

This public disclosure is prepared for Teachers Mutual Bank Limited for the quarter ended the 31st December 2014. It complies with prudential standard APS 330 Capital Adequacy: Public Disclosure of Prudential Information and is unaudited.

## Capital management

Capital levels are managed to ensure compliance with Australian Prudential Regulation Authority (APRA) requirements. Those requirements encompass a framework of three pillars.

**Pillar 1** - Minimum capital requirements, including a specific capital charge for operational risk.

**Pillar 2** - Enhanced supervision of capital management including the application of an internal capital adequacy assessment process.

**Pillar 3** - More extensive disclosure requirements.

### Pillar 1

Capital is measured as prescribed by Australian Prudential Regulation Authority (APRA) prudential standards. These standards act to deliver capital requirements in respect of Credit risk, Market risk and Operational risk.

## Credit risk

Credit risk is measured using the Standardised Approach defined in prudential standard APS112. The capital charge attached to each asset is based on weightings prescribed by APRA as detailed in the table below:

On-statement of financial position exposures	Carrying value	Risk weighting	Risk weighted amount
Cash	1,462,720	0%	-
Deposits in highly rated ADIs	494,981,905	20%	98,996,381
Deposits in less highly rated ADIs	305,752,731	50%	152,876,365
Standard loans secured against eligible residential mortgages up to 80% LVR (up to 90% with Lenders Mortgage Insurance)	3,022,962,594	35%	1,058,036,908
Standard loans secured against eligible residential mortgages over 80% LVR	523,277,385	50%-75%	264,462,049
Other standard mortgage loans	4,665,848	100%	4,665,848
Non-standard mortgage loans	5,340,467	35%-100%	3,299,035
Other loans	277,393,660	100%	277,393,660
Other assets	41,253,426	100%	41,253,426
<b>Total</b>	<b>4,677,090,736</b>		<b>1,900,983,672</b>

Non-market related Off-statement of financial position exposures	Notional principal amount	Credit conversion factor	Credit equivalent amount	Risk weighting	Risk weighted amount
Loans approved and not advanced	99,130,840	100%	99,130,840	35%-100%	46,474,019
Redraws available	402,752,136	50%	201,376,068	35%-100%	75,961,104
Guarantees	100	100%	100	100%	100
Unused revolving credit limits	273,944,601	0%	-		-
Possible contribution to CUFSS	149,731,607	0%	-		-
<b>Total</b>	<b>925,559,284</b>		<b>300,507,008</b>		<b>122,435,223</b>

Market related Off-statement of financial position exposures	Notional principal amount	Credit conversion factor	Potential future exposure	Current exposure	Credit equivalent amount	Risk weighted amount
Residual maturity 1 year or less	25,100,000	0%	-	279	279	56
Residual maturity > 1 year to 5 years	463,000,000	0.5%	2,315,000	-	2,315,000	463,000
<b>Total</b>	<b>488,100,000</b>		<b>2,315,000</b>	<b>279</b>	<b>2,315,279</b>	<b>463,056</b>
<b>Total weighted credit risk exposures</b>						<b>2,023,881,951</b>

## Market risk

The bank is not required to allocate capital against market risk as no trading activity is undertaken and the Standardised Approach does not result in any allocation against interest rate risk in the banking book.

## Operational risk

Operational risk is measured using the Standardised Approach defined in prudential standard APS114. The capital charge is based upon portfolio balances and revenue streams with scaling and risk factors applied to reflect APRA's assessment of the particular risk profiles.

### Operational risk capital requirement for retail banking

	30-Jun-12	31-Dec-12	30-Jun-13	31-Dec-13	30-Jun-14	31-Dec-14
Total gross outstanding loans and advances for retail banking	3,070,330,500	3,212,036,658	3,335,287,137	3,403,852,715	3,686,723,392	3,836,847,647
- multiplied by 3.5% scaling factor	107,461,568	112,421,283	116,735,050	119,134,845	129,035,319	134,289,668
- multiplied by 12% risk factor	12,895,388	13,490,554	14,008,206	14,296,181	15,484,238	16,114,760
<b>Average of the 6 half year results = Total operational risk capital requirement for retail banking</b>						<b>14,381,555</b>

## Operational risk capital requirement for commercial banking

	30-Jun-12	31-Dec-12	30-Jun-13	31-Dec-13	30-Jun-14	31-Dec-14
Total gross outstanding loans and advances for commercial banking	645,359,216	687,158,408	684,350,086	759,279,481	627,518,223	768,823,669
- multiplied by 3.5% scaling factor	22,587,573	24,050,544	23,952,253	26,574,782	21,963,138	26,908,828
- multiplied by 15% risk factor	3,388,136	3,607,582	3,592,838	3,986,217	3,294,471	4,036,324
Average of the 6 half year results = Total operational risk capital requirement for commercial banking						3,650,928

