

CEO'S SPEECH
Annual General Meeting
19 October 2016

Good Afternoon

Thank you Chairman and I would like to extend the welcome and thank you all for taking the time to attend this afternoon.

Firstly, I'd like to say how excited and honoured I am to be with you today, just a month or so short of the first anniversary of my appointment as CEO.

It's been a busy, but very rewarding period as we set the Bank on a new course, made easier because of our solid foundations, but nonetheless challenging when facing a rapidly changing competitive market place.

Our Bank is in a strong financial position and has built its business to be the largest customer-owned bank in Australia. We are very proud of this fact however, it's a mantle that needs to be earned and we can't afford to rest on our laurels. Consequently we have been working hard on redefining our corporate strategy and concentrating on the things that really bring value to our members.

While it's still early days – we have seen our efforts in reshaping our business start to be reflected in our results.

Our asset position of \$8.44b reflects a strong and well diversified book, slightly down from our reported position last year of \$8.56b, as a result of a more active management of our liquidity position, throughout the year. Liquidity reduced from 19.37% in 2015 to 15.94% in 2016 as we adjusted our requirements to reflect a reduced lending demand in the first half of the year.

Overall our loan approvals of \$1.78b were down 3.45% from the previous year; reflecting in the main a slower start in the first six months. This improved significantly in the second half of the year, achieving \$970m growth compared to \$810m in the first half. Our second half growth rate of 7.1% annualised exceeded APRA's reported system growth of 6.7%.

This second half momentum reflects an increased focus on the fundamentals of our business and our decision to differentiate our business into proprietary (branch) and third party (broker) channels. While we have achieved immediate uplifts in our lending business from this decision, we have also achieved a significant improvement in our retail funding base, growing our deposits strongly to \$5.16b, up \$294m or 6.06%, again primarily in the second half of the year.

Pleasingly, our renewed focus is also reversing the trend on customer growth, which for the last few years has largely been static. Customer numbers grew from 308,000 in August 2015 to 316,000 in August 2016, or 2.8%.

While the movement has been modest, it is continuing to trend upward, an important and positive sign for our Bank and for the Mutual sector in general.

We are a retail bank and as the old saying goes – retail is detail. We have instigated a renewed retail focus on our business, together with the corresponding disciplines of ensuring we are delivering excellence in customer service and creating member value through building a Bank that we are all proud of. This continues to be reflected through the asset quality of our book which once again performed to industry lows with a 30 day mortgage arrears rate of 0.30% at 30 June - well below the average of the big banks at 1.00%

So, I'm pleased to report that the combined effects of active management and focus on the business of providing real value to our customers has resulted in a strong and respectable pre-tax profit of \$51.11m, up 6.46% on the previous year profit before tax of \$48.01m. After tax profit was up 7.55% to \$36.14m from the \$33.61m after tax result reported in 2015.

Likewise, our key prudential ratios of capital and liquidity remain well above prudential standards at 13.95% and 15.94% respectively, with capital improving from 13.37% in the prior period.

While our results are sound and solid, we do believe there is room for improvement.

Both the Chairman and I have spoken a little about a change to our strategy. Importantly, there is no change to our People *first* philosophy, nor is there a change from our community commitment and our regional roots. There is however, a recognition that we need to get back to the core business of helping people achieve their financial ambitions – that means we need to be easier to do business with, to continue to find ways to say yes more often, and to continue to deliver the Heritage service we are renowned for, across a whole new range of delivery channels.

We've defined our strategy through a series of goals and values and it starts with our vision and mission:

At Heritage, we are Passionate about Helping People and we are serious about delivering a Great Customer Experience Every Time – and this means delivering that service through a choice of channels, consistently, professionally and at the time that our customers choose to do their banking.

We think our goals are pretty easy to understand and go to the heart of being a Mutual Bank. We believe we are successful when we are:

- Attracting and growing new clients – we need to continue to grow in order to provide the mutual benefit of access to funds and protection of wealth at competitive prices.

We are successful when we are:

- Building and maintaining our existing clients – recognising and respecting our current customers and encouraging them to do more with us to grow and share the benefits of mutuality.

We are successful when we are:

- Creating a strong Bank – that is profitable and well run, has a strong balance sheet and can continue to grow and provide financial support that enables our customers to achieve their financial goals.

We are successful when we are:

- Attracting and growing passionate people – we are proud of the Heritage difference and our team members who have that special something that helps set us apart. We are a proud Australian company and local employer, creating opportunities for people to make a career in financial services – a sector that does so much for the economies and communities where we operate.

And we are proud of our values:

- Passion
- Integrity
- Respect
- and Courage

We won't back down from doing what ultimately is in the best interest of our members. This means making tough decisions, but when we do so, we make them with our values firmly in mind. The recent decision with mini branches is an example.

