Definitions

ADI [An Australian Deposit-taking Institution under the Banking Act.]

APRA [The Australian Prudential Regulation Authority.]

ASX [The Australian Securities Exchange.]

Benchmark [The market rate used to calculate the distribution rate for a Bank Hybrid. For example, BBSW (typically the 90 day bank bill swap rate).]

BBSW [BBSW is a key benchmark interest rate for the Australian money market that moves over time in line with market conditions and monetary policy. It is typically the 90 day bank bill swap rate.]

Capital trigger event [A capital trigger event occurs when the issuing bank determines (or is notified by APRA) that the bank's common equity tier 1 ratio is equal to or less than 5.125%.] [See capital trigger event.]

Conversion conditions [Conversion of some Bank Hybrids may be subject to conversion conditions set out in the prospectus for the particular Bank Hybrid. See Case Study 3, including a worked solution, for further detail.]

Cumulative [If interest is not paid in full, unpaid interest will accumulate and compound for payment at a later date if certain conditions are met.]

Distribution payment conditions [There are certain conditions that must be satisfied before distributions can be paid, including (i) that the payments are at the discretion of the bank, (ii) that the payments will not result in a breach of the bank's regulatory capital requirements or in the bank becoming insolvent, and (iii) that APRA does not object to the payment.]

Face value [The face value is typically the issue price, which will be reduced by any partial conversion or write-off.]

Financial Claims Scheme [A government guarantee for deposits up to an amount per account holder per ADI of $250,000.]

Franking credits [Franking credits represent each holder's share of tax paid by the issuing bank on the profits from which the distributions are paid.]

Issue date VWAP [Generally, the volume weighted average sale price (or VWAP) of the bank's ordinary shares sold on the ASX over the 20 business days prior to the issue date of the Bank Hybrid.]

Margin [The margin is fixed at the time of issue and typically reflects the risk premium of a Bank Hybrid above a floating market rate (e.g., BBSW) at the time of issue.]

Maturity date [The date on which a Tier 2 Bank Hybrid is scheduled to mature.]

Maximum conversion number [The maximum conversion number is a limit or cap on the number of ordinary shares of the bank that may be issued on conversion. For a scheduled or mandatory conversion, the maximum conversion number reflects 50% of the bank's ordinary share price at the time of issue of the Bank Hybrid. For conversion following a non-viability trigger event or a capital trigger event, the maximum conversion number reflects 20% of the bank's ordinary share price at the time of issue of the Bank Hybrid.]

Non-cumulative [Unpaid distributions will not accumulate or be made up by the issuing bank.]

Non-viability trigger event [A non-viability trigger event will occur when APRA notifies a bank in writing that it believes (i) conversion to ordinary shares of some or all of its Bank Hybrids or (ii) a public sector injection of capital or equivalent support, is necessary to prevent the bank becoming non-viable.] [See non-viability trigger event.]

Perpetual [If a security is perpetual, it does not have a fixed maturity date and could exist indefinitely.]

Scheduled or mandatory conversion date [A date on which conversion of a Tier 1 Bank Hybrid is expected to occur (subject to the conversion conditions being met) and set out in the prospectus for the particular Bank Hybrid.] [See scheduled conversion.]

VWAP [Generally, the average of the daily volume weighted average sale price of the bank's ordinary shares sold on ASX over a relevant period.]

Written-off/write-off/write them off [If Bank Hybrids are written-off, investors will lose all of the value of their investment and they will not receive any compensation or unpaid distributions or interest.]

1. Welcome to Westpac's Guide to Bank Hybrids

This Guide has been developed by Westpac to help investors understand some of the typical features and risks associated with an investment in Australian hybrid capital securities (Hybrids). In particular, the Guide focuses on Hybrids typically issued by Australian banks to retail investors (Bank Hybrids). (See [Bank Hybrids] for further details on the features and risks of Bank Hybrids).

At Westpac, we believe it is important for investors to understand the features and risks of an investment in Hybrids, including Bank Hybrids. Australian corporates (including banks) issue Hybrids to meet their funding and capital requirements. As Hybrids are complex instruments, Australian regulators recommend that potential investors fully understand the risks before investing, to determine whether a Hybrid investment suits an investor's risk profile.

This Guide covers:

- [What is a Hybrid?]
- [Why do companies issue Hybrids?]
- [Comparing Australian Bank Hybrids to other Australian bank investments]
- [Assessing the strength of a bank]
- [Types of Bank Hybrids]
- [Case Studies]
- [Checklist]
- [Frequently Asked Questions]

Tip: Click on underlined words throughout this Guide for more information, including definitions and links to sections with further detail.

This Guide only looks at some of the typical features and risks associated with an investment in Hybrids. The Guide does not provide investment advice and cannot address your individual circumstances, objectives or needs. Prior to investing in a Hybrid, you should ensure that you understand the features and risks of the particular Hybrid and you should read the prospectus carefully, paying attention to the investment risks. In the event you need further information, you should seek professional guidance from your stockbroker, solicitor, accountant or other independent and qualified professional adviser.

2. What is a Hybrid?

The term Hybrid is generally used to describe securities that have features of both debt instruments (fixed income) and equity instruments (shares).

Although the terms may vary considerably from one Hybrid to another, Hybrids are generally issued by well-known companies and banks, like Westpac. In addition, Hybrids tend to have complex terms and, due to the higher risks associated with an investment in Hybrids, generally pay higher rates of interest or distributions than bank deposits (savings accounts and term deposits) and vanilla corporate bonds. (See [Bank Hybrids] for further details on the features and risks of Bank Hybrids).

Bank Hybrids are not guaranteed by the issuing bank or the government whereas bank deposits may be protected by a government guarantee under the Australian Government's [Financial Claims Scheme]. An investment in Bank Hybrids is generally considered to have less risk than an investment in a bank's ordinary shares (although unlike ordinary shares, they can be [written-off]) but more risk than a bank deposit or other forms of senior unsecured bank lending (e.g., bank bonds).

Another feature that adds to the complexity of Bank Hybrids is that they may be converted into ordinary shares or [written-off] in certain circumstances (see [Conversion events]). This can lead to a change in the ranking of a holder's investment:

- If Bank Hybrids are converted into ordinary shares, on any subsequent winding-up Bank Hybrid holders will rank equally with ordinary shareholders. The value of ordinary shares an investor receives may be significantly less than the face value of their Bank Hybrid.

