NZX/ASX release
29 August 2023

Heartland's FY2023 result demonstrates resilience

Heartland Group Holdings Limited (**Heartland**) (**NZX/ASX: HGH**) is pleased to announce a net profit after tax (**NPAT**) of $95.9 million for the financial year ended 30 June 2023 (**FY2023**). On an underlying[1] basis, FY2023 NPAT was $110.2 million. NPAT increased $0.7 million (0.8%), and on an underlying basis, $14.1 million (14.6%), compared with the financial year ended 30 June 2022 (**FY2022**).[2]

Highlights for FY2023

Financial highlights

- NPAT of $95.9 million, up 0.8% ($0.7 million) on FY2022 NPAT. Underlying NPAT of $110.2 million, up 14.6% ($14.1 million) on FY2022 underlying NPAT.
- One-off or non-cash technical items had a $14.3 million net[3] impact on NPAT.
- Gross finance receivables (**Receivables**)[4] of $6.8 billion, up 10.1% ($625.5 million).[5]
- Underlying return on equity (**ROE**) of 11.9%, down 68 basis points (**bps**).[6]
- Net interest margin (**NIM**)[7] of 3.97%, down 8 bps. Underlying NIM of 4.00%, down 16 bps.
- Net interest income (**NII**) of $282.0 million, up 12.7%. Underlying NII of $283.9 million, up 14.3%.
- Underlying cost to income (**CTI**) ratio of 42.0%, down 53 bps on FY2022.[8]
- Underlying impairment expense ratio of 0.36%, up 7 bps.[9]
- FY2023 final dividend of 6.0 cents per share (**cps**), resulting in a FY2023 total dividend of 11.5 cps, up 0.5 cps on the FY2022 total dividend.
- Earnings per share (**EPS**) of 14.0 cps, down 2.1 cps. Underlying EPS of 16.0 cps, down 0.3 cps.

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[1] Financial results are presented on a reported and underlying basis. Reported results are prepared in accordance with NZ GAAP and include the impacts of positive and negative one-offs, which can make it difficult to compare performance. Underlying results (which are non-GAAP financial information) exclude any impacts of one-offs. This is intended to allow for easier comparability between periods, and is used internally by management for this purpose. Refer to *Profitability* on page 6 for a summary of reported and underlying results. A detailed reconciliation between reported and underlying financial information, including details about FY2023 one-offs, is set out on page 42 of the FY2023 investor presentation (**IP**). General information about the use of non-GAAP financial measures is set out on page 4 and 38 of the FY2023 IP.
[2] All comparative results are based on the audited full year consolidated financial statements of Heartland and its subsidiaries (the **Group**) for FY2022.
[3] Includes tax impact on one-offs (as and where applicable).
[4] Receivables includes Reverse Mortgages.
[5] Excludes the impact of changes in foreign currency exchange (**FX**) rates.
[6] Underlying ROE refers to ROE calculated using underlying results. When calculated using reported results, ROE was 10.4%, down 169 bps compared with FY2022. For more information, see page 4 of the FY2023 IP.
[7] NIM is calculated as net interest income over average gross interest earning assets.
[8] Underlying CTI ratio refers to the CTI ratio calculated using underlying results. When calculated using reported results, the CTI ratio was 44.9%, up 126 bps compared with FY2022. For more information, see page 4 of the FY2023 IP.
[9] Underlying impairment expense ratio refers to the impairment expense ratio calculated using underlying results. When calculated using reported results, the impairment expense ratio was 0.36%, up 11 bps compared with FY2022. For more information, see page 4 of the FY2023 IP.

Strategic highlights

- $199 million raised through 2022 equity raise to fund growth ambitions for existing businesses and repay acquisition-related bridge debt of $174 million (A$158 million).
- Completed the integration of StockCo Australia into Heartland.
- Signed a conditional share purchase agreement for the purchase of Challenger Bank Limited (**Challenger Bank**) on 20 October 2022, subject to obtaining the requisite regulatory approvals.
- Australian Reverse Mortgages business increased market share to 38.4%.[10]
- Heartland Bank Limited (**Heartland Bank**) awarded Canstar New Zealand's Bank of the Year – Savings award for the sixth consecutive year.[11]
- Nearing completion of the upgrade of Heartland Bank's core banking system.

Strategic vision

Heartland is focused on creating sustainable growth and differentiation by providing products which are the 'best or only' of their kind, through scalable digital platforms. This is underpinned by the following strategic pillars:

1. Frictionless Service at the Lowest Cost – reflected in a superior CTI ratio
2. Expansion in Australia
3. Business as Usual Growth (reported on in *Business performance* from page 9).

Frictionless Service at the Lowest Cost – CTI ratio

Through technology, Heartland has been able to replicate the scale of big banks. This is evidenced by Heartland's CTI ratio, which improved by 53 bps on FY2022 to 42.0% on an underlying basis[8] in FY2023 – much lower than the average CTI ratio of New Zealand's main domestic non-major banks (The Co-operative Bank, Kiwibank, SBS and TSB) and more comparable to the average CTI ratio of Australia's major banks (ANZ, CBA, NAB and Westpac).[12]

Heartland's ambition is to achieve an underlying CTI ratio of less than 35% by FY2028 through revenue growth and ongoing automation and digitalisation initiatives. Key to achieving this ambition is increasing customer self-service functionality and improving efficiency through streamlining and digitising internal processes. This activity is intended to contribute to providing customers with frictionless service and enabling scalable growth possibilities for Heartland.

Ongoing digitalisation enhancements in FY2023 included expanding the secure automatic approval capabilities of the Asset Finance and New Zealand Livestock Finance application processes, reducing friction for customers and the need for manual assessment. This resulted in an uplift in approval rates of 20% and 12% respectively.

The percentage of New Zealand Reverse Mortgage website visitors who used mobile devices increased from 51% as at 30 June 2022 to 54% as at 30 June 2023. This reflects the inroads mobile phone technology is making with older demographics and supports Heartland's digital distribution strategy and lower cost servicing.

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[10] Based on Australian Prudential Regulation Authority (**APRA**) authorised deposit-taking institution (**ADI**) Property Exposure and Heartland Finance data as at 31 March 2023.

[11] Awarded in July 2023.

[12] The average CTI ratio of New Zealand's main domestic non-major banks excluding Heartland (The Co-operative Bank, Kiwibank, SBS and TSB) was 68.9% for the 12 months to 31 March 2023 (data from the RBNZ Financial Strength Dashboard, valid as at 31 July 2023). The average CTI ratio of Australia's major banks (ANZ, CBA, NAB and Westpac) was 45.2% for their most recent respective annual reporting periods.

After initially launching to a small set of customers, the Heartland Finance Mobile App was rolled out to all Australian Reverse Mortgage customers in June 2023, providing the ability to view balances, transactions and request a cash reserve or redraw from a mobile device. Within one month, more than 10% of Australian Reverse Mortgage customers had digital access (via the Heartland Finance Mobile App or online platform). In New Zealand, Heartland Bank has onboarded more than 10,000 new Heartland Mobile App users through recently developed self-service functionality, with Mobile App users up 65% from 1 July 2022.

The upgrade of Heartland Bank's core banking system is nearing completion and is due to go live within this calendar year. The upgraded system provides a platform on which to deliver increased levels of automation and digitalisation, positioning Heartland for increased scalability in the future.

A number of initiatives are being delivered through a systemised programme of work to further enhance digital, self-service and automation capabilities. This programme of work includes the following four key initiatives.

Zero inbound calls

This initiative is focused on digitising basic banking requests to enable customers to self-serve via the Heartland Mobile App, create a seamless user experience for customers, and reduce inbound customer call volumes. In doing so, Heartland's employees will be able to focus on more complex customer requests.

Heartland Bank's ambition is to reduce inbound customer call volumes by approximately 73% by 30 June 2025. To achieve this, mobile app self-service features will be developed to address the top reasons for inbound customer calls.

One-Click Deferral

Customers will be offered increased flexibility to self-manage their Motor Finance loan repayments digitally via the Mobile App, including customers in arrears. Seven new Heartland Mobile App functions and features will be developed to enable customers to self-manage their repayments, reducing the need for them to contact Heartland Bank.

Process automation

Heartland will continue to upgrade its existing back-end technology, and introduce scalable digital technologies to optimise back-end processes and improve efficiency. Increasing automation will improve internal workflows and reduce manual effort, thereby reducing friction for customers and employees. Heartland Bank's ambition is to automate approximately 65% of operations and collections manual processes by 30 June 2025.

Motor digitisation

Continued enhancement of Motor Finance digital capabilities will enable faster and easier access to vehicle finance for customers through online application platforms. Heartland's intention is to rollout seven branded online origination platforms to Motor Finance dealer partners in the financial year ending 30 June 2024 (**FY2024**).

Expansion in Australia

Heartland's focus for expansion in Australia is on:

1. growing its existing Australian Reverse Mortgages business
2. growing its existing Livestock Finance business (StockCo Australia)
3. seeking other opportunities to expand Heartland's 'best or only' strategy in Australia.

Strong growth has continued for Australian Reverse Mortgages, with a compound annual growth rate for the five-year period from 1 July 2018 to 30 June 2023 of 22.8%. Heartland has also maintained its position as the largest active provider of reverse mortgages in Australia, with market share of 38.4% as at 31 March 2023 (up from 33.1% at 31 March 2022)[13]. Further positioning itself as a leader in the sector, Heartland Finance was a finalist for Best Banking Innovation at the Australian Finder Innovation Awards 2022 and received the Excellence Award for Non-Bank of the Year at the Australian Mortgage Awards 2022.

The proportion of the Australian population aged over 65 years is expected to reach 21% by 2041 (up from ~17% in 2021).[14] The addressable market for reverse mortgages is estimated to be A$10-15 billion.[15] Further, the Australian Government's Home Equity Access Scheme continues to contribute to a greater awareness of home equity release options, including reverse mortgages. Non-bank participation in the sector has increased and supports the acceptance of reverse mortgages.

StockCo Australia has been operating in Australia since 2014 and is a leading specialist livestock financier with established direct and distributor networks. The Australian Livestock Finance portfolio experienced direct client growth in FY2023 of 11% (see page 11 for more detail), but subdued dollar growth due to stock market price volatilities and adverse weather conditions. This resulted in a contribution to FY2023 NPAT below the expected A$10-12 million (before any ongoing cost of acquisition debt funding). Global consumption and production of beef and veal, and sheep meat are projected to increase annually by 0.62% and 1.22% respectively between 2022-2031 due to a combination of income and population growth.[16] This, together with good feedstock conditions, makes for a positive outlook. The addressable market for livestock finance is estimated to be A$7 billion.[17]

The Challenger Bank acquisition remains subject to Reserve Bank of New Zealand (**RBNZ**) and APRA approval. The benefits of acquiring Challenger Bank, an established ADI, include:

- access to a deep and efficient pool of funding to support ongoing growth in Australian Reverse Mortgages and Livestock Finance
- potential uplift in margin, to the extent that retail funding rates are less than wholesale rates
- a platform to extend Heartland's 'best or only' strategy in Australia.

Heartland has continued to consider the appropriate group structure to accommodate the Challenger Bank acquisition. The final group structure is now expected to include Heartland Bank acquiring Challenger Bank. If this occurs, Heartland Banking Group's business would be carried out in both New Zealand and Australia.

Subject to completion of the acquisition, Heartland intends to leverage its extensive operational experience in New Zealand to drive expansion into Australia, including in Motor Finance and Asset Finance. Inorganic growth opportunities, through further acquisition, will also be explored in targeted areas of the market consistent with Heartland's 'best or only' strategy, and where there is an opportunity to add value as a means of adding scale or technology.

[13] Based on APRA ADI Property Exposure and Heartland Finance data as at 31 March 2022 and 31 March 2023.
[14] Sourced from ARC Centre of Excellence in Population Ageing Research as at August 2022.
[15] Heartland internal analysis based on information from the ABS December 2022, Census 2021 and Deloitte (2021 Three Pillars Forum). Market size based on reverse mortgage lending from banks and non-banks.
[16] Sourced from OECD FAO Agricultural Outlook 2022-2031.
[17] Based on 2020 ABS total rural debt and 2021 StockCo Australia data.

Operating environment

FY2023 was challenging for customers across Australia and New Zealand, driven by cost of living pressures and increasing interest rates. Low commodity prices and adverse weather events have compounded matters for certain sectors to which Heartland lends, including livestock. In this environment, Heartland's asset quality has performed within expectations. Heartland has worked hard to support its customers, particularly those facing temporary difficulties due to the current economic environment. During the year, Heartland also reduced its risk appetite for unsecured personal and unsecured business lending.

The Auckland flooding and Cyclone Gabrielle weather events had limited impact on Heartland's customers. A small number of customers were significantly affected and Heartland is working with the New Zealand Government under the North Island Weather Events Loan Guarantee Scheme to provide customer support.

Reverse Mortgages

The Reverse Mortgage portfolios in both countries have low average weighted loan-to-value ratios (**LVR**s) and continue to demonstrate resilience. Conservative loan origination standards (such as low LVRs) have enabled Reverse Mortgage customers to weather the challenging combination of falling house prices and higher interest rates over the last year. As at 30 June 2023, after consecutive cash rate increases by the RBNZ and the Reserve Bank of Australia, and successive house price reductions, the average weighted LVR for New Zealand and Australian Reverse Mortgages respectively were 21.3% (up from 18.4% at 30 June 2022) and 21.5% (up from 20.5% at 30 June 2022). Both portfolios remain strong with good headroom to weather any further stress events.

Additionally, following consultation in which Heartland Bank participated, the RBNZ introduced a new lower risk weight bucket of 40% for reverse mortgage loans with LVRs of less than 30% to reflect the credit risk of low LVR loans, which is expected to be effective from 1 September 2023. Heartland Bank welcomes this change which better reflects the resilience of its low LVR reverse mortgage portfolio and is expected to provide additional benefit to Heartland Bank's capital ratio.

Motor Finance

The Motor Finance portfolio has performed as expected given the economic conditions. Arrears have trended upward across the year to 3.95% as at 30 June 2023, however the level of losses remains within cyclical norms. Historically, losses have been correlated to unemployment. While rates of unemployment remain low, current provisions factor in an allowance for the potential impact of rising unemployment.

Online Home Loans

Online Home Loans experienced subdued growth as property sales and new mortgage volumes declined in New Zealand. As at 30 June 2023, no loans were impaired (i.e. 30 days overdue on a payment). The average LVR across the portfolio is circa 59%, despite property value declines since the end of 2021. The portfolio therefore remains well secured. These factors are a result of the product's conservative criteria and strategy of targeting high-quality borrowers.

Livestock Finance

Stock market price volatility is not expected to have a material impact on the quality of the book. Historically, the impact of the variation in market price has, in most cases, been more than offset through livestock weight gains.

The book remains well secured, with producers retaining livestock for longer periods to ensure weight gain exceeds the impact of stock market pricing. StockCo Australia is one of the few livestock providers in Australia to have a dedicated breeder product. This allows producers to hold onto female stock for breeding, with the value of the progeny assisting in increasing their returns when prices are under pressure.

Business

As at 30 June 2023, the balance of Heartland's Economic Overlay of $8.0 million taken in FY2022 was $2.4 million. The Economic Overlay has been allocated to specifically provision for Business Relationship lending and Asset Finance loans that have been impacted by low economic growth, and remained in place at 30 June 2023.

The economic outlook for FY2024 is difficult to predict. Interest rates appear at or near the peak but are forecast to remain elevated until 2025. The rate of unemployment remains low despite forecasts of it rising. The upcoming New Zealand general election provides additional uncertainty. Despite this, and recognising the lag effect of these economic indicators, Heartland expects FY2024 will be a year with broadly similar credit outcomes to FY2023.

Financial results

Profitability

FY2023 reported results have been normalised to exclude one-off or non-cash technical items, including the following.[18]

1. Legacy hedge accounting impacts: a $9.1 million loss contributed by the derivatives that were de-designated from their prior hedge accounting relationships in FY2022. The de-designation resulted in a $16.7 million mark-to-market (**MTM**) accounting gain on these derivatives being recognised in FY2022. This MTM gain is subsequently unwound as a loss as the cashflows from these derivatives are realised. The remaining $7.7 million will unwind across FY2024 and the financial year ending 30 June 2025 (**FY2025**).
2. Fair value loss on equity investment in Harmoney Corp Limited (**Harmoney**): a $4.5 million fair value loss was recognised on investment in Harmoney shares during FY2023. The fair value as at 30 June 2023 was determined based on the closing last traded price of Harmoney shares on the Australian Stock Exchange of A$0.32 per share.
3. Interest expense on the bridging loan for the acquisition of StockCo Australia: a $1.9 million interest expense was recognised in relation to a $174 million (A$158 million) bridging loan taken by Heartland to acquire StockCo Australia. The loan was fully repaid in September 2022 using the proceeds from the 2022 equity raise.
4. Australia Bank Programme costs: $2.2 million of transaction and other costs in relation to acquiring an ADI in Australia. In addition, $6.4 million of costs directly attributable to applying to become an ADI have been capitalised as an intangible asset.

The impact of one-off items on the respective financial metrics is outlined in the table below.

[18] Refer to page 42 of the FY2023 IP for an exhaustive list of FY2023 one-offs and a detailed reconciliation between reported and underlying financial information.

	Reported			Underlying		
	FY2023	FY2022	Movement	FY2023	FY2022	Movement
NOI[19] ($m)	285.3	267.6	17.7	300.7	262.0	38.7
Operating expenses (**OPEX**) ($m)	128.1	116.8	11.3	126.2	111.4	14.9
NPAT ($m)	95.9	95.1	0.7	110.2	96.1	14.1
NIM	3.97%	4.05%	(8 bps)	4.00%	4.16%	(16 bps)
CTI ratio	44.9%	43.6%	126 bps	42.0%	42.5%	(53 bps)
Impairment expense ratio	0.36%	0.25%	11 bps	0.36%	0.29%	7 bps
ROE	10.4%	12.1%	(169 bps)	11.9%	12.6%	(68 bps)
EPS	14.0 cps	16.1 cps	(2.1 cps)	16.0 cps	16.3 cps	(0.3 cps)

NOI

Total NOI was $285.3 million, an increase of $17.7 million (6.6%) from FY2022.

Underlying NOI was $300.7 million, $38.7 million (14.8%) higher than in FY2022, $21.8 million of which was contributed by StockCo Australia. This was largely due to a $35.6 million (14.3%) increase in NII, driven by $1,127.5 million (18.9%) higher average interest earning assets in FY2023 than in FY2022, and a 16 bps decrease in underlying NIM compared with FY2022.

Underlying other operating income increased by $3.1 million (22.7%) from FY2022, mainly driven by increases in upfront Reverse Mortgage income and fee income.

NIM

After recording an 8 bps contraction in underlying NIM in the six months to 31 December 2022 (**1H2023**) compared with the six months to 30 June 2022 (**2H2022**), this trend stabilised in the six months to 30 June 2023 (**2H2023**) through proactive portfolio pricing and margin management. Underlying NIM for FY2023 decreased only 2 bps compared with 1H2023.

The cash rates in New Zealand and Australia have seen a rapid and sharp increase, rising from 2.00% and 0.85% as at June 2022, to 5.50% and 4.10% as at June 2023 respectively. This has created a difficult environment in which to manage margins. Heartland intentionally delayed passing the full impact of these increases onto some borrower customers, and, in the case of Reverse Mortgages in New Zealand and Australia, did not pass on the full increases. With depositors, Heartland was quick to pass on the benefits of the rising cash rate. It is believed that while this did not maximise potential NIM, it was the socially responsible and more sustainable approach.

NIM compressions were also due to the continued shift in portfolio composition towards lower risk exposures. Personal lending and unsecured small-to-medium enterprise (**SME**) lending continued to reduce, while Business and Rural Relationship lending experienced larger repayments of higher risk loans. At the same time, there was growth in higher quality portfolios, such as Reverse Mortgages and Online Home Loans. Motor Finance experienced market share gains at the expense of margin, alongside general margin compression due to a shift in asset quality and competitive pressures. The impacts of this compression were partly offset following the acquisition of StockCo Australia, a higher NIM portfolio.

[19] Net operating income (**NOI**) includes fair value gains/losses on investments.

Through FY2024, NIM will be assisted by older Asset Finance and Motor Finance loans at lower rates continuing to be repaid.

OPEX

OPEX was $128.1 million, an increase of $11.3 million (9.7%) on FY2022. Underlying OPEX was $14.9 million (13.4%) higher compared with FY2022.

Higher underlying OPEX was primarily due to the acquisition of StockCo Australia which contributed $8.9 million to FY2023 OPEX. The remaining underlying OPEX increase is $6.0 million (5.4%), which was mainly driven by a 4.6% increase in staff expenses, an 18.6% increase in upfront Reverse Mortgage expenses (noting this is completely offset by an increase in upfront Reverse Mortgage income), and the balance from increased travel and administration costs.

