The Treasury

South Canterbury Finance Limited Information Release

Release Document

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[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

RECOMMENDATION FOR RETAIL DEPOSIT SCHEME PROVISION

For the Month Ending October 2009

Agreed by the Treasury DGS Provisioning Committee on 9 November2009
Prepared by Craig Murphy, Senior Analyst, DGS Team, The Treasury

1. INTRODUCTION

Information

In the completion of the provisioning recommendation Treasury has used information collected under the monthly monitoring conducted by the Reserve Bank of New Zealand ("RBNZ"), which is to be reconciled with the annual and semi annual reports of the entities to ensure its accuracy. RBNZ are contracted by The Treasury to use this information to provide an assessment of the possible loss to the Crown in event of default of an entity.

The Treasury uses additional information requested directly from the entities covered by the entities in the Deposit Guarantee Scheme ("DGS"), the Inspectors of the inspected entities and information directly sourced from other market participants (Government Agencies, Banks, Professional Services Firms etc) in our assessment of the possible loss to the Crown in event of default of an entity.

Model

To arrive at a loss on liquidation value for an entity, the RBNZ undertakes a loss given default assessment of the loan book to arrive at a discounted loan book, which is then added together with other assets held by the entity (after discounting) to form a total asset position. Total assets are then applied to the Total liabilities to assess the equity shortfall (if any) and the Crown's loss under a liquidation scenario.

In addition, qualitative information is provided by RBNZ based on discussion with the Trustees and other knowledge of the industry.

The RBNZ model output is then reviewed by The Treasury to assess the appropriateness of the indicated loss given the additional information held by The Treasury from inspection reports, information directly sourced from other market participants (government agencies, banks, professional services firms etc) and the entity. Adjustments to the provision are made if required.

The timing of defaults is modeled to produce an estimation of post acceleration interest likely to be incurred and a cash flow forecast of payout and receivers distributions. Cash flows are then discounted using GSF discount rates with the net cost of discounting being added back to ensure the provision reflects the net present value of cash flows.

The provisioning recommendations are then presented to the provisioning committee to assess the probability of default and agree the appropriate level of the provision.

Accounting Standards

The accounting issues and financial reporting standards that The Treasury has followed to establish this provision are as follows:

1. Initial recognition and measurement of the fair value of the guarantee at inception (IAS 39.9);
2. Recognition of premium received (IAS 18);
3. Measurement of a provision (NZIAS37:14 & NZIAS 37:36);
4. Triggering (recognition) of a provision (NZIAS37:14); and
5. Disclosures of the Crown's exposure (NZIAS 39, NZIFRS 7);

A detailed note on these was prepared by Ken Warren (i-manage 1247592), which included commentary on application of the financial reporting standards standards to our specific circumstances.

2. RECOMMENDATION

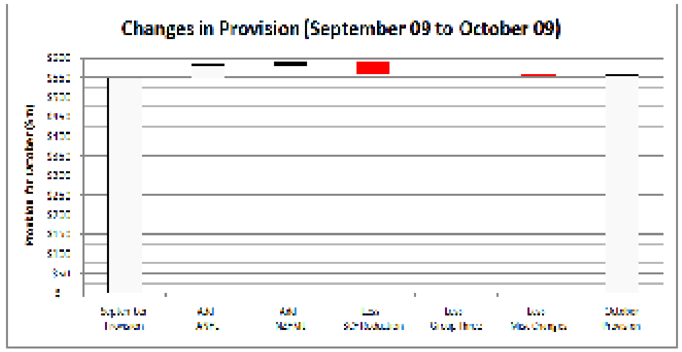
Provision Recommendation

The provision for October 2009 has increased by $33m from the provision of $863m (agreed at the Treasury DGS Provisioning Committee on 22 October 2009) to $896m, being the Crowns Share of the loss given default of $556m plus an allowance for post acceleration interest $263m and the net effect of discounting cash flows $77m.

The $33m change in the provision for October is made up of an increase in the loss given default of $9m to $556m (from $547m), the increase in post acceleration interest of $8m to $263m (from $255m) and the increase in the net effect of discounting cash flows of $16m to $77m (from $61m).

The number of entities covered by the provision has decreased to 9 from 32, a reduction of 23 entities due to several of the former Group Three entities being excluded from the October 2009 provision.