- If Bank Hybrids are written-off, Bank Hybrid holders will lose all of the value of their investment and will not receive any compensation or unpaid distributions (including in a winding-up).

- If Bank Hybrids are not converted or written-off prior to a winding-up, Bank Hybrid holders will typically rank ahead of ordinary shareholders but behind bank deposit holders.

(a) Why do companies issue Hybrids?

Companies issue Hybrids to diversify their sources of funding and capital. In addition, banks need to ensure that they are well capitalised to support their lending activities and meet regulatory capital requirements set by [APRA], the prudential regulator of the Australian financial services industry.

See [Bank Hybrids] for a brief overview of the typical features and risks associated with an investment in Bank Hybrids. For a complete description of the features and risks associated with an investment in a particular Hybrid, you should read the prospectus and review other information (including financial information) relating to the issuer. In the event you need further information, you should seek professional guidance from your stockbroker, solicitor, accountant or other independent and qualified professional adviser.

3. Investing in Australian banks

There are a number of ways to invest in an Australian bank. These include:

- Savings accounts
- Term deposits
- Bank Hybrids
- Ordinary shares
- Additional Tier 1 capital securities (typically called capital notes or convertible preference shares) and
- Tier 2 capital securities (typically called subordinated notes)

Comparing Australian Bank Hybrids to other Australian bank investments

Bank Hybrids differ from other bank investments in terms of their features and risks.

For example, in some circumstances an investment in a Bank Hybrid may be converted into ordinary shares or [written-off] (see [Conversion events] for further details). In addition, holders of bank deposits (savings accounts or term deposits) will rank ahead of holders of Bank Hybrids in a winding-up and may also be protected by a government guarantee under the Australian Government's [Financial Claims Scheme].

To compensate for the higher risk associated with an investment in Bank Hybrids, interest / distribution rates paid on Bank Hybrids are typically higher than interest paid on bank deposits.

The table below outlines some of the key features of different investment options in Australian banks (such as Westpac).

(a) Comparing Australian Bank Hybrids to other Australian bank investments

	Investment type	**Legal Form**	**Typical term**	**Return**							**Investor's ability to realise investment before maturity**		**Government Guarantee and Statutory Protection**	**Events outside investor's control**		
Lower				***Form of return***	***Typical rate of return***	***Is there a potential for returns to include Franking Credits?***	***Typical payment frequency***	***Are payments at the bank's discretion?***	***Will missed payments accumulate?***	***Is there potential for capital growth?***	***Can an investor withdraw or redeem their investment?***	***Can an investor sell?***		***Bank's right of early redemption***	***Conversion into ordinary shares (scheduled or mandatory conversion)***	***Conversion into ordinary shares (non-viability / capital trigger)***
	Savings Account	Deposit	At call	Interest	Variable	No	Monthly	No	Yes	No	Generally, yes. Subject to conditions.	No	Yes. Protection under the Financial Claims Scheme is limited to deposits up to an amount per account holder per [ADI] of $250,000.	No	No	No
Relative Risk	Term deposit	Deposit	One month to five years	Interest	Fixed	No	At specific intervals or at the end of the term	No	Yes	No	Generally, yes. Subject to conditions.	No	Yes. Protection under the Financial Claims Scheme is limited to deposits up to an amount per account holder per [ADI] of $250,000.	No	No	No
	[Tier 2 Bank Hybrid]	Unsecured subordinated debt obligation	Fixed term not less than 5 years	Interest	Floating	No	Quarterly	No	Yes – [Cumulative]	Generally, no. Investors do not ordinarily acquire Bank Hybrids in order to	No	Yes – if quoted on the [ASX]	No	Yes – subject to the terms of the Bank Hybrid and [APRA] approval (which APRA may	No	Yes - if the bank becomes non-viable ([a non-viability trigger event])

										obtain capital growth. However, if sold on the ASX the price may be higher or lower than the purchase price or face value.				withhold)		
Higher	[Tier 1 Bank Hybrid]	Unsecured subordinated debt obligation or preference share	[Perpetual]	Interest or distribution	Floating	Yes	Quarterly or semi-annually	Yes	No – [Non-cumulative]	Generally, no. Investors do not ordinarily acquire Bank Hybrids in order to obtain capital growth. However, if sold on the ASX the price may be higher or lower than the purchase price or face value.	No	Yes – if quoted on the [ASX]	No	Yes – subject to the terms of the Bank Hybrid and [APRA] approval (which APRA may withhold)	Yes - subject to the satisfaction of the [conversion conditions]	Yes - if the bank becomes non-viable ([a non-viability trigger event]) or capital falls below certain levels ([a capital trigger event])
	Ordinary Share	Ordinary share	[Perpetual]	Dividend	Variable (as determined by the issuer)	Yes	Semi-annually	Yes	N/A	Yes - but if sold on the [ASX] the price may be higher or lower than the purchase price or issue price	No	Yes – if quoted on the [ASX]	No	No	N/A	N/A

(b) Assessing the strength of a bank

The risk of an investment in Bank Hybrids depends on, amongst other things, the financial strength of the issuing bank and how strong the issuing bank is relative to its peers. The stronger the bank, the less risk there is of losing part or all of your investment.

The table below lists a number of key measures that may be used to assess the strength of a bank. (Please note that this table is not an exhaustive list.)

