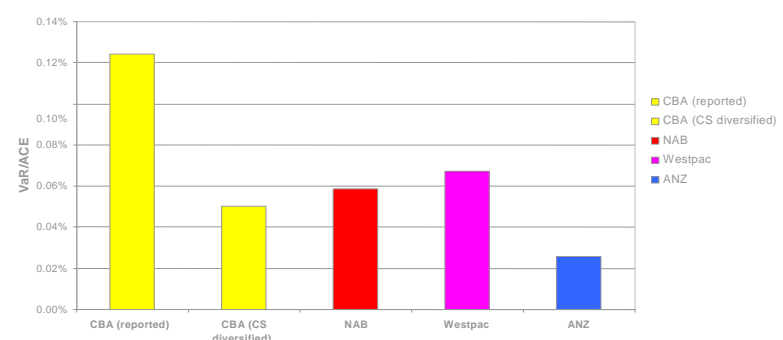


In Line With Market Peers

Value at Risk: Comparison by Bank (99%, One Day)



Value at Risk: Comparison of VaR/Adjusted Common Equity Ratio



Key Messages

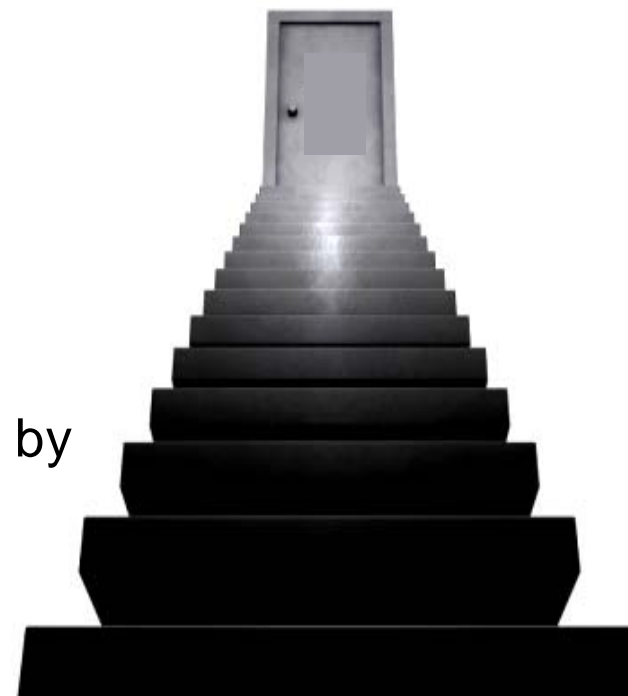
- Robust governance framework
- Experienced hands-on oversight
- Strong risk culture



- VaR in line with domestic competitors (after adjusting for credit spread) and conservative by international standards
- Reported VaR not telling the whole story
- Comprehensive non-VaR controls in place



Risk Optimisation, Not Risk Minimisation



To be Australia's finest financial services organisation through excelling in customer service



Panel Questions



Michael Blythe



Mick Leonard



Jim Evans



David Grafton



Paul Riordan