No	Company Name (credit rating if available)	Crown Share of Loss	Post Acceleration Interest	Total Crown Loss
1	South Canterbury Finance Limited (BB+/Negative/Aug 09)	480	236	716
2	Allied Nationwide Finance Limited	36	16	52
3	Vision Securities Limited	25	3	28
4	Viaduct Capital Limited	5	1	6
5	[3]	4	1	5
6		3	1	4
7	Mutual Finance Limited	2	4	6
8	[3]	1	0	2
9		-	1	1
	SUBTOTAL	556	263	819
	plus Net Effect of Discounting Cashflows			77
	TOTAL			896



The boxes in red in the chart above denote a reduction in the provisioning level.

Key Changes

The former Group One and Group Two entities have been combined into one table (above to the right) and the Group Three entities no longer form part of the provision, however 5 are now in a watch list of entities.

The watch list contains entities that are of interest due to significant credit related issues but that do not warrant a provision at this time.

There have been five significant changes to the loss given default component of the provision for October 2009 which results in the $8m reduction in the loss given default component of the provision recommendation.

The major changes in the provision are:

1. Allied Nationwide Finance Limited has been restated into the provision (+$36m) due to the information provided by KordaMentha in their inspection report;
2. [3] has been included in the provision (+$3m), due to asset quality and liquidity concerns;
3. The South Canterbury Finance Limited ("SCF") provision has reduced (-$27m) due to SCF reducing liabilities, while holding assets static;
4. The former group three entities have be reanalysed and none of these entities require a provision for October 2009 (-$2m) due to increased satisfaction with their overall credit quality, however 5, of these entities are on the watch list.
5. There are minor changes totaling (-$1m) over several entities.

3. RECONCILIATION OF SEPTEMBER TO THE OCTOBER PROVISION

[3]

Comparison of September 2009 Provision & October 2009 Provision (Both tables use October 2009 information)

The table above (left) illustrates those entities provisioned for as at September 2009. The Group Four entities in the table lists those entities that were not provisioned for in September 2009, but are included in either the provision or the watch list for October 2009.

The table above (right) illustrates those entities provisioned for as at October 2009, and those included on the watch list for October 2009. The Group Three entities in the table lists those entities included in the provision for in September 2009, but excluded from either the provision or the watch list for October 2009.

Included in Provision for October 2009

All of the former Group One and Group Two entities provisioned for in September 2009 are provisioned for in October 2009. [3] and Allied Nationwide Finance have been added to the provision for October 2009.

Included in Watch List for October 2009

All of the former Group Three entities have be reanalysed, and none of these entities are provisioned for in October 2009, however, 5 of these entities are on the watch list for October 2009

Seven entities that were no provisioned for in September 2009, are now included on the watch list for October 2009.

4. MAJOR MOVEMENTS IN LOSS GIVEN DEFAULT

Major Movements Summary

The major movements in loss given default for the month relate to:

1. Movements in principle due to changes in the entities in the provision and to the underlying books of those entities;
2. An increase in interest costs associated with the movements of entities in and out of the provision;
3. An adjustment of discount rates to align with the GSF discount rates over the full timescale over which cash flows occur; and
4. Changed assumptions on timing of defaults to reflect market activity during the month. In particular this resulted in the assumed timing for SCF's default

	September $m	October $m	Movement $m	Explanation
Loss Given Default				
Principle	547	556	9	Allied Nationwide Finance Limited included (+$36m), [redacted] included (+$3m), South Canterbury Finance Limited reduced (-$27m), Group Three entities removed (-$2m).
Interest	255	263	8	Reduced by Group Three entionties removal (-$12m), increased by Allied Nationwide Finance Limited (+$18)
Face Value of Loss Given Default	**802**	**819**	**17**	
Impact of discounting cashflows				
Discounting of Payments (Benefit)	(77)	(140)	63	Increased benefit due to higher discount rates in out years: $23m, plus movements in timing of default (in particular SCF) and effect of entities moving in and out of provision
Discounting of receiver distributions - cost	138	217	(79)	Increased cost due to higher discount rates in out years: $58m, plus movements in timing and effect of entities moving in and out of provision
Net impact of discount rates	**61**	**77**	**16**	
Total LGD Provision adjusted for discounting of cashflows	**863**	**896**	**33**	

5. CASHFLOW PROJECTIONS (1 of 2)

Cash flow projections for Investor Payout (including post acceleration interest) and Receiver Distributions

Cash flow forecasts are produced to enable the DMO to plan for the Crown to meet its cash obligations under the Guarantee Scheme, to inform the calculation of post acceleration interest liabilities for defaulting entities and to enable the provision for loss given default to be stated on a net present value basis. The process of forecasting cash flows is fraught with many uncertainties, this paper sets out the assumptions which underpin the forecast for the approval of the provisioning committee.