	Capital levels	**Profitability and earnings**	**Quality of loan portfolio and risk profile**	**Funding and liquidity**	**External influences**
[What to look for]	• how much capital is held • whether capital levels meet or exceed minimum regulatory capital requirements	• consistency of earnings and returns • stronger return on equity may indicate a more profitable bank	• quality of loan portfolio • lower risk activities	• ability to manage liquidity risks • access to a broad range of funding markets and debt investors • liquidity coverage	• political and financial stability of the country the bank operates in • supervision and regulation • economic activity

	Capital levels	Profitability and earnings	Quality of loan portfolio and risk profile	Funding and liquidity	External influences
				ratio	

	Capital levels	Profitability and earnings	Quality of loan portfolio and risk profile	Funding and liquidity	External influences
[Why it's important]	• capital underpins the strength of a bank • strong capital levels provide a buffer to absorb losses that may be incurred on a bank's assets or if the bank experiences financial difficulty • in the event a bank becomes	• a profitable bank is better placed to continue to meet its obligations , including paying interest, distribution s and dividends • strong profitability allows a bank to generate capital and improve its common	• the quality of a bank's assets (for example, home loans) is important to its financial strength • if a bank lends to higher risk activities / higher risk individuals / higher risk companies, it may incur higher bad debts, which in turn may impact profitability	• access to funding is important so that banks may continue lending activities and may repay liabilities (including deposits) • strong liquidity management and liquidity levels may indicate a lower likelihood of a bank failing or becoming non-viable	• external influences may impact the operating environment and economic conditions including interest rates, employment levels, business activity and consumer sentiment • a strong regulatory environment may contribute to a bank's ability to

	Capital levels	Profitability and earnings	Quality of loan portfolio and risk profile	Funding and liquidity	External influences
	non-viable, Bank Hybrids may be converted into ordinary shares or written-off • higher capital may indicate a lower likelihood that the bank will fail or become non-viable and may reduce the likelihood of Bank Hybrids being converted into ordinary	equity Tier 1 capital ratio	and capital • significantly higher risk activities, or operating in higher risk markets, may pose additional threats to long term profitability and capital position		remain viable and meet its commitments, including paying interest or distributions and repaying principal on Bank Hybrids • a strong economy is generally good for banks

	Capital levels	Profitability and earnings	Quality of loan portfolio and risk profile	Funding and liquidity	External influences
	shares or written-off				

	Capital levels	**Profitability and earnings**	**Quality of loan portfolio and risk profile**	**Funding and liquidity**	**External influences**
[Key measures]	• common equity Tier 1 capital ratio • Tier 1 capital ratio • total capital ratio	• net profit after tax • expense to income ratio • return on equity • earnings per share	• loan impairments • bad and doubtful debt provisioning • provisioning coverage ratios	• stable funding ratio • liquidity levels • liquidity coverage ratio	• the country's economic, fiscal and monetary position • strength of the regulators

(c) Where to find performance-related information for Australian banks

Listed Australian banks report their performance to the market at least every six months on the ASX. This information is also generally available on a bank's website.

Information provided to the ASX includes:

- Financial results announcements
- Investor presentations
- Annual Reports
- Pillar 3 reports (providing detailed information on a bank's capital, risks and portfolio quality)

Westpac's results (including profit announcements and annual reports) may be found [here].

See [Bank Hybrids] for a brief overview of the typical features and risks associated with an investment in Bank Hybrids. For a complete description of the features and risks associated with a particular Hybrid, you should read the prospectus and review other information (including financial information) for the issuer. In the event you need further information, you should seek professional guidance from your stockbroker, solicitor, accountant or other independent and qualified professional adviser.

4. Bank Hybrids

This Guide provides only a brief overview of the features and risks associated with an investment in Bank Hybrids. You should read the prospectus for a Bank Hybrid carefully, paying attention to the investment risks. In the event you need further information, you should seek professional guidance from your stockbroker, solicitor, accountant or other independent and qualified professional adviser.

(a) Types of Bank Hybrids

In this Guide, when we refer to Bank Hybrids, we are referring to Tier 1 Bank Hybrids or Tier 2 Bank Hybrids that meet [APRA's] prudential standards to be treated as regulatory capital of the issuing bank.

Bank Hybrids contain terms that enable them to be converted into ordinary shares, or [written-off] completely in certain circumstances (these circumstances may include, for example, if the bank experiences severe financial difficulty). See [Conversion events]. There are a number of measures that may be used to [assess the strength of a bank] and the risk that a bank may experience financial difficulty. Investors should seek to understand what these metrics are and how to measure them.

Tier 1 Bank Hybrids

Term	• [Perpetual] - Tier 1 Bank Hybrids do not have a fixed maturity date and could exist indefinitely. The [face value] of a Tier 1 Bank Hybrid may never be repaid. • Tier 1 Bank Hybrids typically convert into ordinary shares on a fixed date (the [scheduled or mandatory conversion date]), subject to the [conversion conditions] being satisfied. The conversion conditions operate to ensure that upon conversion on the scheduled or mandatory conversion date, investors will receive bank ordinary shares worth approximately $101.01 for each Tier 1 Bank Hybrid (based on a face value of $100 per Tier 1 Bank Hybrid and taking into account a 1% discount to the relevant VWAP). However, there is a risk that the conversion conditions are never satisfied and the Tier 1 Bank Hybrid remains on issue indefinitely.

	- Tier 1 Bank Hybrids may contain an early call feature where the face value of the Tier 1 Bank Hybrid may be repaid early in cash on a specified date (known as the call date or the redemption date) at the election of the issuing bank. To repay a Tier 1 Bank Hybrid early, a bank requires prior approval from [APRA] (which APRA may withhold). - Investors cannot request conversion or early redemption of Tier 1 Bank Hybrids. However, if quoted on the [ASX], an investor may choose to sell their Tier 1 Bank Hybrids at the prevailing market price to realise their investment. The market price may be less than the face value of the Tier 1 Bank Hybrid (or the price at which the Tier 1 Bank Hybrid was purchased for on the ASX), or there may be no liquid market in the Tier 1 Bank Hybrids (i.e., there may not be enough buyers or sellers in the market), which may result in investors suffering loss or not being able to realise their investment on the ASX.
Distributions	- Tier 1 Bank Hybrids pay distributions that are subject to [distribution payment conditions]. Distributions typically have [franking credits] attached. - The distribution rate on Tier 1 Bank Hybrids, assuming they are fully franked, is typically determined as the sum of [BBSW] plus a [margin], together multiplied by (1-tax rate). In effect, the distribution rate is adjusted to take into account the franking credits that are attached to the distribution payments. As distribution payments are based on BBSW, distribution payments are likely to vary over the term of the Tier 1 Bank Hybrid. - For an explanation of how distributions for Tier 1 Bank Hybrids are calculated, see [Case Study 1]. - The ability of an investor to use franking credits, either as an offset to a tax liability or by claiming a tax refund, will depend on the investor's individual