## Operational risk capital requirement for all other activity

	30-Jun-12	31-Dec-12	30-Jun-13	31-Dec-13	30-Jun-14	31-Dec-14
Adjusted gross income	3,906,064	2,075,673	3,722,777	2,484,320	3,524,209	2,568,555
- multiplied by 18% risk factor	703,091	373,621	670,100	447,178	634,358	462,340
Average of the 3 annual results = Total operational risk capital requirement for all other activity						1,096,896

Total operational risk capital requirement	19,129,379
RWA equivalent amount for operational risk capital requirement = Operational risk capital * 12.50	239,117,230
Total credit and operational risk weighted	2,262,999,181

## Capital resources

### Main features of capital

**Common Equity Tier 1 Capital** - The majority of Tier 1 capital consists of retained profits.

**Tier 2 Capital** - Consists of capital instruments that combine the features of debt and equity in that they are structured as debt instruments, but exhibit some of the loss absorption and funding flexibility features of equity. There are a number of criteria that capital instruments must meet for inclusion in Tier 2 capital resources as set down by APRA. Tier 2 capital generally comprises a reserve for credit losses.

A minimum capital ratio of 8% is required to be maintained at all times. Our policy requires reporting to the board if the capital ratio falls below 14%.

The capital ratio can be affected by growth in assets relative to growth in reserves and by changes in the mix of assets. The bank manages capital through reviewing the ratio monthly and monitoring major movements in asset levels. Further, a 3 year capital projection is maintained to assess how strategic decisions or trends may impact on the level of capital. A stress test based on various asset growth and profitability assumptions is conducted annually.

## Pillar 2 risk capital

Pillar 2 of the Prudential Framework relates to any risk factor to which an ADI might be exposed that is not included in Pillar 1.

These risks fall into 3 categories.

- Pillar 1 risks not fully captured by the Pillar 1 process, for example credit concentration risk.
- Inherent risks not covered by Pillar 1, including:
  - interest rate risk in the banking book
  - liquidity risk
  - strategic risk
  - reputation risk
- Risks arising from external factors such as business cycles effects and the macroeconomic environment.

The bank documents, analyses and sets its own internal capital requirements to meet Pillar 2 risks.

The methodologies used to assess the required capital are a combination of quantitative and qualitative assessment and by their nature are based on a degree of collective subjective judgment of senior management and the board.

### Internal capital adequacy management

The bank manages its internal capital levels for both current and future activities through a combination of committees. The outputs of the individual committees are reviewed by the board in its capacity as the primary governing body. The capital required for any change in the bank's forecasts for asset growth or unforeseen circumstances are assessed by the board. The finance department then updates the forecast capital resources models produced and the impact upon the overall capital position of the bank is reassessed.

## Contingency buffer

Based on historical fluctuations in capital the bank incorporates a contingency buffer of 2% when targeting minimum levels of capital and when preparing its Capital Management Plan to cover volatility in the risks identified above.

	RWA	Minimum capital required	% Equivalent of RWA
Credit risk	2,023,881,951	161,910,556	8.00%
Operational risk	239,117,230	19,129,378	8.00%
Total	2,262,999,181	181,039,934	8.00%
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Pillar 2 uplift capital		90,519,967	4.00%
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ICAAP capital required		271,559,901	12.00%
Buffer for business cycle volatility		45,259,984	2.00%
Capital available for future growth and product and service development		42,619,670	1.88%
Risk-based capital ratio		359,439,555	15.88%
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Common Equity Tier 1 capital ratio		345,463,818	15.27%
Tier 1 capital ratio		345,463,818	15.27%
Tier 2 capital ratio		13,975,737	0.61%

## Credit risk

The credit risk of a financial institution is the risk that customers (members), financial institutions and other counterparties will be unable to meet their obligations to the institution which may result in financial losses. Credit risk arises principally from the bank's loan book and investment assets.

## ADI investments

The risk of losses on ADI investments is mitigated through the application of investment limits per counterparty based upon independent ratings of counterparties and by limiting exposure to groups of counterparties within a rating band.

The exposure values associated with each credit quality step are as follows:

Investments with:	No. of institutions	Carrying value	Past due value	Provision	Average gross exposure in the quarter
ADIs-rated A-1+ to A-1 (short-term)	7	363,137,757	-	-	336,501,815
ADIs-rated A-2 or P-2 (short-term)	8	288,096,879	-	-	272,479,562
ADIs-rated AA+ to AA- (long-term)	4	112,000,000	-	-	112,000,000
ADIs-rated A+ to A- (long-term)	4	30,000,000	-	-	34,712,159
ADIs-rated BBB+ (long-term)	1	7,500,000	-	-	3,750,000
Total		800,734,636	-	-	759,443,536

## Loans

Carrying value is the value on the statement of financial position. Maximum exposure is the value on the statement of financial position plus the undrawn facilities (loans approved but not funded, redraw facilities, undrawn overdrafts and credit cards).