Investor Payout & Receiver Distribution Assumptions

The particular variables on which assumptions must be made are set out below:

Variable	Assumption
Which entities will default	The cash flow projection is based on the default of the entities for which provision has been made in the Oct accounts
The timing of any default	Default timing is based on key known triggers identified in provisioning papers – for instance, credit downgrades, liquidity walls, inability to renew prospectuses. Directors are likely to prompt a default in anticipation of the liquidity wall.
The claiming pattern of investors	As the Crown cannot impel investors to make a claim and investors are likely to be eligible for post acceleration interest it is likely investors will fall into three categories - those who need the money immediately and will put in a claim early, - those who will claim when their investment was due to mature (as this was when they expected the money), and - those who will hold off claiming in the interest of continuing to earn high interest rates. The early claimers are expected to net off against the late claimers and thus on average the maturity profile of the entity is the best indicator of claiming pattern. The actual maturity profile of SCF was used and for other entities a normal distribution around the average maturity date (with a 5% tail) was used.
The amount of distribution from receivers	The loss given default per entity has already been calculated for provisioning. This includes the cost of receivership. Therefore the receiver payout is assumed to be the gross amount paid out by Treasury less the loss given default.
The timing of distributions	For most entities the distribution pattern for National finance has been used as the model – the distribution took 3 years with the final payment being about 20% of the total. In SCF's case advice on big receiverships ($1b) was sourced from PWC who advised that the total process could take 6 years, distribution was thus assumed to be spread evenly over the 5 years subsequent to default. In Vision's case the distribution is assumed to be over a shorter period due to the fact that most assets are already in cash.
Discounted cash flows	Cash flows of both payout to investors and distributions from receiverships have been discounted to present value using GSF discounting rates. The net effect is to increase the anticipated loss given default by $76m, due to the extended timeframe for distribution from receiverships exceeding the benefit gained from the spread of the timing of payout.

Departmental costs of Administering the Guarantees

In addition to the actual Crown cash flows for investor monies paid out and receiver distributions, there are likely to be some additional costs incurred for risk monitoring/management and for managing the payout process itself. These costs would be covered by the PLA. These costs are estimated at a further $2.25m for investigations and $10m for payout which is allocated across the years based on the payout pattern.

6. CASHFLOW PROJECTIONS (2 of 2)

Timing Assumptions

Company Name (credit rating if available)	Default assumptions as at	Likely Timing For default	Average Maturity (months) from RB Aug reporting	Month of Average Maturity	Timeframe of % paid out by year: 2009/10 %	2010/11 %	2011/12 %	2012/13 %	2013/14 %	Proportion of receiver payout per year: 2010/11 %	2011/12 %	2012/13 %	2013/14 %	2014/15 %
South Canterbury Finance Limited	Half year accounts, credit rating downgrade	Mar-10	used actual maturity profile, adjusted for two month lag in payout in first year		15%	50%	19%	14%	2%	20%	20%	20%	20%	20%
Allied Nationwide Finance Limited	Weak credit/ fail to renew prospectus/ half year accounts	Mar-10	9	Jul-2010	40%	55%	5%			40%	40%	20%		
Vision Securities Limited	Liquidity, default imminent	Nov-09	13	Nov-10	25%	70%	5%			80%	20%			
[3]	Weak credit/ fail to renew prospectus from Nov to Jan	Jan-10	9	Jul-10	40%	55%	5%			40%	40%	20%		
Mutual Finance Limited					40%	55%	5%			40%	40%	20%		
[3]					40%	55%	5%			40%	40%	20%		
Viaduct Capital Limited					40%	55%	5%			40%	40%	20%		
[3]					40%	55%	5%			40%	40%	20%		
					40%	55%	5%			40%	40%	20%		
Cashflows per annum calculated														