	tax position. • It is possible that distributions on Tier 1 Bank Hybrids may not be paid as they are at the bank's absolute discretion and subject to the distribution payment conditions (including, for example, that the payment of the distribution will not result in either a breach of [APRA's] regulatory capital requirements or the bank becoming insolvent). If a distribution is not paid, the missed payment will not be made up (often referred to as being [non-cumulative]). However, if a distribution is not paid, the bank will be restricted from paying dividends on its ordinary shares or from buying-back its ordinary shares for a specified period. These restrictions (sometimes referred to as "dividend stoppers" or "capital stoppers" respectively) acts as a protection for Tier 1 Bank Hybrid investors.
Potential loss of investment	• If a bank's capital falls below certain capital levels (a [capital trigger event]), or a [non-viability trigger event] occurs (see [non-viability trigger event] for guidance on when APRA may consider a bank to be non-viable), a bank may be required to convert some or all of its Tier 1 Bank Hybrids into ordinary shares. Conversion of Tier 1 Bank Hybrids following a capital trigger event or a non-viability trigger event is not subject to [conversion conditions] being satisfied. If the Tier 1 Bank Hybrids are converted into ordinary shares, the value of ordinary shares an investor receives may be significantly less than the [face value] of their Tier 1 Bank Hybrid. This is because the number of ordinary shares an investor will receive in these circumstances is limited to a [maximum conversion number], which is based on the bank's ordinary share price at the time of issue of the Tier 1 Bank Hybrid (and the bank's ordinary share price may have dropped considerably due to the bank's financial difficulty). If for any reason conversion does not occur and if the ordinary shares are not issued for any reason within a specified period, all rights in relation to the Tier 1 Bank

	Hybrids will be terminated and investors will lose all of the value of their investment and they will not receive any compensation or unpaid distributions.

Tier 2 Bank Hybrids

Term	• [Fixed maturity date] – if a bank is solvent, it must repay the [face value] of its Tier 2 Bank Hybrid on the maturity date. • Tier 2 Bank Hybrids may contain an early call feature where the face value of the Tier 2 Bank Hybrid may be repaid earlier than the maturity date (known as a call date or early redemption date) at the election of the issuing bank. To repay a Tier 2 Bank Hybrid early, a bank requires prior approval from [APRA] (which APRA may withhold). • Investors cannot request conversion or early redemption of Tier 2 Bank Hybrids. However, if quoted on the [ASX], an investor may choose to sell their Tier 2 Bank Hybrids at the prevailing market price to realise their investment. The market price may be less than the face value of the Tier 2 Bank Hybrid (or the price at which the Tier 2 Bank Hybrid was purchased for on the ASX), or there may be no liquid market in the Tier 2 Bank Hybrids (i.e., there may not be enough buyers or sellers in the market), which may result in investors suffering loss or not being able to realise their investment on the ASX.

Interest	• Tier 2 Bank Hybrids pay interest, subject to the solvency of the bank. • Interest on Tier 2 Bank Hybrids is typically determined as the sum of [BBSW] plus a [margin]. As interest payments are based on BBSW, interest payments are likely to vary over the term of a Tier 2 Bank Hybrid. • Any unpaid interest will accumulate and be payable at a later date when the bank is solvent (often referred to as being [cumulative]), unless conversion or [write-off] occurs due to the bank becoming non-viable. • Tier 2 Bank Hybrid interest payments typically do not have [franking credits] attached to them.
Potential loss of investment	• If a [non-viability trigger event] occurs (see [non-viability trigger event] for guidance on when APRA may consider a bank to be non-viable), a bank may be required to convert some or all of its Tier 2 Bank Hybrids into ordinary shares. Conversion of Tier 2 Bank Hybrids following a non-viability trigger event is not subject to [conversion conditions] being satisfied. If the Tier 2 Bank Hybrids are converted into ordinary shares, the value of ordinary shares an investor receives may be significantly less than the [face value] of their Tier 2 Bank Hybrid. This is because the number of ordinary shares an investor will receive in these circumstances is limited to a [maximum conversion number], which is based on the ordinary share price at the time of issue of the Tier 2 Bank Hybrid (and the bank's ordinary share price may have dropped considerably due to the bank's financial difficulty). If for any reason conversion does not occur and if the ordinary shares are not issued for any reason within a specified period, all rights in relation to the Tier 2 Bank Hybrids will be terminated and investors will lose all of the value of their investment and they will not receive any compensation or unpaid interest.

(b) Conversion Events

Conversion of Bank Hybrids into ordinary shares (or write-off) may occur in the following circumstances:

Scheduled conversion (also known as mandatory conversion)

(i) Scheduled or mandatory conversion

Tier 1 Bank Hybrids only

[Tier 1 Bank Hybrids] are [perpetual] but typically have a set date (the [scheduled or mandatory conversion date]) on which the instruments are scheduled to convert into ordinary shares. Whether conversion occurs will depend on the [conversion conditions] being satisfied. If the conversion conditions are not met on the scheduled or mandatory conversion date, then conversion will not occur until the next distribution payment date on which the conversion conditions are met. The conversion conditions operate to ensure that upon conversion on the scheduled or mandatory conversion date investors will receive bank ordinary shares worth approximately $101.01 for each Tier 1 Bank Hybrid (based on a [face value] of $100 per Tier 1 Bank Hybrid and taking into account a 1% discount to the relevant VWAP).

There is a risk that the conversion conditions are never satisfied and scheduled or mandatory conversion of a Tier 1 Bank Hybrid into ordinary shares never occurs. In this case, investors will continue to hold the Tier 1 Bank Hybrid indefinitely.

Capital Trigger Event

(ii) Capital trigger event

Tier 1 Bank Hybrids only

[Tier 1 Bank Hybrids] are generally required to contain a capital trigger event in order to be eligible to be treated as regulatory capital.

A capital trigger event occurs when a bank determines, or [APRA] notifies the bank in writing, that the bank’s common equity Tier 1 ratio is less than or equal to 5.125%.

If a capital trigger event occurs, a bank may be required to convert some or all of its Tier 1 Bank Hybrids into ordinary shares. Conversion of Tier 1 Bank Hybrids following a capital trigger event is not subject to [conversion conditions] being satisfied. Following a capital trigger event, the number of Tier 1 Bank Hybrids that are converted into ordinary shares will be the number (or percentage of face value) as is sufficient to restore the bank to a common equity Tier 1 ratio above 5.125%.