CTI ratio

The underlying CTI ratio further improved by 53 bps on FY2022 to 42.0%.[20]

Heartland's commitment to efficiencies through technology and digitalisation are anticipated to provide ongoing benefits in the form of a reduced CTI ratio. The CTI ratio is expected to remain stable while investment in and delivery of digitalisation initiatives is underway, with CTI benefits to start materialising from late FY2024.

Impairment expense

Impairment expense was $23.2 million, $9.4 million (68.1%) up on FY2022. On an underlying basis, impairment expense was $7.5 million (47.9%) up on FY2022, including an allowance for the potential impact of rising unemployment on the Motor Finance portfolio. The residual increase in underlying impairment expense was mainly contributed to by the Harmoney book amortising at a slower rate in FY2023 compared with FY2022 and, to a lesser extent, by deterioration in the quality of unsecured Personal Lending which is no longer being actively originated in order to manage risk in the current environment. Underlying impairment expense ratio increased to 0.36% in FY2023, up 7 bps compared with FY2022.

As at 30 June 2023, the balance of Heartland's Economic Overlay of $8.0 million taken in FY2022 was $2.4 million. The Economic Overlay has been allocated to specifically provision for Business Relationship lending and Asset Finance loans that have been impacted by low economic growth, and remained in place at 30 June 2023.

ROE

Underlying ROE was 11.9%, down 68 bps compared with FY2022.[21] The result reflects a strengthened capital position following Heartland's equity raise in 1H2023, positioning it well for future growth opportunities.

Financial position

Total assets increased by $657.1 million (9.3%) during FY2023, driven by a $625.5 million (10.1%)[22] increase in Receivables and a $41.7 million (7.1%) increase in liquid assets from FY2022.

[20] Underlying CTI ratio refers to the CTI ratio calculated using underlying results. When calculated using reported results, the CTI ratio was 44.9%, up 126 bps compared with FY2022. See page 4 of the FY2023 IP for more information about the use of the CTI ratio, a supplementary, non-GAAP measure.
[21] Underlying ROE refers to ROE calculated using underlying results. When calculated using reported results, ROE was 10.4%, down 169 bps compared with FY2022. For more information, see page 4 of the FY2023 IP.
[22] Excluding the impact of changes in FX rates.

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Receivables growth was experienced across Heartland's core portfolios of Australian Reverse Mortgages, New Zealand Reverse Mortgages, Motor Finance, Asset Finance and Online Home Loans, partly offset by decreases in Business, Rural Relationship, Open for Business (**O4B**) and Personal Lending.

Borrowings[23] increased by $456.7 million (7.4%) compared with FY2022. Deposits increased by $538.5 million (15.0%) from FY2022, partially offset by a decrease in other borrowings of $81.8 million (3.2%) during FY2023. See further information under *Funding and liquidity* on page 12.

Net assets increased by $222.3 million to $1,031.0 million. Net tangible assets (**NTA**) increased by $207.4 million to $774.2 million, primarily as a result of a $199 million equity raise completed in September 2022, resulting in an NTA per share of $1.09 (30 June 2022: $0.96).

Business performance

New Zealand

Asset Finance

Asset Finance Receivables increased $49.2 million (7.8%) from FY2022 to $682.8 million. Asset Finance NOI was $30.3 million, a decrease of $0.2 million (0.5%) compared with FY2022.

Heartland's focus remains on freight transport and yellow goods sectors. NIM has been affected by a change in the mix of new business weighted toward an improved credit profile. Lower margin loans are being repaid and replaced, and are expected to have a positive contribution to margin in late FY2024.

Business

Overall Business NOI was $31.7 million, an increase of $1.1 million (3.6%) compared with FY2022. Business Receivables decreased $56.6 million (9.0%) to $573.7 million. This was made up of Wholesale Lending and Business Relationship.

Wholesale Lending includes floorplan lending to vehicle retailers and wholesale facilities to other lenders, including for medium enterprises that on-lend to their own customers in the consumer motor and business sectors. Wholesale Lending Receivables decreased $27.1 million (9.9%) from FY2022 to $245.2 million, reflecting lower utilisation of limits as a result of unpredictable inventory conditions continuing into 2H2023.

Business Relationship Receivables decreased $29.5 million (8.2%) from FY2022 to $328.5 million, as this portfolio continues to transition away from legacy business to loans which present lower risk and are more cost efficient to transact.

Open for Business

O4B NOI was $12.9 million, a decrease of $0.8 million (5.7%) compared with FY2022. O4B Receivables decreased $24.1 million (17.1%)[22] to $117.1 million.

Heartland stopped actively originating O4B lending in the second quarter of FY2023 (**Q2**) to manage risk due to the macro-economic challenges for the SME sector. This has resulted in an amortising loan book pending improved conditions.

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[23] Includes retail deposits and other borrowings.

Motor Finance

Motor Finance NOI was $64.2 million, a decrease of $8.7 million (11.9%) compared with FY2022. Motor Finance Receivables increased $186.8 million (13.5%) to $1.57 billion.

Motor Finance has experienced market share gains at the expense of margin, alongside general margin compression due to a shift in asset quality and competitive pressures. While total new and used car sales in the New Zealand market were down by 6.2% in the period[24], Heartland's new business volumes increased by 11.6% from FY2022, with overall growth in FY2023 of 13.5% due to lower early repayments than expected.

Heartland's broad distribution network of dealers and partnerships with key distributors and large dealer franchise groups, along with its digital innovation, have been key contributing factors in achieving growth in a difficult market.

Heartland intends to expand its branded online origination platforms to other dealer partners in FY2024 so they can provide customers with swift digital options to apply for vehicle finance and receive a decision in minutes.

Personal Lending

Personal Lending includes loans originated directly through Heartland Bank, and legacy portfolios originated by Harmoney in New Zealand and Australia. To manage risk in the current environment, this portfolio is not actively originating. In addition, Heartland's Harmoney personal loans channel is closed to new business and running down.

Personal Lending NOI was $6.6 million, a decrease of $3.1 million (32.2%) compared with FY2022. Personal Lending Receivables decreased by $17.8 million (27.3%)[22] to $47.3 million. Harmoney Receivables decreased by $20.3 million (65.7%), made up of a decrease in the New Zealand Harmoney channel of $12.9 million (70.4%) to $5.5 million, and a decrease in the Australian Harmoney channel of $7.3 million (58.9%)[22] to $5.1 million. This is partially offset by Heartland originated personal lending which increased by $2.5 million (7.3%) to $36.7 million in FY2023.

Online Home Loans[25]

Online Home Loans NOI was $3.8 million, an increase of $1.7 million (80.2%) compared with FY2022. Online Home Loans Receivables increased $38.7 million (14.1%) to $313.4 million.

While subdued compared to FY2022, Online Home Loans experienced good growth in a challenging economic environment. This was moderated by a sharp decline in property sales and new mortgage volumes in New Zealand. The number of properties sold in the 12 months to February 2023 was the lowest observed since 1983.[26] Similarly, the monthly level of new mortgages issued has been at or near the lowest levels observed since at least 2014 (when the RBNZ began collating this data).[27]

Competitive pressures in the refinance market remain intense, with competitors generally offering large cash-backs and negotiating on rates. Heartland has remained disciplined in respect of its pricing strategy. Heartland's low-cost digital origination platform has enabled it to consistently offer competitive or market-leading rates. Customer retention remained strong, with retention exceeding 90% for customers whose fixed rates came up for renewal over the course of FY2023.

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[24] Based on data from the Motor Industry Association of New Zealand on new and used vehicle sales from motor vehicle dealers.
[25] Excludes legacy Retail Mortgages.
[26] Based on data from CoreLogic's February 2023 Housing Chart Pack.
[27] Based on RBNZ data on new residential mortgage lending by borrower type.

New Zealand Reverse Mortgages

New Zealand Reverse Mortgages NOI was $42.4 million, an increase of $9.9 million (30.3%) compared with FY2022. Receivables increased $167.3 million (23.2%) to $888.6 million.
The business continues to experience strong demand and growth due to:

- cost of living and cashflow pressures faced by older homeowners, with a reverse mortgage providing an option to fund desired lifestyle enhancements
- increased education, awareness and acceptance of reverse mortgages.

Over the last decade, Heartland has helped more than 22,000 New Zealanders to enjoy a more comfortable retirement by releasing equity from their homes. The outlook for New Zealand Reverse Mortgages remains positive, with additional demand from cost of living pressures driving growth. Website improvements will be released making it easier for mobile users, and streamlining the application process.

Rural

Overall Rural lending NOI was $34.2 million, an increase of $4.1 million (13.5%) compared with FY2022. Overall Rural portfolio Receivables increased by $11.4 million (1.7%) to $700.5 million. This was made up of Livestock Finance, Rural Relationship and Rural Direct.

Livestock Finance Receivables increased by $19.9 million (11.6%) from FY2022 to $191.2 million in a market impacted by falling commodity prices, difficult climatic conditions and Cyclone Gabrielle in the Hawke's Bay and Tairāwhiti regions. Of this growth, 6% originated from the addition of key intermediary partnerships, with the balance from existing customers.

Rural Relationship Receivables decreased by $17.1 million (3.9%) from FY2022 to $424.4 million, due to the continued transition of the book away from large, complex, low margin lending. Heartland's exposure to the dairy sector reduced to 32.8% of the total Rural book.

Rural Direct includes Heartland's Sheep & Beef Direct and Dairy Direct digital platforms which provide online finance to sheep, beef and dairy farmers. Rural Direct Receivables increased by $8.6 million (11.2%) from FY2022 to $84.9 million.

Australia

Australian Reverse Mortgages

Australian Reverse Mortgages NOI was $47.3 million, an increase of $8.2 million (20.9%) compared with FY2022.

Australian Reverse Mortgages Receivables increased by $263.5 million (20.7%)[22] to $1.54 billion, driven primarily by:

- increased debt consolidation and cost of living requests due to the current economic environment
- customers seeking funds for home improvements to ensure ageing well in place (for a person to remain in their home and make it more retirement-friendly as they age)
- customers looking to enjoy retirement with modest lifestyle spending (such as holidays or a new car)
- targeted marketing to new and existing customers to increase uptake and interest at key seasonal points across the year, leading to record settlements in key months.

Heartland has now helped more than 26,000 Australians to live a more comfortable retirement since 2004. Growth is expected to remain strong in FY2024 as ongoing improvements and efficiencies are made to the loan application, approval and maintenance process.

Australian Livestock Finance

Australian Livestock Finance NOI was $31.9 million. Receivables increased $7.7 million (2.1%)[22] from FY2022 to $380.8 million. Subdued growth was due to macroeconomic events affecting livestock prices and demand, including adverse weather conditions, the rising interest rate environment, and low export demand with the USA drought and China's COVID-19 response contributing to freezers being full around the world. This resulted in lower dollars per head on the balance sheet.

Despite this, the volume of livestock financed by StockCo has increased. As at 30 June 2023, cattle transactions were up 25% compared with 30 June 2022. Sheep transactions were flat. This growth was supported by increasing distribution partner networks with consistent onboarding of new clients and increased facility limit usage.

Demand for Australian protein, mainly beef, is expected to increase and have a positive effect on livestock value in FY2024 as the USA drought breaks and their herd rebuild begins, coupled with the Chinese Government looking to stimulate the Chinese economy as people return to pre-COVID-19 activities.

Processor capacity has been strained due to a lack of skilled workers, the ongoing impacts of COVID-19 and adverse weather conditions. Slaughter production in 2022 was down approximately 27% from 2021 volumes. This is expected to improve in the first half of FY2024 and have a positive effect on livestock demand and value, and therefore demand for livestock financing, as processors work through their backlog.

Digitalisation of the direct channel application is underway to improve efficiency in the application process. A white label offering is also in development to strengthen and expand the existing distribution network, supporting ongoing growth through FY2024.

Funding and liquidity

Heartland increased borrowings by $456.7 million (7.4%) from FY2022 to $6,627.4 million.

New Zealand

Heartland Bank increased borrowings by $399.5 million (9.2%) from FY2022 to $4,746.2 million.

Deposits[28] grew $533.9 million (14.8%) during FY2023 to $4,131.0 million, which was driven by competitive pricing on targeted products, including Heartland's Notice Saver offerings which both received Canstar New Zealand recognition in FY2023. Heartland Bank's 32-day Notice Saver won a 5-Star Rating and the 90-day Notice Saver achieved a Rising Star Rating with all the makings of a 5-star account in the future. In July 2023, Heartland Bank was awarded Canstar New Zealand's Bank of the Year – Savings for the sixth year in a row. In the first and second quarters of FY2023, Heartland Bank experienced the highest growth rate in retail deposits of all main and domestic banks in New Zealand.[29]

[28] Includes intercompany deposits received by Heartland Bank (30 June 2023: nil; 30 June 2022: $4.6 million).
[29] Based on balance sheet data from the RBNZ.

Notice Saver increased by $206.1 million (40.1%) from FY2022. Term deposits increased by $439.6 million (20.1%), while call deposits decreased by $111.8 million (12.5%) during FY2023. The call to total deposit ratio decreased to 19% as at 30 June 2023 (30 June 2022: 25%).

Other borrowings decreased by $134.4 million (17.9%) from FY2022, largely due to the maturity of a $150 million retail bond, as well as the amount drawn down in Heartland Bank's committed auto warehouse facility decreasing by $40.7 million. This was partially offset by Heartland Bank's issuance of $100 million of unsecured subordinated notes to the retail market in 2H2023, which qualify as Tier 2 capital for regulatory purposes, further solidifying Heartland Bank's regulatory capital position.

Heartland Bank's total liquidity (including liquid assets and available committed lines) strengthened further in FY2023, increasing by $76.3 million (12.1%) to $704.2 million, well in excess of regulatory minimums.

Heartland Bank's regulatory capital ratio increased to 14.69% as at 30 June 2023 (30 June 2022: 13.49%). Heartland Bank continues to operate significantly in excess of regulatory minimums and is well positioned to meet the RBNZ's future higher capital requirements. These requirements are for a common equity tier 1 ratio of 11.50% and a total capital ratio of 16.00% by 1 July 2028.

Australia

Heartland Australia (comprising Heartland Australia Holdings Pty Ltd and its subsidiaries) increased borrowings by A$282.0 million (23.5%) from FY2022 to A$1,482.2 million.

A A$30 million tap issue was completed in August 2022 and a further A$50 million Medium Term Note (**MTN**) was issued in October 2022. Heartland Australia's April 2023 A$120 million MTN maturity was refinanced. The aggregate outstanding issuance under Heartland Australia's MTN programme was A$240 million as at 30 June 2023 (30 June 2022: A$280 million).

The maturities of the two Reverse Mortgage securitisation warehouses were extended by two and three years respectively, and aggregate senior limits were expanded by A$100 million, providing Heartland Australia with access to A$1.54 billion of committed funding in aggregate. Conversations are underway with securitisation lenders to increase headroom in both facilities to support continued growth experienced in the portfolio.

StockCo Australia (comprising StockCo Australia Management Pty Ltd, StockCo Holdings 2 Pty Ltd and their subsidiaries) increased borrowings by A$17.2 million (5.2%) from FY2022 to A$346.4 million. StockCo Australia was transferred from Heartland to Heartland Australia Holdings Pty Ltd on 1 August 2023.

Regulatory update

Heartland continues to monitor and prepare for the significant volume of regulatory change in New Zealand.

In June 2023, it was announced that the Commerce Commission (**ComCom**) would conduct a market study into any factors that may affect competition for the supply or acquisition of personal banking services. A Preliminary Issues Paper for the market study was published on 10 August 2023 which sets out the context and proposed focus areas of the study. It is currently proposed that the study will focus on deposit accounts (transaction, savings, and term deposits, including overdraft facilities) and home loans. The ComCom will engage with stakeholders and conduct information gathering with a final report on its findings due 20 August 2024, which will include recommendations that identify ways to improve competition in the sector. Heartland Bank welcomes the opportunity to participate in the market study.

The Financial Markets (Conduct of Financial Institutions) Amendment Act 2022 (**Conduct Act**) was passed in June 2022, and will come into force on 31 March 2025, following a transitional period. The Conduct Act applies to registered banks, licensed insurers and licensed non-bank deposit takers. The Conduct Act introduces a new conduct licensing regime, the requirement to establish, implement, maintain and comply with a fair conduct programme, and the regulation of incentives (including the prohibition of sales incentives based on volume or value targets). Incentives regulations will apply both to Heartland Bank and its intermediaries involved in the distribution of its products. Heartland Bank is preparing for licensing and compliance with the Conduct Act.

The Deposit Takers Act received royal assent (and became law) on 6 July 2023 (**DT Act**). The DT Act strengthens the regulatory framework for all institutions that take deposits (including Heartland Bank) and introduces a new depositor compensation scheme (**DCS**), overseen by the RBNZ.

Very little of the DT Act comes into force immediately, but Heartland Bank has begun considering the impact of the DT Act on its operations and is actively participating in submissions on the DCS and other regulations, guidance and prudential standards relating to the DT Act. The DT Act is expected to be fully in force by around 2028.

Initial changes to the Credit Contracts and Consumer Finance Act 2003 (**CCCFA**) came into force on 1 December 2021, with additional changes effective 7 July 2022. Heartland Bank implemented new processes and technologies to enable it to comply with these changes. Following the completion of the New Zealand Government's investigation into the impact of the December 2021 changes, more amendments to the CCCFA came into force in May 2023. Heartland Bank has further amended its processes to reflect these most recent amendments. On 9 August 2023, the Government announced further changes to the CCCFA, including a wider review of the CCCFA with terms of reference to be announced in due course. Heartland Bank will monitor for further developments in regards to these changes.

In July 2021, the New Zealand Government announced it would implement a legislative framework for a new consumer data right (**CDR**), with a decision announced in November 2022 to designate banks into the new regime first. The Ministry of Business, Innovation and Employment recently consulted on an exposure draft of the Customer and Product Data Bill. A consumer data right in the banking sector (in other words, 'open banking') would allow customers to consent to share their banking data with third parties.

Continued preparation is underway to meet the Climate-Related Disclosures obligations introduced through the Financial Sector (Climate-Related Disclosures and Other Matters) Amendment Act 2021, with Heartland's first climate statement required as part of reporting for FY2024.

In Australia, Heartland continues to monitor changes to Australian regulatory requirements for its existing businesses, and is preparing for the acquisition of Challenger Bank (subject to the requisite regulatory approvals), which is an APRA regulated ADI.

Sustainability update

Heartland's sustainability strategy continues to evolve as it matures. The framework is built on three pillars: environment, people and financial wellbeing. Highlights for FY2023 are outlined below. For more detail, visit heartlandgroup.info/sustainability.

Environment

- Heartland's unaudited operational Greenhouse Gas (**GHG**) emissions for FY2023 saw a 17% reduction on the base year for the financial year ended 30 June 2019 (**FY2019**). This comprised strong reductions in Scope 1 and Scope 2 emissions, but an increase in travel-related emissions as a result of business travel requirements between New Zealand and Australia.
- Introduced an environment risk screening tool in the credit decisioning process to understand the sustainability of larger business and rural borrowers by reference to environmental, climate, reputational and regulatory factors (and mitigating actions being employed by borrowers).
- Undertook Australian and New Zealand Standard Industrial Classification (**ANZSIC**) code analysis to understand Heartland's exposure to high emitting industries or industries subject to a heightened degree of transitional risk as a result of climate factors. Heartland has a low exposure to customers in those industries.
- More than doubled lending to new generation vehicles through the Motor Finance portfolio, from 5% of all lending in FY2022 to 11% in FY2023. The increase was supported by the launch of a green vehicle rate in December 2022, and a guaranteed future value product across the Opel range, including two dedicated electric vehicles.

People

- Through its Manawa Ako internship programme, Heartland Bank welcomed 25 Māori and Pasifika interns to Heartland Bank in December 2022. More than 110 rangatahi (young people) have participated in the programme since inception in 2017.
- Heartland Bank maintained accreditation for the Rainbow Tick, as a Hearing Accredited Workplace, and Living Wage Employer.
- More than $710,000 provided to community groups and organisations by the Heartland Trust, in the areas of education, arts and culture, and wellbeing. The Heartland Trust is Heartland's registered charitable trust which is independent from, but closely supported by Heartland.
- Heartland Bank's products recognised as providing exceptional value for customers through Canstar New Zealand awards for Savings Bank of the Year and Outstanding Value Home Lender.

Financial wellbeing

- Supported more than 48,000 people in New Zealand and Australia to live a more comfortable retirement by releasing equity from their homes with a reverse mortgage.
- Heartland Bank continued to offer the Heartland Extend product to consumer customers, supporting customers in arrears to make their existing loan repayments more manageable.
- Development of new features and automation in Heartland Bank's mobile app and some online application forms to enable customers to control their own finances in their own time, without needing to speak with someone.