Company Name (credit rating if available)	Gross cashflows: Total to be paid out incl interest $m	Expected amounts from receivership $m	Treasury Estimated loss-given default $m	Payout per year: 2009/10 $m	2010/11 $m	2011/12 $m	2012/13 $m	2013/14 $m	Receiver Distributions per year: 2010/11 $m	2011/12 $m	2012/13 $m	2013/14 $m	2014/15 %
South Canterbury Finance Limited	2,068	1,352	716	287	994	412	326	49	270	270	270	270	270
Allied Nationwide Finance Limited	219	168	52	85	122	12	-	-	67	67	34	-	-
Vision Securities Limited	39	11	28	10	28	2	-	-	9	2	-	-	-
[3]													
Mutual Finance Limited	7	5	2	3	4	0	-	-	2	2	1	-	-
[3]													
Viaduct Capital Limited	14	7	6	5	8	1	-	-	3	3	1	-	-
[3]													
Total cash flow	2,442	1,623	819	426	1,208	433	326	49	383	376	322	270	270
Net Present value of cashflows	2,302	1,406		426	1,163	395	279	39	369	343	275	216	202
Discount (benefit)/cost	(140)	217	77										
Loss Given Default post discounting			896										

7. SOUTH CANTERBURY FINANCE LIMITED

Issues

SCF is the largest finance company in New Zealand with a total lending book of $1,687m and a Crown Guaranteed deposit book of $1,855m covering in excess of 40,000 depositors.

SCF has grown rapidly over the past five years, and its policies and procedures have not kept pace with the growth. Overall, the management, risk management and lending of SCF is below the standard KordaMentha would expect of an organisation of SCF's size.

SCF's book covers most sectors, but key issues are in the Business ($555m) and Property ($542m) books. The key characteristics of the Property and Business books is the absence of covenants, annual reviews, valuations, high levels of capitalised interest, second charges, and a lack of risk grading. These are generally characteristics of poor lending practices. It is KordaMentha's assessment that a total of $1,100m of SCF lending is illiquid, the bulk of which is in the Property and Business books.

SCF have adopted an impaired asset expense of $106m for the year ending June 2009. KordaMentha estimate that this could be as high as $209m, and have identified an additional $233m of lending that exhibit signs of impairment. It is worth noting that KordaMentha have sampled SCFs book, and the quality of the information and state of the files have hampered their review. A full review could identify further impaired assets

If SCF provisioned at the level KordaMentha recommended there would be $101m of equity remaining in SCF (pre underwrite of $25m), which would put SCF in breach of its trust deed. SCF has several equity investments which were assessed by RBNZ at nil value. This has been revised based on information in the investigators reports to a recovery of 15% ($61m).

SCF requires additional cash equity injection to maintain sufficient capital levels and liquidity due to impairment of assets. Although discussed, Alan Hubbard is not believed to be in a position to inject sufficient equity into SCF to ensure its survival.

S&P downgraded SCF to BB+ negative outlook on the 21st of September due to several issue which SCF are working through which include;

1.the issuance of a new prospectus;
2.the appointment of three new independent directors; and
3.working through the issues with the USPP with the announcement that Torchlight Credit Fund LP ("Torchlight") led by Gorge Kerr has invested $75m in SCF (as a prior ranking charge). This allows the part repayment of the USPP which has been rescheduled to occur over the next five months.

The fact that the Torchlight loan is a prior ranking charge has been reflected in the Total Crown Loss figure below, and is a "Treasury" override to the RBNZ model. In addition, it should be noted that until the USPP is fully repaid the original terms of the facility remain, that is the make good clause remains until the USPP is repaid in full.

Although progress is being made, significant liquidity, asset quality and subsequently equity issues lead to the conclusion that it is probable that SCF will default under the existing Crown Guarantee

Recommendation

Based upon the information held by Treasury and the issues outlined above, it is considered probable that SCF will default under the existing Crown Guarantee and therefore a provision is required.

The loss given default has reduced from September 2009 due to the reduction in SCF's liabilities, with out a reduction in assets.

The quantum of the provision recommended is $716m, being the Crown's Share of the loss given default of $480m plus an allowance for post acceleration interest of $236m.