If Tier 1 Bank Hybrids are converted into ordinary shares, investors will receive a variable number of ordinary shares, limited to a [maximum conversion number]. Depending on the price of the ordinary shares at the relevant time, investors may suffer loss as the value of ordinary shares received by an investor may be significantly less than $101.01 for each Tier 1 Bank Hybrid (based on a face value of $100 per Tier 1 Bank Hybrid and taking into account a 1% discount to the relevant VWAP). This is because the maximum conversion number is based on the bank's ordinary share price at the time of issue of the Tier 1 Bank Hybrid (and the bank's ordinary share price may have dropped considerably due to the bank's financial difficulty). If for any reason conversion does not occur and ordinary shares are not issued for any reason within a specified period, all rights in relation to the Tier 1 Bank Hybrids will be terminated and investors will lose all of the value of their investment and they will not receive any compensation or unpaid distributions.

Tier 1 Bank Hybrids are generally required to be converted into ordinary shares (or written-off in certain circumstances) before [Tier 2 Bank Hybrids] are converted into ordinary shares (or [written-off]).

Non-viability trigger event

(iii) Non-viability trigger event

Tier 1 and Tier 2 Bank Hybrids

In order to be treated as regulatory capital by [APRA], the terms of [Tier 1 Bank Hybrids] and [Tier 2 Bank Hybrids] must contain a non-viability trigger event.

A non-viability trigger event occurs when APRA notifies a bank in writing that it believes:

- conversion to ordinary shares of some or all of its Bank Hybrids or
- a public sector injection of capital or equivalent support

is necessary to prevent the bank becoming non-viable. Whether a non-viability trigger event will occur is at the discretion of APRA.

If a non-viability trigger event occurs, the bank may be required to convert some or all of its Tier 1 Bank Hybrids or Tier 2 Bank Hybrids into ordinary shares. Conversion of Bank Hybrids following a non-viability trigger event is not subject to [conversion conditions] being satisfied. If Bank Hybrids are converted into ordinary shares, investors will receive a variable number of ordinary shares, limited to a [maximum conversion number]. Depending on the price of the ordinary shares at the relevant time, investors may suffer loss as the value of the ordinary shares received by an investor is likely to be significantly less than $101.01 for each Bank Hybrid (based on a face value of $100 per Bank Hybrid and taking into account a 1% discount to the relevant VWAP). This is because the maximum conversion number is based on the bank's ordinary share price at the time of issue of the Bank Hybrid (and the bank's ordinary share price may have dropped considerably due to the bank's financial difficulty).If for any reason conversion does not occur and ordinary shares are not issued for any reason within a specified period, all rights in relation to the Bank Hybrids will be terminated and investors will lose all of the value of their investment and they will not receive any compensation or unpaid distributions / interest.

APRA has not provided guidance on when it will consider an entity to be non-viable and there are currently no Australian precedents for determining non-viability. However, it is likely that APRA may consider a bank to be non-viable when a bank is:

- suffering from significant financial stress;
- insolvent; or
- unable to raise money in the public or private market.

Tier 1 Bank Hybrids are generally required to be converted into ordinary shares (or [written-off] in certain circumstances) before Tier 2 Bank Hybrids are converted into ordinary shares (or written-off).

5. Case Studies & Checklist

(a) Case Studies

The following Case Studies are for illustrative purposes only. Any rates or calculations on which the Case Studies are based are for illustrative purposes only and do not indicate actual payments or rates and are not based on real market conditions. The Case Studies are not a guarantee or forecast of the actual payments or rates that may be achieved. Past performance is not a reliable indicator of future performance.

Case Study 1 Tier 1 Bank Hybrid distributions

(i) Calculation of Tier 1 Bank Hybrid franked distributions

Case Study 1 provides an example of how to calculate distribution rates and distribution amounts for a [Tier 1 Bank Hybrid] where distributions are fully franked. Distributions are only payable subject to the satisfaction of the [distribution payment conditions]. [Franking credits] are generally taken into account in calculating distributions on Tier 1 Bank Hybrids.

Distribution rate calculation (%)

For example, if

[margin] = 3.00% per annum
[BBSW] = 2.00% per annum
[face value] of Tier 1 Bank Hybrid = $100

Step 1

the equivalent unfranked distribution rate = BBSW + margin
= 2.00% + 3.00%
= 5.00% per annum

Step 2

The equivalent unfranked distribution rate is then adjusted down to take account of the franking credits to be attached to the distribution to arrive at the cash distribution rate:

cash distribution rate = equivalent unfranked distribution rate × (1-tax rate)

=	5.00% × (1.00 - 0.30) (assuming a corporate tax rate of 30% and expressed as a decimal in the calculation)

=	3.50% per annum

Result

In total the investor will receive in percentage terms:

3.50% as a cash distribution on the distribution payment date and

1.50% as franking credits

Cash distribution amount ($)

cash distribution rate	3.50% per annum
multiplied by the face value of each Tier 1 Bank Hybrid	× $100.00
multiplied by the number of days in the relevant distribution period (assuming 90 days for a quarterly distribution period)	× 90
divided by the number of days in the year	÷ 365
Cash distribution amount for each Tier 1 Bank Hybrid	= $0.8630

Franking credits ($)

Amount of franking credits per cash distribution amount	= cash distribution amount × $\frac{\text{corporate tax rate}}{1 - \text{corporate tax rate}}$
	= $0.8630 × $\frac{0.30}{0.70}$
	= $0.3699

Result

In total, the investor receives in dollar terms:

The investor will receive for each Tier 1 Bank Hybrid of $100:	$0.8630 as a cash distribution on the distribution payment date and
	$0.3699 as franking credits

In this example, for an investment of 500 Tier 1 Bank Hybrids, the investor receives:

cash distribution amount	$0.8630 × 500 = $431.50
franking credit amount	$0.3699 × 500 = $184.95

Please note that the ability of an investor to use franking credits, either as an offset to a tax liability or by claiming a tax refund, will depend on each investor’s individual tax position. Any benefit will only be received after an investor’s tax return is lodged.

(ii) Case Study 2 Non-viability

Conversion of a Bank Hybrid following a non-viability trigger event

Case Study 2 provides an example of how to calculate the number of ordinary shares that an investor might receive following conversion of a Bank Hybrid after the occurrence of a [non-viability trigger event].

