

Half-Yearly Report for the period ended 31 December 2010



# Half-Yearly Report

## for the period ended 31 December 2010

The Board and management of Heritage Building Society Limited are pleased to announce our results for the six months ended 31 December 2010. The financial statements for this period have been the subject of an audit review.

Key performance measures are set out in Table 1:

- Our performance for the six months to December 2010 was extremely solid, given the prevailing market pressures. The \$19.97 million pre-tax profit was slightly higher than the \$19.45 million recorded in the first six months of calendar 2010, though down on the six months to December 2009. Higher costs of funding in 2010 were the key reason for the difference in profitability. Despite those funding costs, Heritage restrained mortgage interest rate increases through most of 2010 to avoid additional cost imposts on our members.
- Heritage's *People first* philosophy was reflected in the Society recording the highest customer satisfaction of any banking institution in Australia in Roy Morgan Research as at December 2010.
- After holding back as long as possible, the Society took the difficult decision in November 2010 to increase most lending rates by more than the Reserve Bank's cash rate increase. Even after those increases, Heritage's rates remain far better than the big banks and most other ADIs. Based on current projections, we expect the Society to generate profits for the full year similar to those for the year ended 30 June 2010.
- A surge in retail deposits in the half-year to December is helping with that performance improvement. Retail deposits grew by \$183 million in this period, a 64% increase on the same period in the previous year. Competition for retail funding remains at a very high level and Heritage carried out a major restructure of interest rates and transaction fees on its savings products during this six-month period to help attract a higher level of retail funds.

Table 1

	Six months to 31 December 2010	Six months to 31 December 2009	Increase (Decrease)
	\$ million	\$ million	%
Profit before tax	19.97	22.89	(12.8)
Profit after tax	14.46	16.05	(9.9)
Loan approvals	806.41	830.74	(2.9)
Retail deposit growth	183.41	111.56	64.4

A key initiative was the arrangement entered into with Westpac in October giving Heritage members direct fee free access to almost 3,000 ATMs around Australia.

- Heritage's actions have proven extremely successful and total retail deposits at 31 December 2010 grew to slightly in excess of \$3.5 billion.
- One of the challenges for a member-owned organisation like the Society is balancing the need for profits to provide capital to grow the business while also providing members with attractively priced products and services. Our full-year financial results will reflect that balance, as it has in previous years.
- Heritage also faces an additional delicate balancing act between lending at levels which will enable the business to grow and at the same time being able to fund the new lending at reasonable rates. The margin pressure continues as older and less expensive funding facilities are retired and replaced

by more expensive funding facilities. The total mortgage loan portfolio at 31 December 2010 was approximately \$6.1 billion of the total loan book of \$6.4 billion.

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

- Total consolidated assets grew 1.9% from \$7.56 billion at 30 June 2010 to \$7.71 billion at 31 December 2010. This growth is being managed around the various pressures to ensure that the best interests of the members of the Society are maintained.
- The regulatory ratios of capital adequacy and liquidity are managed to stay comfortably above regulatory guidelines.
- The rate of mortgage loan arrears over 30 days at 31 December 2010 was up slightly at 0.43%, but the increase is off an extremely low base by comparison with others in the industry. Increases in underlying cash rates are probably one of the significant factors in this increase. Notwithstanding this, the Society has

Table 2

	31 December 2010	30 June 2010
Total consolidated assets	\$7.71 billion	\$7.56 billion
Retained profits	\$245.5 million	\$231.4 million
Capital adequacy ratio	14.33%	13.85%
Liquidity ratio	18.45%	19.21%
Mortgage loan arrears	0.43%	0.33%

a very good portfolio, which reflects prudent underwriting and management.

### Natural disasters

Australia has experienced widespread natural disasters this summer. Flooding has created a substantial impact in Queensland, where Heritage is based. The Society has responded in line with our *People first* philosophy through a range of measures designed to help both members and the wider community.

The total financial assistance that the Society has provided to flood relief, through both direct donations and other measures, is now just under \$300,000. The Society has contributed \$100,000 to the Queensland Premier's Disaster Relief Appeal; \$15,000 to the Grantham Flood Support appeal; and a further \$15,000 to the Toowoomba Disaster Appeal set up by the Toowoomba Chamber of Commerce. In addition, Heritage temporarily charged no direct fees on its ATM fleet in south-east Queensland and abolished application fees on its personal loans for a month as well. The Society has a robust hardship relief policy in place and, as expected, we have had an increase in the number of hardship applications, mainly due to people whose incomes have been affected by the flood impacts.

At this stage the full financial impact of the floods is difficult to determine. The Society has only a very small number of mortgage secured properties which have been affected by the floods – only 0.22% by value. There is still only an extremely small percentage of members – less than 0.55% – who are subject to hardship

arrangements. Bearing this in mind we do not expect any significant financial impact from the disasters or hardship arrangements as employment returns to normal levels. The Society had one branch completely inundated however the financial impact of this and damage to other property is covered by insurance.

### Regulatory issues

The Society has obtained an Australian Credit Licence. This was a requirement of the new National Credit Code. There has been a substantial cost and work required to meet the requirements of the new legislation although we do not think there is a commensurate benefit to the Society or its customers.

Since 1 July 2009 Heritage has provided financial planning services through a joint venture arrangement with HeritageMAP Pty Ltd. The Society has now had its Australian Financial Services Licence expanded to include the ability to undertake financial planning on its own account. This new arrangement is expected to commence on 1 March 2011.

The Australian Government's Competitive and Sustainable Banking announcement in December covered three broad streams of reform to empower consumers to get a better deal in the banking system, to support smaller lenders so more competitive pressure could be put on the big banks and sustainability of the financial system so it will continue to provide reasonably priced credit to Australian households and small business. While there is support for

some of the issues raised we watch with interest to see if there are any substantial benefits which might flow to smaller organisations, most of which are member-owned. We hope that the realities are reflective of all the praise the Government has heaped upon itself.

### 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 the continuing success of the business and provide the service so valued by our members.



Brian R Carter  
Chairman



John F Minz  
Chief Executive Officer

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Registered Office:  
6th Floor, 400 Ruthven Street, Toowoomba, Qld 4350  
Postal Address:  
PO Box 190, Toowoomba, Qld 4350  
Telephone 07 4690 9000 Fax 07 4690 9090

[www.heritageonline.com.au](http://www.heritageonline.com.au)

Heritage Building Society Limited ABN 32 087 652 024  
AFSL/ACL 240984 DMS 1102040B