South Canterbury Finance Limited (BB+/Negative/Aug 09)

ASSETS		LIABILITIES	
Trade Creditors (@ 50%)	12	Guaranted Deposits	1,832
Fixed Assets (@ 10%)	10	Liquidation Costs (@ 5% of Book)	5
Equity Investments (@ 25%)	21	Other Liabilities (inc Bank Funding)	174
Cash (@ 100%)	67	Total Liabilities	2,011
Other Liquid Assets (@ 80%)	90		
Other Assets (@ 15%)	-	Equity (Loss)	(513)
Net Loan Book	1,304		
Total Adjusted Assets	1,498	Total Adjusted Assets	1,498
		Crown Share of Loss	480
		Post Acceleration Interest	263
		Total Crown Loss	743

8. ALLIED NATIONWIDE FINANCE LIMITED

Issues

ANFL has a total lending book in excess of $300m (including a securitised book of circa $100m) and a Crown Guaranteed deposit book in excess of $200m covering 6,323 depositors.

ANFL is owned by the NZX listed Allied Farmers Limited ("AFL"), which is a rural services provider.

ANFL has grown rapidly over the past two years as a result of the amalgamation of Allied Prime Finance Limited, Speirs Finance Limited and Nationwide Finance Limited. and its policies and procedures have not kept pace with the growth.

ANFL book covers several sectors (inc business, commercial, rural, property, factoring, floorplan finance and leasing). KordaMentha have indicated that the key issues are in the Consumer ($20m) and Property ($49m) books. A "Treasury Override" to the RNBZ model has been used to reflect this view.

KordaMentha do not consider ANFL provisioning methodology to be in line with best market practice for an entity of this size, and that the methodology adopted by ANFL materially underestimates the ultimate provisioning requirement for the entity.

ANFL have adopted an impaired asset expense of $7m for the year ending June 2009. KordaMentha estimate that this could be as high as $16m. Provisioning at this level ($16m) would cause ANFL and AFL to fail, however, any additional provisioning above the $7m put forth by ANFL will case a breach of the Total Liabilities to Total Tangible Assets covenant.

ANFL faces several challenges in the next six to eight months which could crystallise their failure, these are:

- The half year financial result (December 2009);
- The liquidity wall commencing March 2010;
- The March 2010 requirement for a min BB rating for entry into the extended DGS;
- The 2010 financial result a (June 2010) and audit opinion;
- Renewal of the prospectus (June 2010);
- The continuous disclosure requirements of AFL;
- The requirement to update the prospectus for a material adverse change; and
- Potential interest of the Securities Commission and/or the Companies Office in regard to the KordaMentha report.

A credit rating is a key milestone for ANFL, as it will enable them to raise longer dated money. ANFL are currently working through the process with Standard and Poor's, but due to the low level of capital, poor profitability, questionable credit quality and liquidity issues faced by ANFL it is considered unlikely that ANFL will receive a BB or better.

ANFL have a $5m underwrite (which we have treated as a cash injection essentially) from AFL to allow provisioning to take place at the $7m level, as without the underwrite ANFL will cause a breach of the Total Liabilities to Total Tangible Assets covenant. This facility currently has $3.9m allocated to it.

Without a BB credit rating ANFL would be ruled out of the Government Guarantee scheme extension, which would crystallize a significant liquidity issue from March next year (as the asset quality of ANFL's book is such that they will not be able to liquidate their assets fast enough to repay the maturing debt) and ANFL is expected to default under the current Crown Guarantee due to liquidity issues brought about by a significant asset quality issues.

With a BB rating, ANFL still have significant management and asset quality issue to overcome, which will require a significant change in management direction and a significant equity injection

Recommendation

Based upon the information held by Treasury and the issues outlined above, it is considered probable that ANFL will default under the existing Crown Guarantee and therefore a provision is required.

The quantum of the provision recommended is $52m, being the Crown's Share of the loss given default of $36m plus an allowance for post acceleration interest of $16m.

Allied Nationwide Finance Limited

ASSETS		LIABILITIES	
Trade Creditors (@ 50%)	2	Guaranted Deposits	204
Fixed Assets (@ 10%)	0	Liquidation Costs (@ 5% of Book)	5
Equity Investments (@ 25%)	-	Other Liabilities (inc Bank Funding)	6
Cash (@ 100%)	4	Total Liabilities	215
Other Liquid Assets (@ 80%)	28		
Other Assets (@ 20%)	4	Equity (Loss)	(32)
Net Loan Book	139		
Total Adjusted Assets	182	Total Adjusted Assets	182
		Crown Share of Loss	36
		Post Acceleration Interest	16
		Total Crown Loss	52

9. VISION SECURITIES LIMITED

Issues

VSL is a mezzanine property finance lender with a book of $34m, made up of 16 loans.