- John invests $10,000 in Bank Hybrids (100 Bank Hybrids at a [face value] of $100.00 per Bank Hybrid).
- The bank experiences severe financial difficulty and [APRA] determines that a non-viability trigger event has occurred.
- Following the non-viability trigger event, John’s entire investment is converted into ordinary shares.
- Conversion in the case of a non-viability trigger event does not require [conversion conditions] to be satisfied prior to conversion.
- On conversion, the number of ordinary shares John will receive will be the lesser of:
  - the conversion number (see Formula A below) and
  - the [maximum conversion number] (see Formula B below).

Formula A - calculation of conversion number

For example, if

[face value] = $100.00

VWAP = $2.00 (calculated as the [VWAP] during the 5 business days prior to conversion, not including the date of conversion)

Conversion discount = 1% (reflected as 0.99 in the formula below)

conversion number per Bank Hybrid	=	$\frac{\text{face value}}{0.99 \times \text{VWAP}}$
	=	$\frac{\$100.00}{0.99 \times \$2.00}$

conversion number per Bank Hybrid	=	50.5051 ordinary shares

The 1% discount on conversion is designed to compensate investors for transactions costs (i.e., brokerage costs) which may be incurred on the disposal of ordinary shares the investor receives on conversion.

Formula B - maximum conversion number

The [maximum conversion number] in this example is based upon the [issue date VWAP]. The issue date VWAP is then multiplied by a factor of 0.20 as required by [APRA] (i.e., to broadly reflect 20% of the bank's ordinary share price at the time of issue of the Bank Hybrid).

For example, if:

[face value] = $100.00

issue date VWAP = $20.00

maximum conversion number per Bank Hybrid	=	$\frac{\text{face value}}{0.20 \times \text{issue date VWAP}}$
	=	$\frac{\$100.00}{0.20 \times \$20.00}$
maximum conversion number per Bank Hybrid	=	25 ordinary shares

Result

conversion number per Bank Hybrid	=	50.5051 ordinary shares
maximum conversion number per Bank Hybrid	=	25 ordinary shares

On conversion John will receive the lesser of the conversion number and the [maximum conversion number] of ordinary shares. As the share price has fallen significantly from the issue date of the Bank Hybrid, the maximum conversion number of ordinary shares will apply and John will receive 25 ordinary shares for each Bank Hybrid.

- For 100 Bank Hybrids, John receives 2,500 ordinary shares (100 × 25 ordinary shares). If the market price of ordinary shares at the time of conversion is $2.00 per ordinary share, the value of John's investment will be approximately $5,000 (2,500 ordinary shares at $2.00 per ordinary share).

- If John sells his ordinary shares when he receives them he will realise a loss of $5,000 on his initial investment of $10,000.

It is not possible to predict the price of a bank's ordinary shares or whether a market would exist for a bank's ordinary shares following a non-viability trigger event.

(iii) Case Study 3 – Scheduled or mandatory conversion

Scheduled or mandatory conversion

Case Study 3 provides an example of how to calculate the number of ordinary shares an investor will receive following scheduled conversion.

- Bank XYZ issues [Tier 1 Bank Hybrids] in September 2015.

- Shirley purchases $10,000 of Tier 1 Bank Hybrids on the [ASX] in November 2015.

- At the time of purchase the market price is $100.00 per Tier 1 Bank Hybrid. Shirley receives 100 Tier 1 Bank Hybrids.

- The Tier 1 Bank Hybrids have the following key dates set out in the prospectus:

Optional redemption / conversion	Scheduled or mandatory

date	conversion date
September 2020	September 2022
Bank can elect to: • convert into bank ordinary shares (subject to the [conversion conditions]) or • redeem for cash (subject to [APRA's] prior approval, which APRA may withhold)	Scheduled or mandatory conversion into bank ordinary shares (subject to the conversion conditions)

On the optional redemption / conversion date in September 2020, the bank elects not to redeem or convert the Tier 1 Bank Hybrids to ordinary shares. Shirley decides to continue to hold her investment until the [scheduled or mandatory conversion date] of September 2022 rather than sell the Tier 1 Bank Hybrids on the [ASX] at the prevailing market price.

- In September 2022 on the scheduled or mandatory conversion date, a number of conversion conditions need to be satisfied for Shirley's Tier 1 Bank Hybrids to be converted into ordinary shares.
- If the conversion conditions are not satisfied on the scheduled or mandatory conversion date, conversion will not occur on this date and will be retested on the next distribution payment date.

Step 1: Scheduled conversion conditions

Condition 1 the [VWAP] of ordinary shares on the 25th business day before (but not including) the potential [scheduled or mandatory conversion date] must be greater than 56.12% of the [issue date VWAP]; and

Condition 2 the VWAP of ordinary shares during the 20 business days before (but not including) the potential scheduled or mandatory conversion date must be greater than 50.51% of the issue date VWAP.

The conversion conditions are intended to ensure that upon conversion on the scheduled or mandatory conversion date, investors will receive bank ordinary shares worth approximately $101.01 for each Tier 1 Bank Hybrid held (based on a [face value] of $100 per Tier 1 Bank Hybrid and taking into account a 1% discount to the relevant VWAP).

For example, if

face value = $100.00

issue date VWAP = $20.00

Condition 1 VWAP of ordinary shares on the 25th business day before (but not including) the scheduled or mandatory conversion date = $30.00 (which is greater than 56.12% of the issue date VWAP) calculated as

56.12% × $20.00 = $11.22

Condition 2 VWAP of ordinary shares during the 20 business days before (but not including) the scheduled or mandatory conversion date = $32.00 (which is greater than 50.51% of the issue date VWAP) calculated as

50.51% × $20.00 = $10.10

Result

Both [conversion conditions] are met, therefore conversion will occur on the scheduled or mandatory conversion date.

Step 2: The number of ordinary shares received on conversion is calculated as follows:

For example, if

- [face value] = $100.00
- [VWAP] of ordinary shares during the 20 business days before (but not including) the conversion date = $32.00 (see above)
- conversion discount = 1% (reflected as 0.99 in the formula below)

conversion number for each Tier 1 Bank Hybrid	=	$\frac{\text{face value}}{0.99 \times \text{VWAP}}$
	=	$\frac{\$100.00}{0.99 \times \$32.00}$

	=	3.1566 ordinary shares

The 1% discount on conversion is designed to compensate investors for transaction costs (i.e., brokerage costs) which may be incurred on the disposal of ordinary shares the investor receives on conversion.