Final dividend

Heartland is pleased to declare a FY2023 final dividend of 6.0 cps, taking the FY2023 total dividend to 11.5 cps, up 0.5 cps on FY2022. Heartland's final dividend yield of 9.3%[30] compares with 7.1%[31] in FY2022.

The final dividend will be paid on Wednesday 20 September 2023 (**Payment Date**) to shareholders on the company's register as at 5.00pm NZST on Wednesday 6 September 2023 (**Record Date**) and will be fully imputed.

[30] FY2023 total fully imputed dividends divided by the closing share price as at 25 August 2023 of $1.72.
[31] FY2022 total fully imputed dividends divided by the closing share price as at 19 August 2022 of $2.16.

Heartland has a Dividend Reinvestment Plan (**DRP**), giving eligible shareholders the opportunity to reinvest some or all of their dividend payments into new ordinary shares. The DRP will apply to the final dividend with a 2.0% discount.[32] The DRP offer document and participation form is available on Heartland's website at heartlandgroup.info/investor-information/dividends.

Looking forward

Heartland's result in FY2023 is pleasing amidst a challenging economic background in New Zealand and Australia. Portfolio performance demonstrated the resilience of Heartland's products and 'best or only' strategy.

Heartland's strength is in its track record of strong growth in core lending portfolios. The business as usual growth focus in FY2024 will be on Reverse Mortgages (New Zealand and Australia), Motor Finance, Asset Finance and Livestock Finance (New Zealand and Australia). Growth will be supported by increased digitalisation and automation, and leveraging the demographic-driven demand being experienced in Reverse Mortgages.

Key to Heartland's expansion in Australia is obtaining an ADI licence. Heartland intends to do this through the acquisition of Challenger Bank, which remains subject to regulatory approvals. Heartland's desire is to complete the acquisition during the 2023 calendar year, after which its focus will be on integration and leveraging its common distribution channels in New Zealand to expand into Australia.

Heartland's NIM outlook is stable with repayment and replacement of lower margin Motor Finance and Asset Finance loans. The growth mix will continue to influence margin, causing acceptable contraction offset by corresponding growth.

Underpinning everything is Heartland's ambition to achieve an underlying CTI ratio of less than 35% by FY2028. This requires change and will take time. Initiatives are underway to increase customer self-service, reduce telephony and increase automation.

Through a continued focus on the execution of Heartland's strategic vision and achieving its underlying CTI ratio ambition, Heartland's ambition is to double underlying NPAT within five years – continuing Heartland's track record of income growth. Since 2012, Heartland's NPAT has more than tripled from $23.6 million at 30 June 2012.

Heartland expects NPAT for FY2024 to be within the guidance range of $116 million to $122 million, excluding any impacts of fair value changes on equity investments held, the impact of the de-designation of derivatives, and any costs related to the acquisition of Challenger Bank, which remains subject to RBNZ and APRA approval. As the acquisition nears completion, guidance will be updated to reflect the impact of Challenger Bank becoming part of Heartland.

– ENDS –

[32] That is, the strike price under the DRP will be 98.0% of the volume weighted average sale price of Heartland shares over the five trading days following the Record Date. For the full details of the DRP and the Strike Price calculation, refer to the Heartland DRP offer document dated 10 December 2018.

The person(s) who authorised this announcement:

Jeff Greenslade, Chief Executive Officer

Andrew Dixson, Chief Financial Officer

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About Heartland

Heartland is a financial services group with operations in Australia and New Zealand. Heartland has a long history with roots stretching back to 1875, and is listed on the New Zealand and Australian stock exchanges (NZX/ASX: HGH) with a market cap in excess of NZ$1 billion.

Heartland's New Zealand business, Heartland Bank, provides customers with savings and deposit products, online home loans, reverse mortgages, business loans, car loans and rural loans. In Australia, Heartland's main business is currently in reverse mortgages through Heartland Finance which is a market leader. Heartland also operates StockCo Australia, a specialist livestock financier, which was acquired by Heartland in May 2022. In October 2022, Heartland announced its intention to purchase Challenger Bank, a digital bank based in Melbourne, Australia, subject to obtaining the requisite regulatory approvals.

Heartland's point of differentiation is its 'best or only' strategy – where it focuses on providing products which are the best or only of their kind through scalable digital platforms. Heartland is committed to delivering financial solutions through speed and simplicity, particularly via digital platforms which reduce the cost of onboarding and make it easier for customers to open accounts or apply for funds when they need it.

More about Heartland: heartlandgroup.info

FY2023 results Investor presentation

For the year ended 30 June 2023

HEARTLAND GROUP

Contents

01

Highlights & strategic update

Jeff Greenslade
Chief Executive Officer Heartland Group

01

Presentation of results

Financial results in this investor presentation are presented on a reported and underlying basis.

- Reported results are prepared in accordance with NZ GAAP and include the impacts of one-offs, both positive and negative, which can make it difficult to compare performance between periods.
- Underlying results exclude the impacts of fair value changes on equity investments held, the de-designation of derivatives, and other one-offs. This is intended to allow for easier comparability between periods, and is used internally by management for this purpose.

Adjustments for underlying results impact NOI, OPEX, NPAT, NIM and EPS. Underlying ROE, underlying CTI ratio and underlying impairment expense ratio measures are supplementary, non-GAAP measures that may be used by investors, industry analysts and others in assessing and benchmarking profitability and performance against the industry and/or other companies. A GAAP and non-GAAP comparative is provided for each of these measures.

Refer to Appendix 3 on page 42 for a detailed reconciliation between reported and underlying financial information, including details about one-offs in the periods covered in this investor presentation.

General information about the use of non-GAAP financial measures is set out on page 38 of this investor presentation.

01

Group financial highlights

	NPAT	NIM		CTI ratio	Impairment expense ratio	ROE	EPS
Reported	$95.9m ↑ 0.8% vs FY2022	3.97% ↓ 8 bps vs FY2022		44.9% ↑ 126 bps vs FY2022	0.36% ↑ 11 bps vs FY2022	10.4% ↓ 169 bps vs FY2022	14.0 cps ↓ 2.1 cps vs FY2022
Underlying[1]	$110.2m ↑ 14.6% vs FY2022	4.00% ↓ 2 bps vs 1H2023	4.00% ↓ 16 bps vs FY2022	42.0% ↓ 53 bps vs FY2022	0.36% ↑ 7 bps vs FY2022	11.9% ↓ 68 bps vs FY2022	16.0 cps ↓ 0.3 cps vs FY2022

Receivables[2]	Borrowings	Equity	Final dividend
$6,791m ↑ 10.1%[3] vs June 2022	$6,627m ↑ 7.4% vs June 2022	$1,031m ↑ 27.5% vs June 2022	6.0 cps ↑ 0.5 cps vs FY2022

[1] Refer to Appendix 3 for a reconciliation between reported and underlying NPAT result. [2] Receivables also includes Reverse Mortgages. [3] Excluding the impact of changes in FX rates.

Strategic update

FY2023 achievements

Demonstrated resilience in 'best or only' strategy

- Growth in core lending portfolios despite macroeconomic environment, demonstrating resilience of 'best or only' products.
- Motor Finance grew 13.5% in a market where new and used vehicles declined 6.2%.
- Heartland Bank awarded Canstar NZ's Bank of the Year – Savings award and Outstanding Value Home Lender Award.

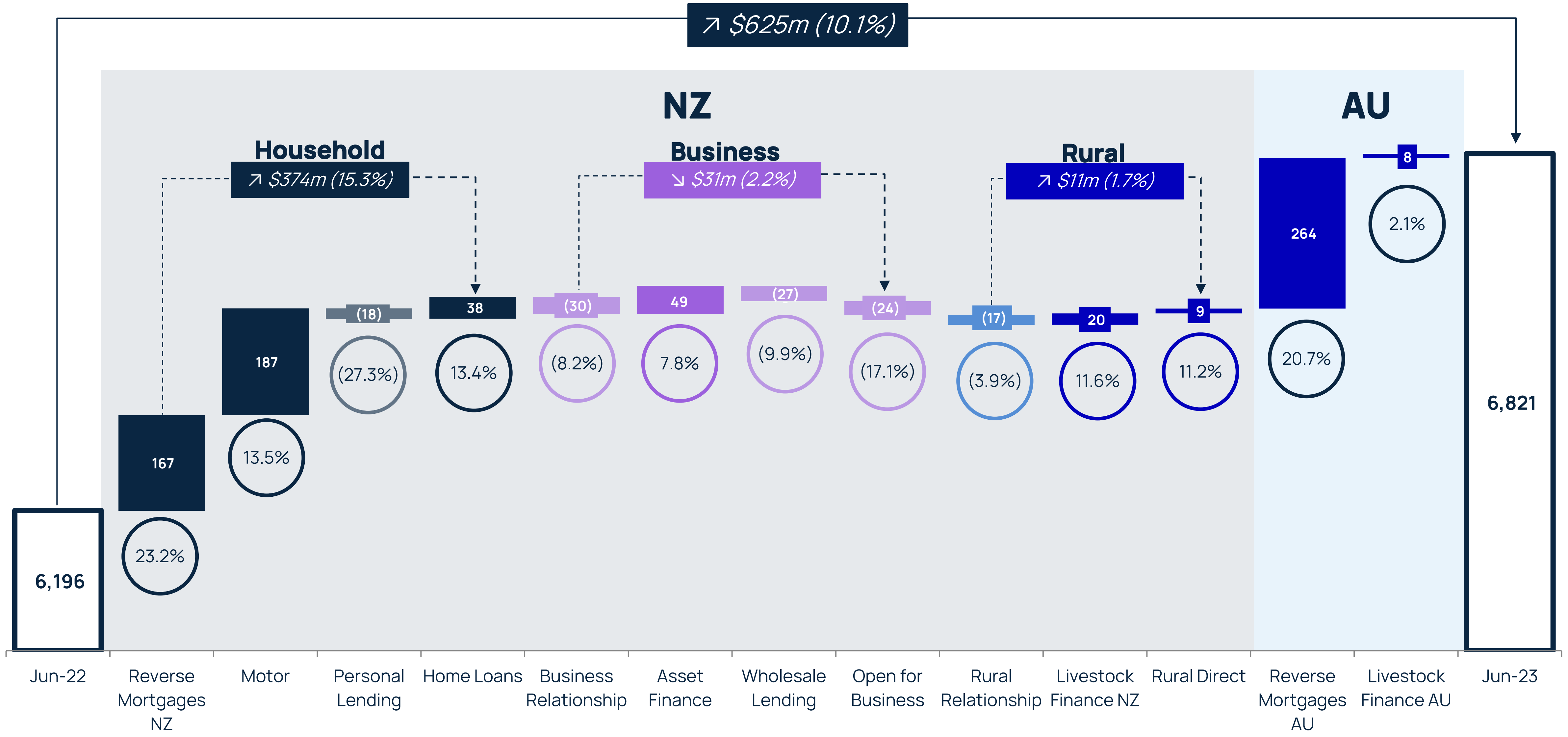
FY2024 focus

Growth in core product portfolios

- Continued growth in core product portfolio, plus higher contribution from AU Livestock Finance.

Continue to wind down legacy lending

- Continue the transition away from legacy business and focus on lower risk lending which is more cost efficient to transact.



Note: The graph shows FY2023 growth in receivables by portfolio excluding the impact of changes in FX rates and intercompany balances. All figures in NZ$m.

Strategic update

FY2023 achievements

Replicating the scale of big banks

- Underlying CTI ratio of 42.0%, much lower than the average CTI ratio of non-major NZ banks and more comparable to the average CTI ratio of major AU banks.[1]

Increasing uptake of mobile platforms

- Expanded secure automatic approval capabilities of Asset Finance and NZ Livestock Finance application processes, reducing friction for customers and the need for manual assessment. This resulted in an uplift in approval rates of 20% and 12% respectively.
- The Heartland Finance Mobile App was rolled out to all AU Reverse Mortgage customers in June 2023. Within one month, more than 10% of customers had digital access.
- Heartland Mobile App users up 65% from 1 July 2022.
- The percentage of NZ Reverse Mortgage website visitors who used mobile devices increased from 51% as at 30 June 2022 to 54% as at 30 June 2023.

FY2024 focus

Ambition to achieve underlying CTI ratio < 35% by FY2028

- Ambition to reduce the CTI ratio further over time through revenue growth and ongoing automation and digitalisation initiatives.

Increasing efficiency through digitalisation and automation

- Deliver One-Click Deferral, enabling customers to self-manage loan repayments.
- Develop self-service mobile app functionality to reduce friction for customers – progress toward reducing inbound customer calls by 73% by 30 June 2025.
- Improve efficiency in loan servicing and administration through process automation – progress toward automating 65% of manual back-end processes by 30 June 2025.
- Expand branded online origination platforms to more Motor Finance dealer partners to provide customers with swift digital options.

Implementation of upgraded core banking system

- Due to go live within this calendar year.
- The core banking upgrade provides a platform on which to deliver increased levels of automation and digitisation.

[1] The average CTI ratio of New Zealand's main domestic non-major banks excluding Heartland (The Co-operative Bank, Kiwibank, SBS and TSB) was 68.9% for the 12 months to 31 March 2023 (data from the RBNZ Financial Strength Dashboard, valid as at 31 July 2023). The average CTI ratio of Australia's major banks (ANZ, CBA, NAB and Westpac) was 45.2% for their most recent respective annual reporting periods.

Strategic update

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FY2023 achievements

Largest active provider of AU reverse mortgages

- Maintained position as largest active provider of reverse mortgages in Australia, with market share of 38.4% at 31 March 2023 (up from 33.1% at 31 March 2022).[1]
- Heartland Finance was a finalist for Best Banking Innovation at the Australian Finder Innovation Awards 2022 and received the Excellence Award for Non-Bank of the Year at the Australian Mortgage Awards 2022.

Integration of StockCo Australia

- Completed the integration of StockCo Australia into Heartland, and repaid acquisition-related bridge debt of $174 million (A$158 million) using proceeds from Heartland's equity raise in 1H2023.

Challenger Bank acquisition

- Signed a conditional share purchase agreement on 20 October 2022 for the purchase of Challenger Bank, subject to obtaining the requisite regulatory approvals.

FY2024 focus

Grow Reverse Mortgages

- Leverage demand being experienced through the growing ageing population to continue to increase market share with the addressable market estimated to be A$10-15 billion.[2]

Grow Livestock Finance

- Grow the Australian Livestock Finance business through product developments and digitalisation. Increasing demand for export is expected to contribute to growth, noting the addressable market estimated to be A$7 billion[3].

Become an ADI in Australia

- Complete the acquisition of Challenger Bank, enabling sustainable growth of existing AU portfolios through access to retail deposits.
- Leverage NZ expertise to expand product offering in the Australian market consistent with Heartland's 'best or only' strategy.
- Opportunity for targeted entry into Motor and Asset Finance markets in Australia.

[1] Based on APRA ADI Property Exposure and Heartland Finance data as at 31 March 2022 and 31 March 2023. [2] Heartland internal analysis based on information from the ABS December 2022, Census 2021 and Deloitte (2021 Three Pillars Forum). Market size based on reverse mortgage lending from banks and non-banks. [3] Based on 2020 ABS total rural debt and 2021 StockCo Australia data.

Sustainability

Heartland's sustainability framework is built on three key pillars: environment, people and financial wellbeing.

Environment

- Support the just transition to a net-zero economy.

Unaudited operational GHG emissions for FY2023 saw a 17% reduction on the FY2019 base year.

Introduced an **environment risk screening tool** in the credit decisioning process to understand the sustainability of larger business and rural borrowers.

Undertook **ANZSIC code analysis to understand Heartland's exposure to customers in high emitting industries**, or industries subject to a heightened degree of transitional risk as a result of climate factors.

Lending to new generation vehicles more than doubled from 5% of all lending in FY2022 to 11% in FY2023.

People

- Create a pathway and place for Heartland's people to grow, thrive and be empowered to achieve Heartland's goals as one team.
- Care for the communities Heartland operates in.
- Care for Heartland's customers.

The Manawa Ako internship welcomed 25 Māori and Pasifika interns in its sixth intake. **More than 110 interns welcomed since 2017.**

Heartland Bank maintained accreditation for the **Rainbow Tick, as a Hearing Accredited Workplace, and Living Wage Employer**.

More than $710,000 granted through the Heartland Trust in the areas of education, arts and culture, and wellbeing.[1]

Heartland Bank's products recognised as providing exceptional value for customers through Canstar NZ awards for **Savings Bank of the Year** and **Outstanding Value Home Lender.**

Financial wellbeing

- Support the financial wellbeing of Heartland's customers and communities.

Supported more than 48,000 people in NZ and AU to live a more comfortable retirement by releasing equity from their homes with a reverse mortgage.

Continued to offer Heartland Extend to consumer customers, supporting customers to make existing loan repayments more manageable.

Development of new features and automation to Heartland Bank's mobile app and some online application forms to **enable customers to control their own finances in their own time**.

[1] The Heartland Trust is Heartland's registered charitable trust which is independent from, but closely supported by Heartland.

02

Financial results, funding & liquidity

Andrew Dixson
Chief Financial Officer Heartland Group

Group financial results

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		Reported			Underlying		
Financial performance	NII	$282.0m	↑	12.7% vs FY2022	$283.9m	↑	14.3% vs FY2022
	OOI[1]	$3.3m	↓	81.0% vs FY2022	$16.9m	↑	22.7% vs FY2022
	NOI	**$285.3m**	↑	**6.6% vs FY2022**	**$300.7m**	↑	**14.8% vs FY2022**
	OPEX	$128.1m	↑	9.7% vs FY2022	$126.2m	↑	13.4% vs FY2022
	Impairment Expense	$23.2m	↑	68.1% vs FY2022	$23.2m	↑	47.9% vs FY2022
	Tax Expense	$38.1m	↓	9.0% vs FY2022	$41.1m	↑	5.8% vs FY2022
	NPAT[2]	$95.9m	↑	0.8% vs FY2022	$110.2m	↑	14.6% vs FY2022
	NIM	3.97%	↓	8 bps vs FY2022	4.00%	↓	2 bps vs 1H2023
						↓	16 bps vs FY2022
	CTI	44.9%	↑	126 bps vs FY2022	42.0%	↓	53 bps vs FY2022
	Impairment Expense Ratio[3]	0.36%	↑	11 bps vs FY2022	0.36%	↑	7 bps vs FY2022
	ROE	10.4%	↓	169 bps vs FY2022	11.9%	↓	68 bps vs FY2022
	EPS	14.0 cps	↓	2.1 cps vs FY2022	16.0 cps	↓	0.3 cps vs FY2022

		Reported		
Financial position	Receivables[4]	$6,791m	↑	10.1%[5] vs June 2022
	Borrowings	$6,627m	↑	7.4% vs June 2022
	Equity	$1,031m	↑	27.5% vs June 2022
	Equity/Total Assets	13.3%	↑	1.9 pps vs June 2022

[1] OOI includes fair value gains/losses on investments. [2] Refer to Appendix 3 for a reconciliation between reported and underlying NPAT result. [3] Impairment expense as a percentage of average Receivables.
[4] Receivables also includes Reverse Mortgages and StockCo Australia. [5] Excluding the impact of changes in FX rates.

