

Half-Yearly Report for the period ended 31 December 2011

People first.



Half-Yearly Report

for the period ended 31 December 2011

The Board and management of Heritage Bank Limited are pleased to announce our results for the six months ended 31 December 2011. The financial statements for this period have been the subject of a review by our external auditors. Key performance measures are set out in Table 1.

- Our profit performance for the six months to December 2011 was extremely good, given the difficult market conditions.
- The \$21.05 million pre-tax profit was up 5.4% on the \$19.97 million recorded in the same period of 2010, despite continuing high costs of funding and margin pressure. Heritage lived its *People first* philosophy by continuing to offer members the best mortgage interest rates possible, including being one of the first financial institutions to pass on the full 25 basis points cut after the Reserve Bank reduced the official cash rate in December. Heritage's rates remain far better than the big banks and most other Authorised Deposit-taking Institutions (ADIs).
- Profit after tax is also up 1.9% to \$14.74 million compared to the same period last year.
- Retail deposits continued to grow strongly, increasing by 11.95% or \$205.32 million compared to \$183.41 million in the same period last year. This trend reflected our continued competitiveness in the term deposit market.
- National and international factors have caused a significant contraction of the total home loan market in Australia, as well as generating fierce competition among ADIs and other mortgage lenders. Those factors are reflected in the decrease in our loan approvals, which were down to \$568.94 million compared to \$806.41 million in the same period last year.
- One of the challenges for a customer-owned organisation like Heritage is balancing the need for profits to provide capital to grow the business, while also providing members with attractively priced products and services.

Table 1

	Six months to 31 December 2011	Six months to 31 December 2010	Increase (Decrease)
	\$ million	\$ million	%
Profit before tax	21.05	19.97	5.4
Profit after tax	14.74	14.46	1.9
Loan approvals	568.94	806.41	(29.4)
Retail deposit growth	205.32	183.41	11.95

Details of key period end information are set out in Table 2.

- Total consolidated assets under management grew 0.4% from \$8.045 billion at 30 June 2011 to \$8.078 billion at 31 December 2011. This growth is being managed around the various pressures in the best interests of Heritage members.
- The regulatory ratios of capital adequacy and liquidity are managed to stay comfortably above regulatory guidelines and internal benchmarks. Our capital adequacy ratio has decreased slightly in this period. That reflects a number of factors, including the redemption of \$35 million of term subordinated debt and the fact that the industry is still waiting on a final capital adequacy standard from the Australian Prudential Regulation Authority (APRA). Once APRA does release the standard, Heritage intends investigating options to issue a qualifying capital instrument.
- The rate of mortgage loan arrears over 30 days at 31 December 2011 was up

slightly at 0.53%, but the increase is off an extremely low base by comparison with others in the industry. This remains an excellent figure, which reflects prudent underwriting and management.

HERITAGE BANK

Our change of name to Heritage Bank in December represented an important strategic milestone that will better position us for future success. A key to our ongoing growth lies in expanding the Heritage brand beyond the south-east corner of Queensland. The name Heritage Building Society, while meaningful to many people in the Darling Downs region, did not resonate outside our heartland and interstate. Potential members simply did not understand what a "building society" was all about. As Heritage Bank, our function and role is immediately recognisable. It will provide greater cut-through in a crowded marketplace and clarify our proposition to members.

The change of name on 1 December took effect smoothly and with little or no impact on our customers, which is a reflection

Table 2

	31 December 2011	30 June 2011
Total consolidated assets	\$8.078 billion	\$8.045 billion
Retained profits	\$276.09 million	\$262.94 million
Capital adequacy ratio	12.99%	14.14%
Liquidity ratio	19.09%	18.88%
Mortgage loan arrears	0.53%	0.40%

of the professionalism and dedication of all Heritage staff. The change has been accepted well by members. We have placed great emphasis on telling our members that this was a change of name only – there will be no change to our mutual ownership structure or our focus on providing the best possible value to members.

EXPANSION OF BROKER NETWORK

Changing our name to Heritage Bank is allied to another key strategic move we announced in December – the decision to expand our mortgage broker network throughout Australia. We had previously originated loans via mortgage brokers in Queensland, New South Wales, Victoria, South Australia and the ACT for up to 15 years. We announced in December that we would expand that network to include Western Australia, Tasmania and the Northern Territory. That decision means Heritage will now have home loan customers throughout the country and will be a truly national player in the home loan market. Our change of name to Heritage Bank is an advantage for us as we seek to establish a foothold in these markets and increase our loan volumes in the rest of Australia.

HIGHEST SATISFACTION RATING IN AUSTRALIA

Heritage's *People first* philosophy has long been reflected in our outstanding customer satisfaction results. That has been no different in this period. In fact, Heritage's performance has been at an all-time high.

We ended 2011 with a main financial institution (MFI) customer satisfaction rating of 97.1% in Roy Morgan Research surveys for the six months to December. This was the highest customer satisfaction rating that Heritage has ever scored since the survey started in 1996. It is easily the highest satisfaction rating of any bank in Australia, and in fact is the highest MFI satisfaction rating of any ADI in the country. Our consistently superior customer satisfaction rating is a potent measure of our success in living our *People first* values.

SECURITISATION DEAL

This six-month period began with the finalisation in July of an \$800 million public securitisation term issue, our tenth and largest domestic securitisation transaction. This was our first public residential mortgage backed securities (RMBS) transaction in five years, representing a return to one of our traditional sources of funding and helping with the diversification of our funding mix.

RATINGS

Ratings agency Moody's reviewed Heritage during this six-month period and confirmed our rating of A3/P-2 with a Stable outlook. We believe this is an accurate reflection of Heritage's standing, given our continuing strong financial results and track record of sound economic management. Less understandable was Standard & Poor's (S&P's) decision to downgrade Heritage a notch. It is worth noting that this decision came after a change to S&P's rating methodology, and

at the same time as a number of other Australian financial institutions had their rating reduced by S&P. Still, we believe their decision was inexplicable.

THE HERITAGE WAY

People first underpins the way we do business. We exist for our members who are our customers. We seek to provide our customers with competitively priced financial services in a customer friendly way.

We have an engaged staff who live the Heritage values and provide the service so prized by our members. Our ability to continue providing that service along with great products will underpin our future success.

Brian R Carter
Chairman

John F Minz
Chief Executive Officer

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