Result

- Under Step 1, both [conversions conditions] are met and conversion will occur on the [scheduled or mandatory conversion date].
- Under Step 2, on the conversion date Shirley receives 315 ordinary shares (100 Tier 1 Bank Hybrids × 3.1566).
- As Shirley would like to realise her Tier 1 Bank Hybrid investment, she sells the 315 ordinary shares on the [ASX] at a net price of $35.50 per ordinary share, after brokerage costs:

  315 ordinary shares × $35.50 = $11,182.50

- In this example Shirley receives $11,182.50 for her ordinary shares, which is a small profit on her original Tier 1 Bank Hybrid investment of $10,000.

If the market price for the ordinary shares is less than $31.75 at the time Shirley sells, she will incur a loss on her Tier 1 Bank Hybrid investment of $10,000.

(iv) Case Study 4 – Selling Bank Hybrids on the ASX

Selling Bank Hybrids on the ASX

Case Study 4 provides an example of an investor selling Bank Hybrids on the ASX.

Julie purchases 500 Bank Hybrids at $100 per Bank Hybrid for $50,000.

- Two years later, Julie decides to sell the Bank Hybrids when the market price on the ASX is $99.50 per Bank Hybrid.
- Through her broker, Julie sells the 500 Bank Hybrids and receives $49,750 after brokerage costs. Julie has made a loss on her principal investment of $250 although she consistently received

distributions each quarter during the two years she held the Bank Hybrids.

- If Julie sold the Bank Hybrids at a market price that was higher than the purchase price of the Bank Hybrids, Julie may have made a profit on her Bank Hybrid investment, after any brokerage costs.

(b) Checklist

When considering an investment in a Bank Hybrid, you may want to consider the following questions and you should ensure that you understand the key features and risks of Bank Hybrids. You should also read the prospectus carefully, paying attention to the investment risks. In the event you need further information, you should seek professional guidance from your stockbroker, solicitor, accountant or other independent and qualified professional adviser.

(i) General

- What are the risks of investing – now and in the future?
- Will an investment in a Bank Hybrid help me achieve my long-term personal objectives and goals?
- Does the investment suit my timeframe and personal risk profile?
- How strong is the bank I am investing in?

(ii) Term

- Does the Bank Hybrid have a [maturity date] or is it [perpetual]?
- Can the bank repay the investment early or could the Bank Hybrid remain on issue for a very long time or indefinitely?
- Can I exit this investment if my circumstances change and will I be able to get my initial investment back?
- If I sell the Bank Hybrid on the ASX, how does the price compare to what I paid and is there a liquid market for the Bank Hybrid?

(iii) Distributions/Interest

- Will the investment returns adequately compensate me for the risk of investing in the Bank Hybrid?

- How does the distribution / interest rate compare with other bank investments, taking into account the different levels of risk?
- Can other less risky or less complex bank investments provide similar or better returns?
- Does the bank have to pay interest or distributions? If not, are missed payments [cumulative] or [non-cumulative]?
- Are there conditions that need to be satisfied prior to payment of any distribution or interest payment?
- Is interest fixed for the term of the Bank Hybrid or calculated by reference to a floating rate?
- If interest is calculated by reference to a floating rate, what is the [benchmark] and what is the [margin]?
- Will the distributions have [franking credits] attached and, if so, are they of value to me?

(iv) Early redemption, conversion or transfer

- Does the bank have an option to convert, redeem or transfer the Bank Hybrid early?
- Is redemption subject to APRA approval?
- Will I be able to reinvest my principal at a similar rate of return at the time of early redemption or transfer?

(v) Scheduled or

- Is there a [scheduled or mandatory

mandatory conversion

conversion date]? When is it?

- How many ordinary shares do I receive on conversion? How is the number of ordinary shares calculated?
- Do [conversion conditions] need to be satisfied prior to conversion?
- Is there a minimum or maximum number of ordinary shares I will get on conversion? Can I receive less than the [face value] of my initial investment?
- At the scheduled or mandatory conversion date does the bank have a choice to either pay cash or convert the Bank Hybrid into ordinary shares?

(vi) Conversion following a non-viability trigger event or a capital trigger event

- What might happen to the Bank Hybrid if the bank experiences severe financial difficulty?
- Are there trigger events in the Bank Hybrid that may result in the conversion into ordinary shares, or that may result in the Bank Hybrid being written-off completely?
- What happens if a [non-viability trigger event] or a [capital trigger event] occurs? Is conversion into ordinary shares or [write-off] possible?
- What are the terms of the conversion?
- Is there a cap on the number of ordinary shares I will receive? Are there conditions that must be

satisfied prior to conversion? Can I receive less than the [face value] of my initial investment?

- Are there circumstances in which the Bank Hybrid might be terminated and I might receive no compensation for my investment?

Further guidance on investing in [bank hybrid securities] can be found on ASIC's MoneySmart website. Their website also has a hybrid securities [quiz] that you can use to test your knowledge.

In addition, for further information see the [ASX] website [here].

6. Frequently Asked Questions

Do Bank Hybrids provide a regular income stream?

Bank Hybrids may not always provide a regular income stream.

[Tier 1 Bank Hybrids] pay distributions at the absolute discretion of the bank and are subject to the [distribution payment conditions]. If a distribution is not paid, the missed payment will not be made up (often referred to as being [non-cumulative]). As distribution payments are based on [BBSW], distribution payments are likely to vary over the term of the Tier 1 Bank Hybrid.

For an example of how to calculate distributions for Tier 1 Bank Hybrids, see [Case Study 1].

[Tier 2 Bank Hybrids] pay interest, subject to the solvency of the bank. Interest is typically determined as the sum of BBSW plus a [margin]. Any unpaid interest will accumulate and be payable at a later date, when the bank is solvent (often referred to as being [cumulative]) unless conversion or [write-off] occurs due to the bank becoming non-viable. As interest payments are based on BBSW, interest payments are likely to vary over the term of the Tier 2 Bank Hybrid.

Will the distribution / interest rate be the same for the life of a Bank Hybrid?