Growth in profitability

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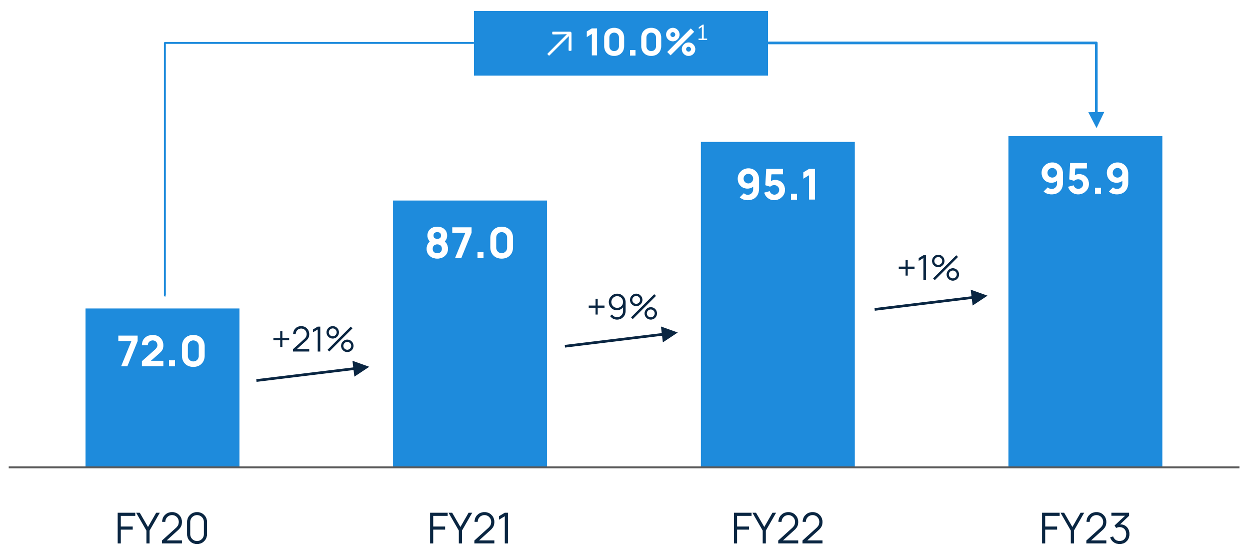
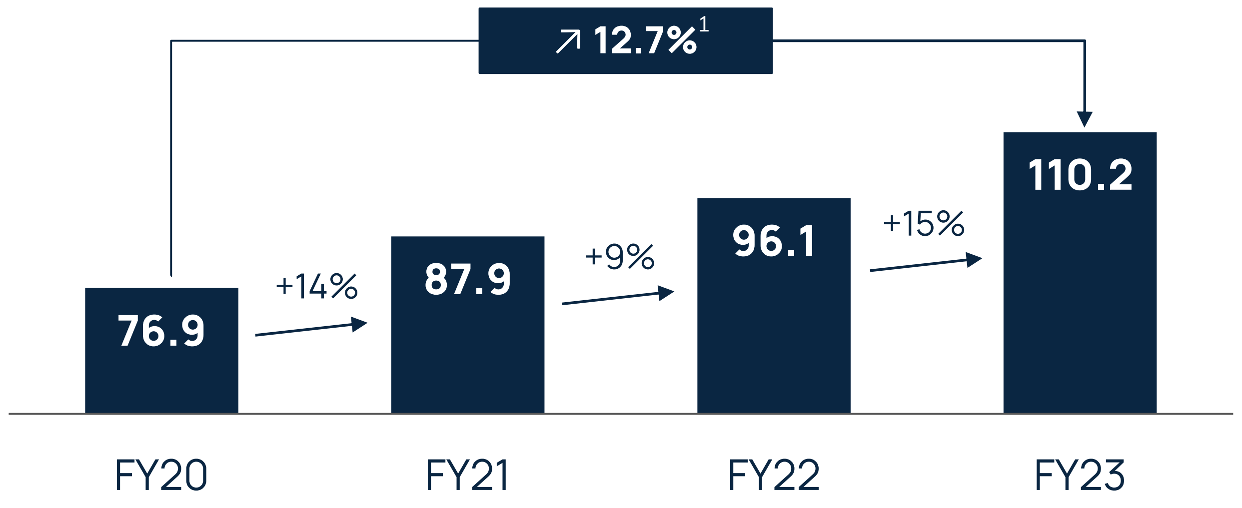
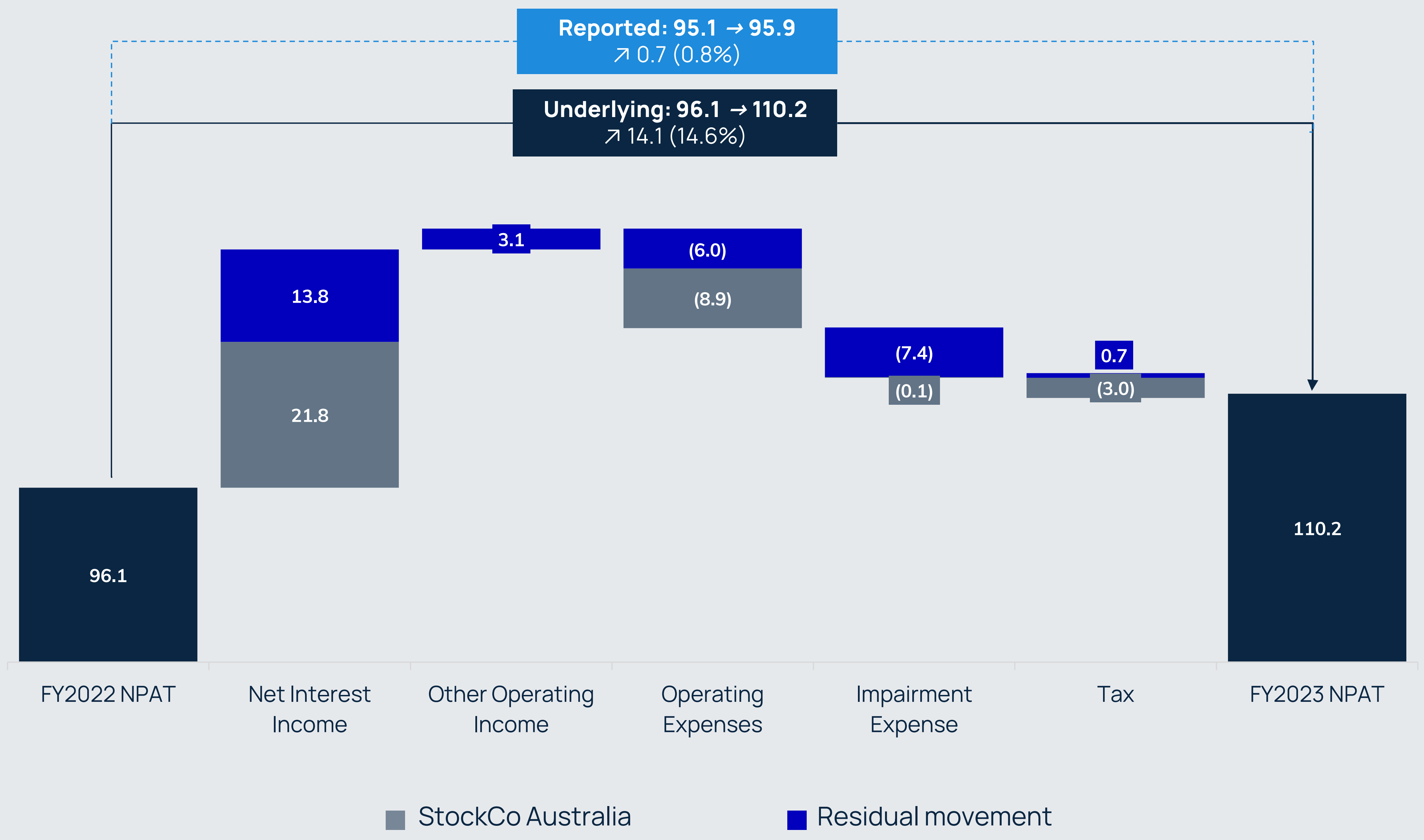
NPAT ($ million)



Underlying NPAT ($ million)





[1]Compounded annual growth rate for the period FY2020-FY2023.

Note: All figures in NZ$m. Refer to Appendix 3 for a reconciliation between reported and underlying NPAT result. Chart is not to scale.

02

Net interest margin

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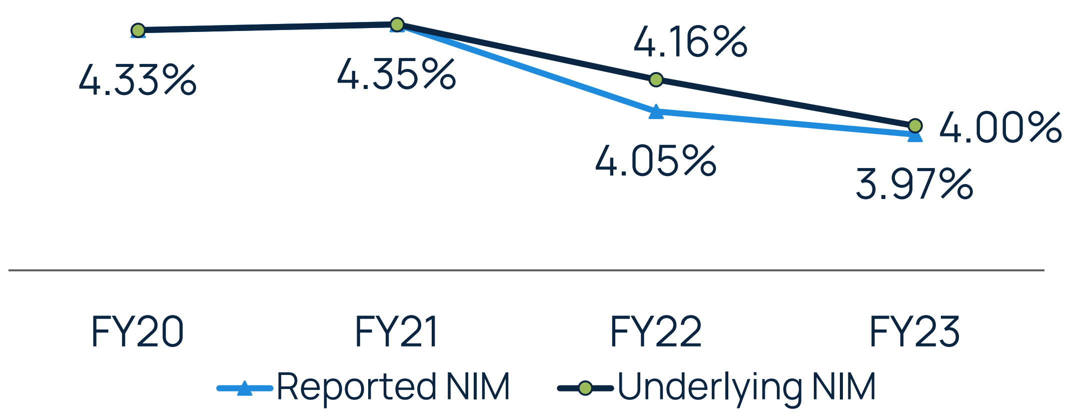
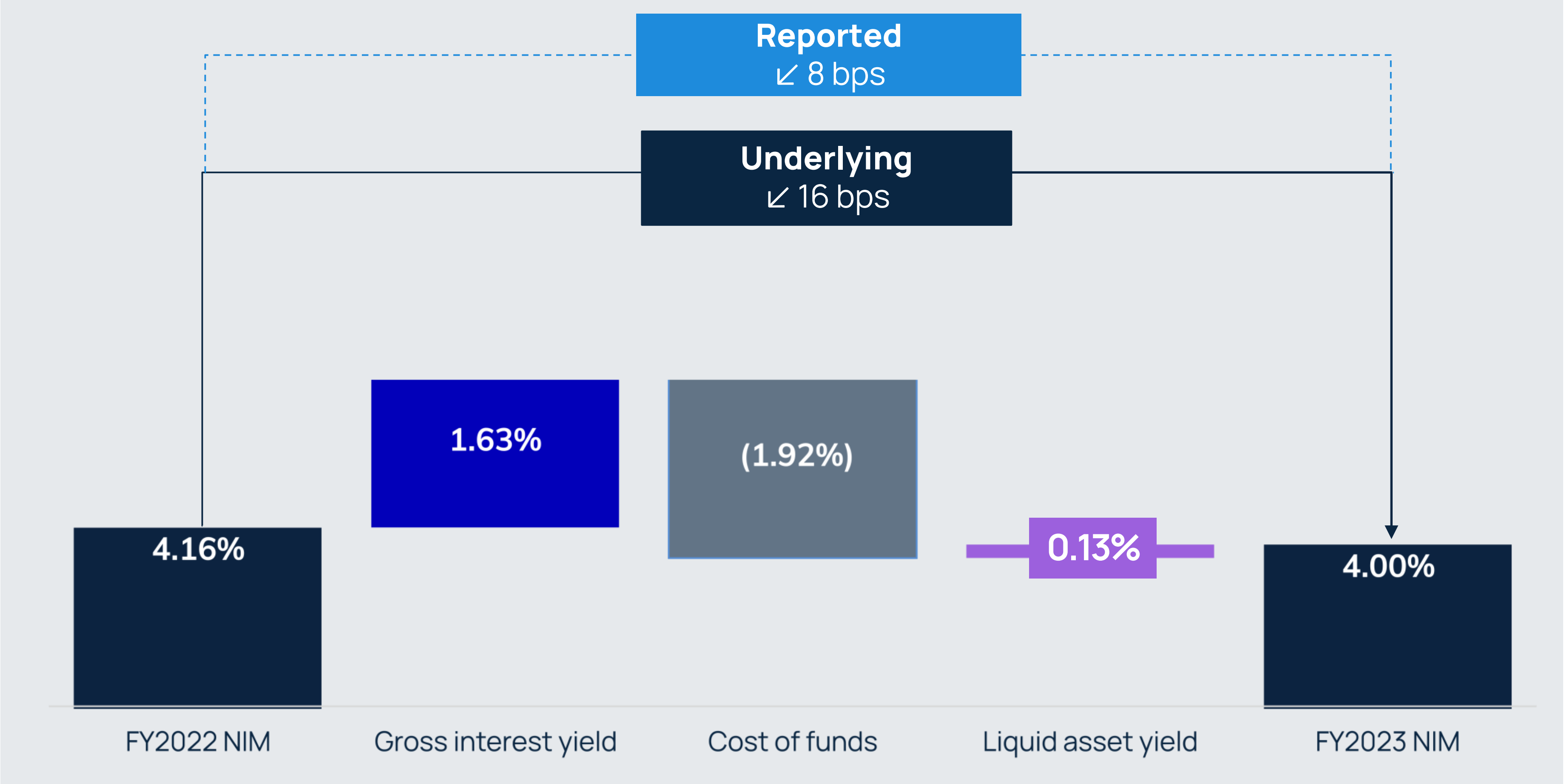
NIM



Underlying Gross interest yield
7.88%
NIM contribution ↗ 163bps[1] vs FY22

Underlying Cost of funds
3.81%
NIM contribution ↘ 192bps[2] vs FY22

Underlying Liquid assets yield
2.63%
NIM contribution ↗ 13bps[3] vs FY22



FY24 NIM outlook

Expected to remain stable through proactive portfolio pricing and margin management.

Note: NIM is calculated as net interest income/average gross interest earning assets.
[1] Underlying gross interest yield increased 174 bps vs FY2022 to 7.88%, contributing a 163 bps increase in NIM vs FY2022.
[2] Underlying cost of funds increased 211 bps vs FY2022 to 3.81%, contributing a 192 bps decrease in NIM vs FY2022
[3] Underlying liquid asset yield increased 155 bps vs FY2022 to 2.63%, contributing a 13 bps increase in NIM vs FY2022

Cost to income ratio

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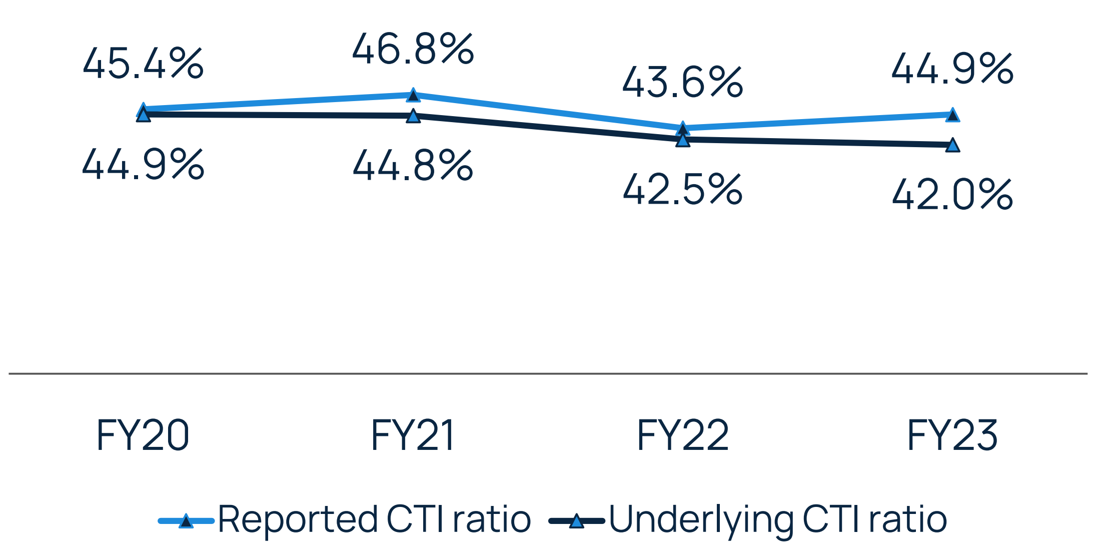
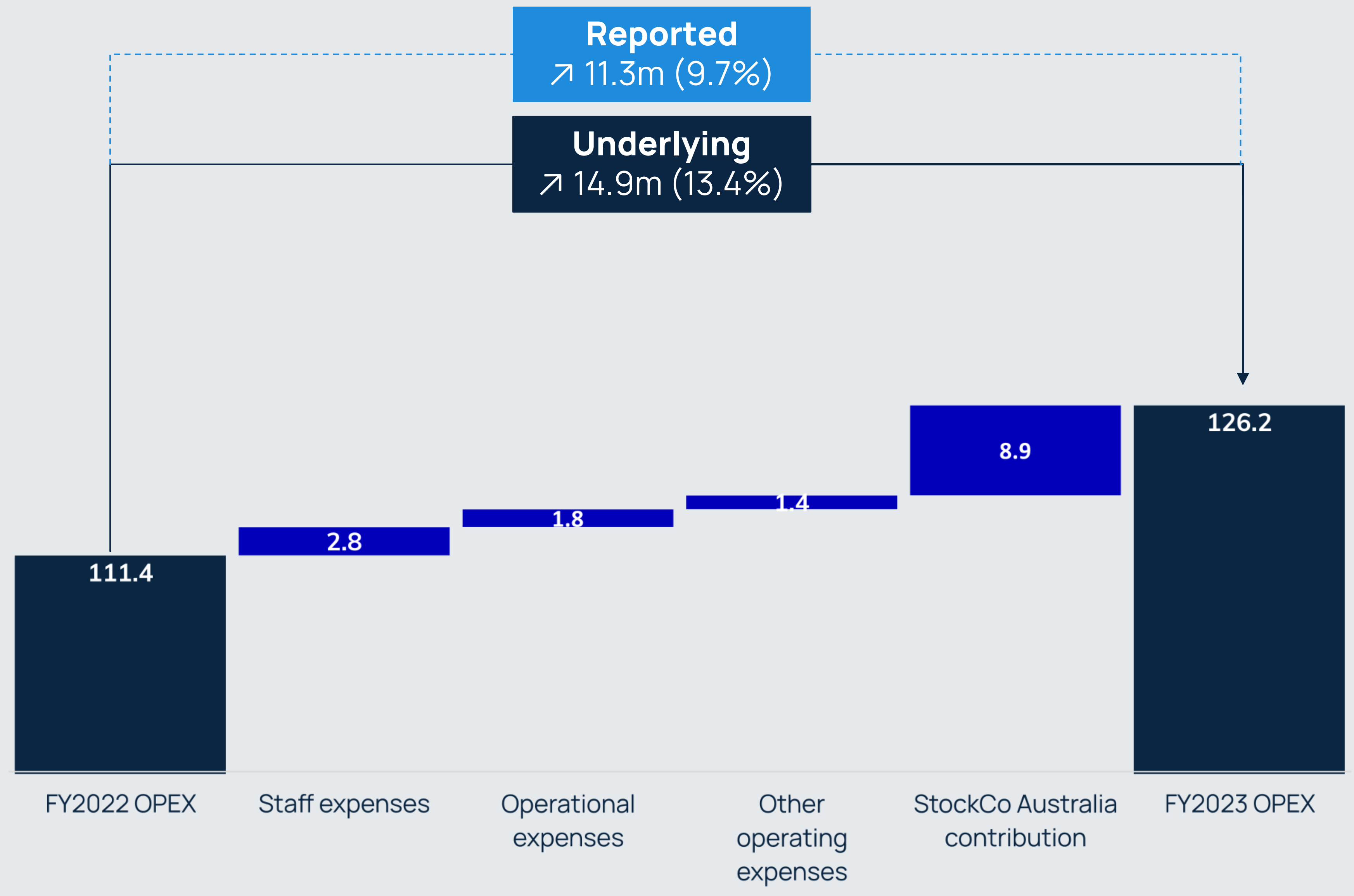
CTI ratio





FY24 CTI ratio outlook

Expected to gradually improve, via continued cost discipline, efficiency and digitalisation initiatives.

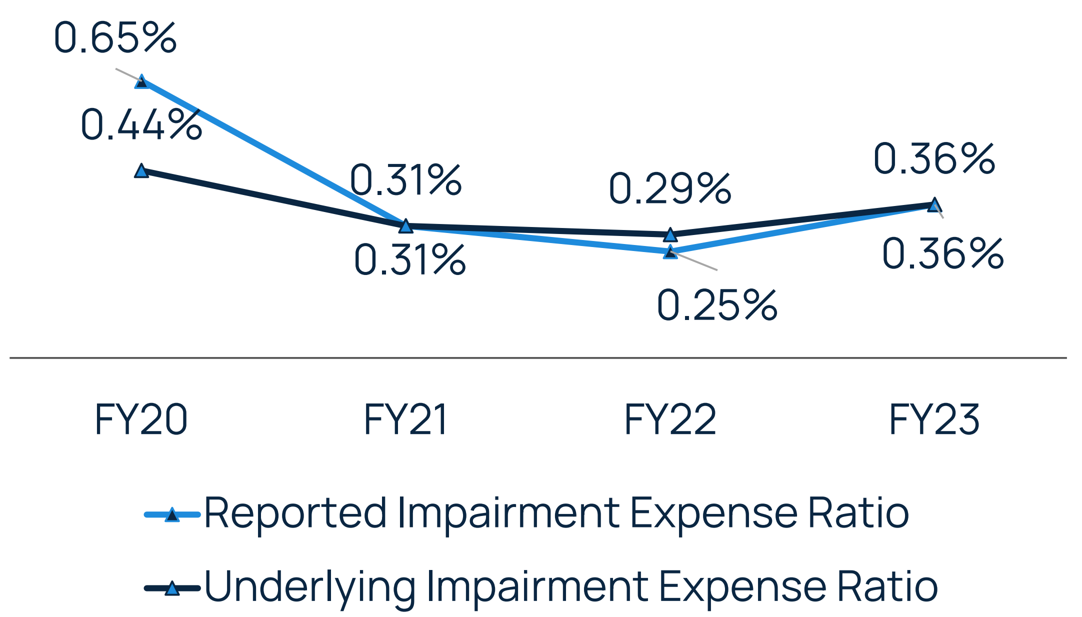
Note:
- CTI ratio is calculated as OPEX/NOI.
- Underlying CTI ratio excludes one-off impacts. Refer to Appendix 3 for a reconciliation between reported and underlying result.