The key metrics of the VSL book are:
- 60% of the book is completed stock or land banks;
- 80% of the book is due to expire before 31 December 2009;
- 20% of the book is active land developments;
- 97% of the book has interest capitalising;
- 78% are second mortgages, but an additional 19% of mortgages are duel first and second mortgages; and
- Many loans are subordinated and postponed, and in some cases VSL are paying the first mortgagee's interest.

VSL has no banking facilities, but does have $10m in cash, and this is being consumed at a rate of $0.300m to $0.500m per month due to operating costs and the payment of first mortgagee interest (VSL has only nominal cash flow from its book). At this rate, VSL have approximately two years before they run out of cash and fail.

VSL has a provision for impaired loans of $2m in its annual accounts to 31 March 2009. Deloitte's view on the likely level of provisioning required which is between $19m and $28m. This will make VSL insolvent.

VSL is not expected to gain a BB credit rating from Standard and Poor's. This would rule VSL out of the extension to the Government Guarantee scheme, and will significantly effect investment and reinvestment rates in VSL.

VSL has $24.5 million (65.8%) of VSL's secured debenture stock is due to mature before October 2010. The repayment of this level of debenture funding will crystallize a significant liquidity issue for VSL, as the asset quality of VSL's book is such that they will not be able to liquidate their assets to repay the debenture holders without raising additional debenture funding which it is unlikely that they will be able to do with out the Crown Guarantee, and therefore will fail.

The proposed recapitalisation plan which would have seen VSL purchase from Arrow International Group Limited $5m of shares in the related company Vision Senior Living Limited essential for a nominal price will not now occur.

Without the recapitalisation, Vision advise they will be in breach of their capital requirements under the Trust Deed. Vision are now considering whether a management lead wind-down of the business is feasible (this is to be discussed with their Trustee). If not considered feasible, it is considered more likely than not that the Trustee will move to appoint a receiver.

Recommendation

Based upon the information held by Treasury and the issues outlined above, it is considered probable that VSL will default under the existing Crown Guarantee and therefore a provision is required.

The quantum of the provision recommended is $28m, being the Crown's Share of the loss given default of $25m plus an allowance for post acceleration interest of $3m.

ASSETS		LIABILITIES	
Trade Creditors (@ 50%)	0	Guaranted Deposits	36
Fixed Assets (@ 10%)	-	Liquidation Costs (@ 5% of Book)	2
Equity Investments (@ 25%)	-	Other Liabilities (inc Bank Funding)	2
Cash (@ 100%)	0	Total Liabilities	40
Other Liquid Assets (@ 80%)	12		
Other Assets (@ 20%)	-	Equity (Loss)	(27)
Net Loan Book	0		
Total Adjusted Assets	12	Total Adjusted Assets	12
		Crown Share of Loss	25
		Post Acceleration Interest	3
		Total Crown Loss	28

10. COMMENTARY ON SMALLER ENTITIES PROVISIONED FOR

No	RBNZ Relative Riskiness	Company name	*Ranking* Liquidity[1] %	Asset Quality[2] %	Income margin[3] %	Capital Ratio[4] %	Guaranteed Depositors #	Guaranteed Deposits $m	Crown Share of Loss	Post Acceleration Interest	Total Crown Loss
1	High	Viaduct Capital Limited	4	54	12.2	2.9	196	12.5	5	1.0	6
2	High										[3]
3	High										
4	High	Mutual Finance Limited	11	60	6.7	12.6	-	6	2	4	6
5	High										[3]
6	High										
						Total	3,306	107	15	8	23

Notes
[1]Liquid assets + 50% committed facilities as a percentage of guaranteed deposits
[2]Impaired + past due + 75% Cap Interest + 50% restructured loans as a percentage of total loans
[3]Net margin: Annualised net-interest-income + Fee Income to gross loans
[4]Capital ratio methodology utilising the proposed capital framework for NBDTs
Entities shaded have been inspected.