It wasn't an easy decision, but before we acted we examined each site on an individual basis and made sure our customers had alternatives. We engaged with stakeholders and we looked to make sure our customers weren't impacted financially.

We acknowledge this meant change for some people, and change is challenging, so we are working through cases individually where appropriate.

There are many changes facing our business and our industry. In fact, change is the one constant in our business that we can bank on.

For us, we are facing the challenge of a new way of banking as our customers demand and expect banking services that are modern, adaptive, and available 24/7 through a variety of channels. The digital age is well and truly upon us and this creates enormous demands for traditional banking models like Heritage.

We have become accustomed to operating as a physical banking model - via our branches, ATMs, and call centres - with recently added digital

capability through smart apps and mobile banking. In effect we're acting like a physical bank with a digital presence.

The new world will be different, and we are already seeing it with the new Fintech start-ups and the demands of the millennials. To be truly relevant in this new market, we need to create, operate and think like a digital bank. For us, this means becoming a digital bank with a physical presence.

There is a difference in the two statements and it's not subtle, in fact it creates an enormous challenge for all of us, including the investment challenge that we face in making this transformation.

As a mutual, we rely on our profitability to fund our capital base. Traditionally, this has been returned to customers primarily through the pricing on our product range, but it is also needed to fund our capital investment program and our strategic goals. Innovation and change require investment and a different way of looking at the things we are currently doing.

We see this as part of becoming a Better Bank. With a rich 141 year history, we have always been able to move and adapt, often as one of the early innovators. This approach made us the Bank we are today and we now need to continue to make decisions that will allow us to grow and prosper and allow us to become the Bank of the future – to continue to hold the mantle of Australia's largest customer-owned Bank.

As part of our Better Bank program we are beginning this process of change – we are examining all areas of our business and we are determined to introduce the efficiencies that will deliver a better customer service, making us easier to do business with, across the full range of our products and services and across a multiple range of distribution channels.

This next year will be marked by our investment in the Better Bank program, moving through to our Even Better Bank then our Best Bank model over the next few years. Over this time our Bank will transform into a modern and digitally enabled Bank that respects and builds on its heritage, but is also known for its ability to attract a new brand of customer – customers who share our values and belief in the power of Mutuality – and see and believe in the alternative of the Customer-Owned Banking Model.

I believe we are well placed to undertake this journey. We have a great Bank with solid foundations and we are already recognised nationally across a myriad of awards.

This is in no small way attributable to our fantastic teams of people – delivering every day the Heritage difference through our People *first* ethos.

A big thank you has to go out to all of our teams. Without you we couldn't boast about all of the awards the Chairman referenced.

- *The highest Roy Morgan customer satisfaction score across all Queensland financial institutions of 94.3% as at 30 June.*
- *A customer advocacy score of 38.4 – one of the highest in Queensland and well above the average of the big banks at 6.6.*
- *The Canstar Blue most satisfied customer award in the Challenger Bank sector for 2016*
- *The Australian Business Awards Employer of Choice - for the sixth year in a row!*
- *The Mozo People's Choice Award for Customer Satisfaction*
- *The Adviser's Rising Star Award and...*
- *The AFR Smart Investor Blue Ribbon Award for Regional Bank of the Year 2016.*

Of course and most importantly, we couldn't celebrate these awards without the support of our customers. Thank you for banking with us, and for the support and loyalty you have to Heritage Bank. We appreciate your support and don't take it for granted.

For our part, we remain committed to serve and support the communities where we operate. In 2015/16 alone we put more than \$600,000 into sponsoring and supporting community events, as well as raising more than \$75,000 for charities through our annual golf day and calendar sales.

As a Toowoomba-based organisation, we are strong supporters of activities in this region, including the Toowoomba Show, the Carnival of Flowers, the Toowoomba Business Excellence Awards and many others.

But we also support events and organisations across our geographic footprint, totalling almost 200 separate sponsorships in 2015/16.

Another great example is our Community Branch model. Since we established our first Community Branch in Crows Nest in 1999, we have collectively put more than \$37 million back into the seven local communities where these sites operate, through funding grants, wages, rent and payments for other goods and services. It's fantastic to see just what a difference these models make.

To sum up, I believe the Bank has had a good year with a lot of changes. Our new strategic direction and the focus of the team has already seen a new momentum and energy come into the business. We recognise the industry is facing challenges and we are prepared to make the decisions that will ensure Heritage is in a position to meet and grow with those challenges.

As a final comment, I'd like to thank the Board and my Senior Executive team for helping me make the transition to Heritage and indeed Queensland and Toowoomba such an easy and enjoyable experience.

We have a fantastic Bank and it's a great privilege and honour to be able to lead this organisation. I commend these results to you.

Thank you.

Peter Lock

CEO