Loan provisions

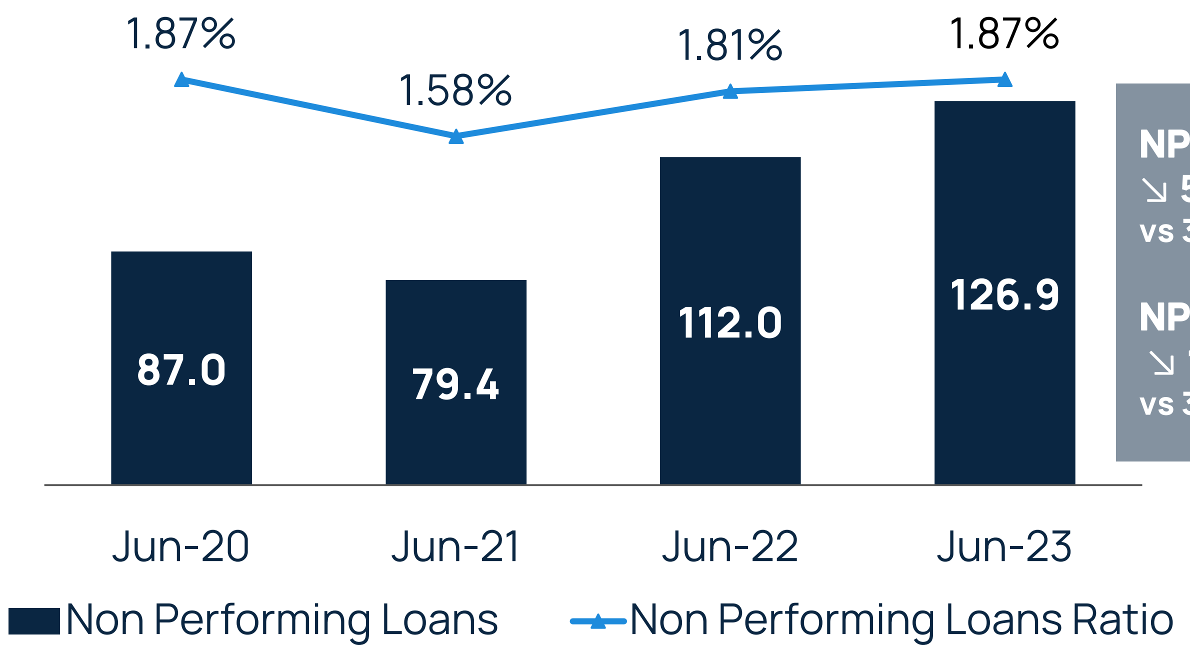
- Impairment expense was $23.2 million (68.1% up on FY2022).
- Underlying impairment expense up $7.5 million (47.9%) on FY2022.
- Increase in underlying impairment expense due to:
  - an allowance for the potential impact of rising unemployment on Motor Finance
  - the Harmoney book amortising at a slower rate in FY2023 compared with FY2022
  - deterioration in the quality of unsecured Personal Lending, no longer actively originating.

- As at 30 June 2023, the balance of Heartland's Economic Overlay of $8.0 million taken in FY2022 was $2.4 million. The Economic Overlay has been allocated to specifically provision for Business Relationship lending and Asset Finance loans that have been impacted by low economic growth, and remained in place at 30 June 2023.

Impairment Expense Ratio



Non-Performing Loans



NPL
↘ 5.5m
vs 31 December 2022

NPL ratio
↘ 18 bps
vs 31 December 2022

FY24 outlook

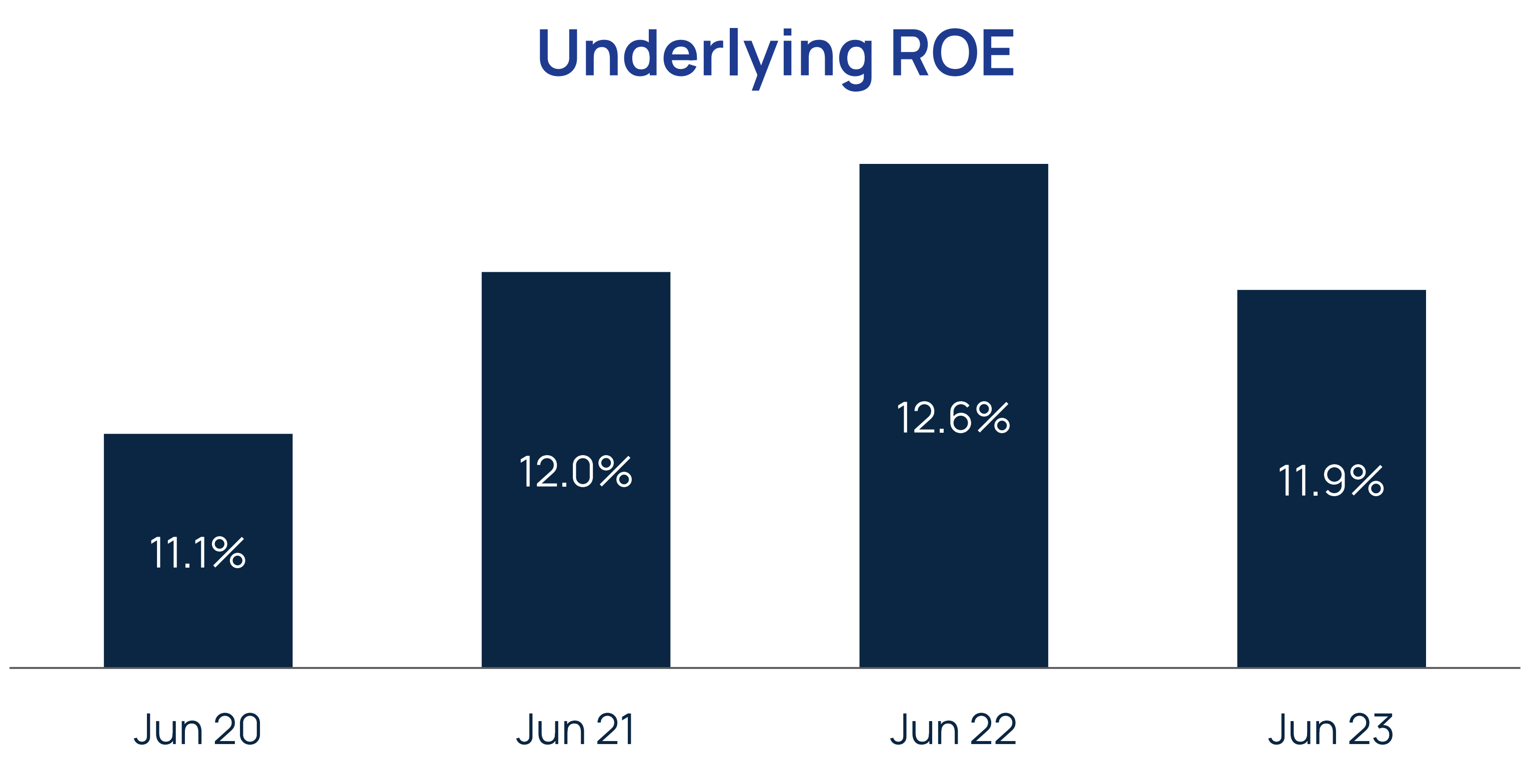
FY2024 economic outlook is difficult to predict. Interest rates appear at or near the peak but are forecast to remain elevated until 2025. The rate of unemployment remains low despite forecasts of it rising. The upcoming NZ general election provides additional uncertainty.

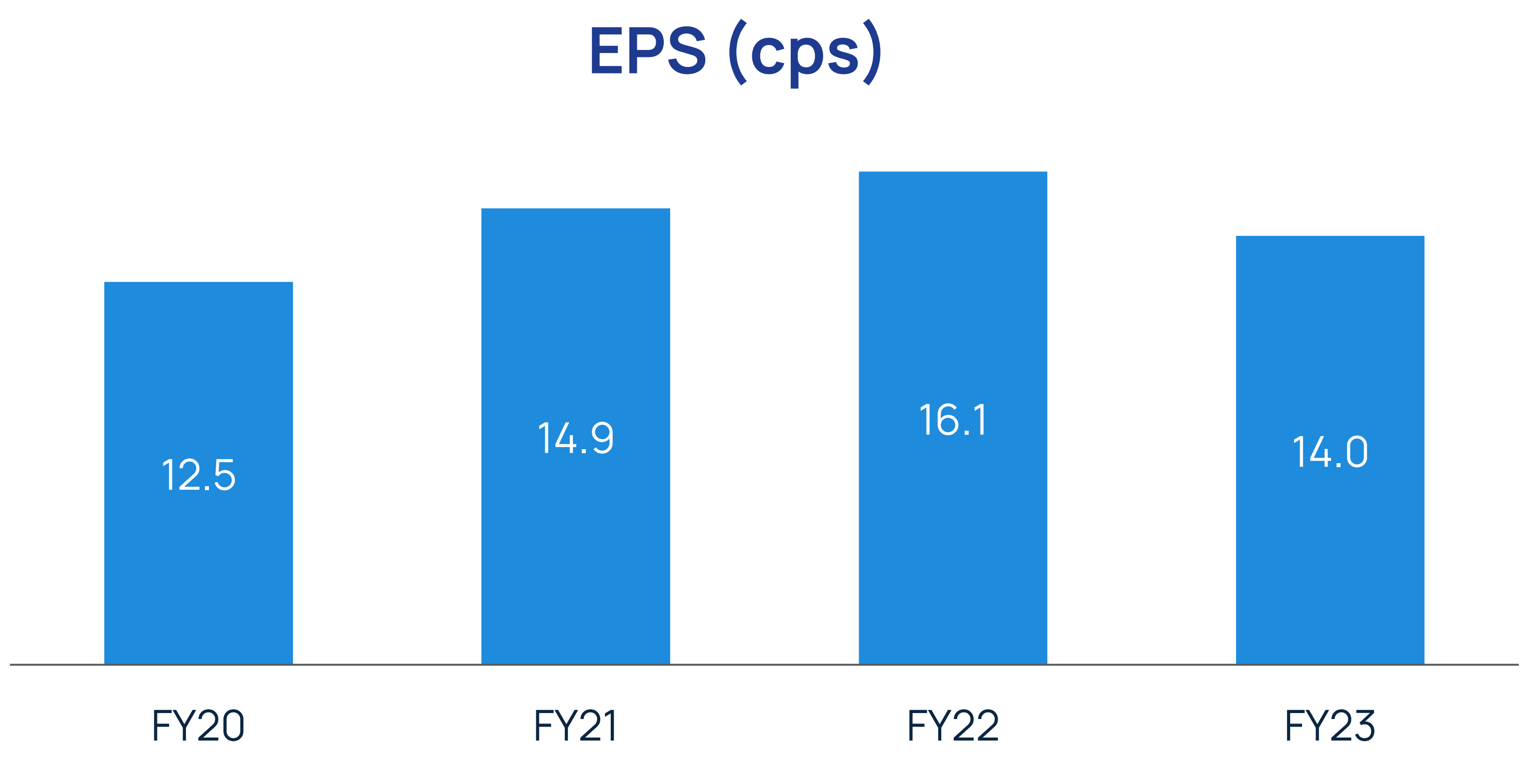
Despite this, and recognising the lag effect of these economic indicators, Heartland expects FY2024 to have broadly similar credit outcomes to FY2023.

Note: Impairment expense ratio is calculated as impairment expense/average gross finance receivables.

Shareholder return

- Underlying ROE of 11.9% (down 68 bps vs FY2022).[1]
- EPS of 14.0 cps, down 2.1 cps compared with FY2022.
- Underlying EPS of 16.0 cps (down 0.3 cps vs FY2022).
- Final dividend of 6.0 cps, taking FY2023 total dividend to 11.5 cps, up 0.5 cps on FY2022.
- Dividend yield of 9.3%[2] (FY2022: 7.1%[3]).
- Heartland's DRP will apply to the final dividend with a 2.0% discount.[4]





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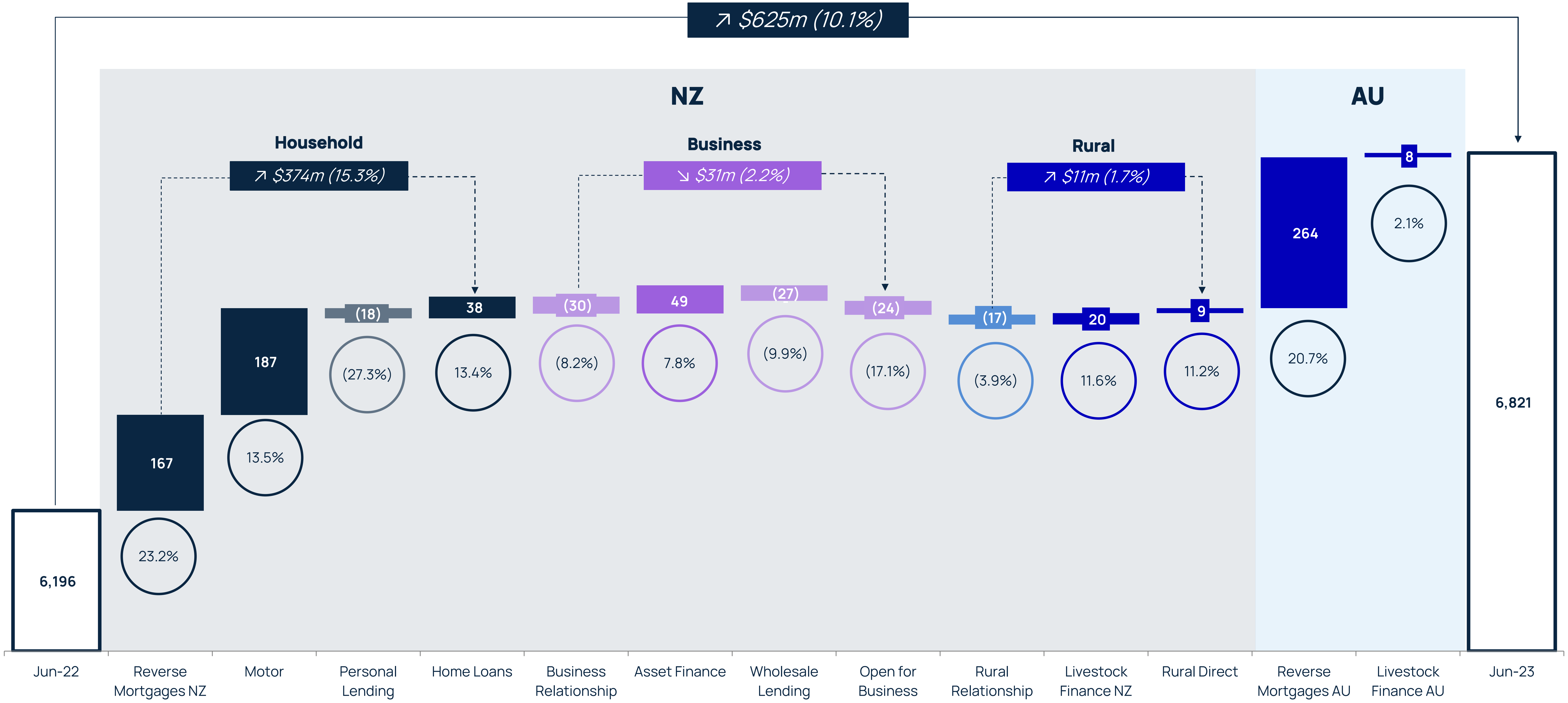
[1] Underlying ROE refers to ROE calculated using underlying results. When calculated using reported results, ROE was 10.4%, down 169 bps. See page 4 for more information about the use of ROE, a supplementary, non-GAAP measure.
[2] Total fully imputed dividends divided by the closing share price as at 25 August 2023 of $1.72.
[3] Total fully imputed dividends divided by the closing share price as at 19 August 2022 of $2.16.
[4] That is, the strike price under the DRP will be 98.0% of the volume weighted average sale price of Heartland shares over the five trading days following the Record Date. For the full details of the DRP and the Strike Price calculation, refer to the Heartland DRP offer document dated 10 December 2018.

Growth in receivables



Note: The graph shows FY2023 growth in receivables by portfolio excluding the impact of changes in FX rates and intercompany balances. All figures in NZ$m.

NZ funding & liquidity

New Zealand

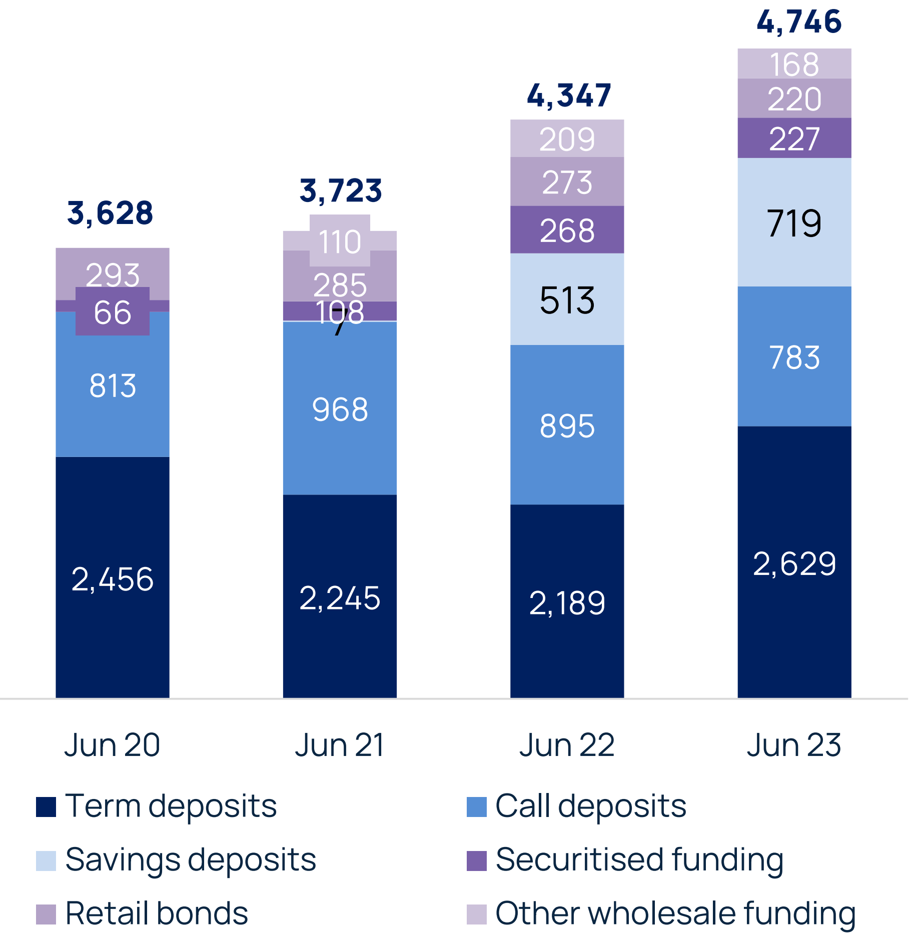
- Heartland Bank increased borrowings by $399.5 million (9.2%) to $4,746.2 million.
  - Deposits grew $533.9 million (14.8%) to $4,131.0 million, driven by competitive pricing on targeted products, including Heartland's Notice Saver offerings which both received Canstar New Zealand recognition in the year.[2]
  - In Q1 and Q2, Heartland Bank experienced the highest growth rate in retail deposits of all main and domestic banks in NZ.[1]
  - Other borrowings decreased by $134.4 million (17.9%), largely due to the maturity of a $150 million retail bond, as well as the amount drawn down in Heartland Bank's committed auto warehouse facility decreasing by $40.7 million. This was partially offset by an issuance of $100 million of unsecured subordinated notes to the retail market in 2H2023, which qualify as Tier 2 capital for regulatory purposes.
  - Total liquidity strengthened, increasing by $76.3 million (12.1%) to $704.2 million.
- Heartland Bank holds liquidity well in excess of regulatory minimums and maintains strong regulatory liquidity ratios.