The distribution / interest rate is typically based on a [margin] above [BBSW]. As BBSW is a floating market rate of interest (usually the 90 day bank bill swap rate), payments are likely to vary over the term of a Bank Hybrid. The margin typically reflects the risk premium of the Bank Hybrid above a floating market rate of interest at the time of issue.

For an example of how to calculate distributions for [Tier 1 Bank Hybrids], see [Case Study 1].

Under what circumstances may an investor receive less than the face value of a Bank Hybrid investment?

If Bank Hybrids are quoted on the [ASX], an investor may choose to sell their Bank Hybrid investment at the prevailing market price to realise their investment. That market price may be less than the [face value] of the Bank Hybrid (or the price at which the Bank Hybrid was purchased on market), or there may be no liquid market in the Bank Hybrids (i.e., there may not be enough buyers or sellers in the market), which may result in investors suffering loss.

[Tier 1 Bank Hybrids] - If a bank's capital falls below certain capital levels (a [capital trigger event]) or a [non-viability trigger event] occurs (see [non-viability trigger event] for guidance on when APRA may consider a bank to be non-viable), the bank may be required to convert some or all of the Tier 1 Bank Hybrids into ordinary shares or completely [write them off].

[Tier 2 Bank Hybrids] - If a non-viability trigger event occurs (see [non-viability trigger event] for guidance on when [APRA] may consider a bank to be non-viable), the bank may be required to convert some or all of its Tier 2 Bank Hybrids into ordinary shares or completely write them off.

Conversion of Tier 1 Bank Hybrids following a capital trigger event or a non-viability trigger event, and conversion of Tier 2 Bank Hybrids following a non-viability trigger event, is not subject to [conversion conditions] being satisfied. If Bank Hybrids are converted into ordinary shares, the value of ordinary shares an investor receives may be significantly less than the [face value] of the Bank Hybrid. This is because the number of ordinary shares an investor will receive following a conversion in these circumstances is limited to a [maximum conversion number], which is based on the share price at the time of issue and the bank's ordinary share price may have dropped considerably due to the bank's financial difficulty. If for any reason conversion does not occur and if the ordinary shares are not issued for any reason within a specified period, all rights in relation to the Bank Hybrids will be terminated and investors will lose all of the value of their investment and they will not receive any compensation or unpaid distributions / interest.

See [Case Study 2] for conversion following a non-viability trigger event.

Will I receive franking credits? How will these be paid to me?

[Tier 1 Bank Hybrids] may have [franking credits] attached to distribution payments (see [Case Study 1]). The ability of an investor to use franking credits, either as an offset to a tax liability or by claiming a tax refund, will depend on each investor's individual tax position.

[Tier 2 Bank Hybrid] interest payments typically do not have franking credits attached to them.

How can I get my money back after investing in a Bank Hybrid?

[Tier 1 Bank Hybrids]:

1. Sale of the Tier 1 Bank Hybrid on the [ASX] (assuming the Tier 1 Bank Hybrid is quoted on the [ASX]). See [Case Study 4];

2. Early redemption or transfer at the absolute discretion of the bank (redemption is subject to [APRA's] prior approval, which APRA may withhold); and

3. Scheduled conversion into ordinary shares on the [scheduled or mandatory conversion date] (subject to conversion conditions), and subsequent sale of the ordinary shares on the ASX. See [Case Study 3].

[Tier 2 Bank Hybrids]:

1. Sale of the Tier 2 Bank Hybrid on the ASX (assuming the Tier 2 Bank Hybrid is quoted on the [ASX]). See [Case Study 4];

2. Early redemption at the absolute discretion of the bank (redemption is subject to APRA's prior approval, which APRA may withhold); and

3. Redemption on the [maturity date].

There is the risk that investors may not get some or all of their money back after investing in a Bank Hybrid. See the FAQ above, ["Under what circumstances may an investor receive less than the face value of a Bank Hybrid investment?"].

If a Bank Hybrid is 'perpetual', when will my investment be returned to me?

[Tier 1 Bank Hybrids] are [perpetual], but typically have a set date (the [scheduled or mandatory conversion date]) on which the instruments are scheduled to convert into ordinary shares. Whether conversion occurs will depend on [conversion conditions] being satisfied. If the conversion conditions are not satisfied on the scheduled conversion date, then scheduled or mandatory conversion will not occur until the next distribution payment date on which the conversion conditions are met. However, there is a risk that the conversion conditions are never satisfied and the Tier 1 Bank Hybrid remains on issue indefinitely.

If Tier 1 Bank Hybrids are quoted on the [ASX], investors may sell their Tier 1 Bank Hybrids on the ASX whenever they choose. Any sale will however be at the market price at the time of sale, which may be more or less than the [face value] of the Tier 1 Bank Hybrids (or the purchase price of the Tier 1 Bank Hybrid if purchased on the ASX) and may incur brokerage costs.

[Tier 2 Bank Hybrids] are not perpetual and have a fixed [maturity date].

What are my options at maturity?

Tier 1 Bank Hybrids are [perpetual] and do not have a maturity date but are scheduled to convert into ordinary shares on a specified date (the [scheduled or mandatory conversion date]), subject to the [conversion conditions] being satisfied. The conversion conditions operate to ensure that upon conversion on the scheduled or mandatory conversion date, investors will receive ordinary shares worth approximately $101.01 for each Tier 1 Bank Hybrid (based on a face value of $100 per Tier 1 Bank Hybrid and taking into account a 1% discount to the relevant VWAP). However, there is a risk that the conversion conditions are never satisfied and the Tier 1 Bank Hybrid remains on issue indefinitely.

Tier 2 Bank Hybrids are generally redeemed in cash on a fixed maturity date or may be repaid earlier on a call date or an early redemption date (subject to [APRA's] prior approval, which APRA may withhold).

[Tier 1 Bank Hybrid] investors and [Tier 2 Bank Hybrid] investors cannot request conversion or early redemption.

How do I invest in Bank Hybrids?

You may subscribe to a Bank Hybrid offer when it is first offered or issued under a prospectus by contacting the relevant wealth management, private banking, stockbroking or financial advisory firms distributing the offer. Whether you can subscribe to the initial offer will depend on a range of factors including the eligibility requirements. Bank Hybrids may also be bought on the ASX through a stockbroker after they have been issued. The purchase price of Bank Hybrids bought on market may be higher or lower than the face value of the Bank Hybrids at the time of issue.