($m)	Viaduct Capital Limited	[3]	Mutual Finance Limited	[3]
Trade Creditors (@ 50%)	0		0	
Fixed Assets (@ 10%)	0		-	
Equity Investments (@ 25%)	-		-	
Other Assets (RBNZ View)	1		0	
Cash (@ 100%)	0		1	
Other Liquid Assets (@ 80%)	-		-	
Net Loan Book	6		4	
Total Adjusted Assets	**8**		**5**	
Guaranted Deposits	13		6	
Liquidation Costs (@ 5% of Book)	1		0	
Other Liabilities (inc Bank Funding)	0		0	
Total Liabilities	**13**		**7**	
Equity (Loss)	**(6)**		**(2)**	
Crown Share of Loss	**5**		**2**	
Post Acceleration Interest	1		4	
Total Crown Loss	**6**		**6**	

Issue

Each of these 6 entities has significant credit issues combined with either a low level of capital, poor profitability, and/or eligible for the DGS extension (if they seek a credit rating).

The asset quality of all six entities in this group is such that they will not be able to liquidate their assets to repay the debenture holders without raising additional debenture funding, which they will be unable to do without entry into the extended DGS, therefore it is considered probable that each of these six entities will fail and a provision should be made for each entity.

[3]

11. WATCH LIST

No	RBNZ Relative riskiness	Company name (credit rating if available)	*Relative Risk Ranking measures* Liquidity[1] %	Asset Quality[2] %	Income margin[3] %	Capital Ratio[4] %	Guaranteed Depositors #	Guaranteed Deposits $m
1	High	Equitable Mortgages Limited (BB/Negative/Feb 09)	11	59	0.8	7.9	5,032	163
2	High	[redacted]						
3	Medium	[redacted]						
4	Medium	[redacted]						
5	Medium	[redacted]						
6	Medium	Rockforte Finance Limited	9	27	9.7	17.2	114	4
7	Medium	[redacted]						
8	Medium	[redacted]						
9	Medium	[redacted]						
10	Medium	[redacted]						
11	Medium	[redacted]						
12	Medium	[redacted]						
						Total	68,944	2,253

Notes
[1]Liquid assets + 50% committed facilities as a percentage of guaranteed deposits
[2]Impaired + past due + 75% Cap Interest + 50% restructured loans as a percentage of total loans
[3]Net margin: Annualised net-interest-income + Fee Income to gross loans
[4]Capital ratio methodology utilising the proposed capital framework for NBDTs
Entities shaded have been inspected.

Watch List Outline

All 12 of these entities are ranked either high (2) or medium (10) risk by the RBNZ and it is reasonable therefore to draw the conclusion that any deterioration of the liquidity, credit quality or capital metrics is likely to result in a provision being required to be made. All of these entities form part of the stage two investigation/analysis process, and will be monitored to ensure that any deterioration in their key financial metrics is detected to enable a provision to be made as necessary.

Of the 12 entities 5 [redacted] and **Rockforte Finance Limited**) were provisioned for in September 2009 (they formed part of Group Three). The Capital Ratio, Asset Quality and Liquidity of these entities is such that they are no longer considered to have a greater than 50% chance of failing, however, they do have asset quality, liquidity, capital adequacy and/or liquidity issues that require ongoing monitoring.

Of the 12 entities 3 (**Equitable Mortgage Limited** [redacted]) have been inspected, but are not considered to have a greater than 50% chance of failing, however, they do have asset quality, liquidity, capital adequacy and/or liquidity issues that require ongoing monitoring.

Of the 12 entities 4 [redacted] have had limited focus on them to date, but the Capital Ratio, Asset Quality and Liquidity of these entities is such that they require ongoing monitoring.

12. REMOVAL OF THE FORMER GROUP THREE - SMALL ENTITIES

Former Group Three Entities

Without the benefit of the extended deposit guarantee scheme (which none of these entities are expected to participate in due to cost or credit rating reasons), the entities in the table below would be competing for deposits against other Finance Companies, Buildings Societies and Credit Unions, who hold a Crown Guarantee which may impact their ability to raise funds from the public and this survive. However, when a line by line analysis of these entities in completed it become apparent that currently all of these entities have adequate credit quality and other beneficial factors (strong parent etc) and thus should not be provisioned for at this time.

Company name (credit rating if available)	Last month rank	Material movement	*Relative Risk Ranking measures* Liquidity[1] %	Asset quality[2] %	Income margin[3] %	Capital ratio[4] %	Guaranteed depositors #	Guaranteed deposits $m
							57,946	214