Core funding ratio
89.6%
as at Jun 23
vs 75% regulatory minimum
↓ 0.6 pps vs Jun 22

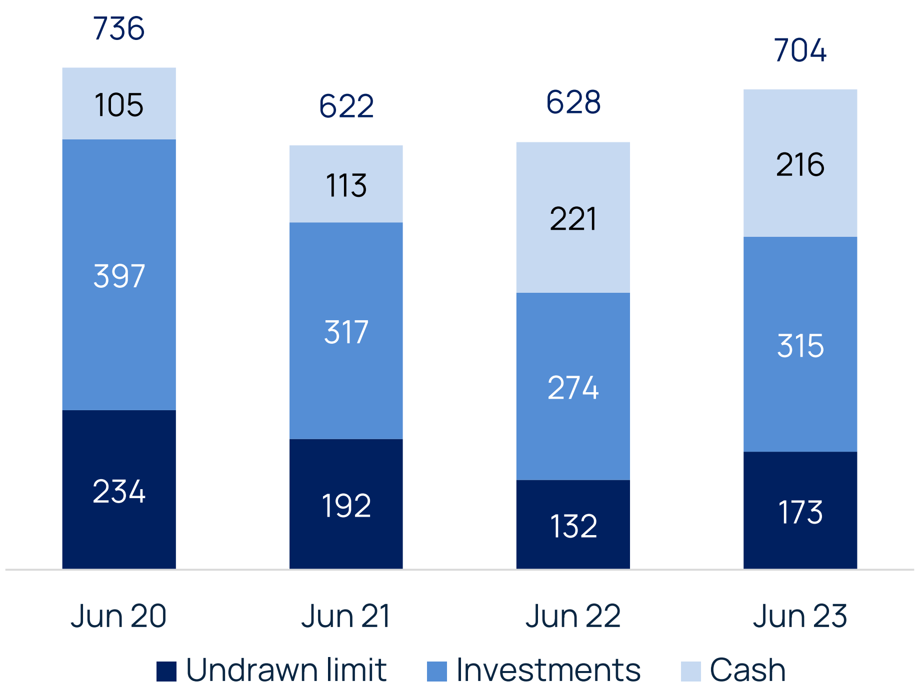
1-week mismatch
8.66%
as at Jun 23
vs 0% regulatory minimum
↑ 1.5 pps vs Jun 22

1-month mismatch
8.31%
as at Jun 23
vs 0% regulatory minimum
↑ 1.4 pps vs Jun 22

HBL Funding Composition[3] $m



HBL Liquidity Composition $m



[1] Based on balance sheet data from the RBNZ. [2] Awarded July 2022 and July 2023. [3] Includes intercompany deposits.

AU funding & liquidity

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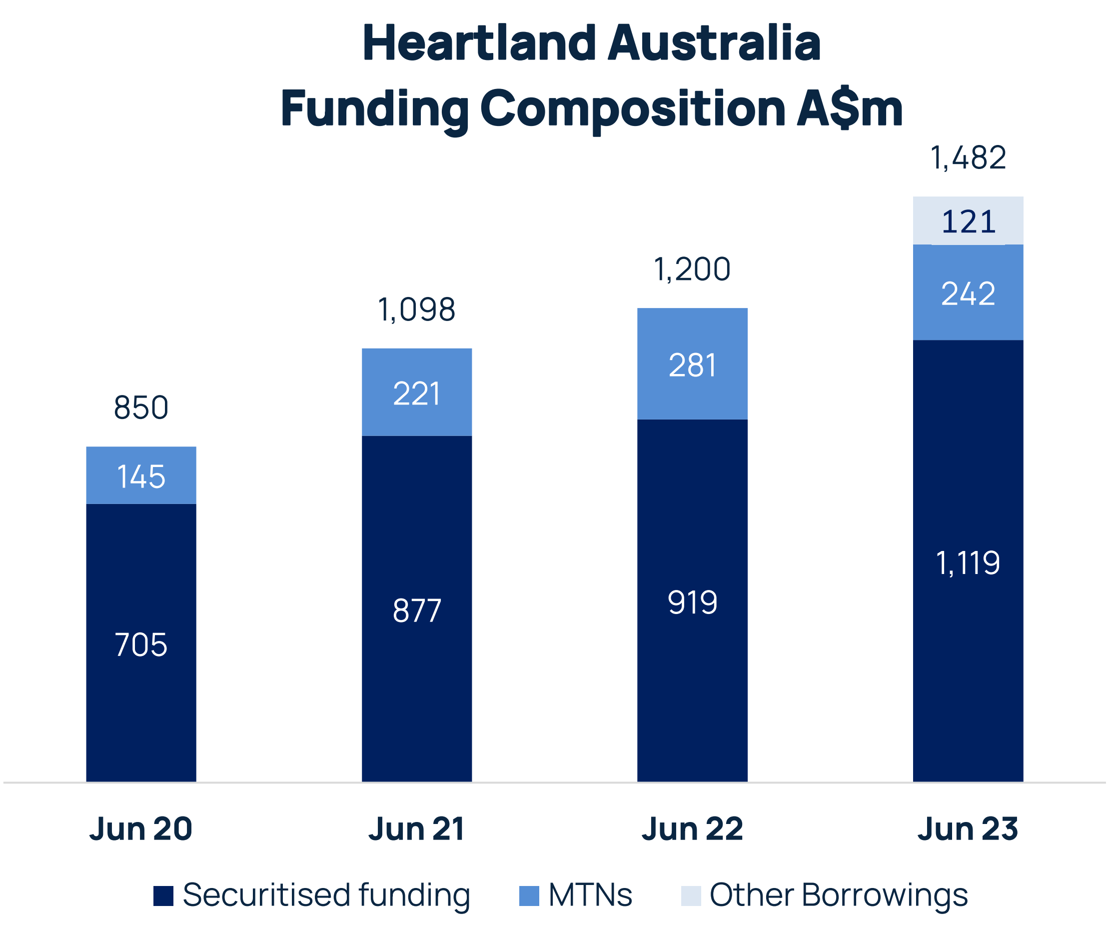
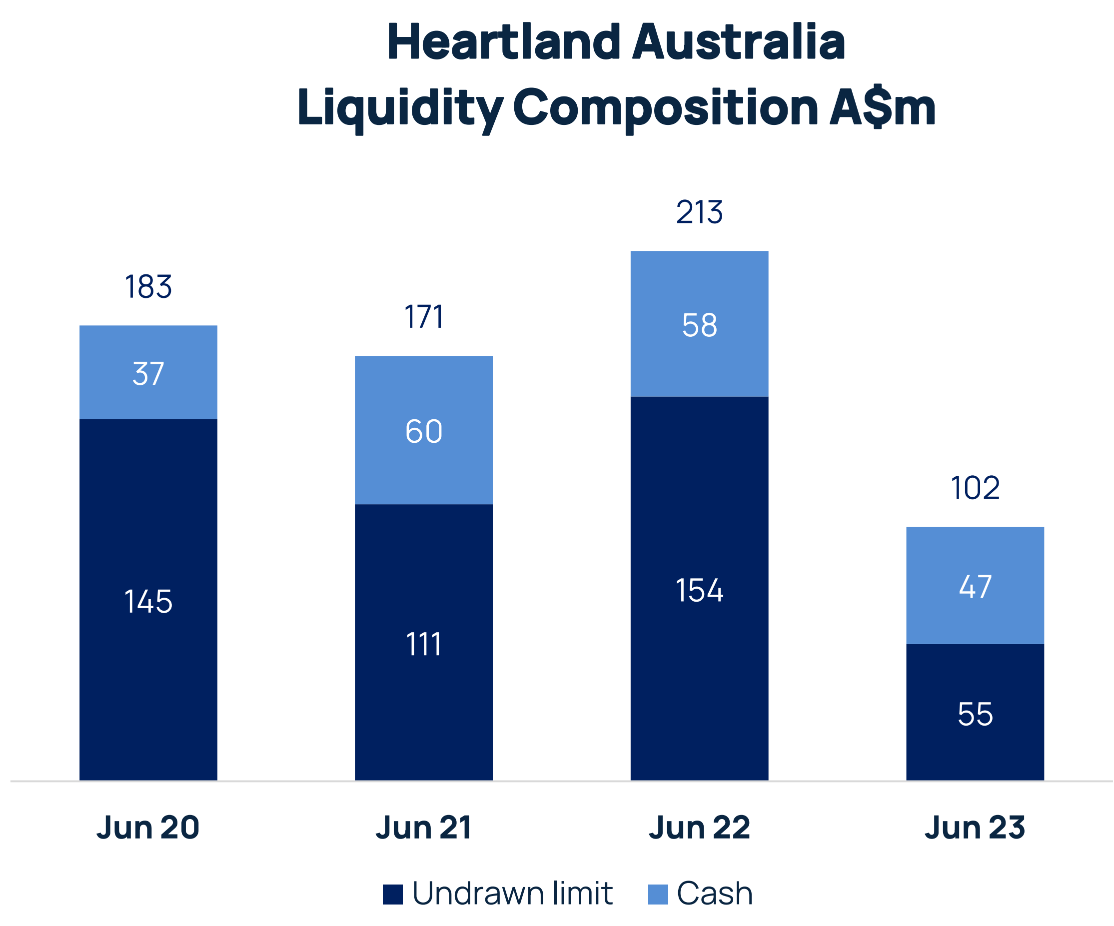
Heartland Australia[1]

- Heartland Australia increased borrowings by A$282.0 million (23.5%) to A$1,482.2 million.
- A A$30 million tap issue was completed in August 2022 and a further A$50 million MTN was issued in October 2022. Heartland Australia's April 2023 A$120 million MTN maturity was refinanced. This now takes the aggregate outstanding issuance under Heartland Australia's MTN programme to A$240 million as at 30 June 2023.
- Maturity of Reverse Mortgage securitisation warehouses were extended by two and three years, and aggregate senior limits were expanded by A$100 million, providing additional headroom to fund future growth in the portfolio. This provides Heartland Australia with access to A$1.54 billion of committed funding in aggregate.





StockCo Australia[2]

- StockCo Australia increased borrowings by A$17.2 million (5.2%) to A$346.4 million.

[1] Comprised of Heartland Australia Holdings Pty Ltd and its subsidiaries. [2] Comprised of StockCo Australia Management Pty Ltd, StockCo Holdings 2 Pty Ltd and their subsidiaries.

Capital

- Heartland Bank's regulatory capital ratio increased to 14.69% as at 30 June 2023 (30 June 2022: 13.49%). Heartland Bank continues to operate significantly in excess of regulatory minimums and is well positioned to meet the RBNZ's future higher capital requirements.
- In order to accelerate this journey, diversify its capital base and accommodate future projected growth, Heartland Bank issued $100 million unsecured subordinated Tier 2 capital notes in 2H2023.
- The RBNZ future capital requirements are for a core capital ratio of 11.50% and a total capital ratio of 16.00% by 1 July 2028.

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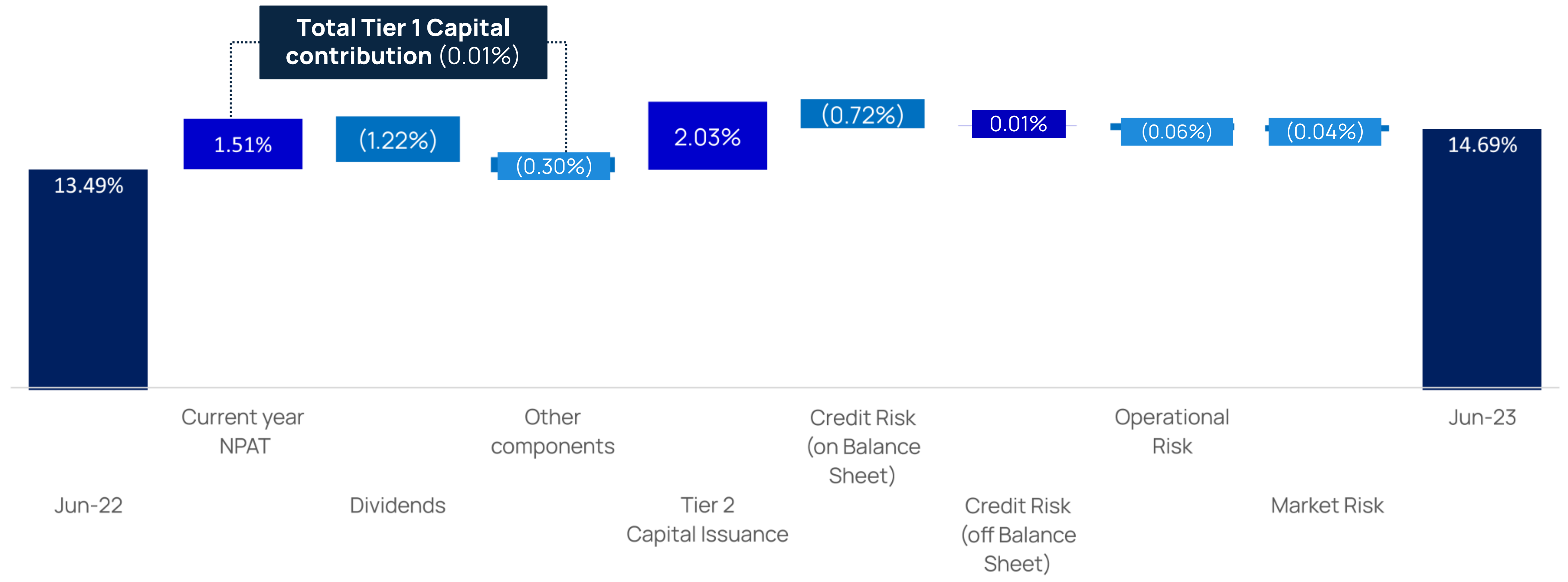
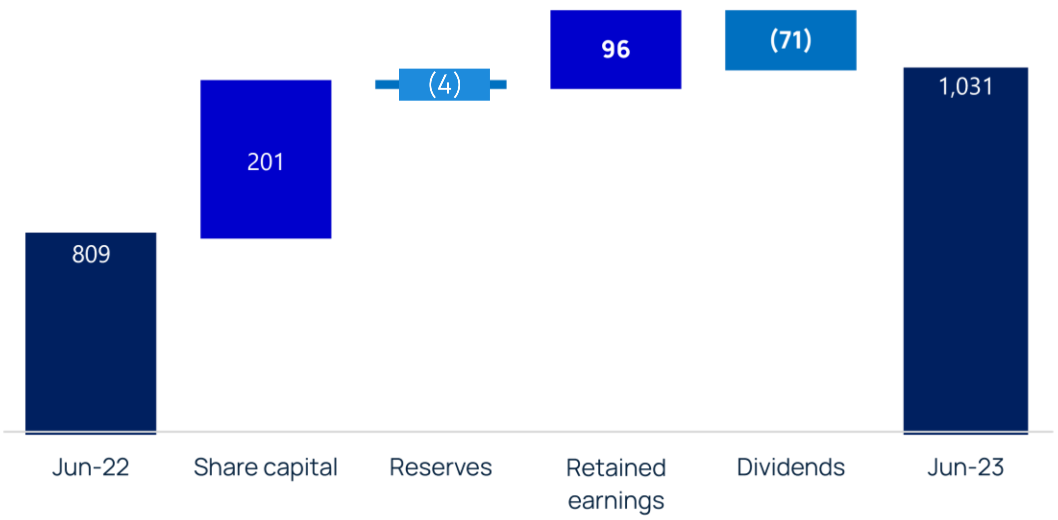
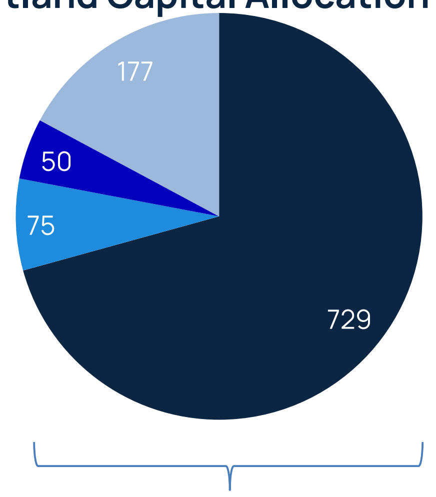
Heartland Bank Total Capital Ratio



Heartland Capital Movement $m



Heartland Capital Allocation $m



$1,031 million (13.3% of total assets) as at 30 June 2023

- Heartland Bank
- Heartland Australia
- StockCo Australia
- Heartland Group Holdings

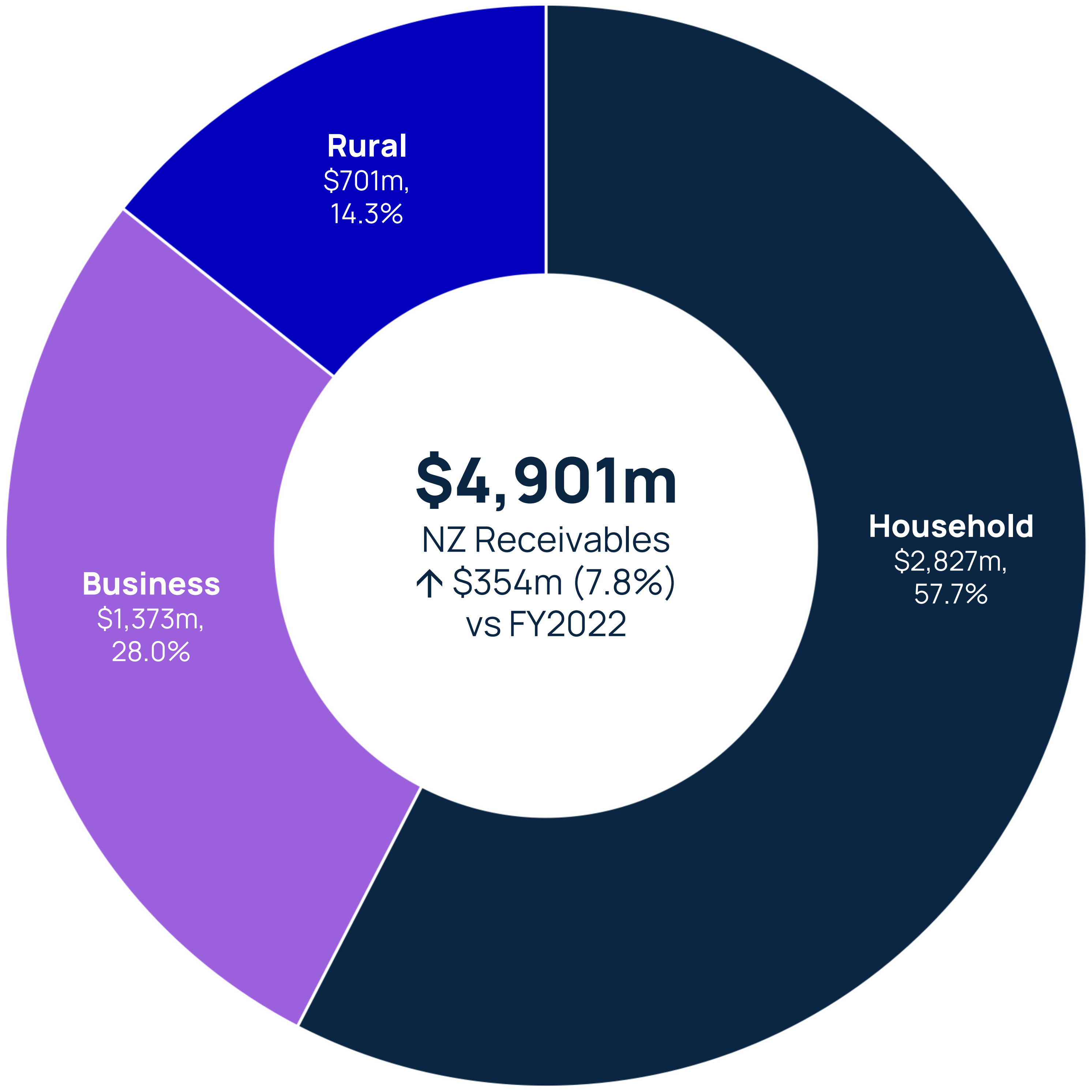
Note:
1. Increase in share capital is primarily as a result of a $199 million equity raise completed in September 2022.
2. Retained earnings includes current NPAT.

