

# Half-Yearly Report

For the period ended 31 December 2012

People first.

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The Board and management of Heritage Bank Limited are pleased to announce our results for the six months ended 31 December 2012. The financial statements for the period have been reviewed by our external auditors. Key performance measures are set out in Table 1.

- Our profit performance for this period was excellent, reflecting both strong underlying business activity and several abnormal items that contributed to higher than normal profit growth.
- The \$27.887 million pre-tax profit was up 32.5% on the \$21.054 million in the same period the previous year. A large part of this increase is due to the gain made on the sale of Visa shares and fair value adjustments required under Australian Accounting Standards and International Financial Reporting Standards (IFRS). The underlying profit which excludes the one-off sale of Visa shares and other IFRS adjustments has risen from \$20.511 million to \$23.855 million (16.3%). This underlying performance remained strong in a competitive and subdued lending market.
- Profit after tax was \$19.558 million, up 32.7% on the corresponding period in the previous year.
- Heritage continues to champion its *People first* philosophy which focuses on providing its customers with the best possible rates, products and services. This is reflected in the fact that Heritage tries to ensure that its retail banking offering remains consistently better value than the big banks and many other ADIs.
- Heritage experienced marked growth in lending this period. Loan approvals totalled \$804.94 million, a 41.5% increase on the \$568.94 million achieved in the same period in 2011. This was a factor of the expansion to our nationwide broker arrangements, new branches, the new discount variable lending product and market conditions that negatively affected lending in the corresponding period of 2011. Heritage continues to offer extremely competitive rates and great service, which translates into excellent performance in the marketplace.
- Retail deposit growth also increased significantly, up 47.8% from \$205.32 million to \$303.52 million. This is a remarkable achievement in an environment where all ADIs were competing fiercely on term deposit rates for a share of domestic investment funds.

TABLE 1.

	Six months to 31 December 2012	Six months to 31 December 2011	Increase (Decrease)
	\$ million	\$ million	%
Profit before tax	27.89	21.05	32.5
Profit after tax	19.56	14.74	32.7
Loan approvals	804.94	568.94	41.5
Retail deposit growth	303.52	205.32	47.8

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

- Heritage continues to face the ongoing issue of balancing the need for profits to boost retained earnings and capital, while also providing customers with attractively priced products and services. With prudential requirements tightening in the post-GFC environment, the pressure on this balance is likely to grow.
- This pressure is reflected in the ongoing slow growth in total consolidated assets, which increased 0.6% from \$8.221 billion to \$8.271 billion in the six months to 31 December 2012.
- The regulatory ratios of capital adequacy and liquidity are managed to stay comfortably above regulatory guidelines and internal benchmarks. Both declined marginally in the six months to 31 December 2012, with the capital adequacy ratio at 12.14% and the liquidity ratio at 18.02%.
- Heritage's rate of mortgage loan arrears over 30 days was 0.44% at 31 December 2012, a slight decrease from the 30 June 2012 figure. Heritage is extremely proud of this achievement, which is around one third of the industry average. This flows from the extremely responsible approach we take in assessing loan candidates to ensure that our customers can afford the debts that they will incur. If people do encounter payment difficulties, we work closely with them to set up a repayment plan that suits both parties.

## CORPORATE RATINGS

In late 2011, Standard & Poors' (S&P) downgraded Heritage to BBB-/A3 after a world-wide review of their ratings methodology. Heritage disputed the one-size-fits-all approach with S&P, but they would not review their decision, which we contend was also based on erroneous assumptions. Heritage removed S&P from our panel of ratings agencies as we believed their rating was not a fair assessment of our organisation. We continue to hold strong ratings from other agencies. These include Moody's at A3/P2 and Fitch BBB+/F2. Heritage issued \$227.5 million in senior bonds in 2012. Australia Ratings provided a BBB+ rating for the transaction. These independent assessments of Heritage's quality and resilience speak volumes about our long-term sustained financial, risk management and operational outcomes.

## DISTRIBUTION MEETING OUR CUSTOMERS' NEEDS

As a customer-owned bank, Heritage prides itself on a *People first* approach that is continually working to improve the customer experience. In 2012, Heritage opened two new full-service branches, in the Brisbane CBD and in Bundaberg, to broaden our geographic footprint. We also took the innovative step in February 2012 of expanding our mortgage broker network nationwide, so that we became a truly national player in the home loan market. Heritage now has offices in Sydney, Melbourne, Adelaide, Perth and Brisbane to administer and assist our mortgage broking partners. By the end of December 2012, Heritage had written approximately \$45 million in home loans in the three new states of Western Australia, Tasmania and the Northern Territory. The move has been so successful that Heritage is now moving to make personal loans available throughout Australia as well.