	Carrying value on-statement of financial position	Commitments	Other non-market off-statement of financial position exposures	Maximum exposure	Average gross exposure in the quarter
	\$'000	\$'000	\$'000	\$'000	\$'000
Housing	3,244,756	450,904	-	3,695,660	3,652,429
Personal	590,629	324,874	-	915,503	914,627
Total-natural persons	3,835,385	775,778	-	4,611,163	4,567,056
Corporate borrowers	1	49	-	50	50
Total	3,835,386	775,827	-	4,611,213	4,567,106

## The commitments set out above comprise

<b>Outstanding loan commitments</b>	<b>\$'000</b>
The loans approved but not funded	99,131
<b>Loan redraw facilities</b>	
The loan redraw facilities available	402,752
<b>Undrawn loan facilities</b>	
Loan facilities available to members for overdrafts and credit cards are as follows:	
Total value of facilities approved	367,633
Less: amount advanced	(93,689)
Net undrawn value	273,944
These commitments are contingent on members maintaining credit standards and ongoing repayment terms on amounts drawn.	
Total loan commitments	775,827

## Impairment

Impairment of a loan is recognised when there is reasonable doubt that not all the principal and interest can be collected in accordance with the terms of the loan agreement. Impairment is assessed by specific identification in relation to individual loans and by estimation of expected losses in relation to loan portfolios where specific identification is impracticable.

Bad debts were written off when identified and are recognised as expenses in the statement of comprehensive income.

All loans and advances are reviewed and graded according to the anticipated level of credit risk. The classification adopted is described below:

Non-accrual loans are loans and advances, including savings accounts drawn past their approved credit limit, where the recovery of all interest and principal is considered to be reasonably doubtful. Interest charged and not received on this class of loan is not recognised as revenue. APRA has made it mandatory that interest is not recognised as revenue after irregularity exceeds 90 days for a loan facility or 15 days for an over limit overdraft and credit card facility or 15 days for overdrawn savings account.

Restructured loans arise when the borrower is granted a concession due to continuing difficulties in meeting the original terms and the revised terms are not comparable to new facilities of comparable risk. Loans, where interest has been stopped or is less than the bank's average cost of funds, are included in non-accrual loans.

The level of impaired loans by class of loan is set out below:

- Carrying value is the balance gross of provision (net of deferred fees).
- Past due loans as per APS 220 Credit Quality is the 'on-statement of financial position' loan balances which are behind in repayments by 90 days or more, well-secured and not impaired.
- Impaired loans value is the 'on-statement of financial position' loan balance and includes non-accrual loans and restructured loans. Provision for impairment is the amount of the impairment provision allocated to the class of impaired loans.
- The losses in the quarterly period equate to the additional provisions set aside for impaired loans and bad debts written off in excess of previous provision allowances.

	Carrying value on-statement of financial position	Value of loans that are past due	Value of loans that are impaired	Provision for impairment	Provision for impairment quarterly movement	Bad debts in the quarter
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Housing	3,244,756	1,353	10,564	34	-	-
Personal	590,629	44	5,218	1,712	31	664
Total-natural persons	3,835,385	1,397	15,782	1,746	31	664
Corporate borrowers	1	-	-	-	-	-
Total	3,835,386	1,397	15,782	1,746	31	664

The impaired loans are generally not secured against residential property. Some impaired loans are secured by mortgage over motor vehicles or other assets of varying value. It is not practicable to determine the fair value of all collateral as at the balance date due to the variety of assets and condition.

### Reserve for credit losses

The General Reserve for Credit Losses is a reserve in respect of credit losses prudently estimated but are not certain to arise over the full life of all the individual facilities comprising the business of the bank.

The methodology to calculate the reserve is a Probability of Default and Loss Given Default approach.

The Board utilises the model described above when exercising experienced credit judgment as well as considering any other internal and external factors to determine the appropriate reserve balance required.

The amount of the reserve is currently \$13,975,737.

### Securitisation exposures

**On-statement of financial position** - The bank has established an internal securitisation of residential mortgages, linked to a repurchase agreement facility with the Reserve Bank of Australia, as a liquidity contingency. The bank has not derecognised these loans from the statement of financial position and does not qualify for capital relief under APS 120 Securitisation. The amount of the facility is currently \$657,995,400 consisting of mortgages secured loans. During the quarter \$279M loans were securitised.