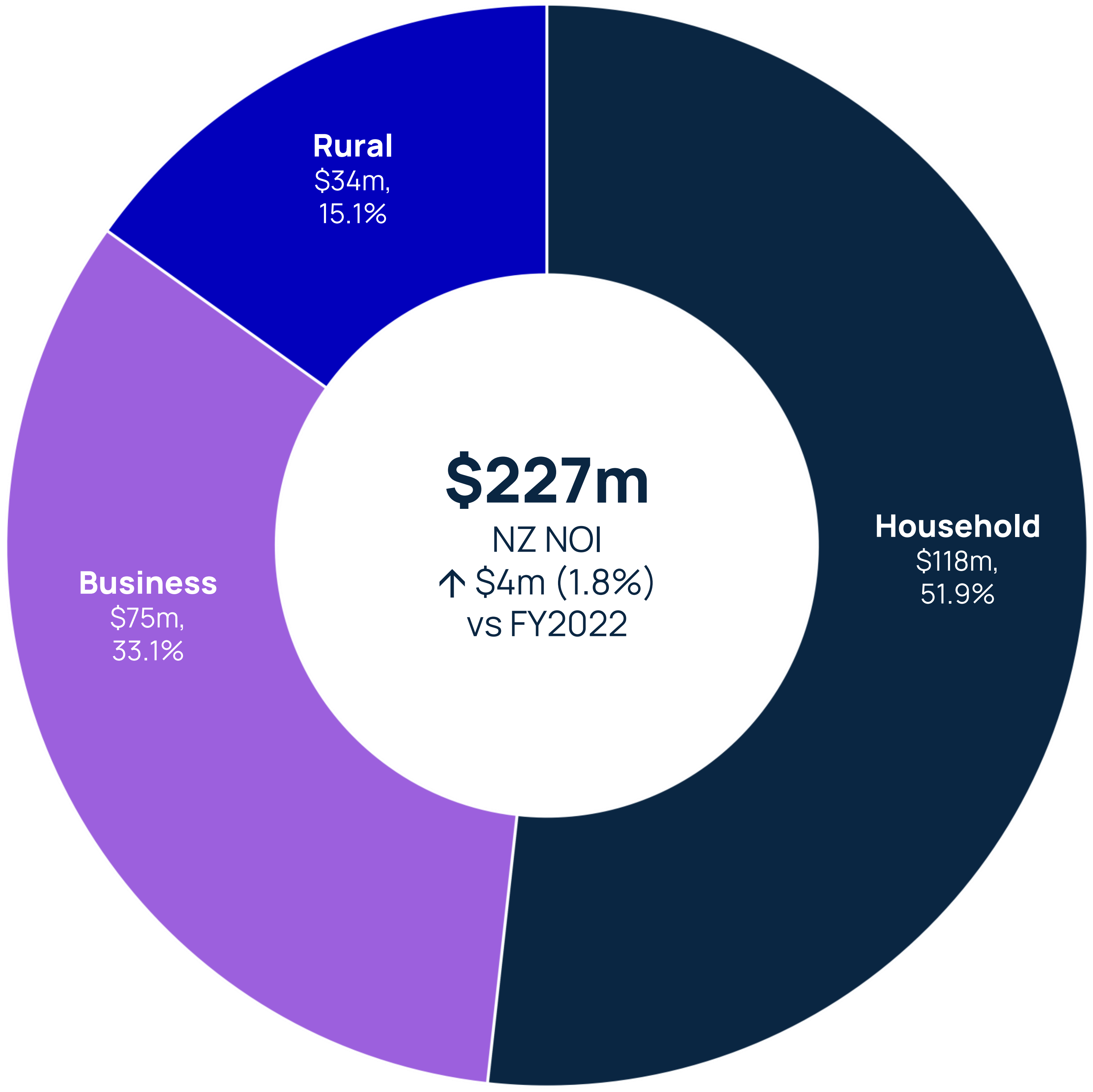
03

NZ divisional summary

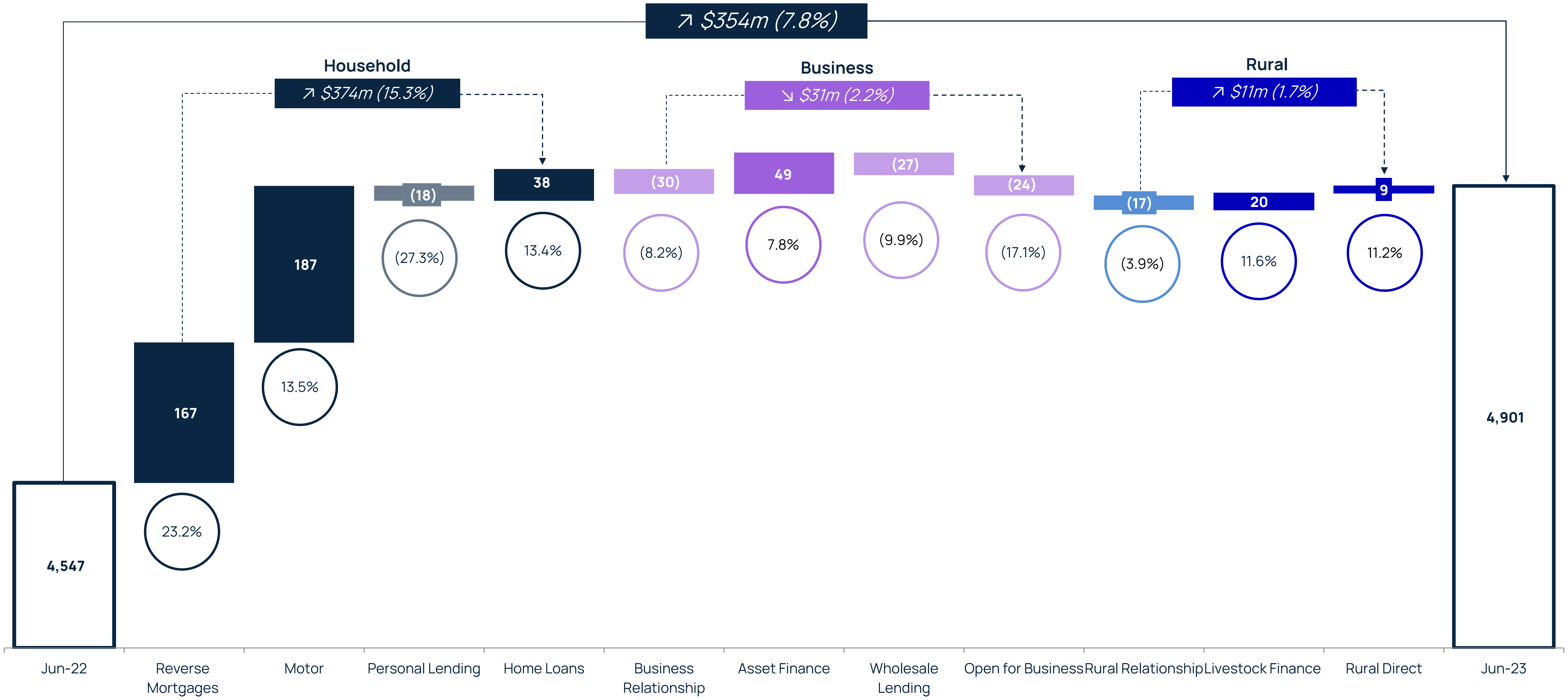
Leanne Lazarus
Chief Executive Officer Heartland Bank

NZ divisional summary



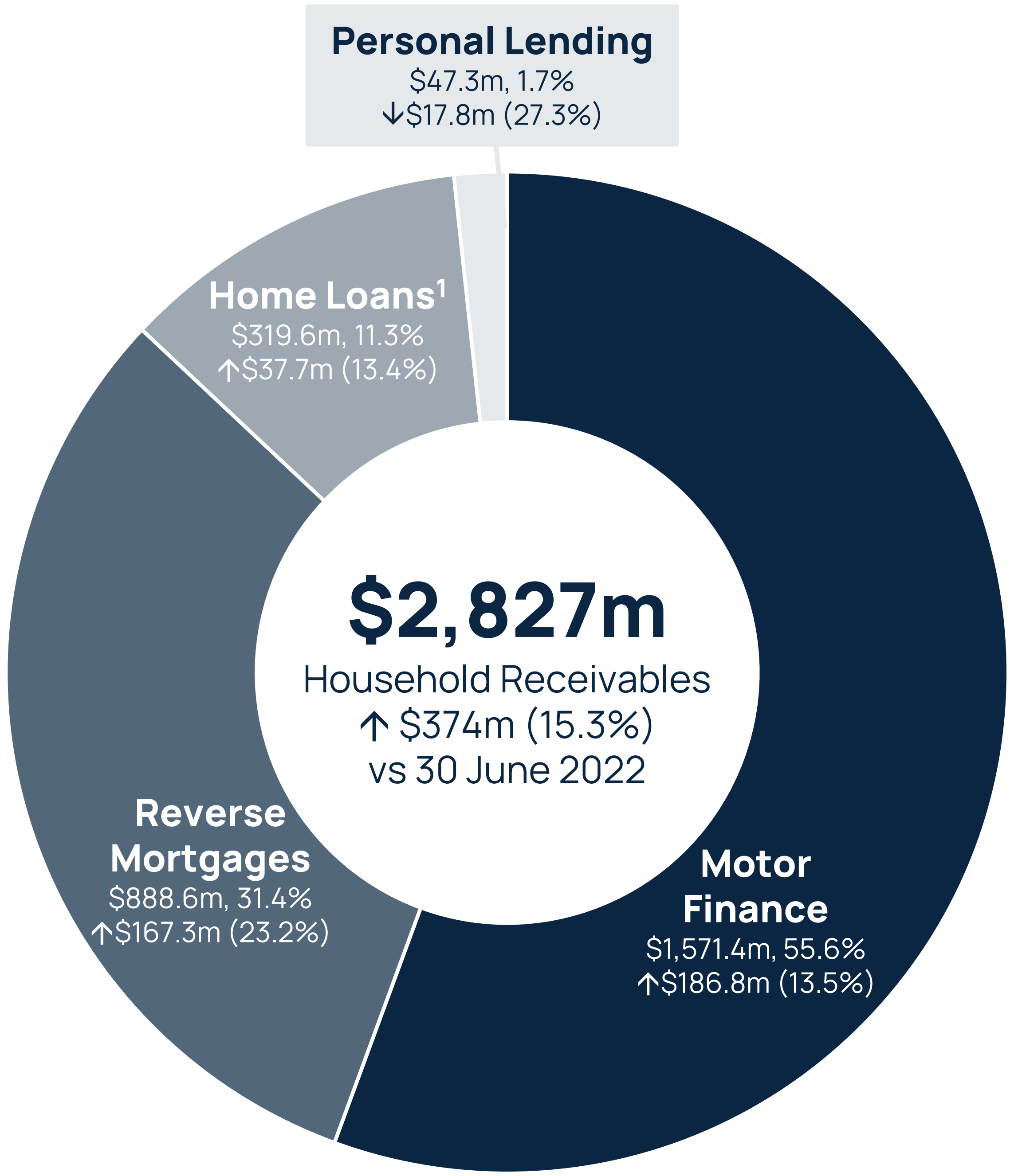


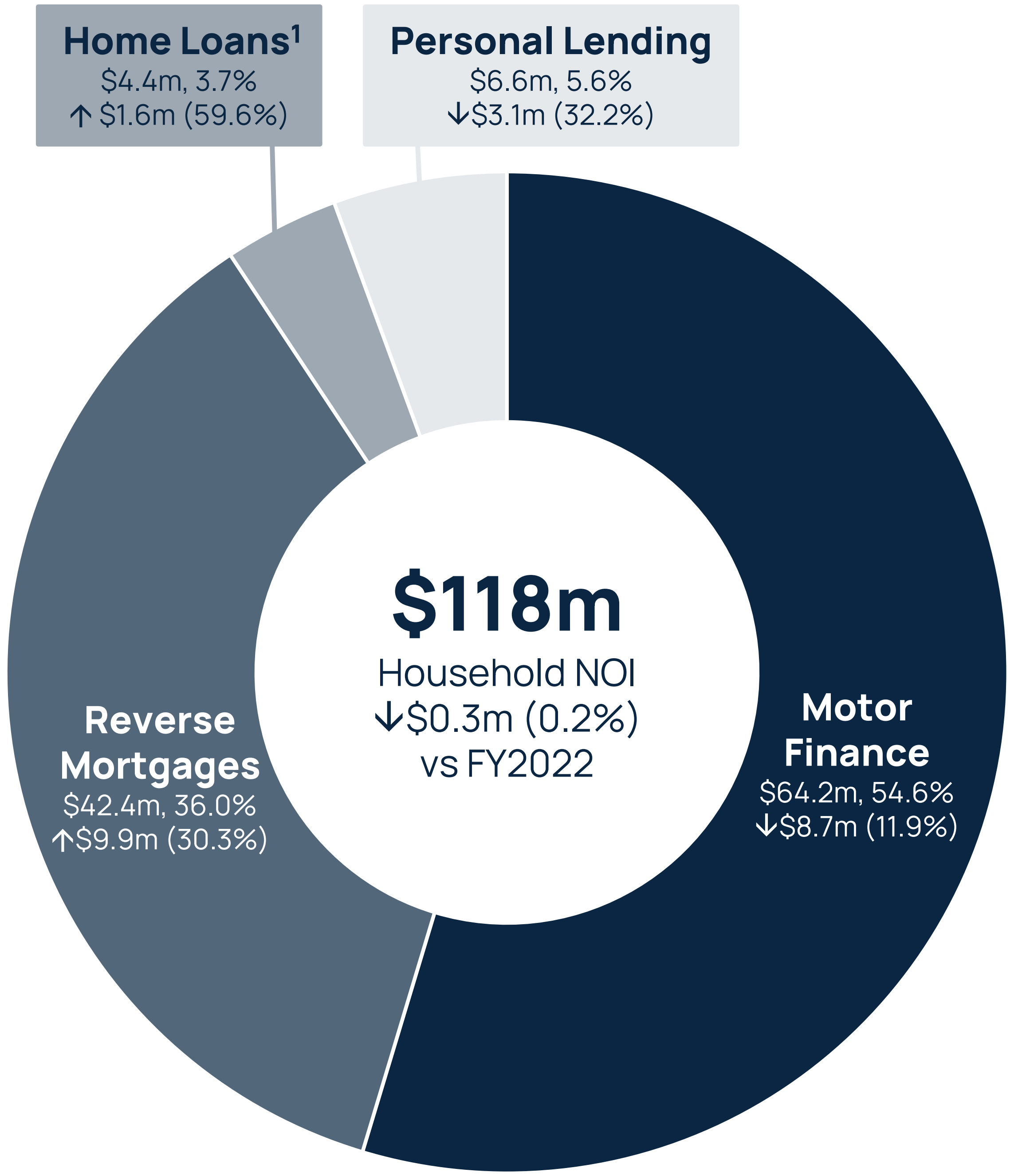
NZ divisional summary



Note: The graph shows FY2023 growth in receivables by portfolio excluding the impact of changes in FX rates and intercompany balances. All figures in NZ$m.

NZ Household





Motor Finance

- Strong growth of 13.5%. Market share gains made at the expense of margin, alongside general margin compression due to a shift in asset quality and competitive pressures.
- Broad distribution network and digital innovation were key contributing factors in achieving system growth in a difficult market.

Reverse Mortgages

- Strong demand due to increased education and awareness of reverse mortgages as a solution to the ongoing strains placed on older homeowners by cost of living and cash flow pressures.

Online Home Loans

- While subdued compared to FY2022, Online Home Loans experienced growth in a challenging economic environment.
- Retention exceeded 90% for customers whose fixed rates came up for renewal in FY2023.

Personal Lending[2]

- Includes loans originated directly through Heartland Bank, and those originated by Harmoney in NZ and AU.
- To manage risk in the current environment, this portfolio is not actively originating.
- The Harmoney personal loans channel is closed to new business and running down.

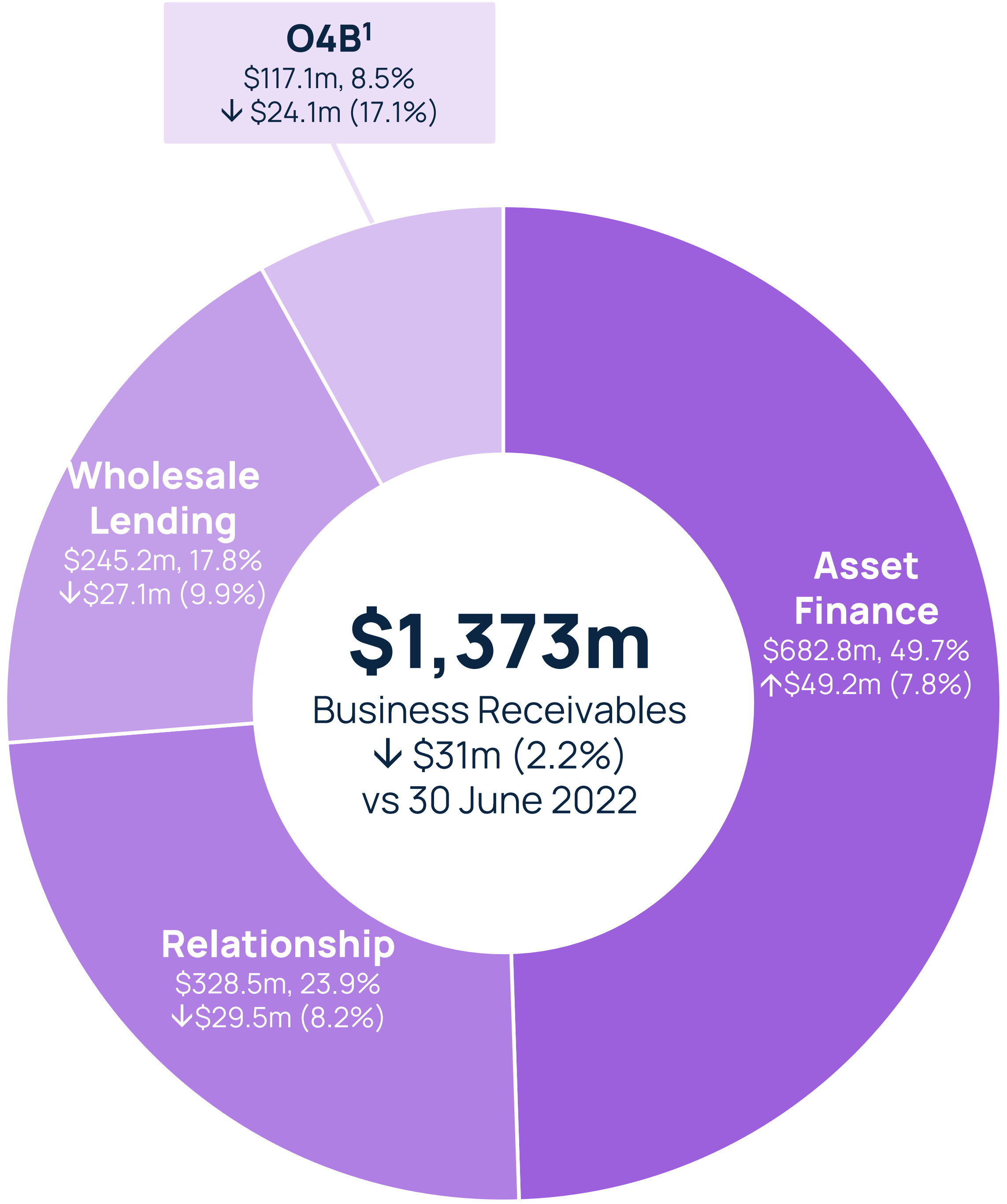
[1] Includes Online Home Loans and legacy Retail Mortgages.
[2] Excluding the impact of changes in FX rates.