**TABLE 2.**

	31 December 2012	30 June 2012
Total consolidated assets	\$8.271 billion	\$8.221 billion
Members' funds	\$314.73 million	\$296.60 million
Capital adequacy ratio	12.14%	12.51%
Liquidity ratio	18.02%	19.09%
Mortgage loan arrears	0.44%	0.47%

## FINANCIAL BENEFITS TO CUSTOMERS

Heritage lives its mutual status as a key advantage in delivering a comprehensive suite of products and services to customers at competitive rates, with service excellence a point of differentiation.

That approach has translated into significant financial benefits for our members. Independent analysis by CANSTAR found that Heritage customers were more than \$33.8 million a year better off through banking with Heritage rather than one of the big four banks\*. Our customers gained a \$11.4 million benefit through better fees, and around \$22.4 million because of better interest rates on both deposits and loans. These benefits are shared by all our customers.

## EXTERNAL RECOGNITION

Importantly, external recognition validates our success in delivering a great customer experience. In 2012, Heritage achieved the following accolades

- AFR Smart Investor awarded Heritage the Mutual Bank of the Year title.
- Canstar awarded us five stars for 16 of our home loan products – the most of any financial institution in Australia.
- Heritage was a winner of the Top 5 Bank and Top 5 Home Loans Provider awards in the 2012 Mozo People's Choice Awards.
- Heritage won the Recommended Employer in the Australian Business Awards for the second year in a row.
- Heritage won the HR Team of the Year in the Australian HR Awards, as well as the HR Team award and the Talent Management award in the Australian Human Resource Institute national awards.

## OPTUS PARTNERSHIP

In December 2012, Heritage announced an exciting collaboration with Australia telecommunications giant Optus and global payments firm Visa to develop a product that enables people to use their smartphone as a virtual wallet, paying for day-to-day purchases with a swipe of the phone. Trials and further development are underway with a view to a commercial launch later in 2013. Heritage is contributing its prepaid card expertise to the project. The contactless payment system will allow customers to use their smartphones to "wave and go" to pay for day to day purchase transactions such as buying coffee, petrol, grocery items and movie tickets at hundreds of thousands of retailers nationally and internationally where Visa payWave is accepted.

The collaboration with Optus and Visa holds exciting prospects for Heritage. Our traditional strength in payment systems has now positioned us to be a major player in mobile payments innovation. This provides funding, non-interest income and brand benefits.

## EMERGING BUSINESS STREAMS

Heritage's sustained superior results come from many facets – brand, culture, leadership and strategy. In relation to strategy, Heritage has made the conscious decision to allocate priority and resourcing to our new Emerging Business Streams (EBS). This area of operations introduced and is optimising the Retirement Savings Account. One of the most exciting outputs of the EBS is the prepaid card schemes. Heritage is one of the largest issuers of prepaid card schemes in Australia. We issue all of Access Prepaid and Travelex travel cards in Australia. Heritage issues both the Australian currency and multi-currency Load&Go card through Australia Post. We issue in five currencies and manage the Load&Go foreign currency operations. Our EBS team are also coordinating our involvement with the Optus contactless card project.

\*As at December 2012

## COMMUNITY BANKING BENEFITS

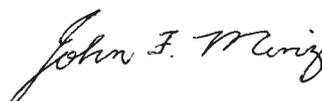
Community is one of Heritage's core values and is lived by the organisation, as well as the individuals who work here. Our community focus is another way we translate the mutual philosophy into practice. Heritage operates seven community branches across southern Queensland, which are joint ventures between Heritage and local investors. Heritage established the community branches in areas which were being abandoned by other banks, to ensure local residents had access to a full banking service in their local area. One function of the community branches is to return a share of the profits they make to the community via grants to worthwhile local events, organisations and charities. In 2012, Heritage hit the milestone of \$22 million that the community branches have returned to their local communities via funding

grants, wages, rents and payments for other goods and services. This included providing grants from the Millmerran and Karalee community branches for the first time ever in December 2012.



**KERRY J. BETROS**

Chairman



**John F Minz**

Chief Executive Officer

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