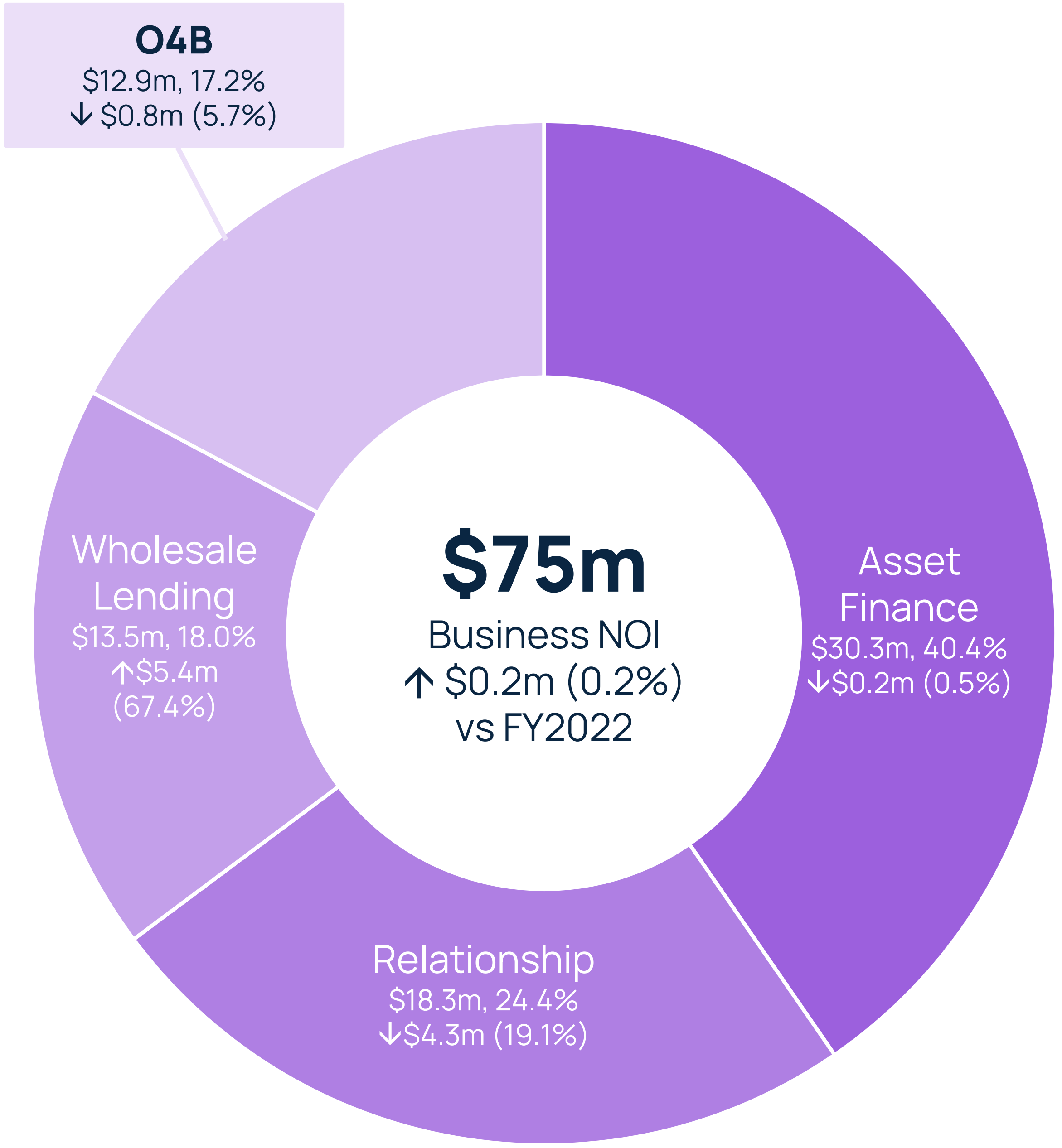
NZ Reverse Mortgages portfolio analytics

$889m NZ Reverse Mortgages +$167m (23.2%) vs June 2022	**$128,938** Average loan size	**78** Weighted average borrowers' age	**16.4%** Compounded annual growth rate[1]
9.8% Average origination LVR	**21.3%** Weighted average LVR	**0.0%** Proportion of the loan book over 75% LVR	**0** Number of loans in the book over 75% LVR
$197m (+$32m vs FY2022) FY2023 origination	**$97m** (+$12m vs FY2022) Total repayments in FY2023	**13.4%** (vs 14.0% in FY2022) FY2023 repayment rate	**31.8%** (vs 32.1% in FY2022) Repayments from vintage loans (+11 years)

[1] Compounded annual growth rate for the period 1 July 2018 – 30 June 2023.

NZ Business





Asset Finance

- Solid growth with continued focus on freight transport and yellow goods sectors.
- NIM affected by change in mix of new business weighted toward an improved credit profile. Lower margin loans being repaid and replaced, and expected to have a positive contribution to margin in late FY2024.

Wholesale Lending

- Includes floorplan lending to vehicle retailers and wholesale facilities to other lenders, including for medium enterprises that on-lend to their own customers in the consumer motor and business sectors.
- Utilisation of floorplan lending limits decreased due to unpredictable inventory conditions.

Relationship

- Includes legacy Business Relationship lending being run down as Heartland transitions to loans which present lower risk and are more cost efficient to transact.

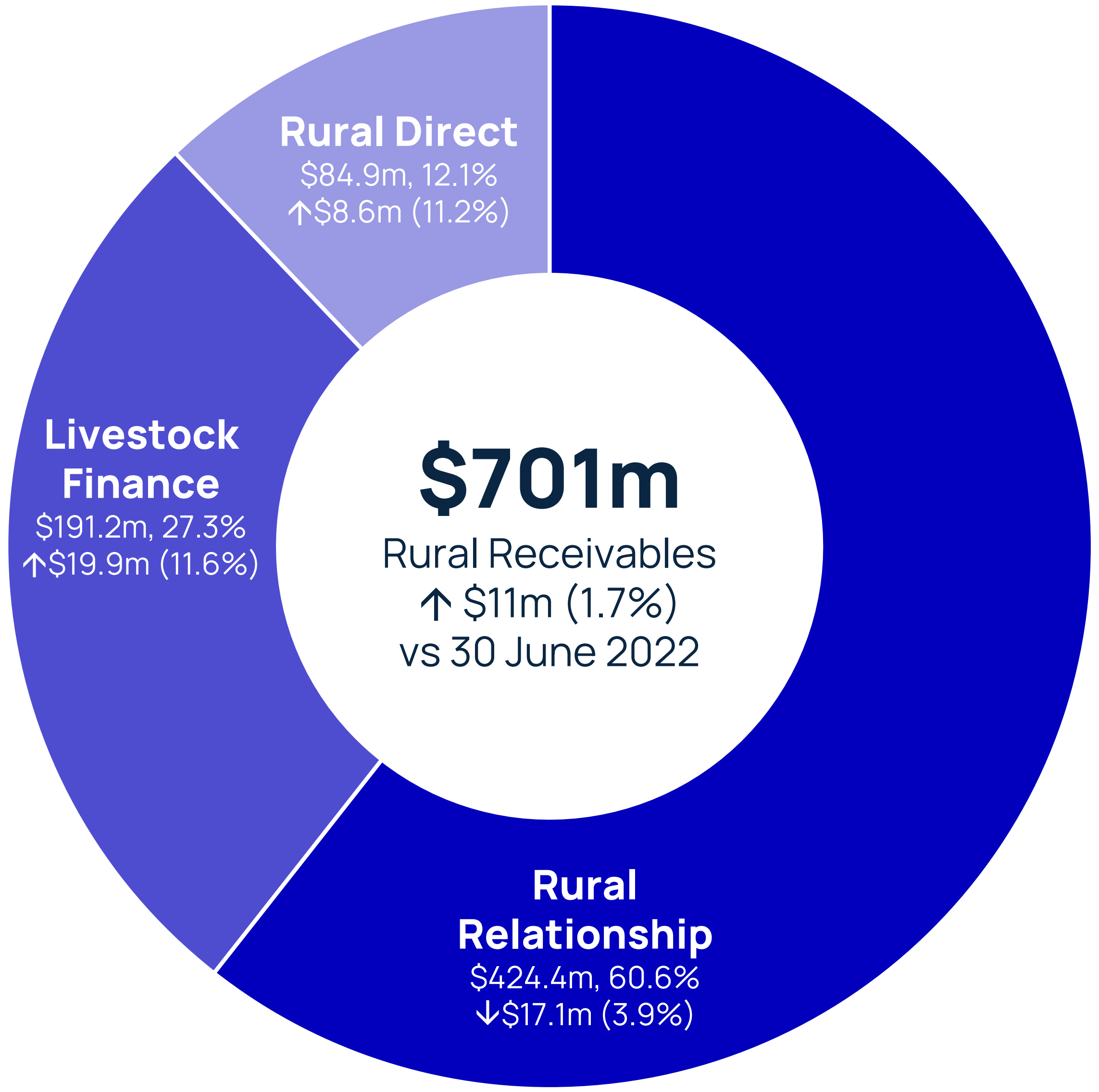
O4B[1]

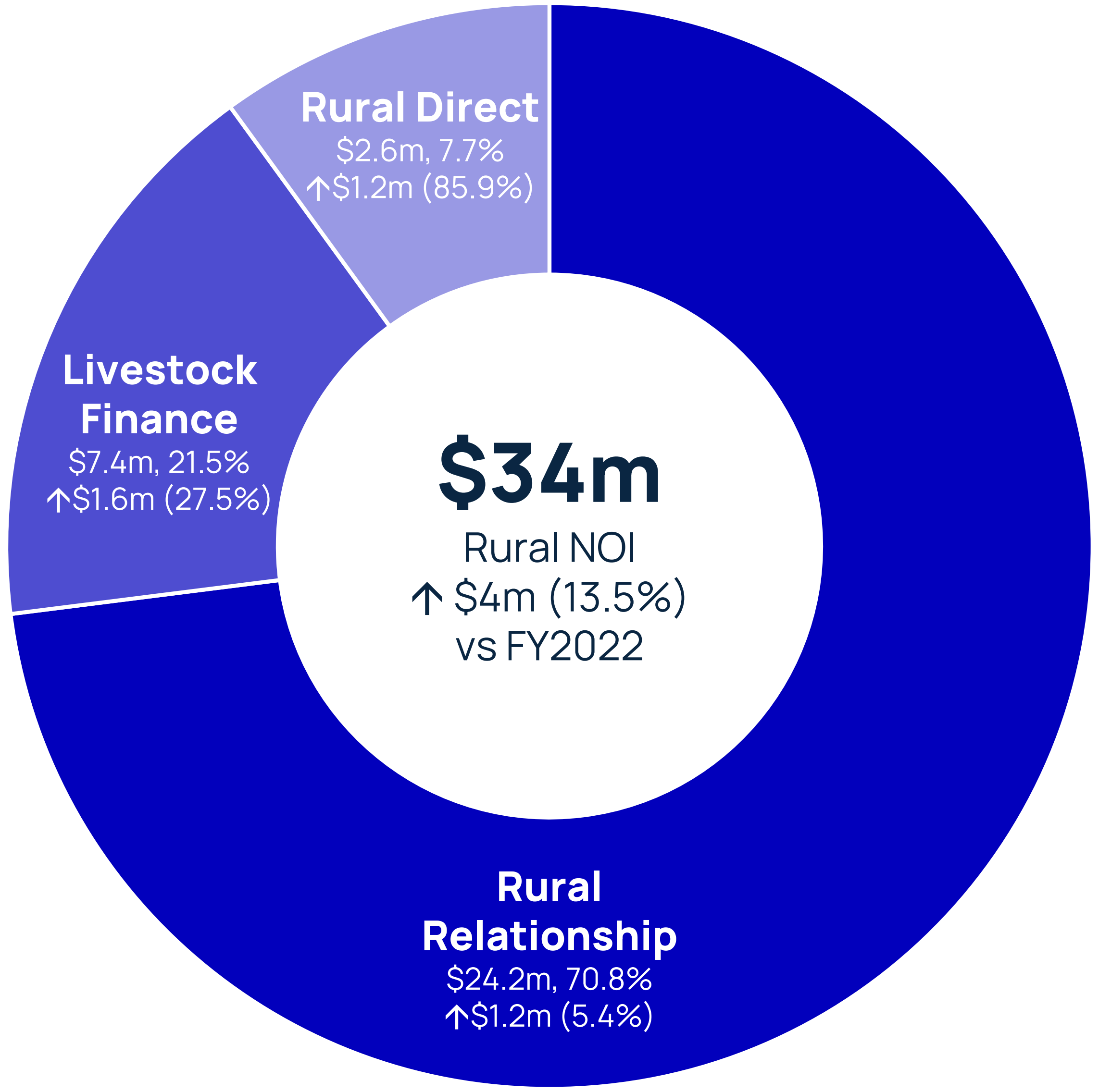
- Stopped actively originating in Q2 to manage risk due to the macro-economic challenges for the SME sector.

[1] Excluding the impact of changes in FX rates.

03

NZ Rural





Rural Relationship

- Reduction in Receivables of $17.1m due to the continued transition of the book away from large, complex, low margin lending.
- Heartland's exposure to the dairy sector reduced to 32.8% of the total Rural book.

Livestock Finance

- Growth of 11.6% in a market impacted by falling commodity prices, difficult climatic conditions and Cyclone Gabrielle in the Hawke's Bay and Tairāwhiti regions.
- 6% of growth originated from the addition of key intermediary partnerships, with the balance from existing customers.

Rural Direct

- Online platforms which are lower risk and cost efficient to transact.
- Includes Heartland's Sheep & Beef Direct and Dairy Direct products, providing online finance to sheep, beef and dairy farmers.

CTI ratio reduction initiatives

A number of initiatives are being delivered through a systemised programme of work to enhance digital, self-service and automation capabilities.

Four key automation and digitalisation initiatives:

Zero inbound calls

Digitise basic banking requests to enable customers to self-serve via the Heartland Mobile App, create a seamless user experience, and reduce inbound customer call volumes. In doing so, employees will be able to focus on more complex customer requests.

- **Heartland Bank's ambition is to reduce inbound customer call volumes by approx. 73% by 30 June 2025 by developing Mobile App self-service features to address the top reasons for inbound customer calls.**

One-Click Deferral

Offer flexibility for customers to self-manage their Motor Finance loan repayments digitally via the Mobile App, including customers in arrears.

- **Develop seven new functions and features to enable customers to self-manage repayments, reducing the need for customers to contact Heartland Bank.**

Process automation

Upgrade and introduce scalable digital technologies to optimise back-end processes and improve efficiency.

Increase automation to improve workflows and reduce manual effort, reducing friction for customers and employees.

- **Heartland Bank's ambition is to automate approx. 65% of operations and collections manual processes by 30 June 2025.**

Motor digitalisation

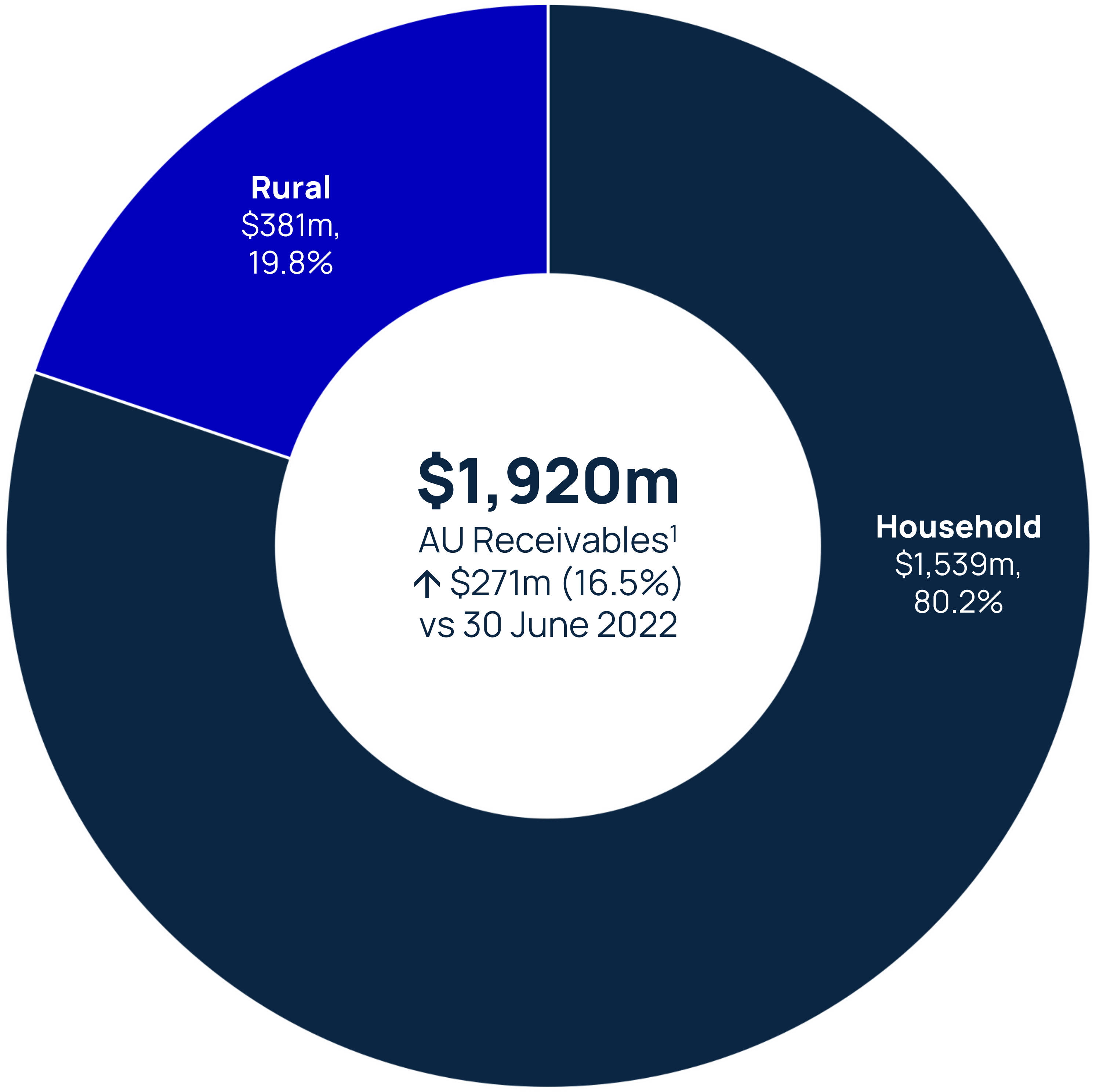
- Continued enhancement of Motor Finance digital capabilities to enable faster and easier access to vehicle finance through online application platforms.
- **Intention to rollout seven branded online origination platforms to Motor Finance dealer partners in FY2024.**

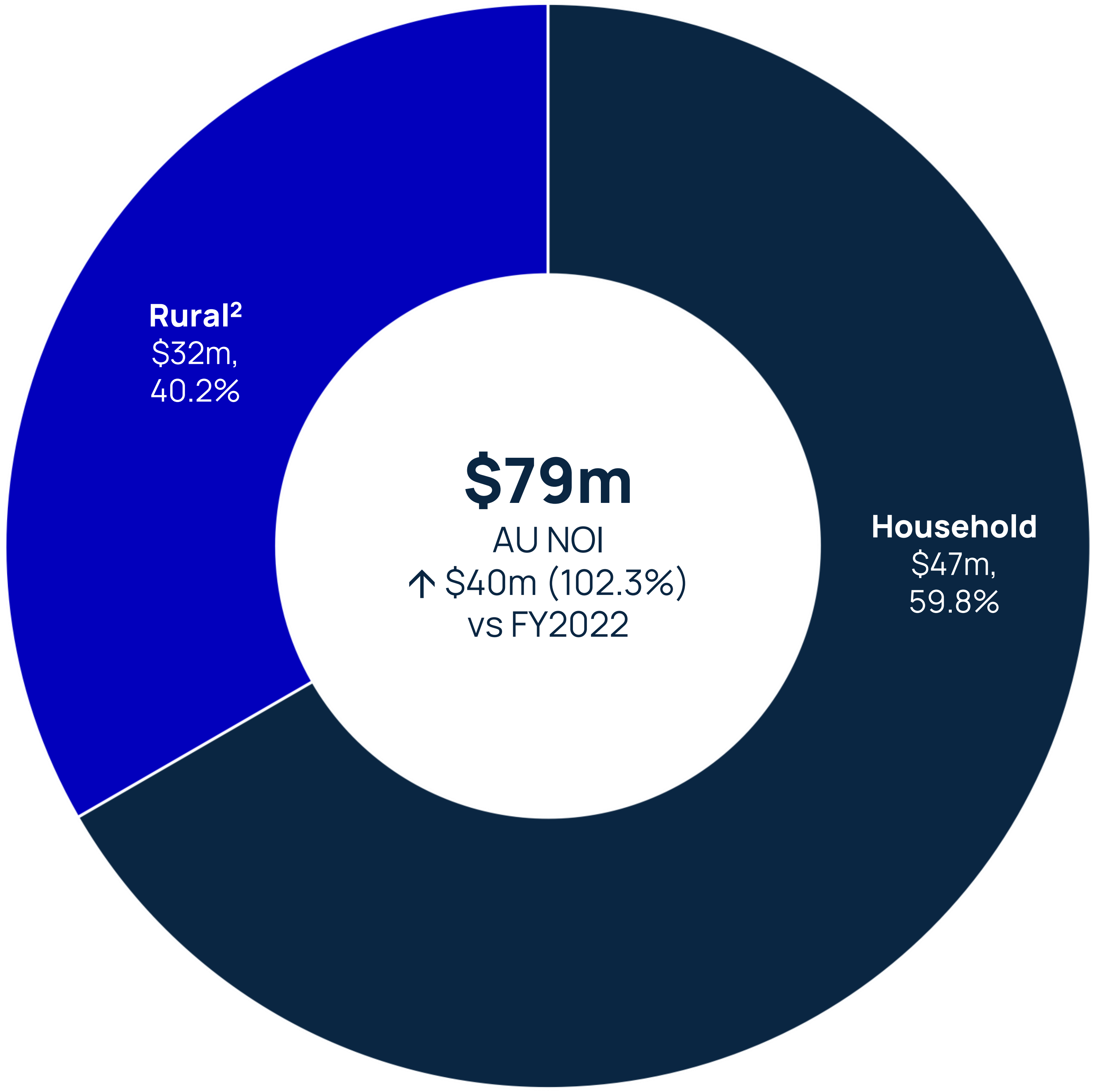
04

AU divisional summary

Chris Flood
Deputy Chief Executive Officer Heartland Group

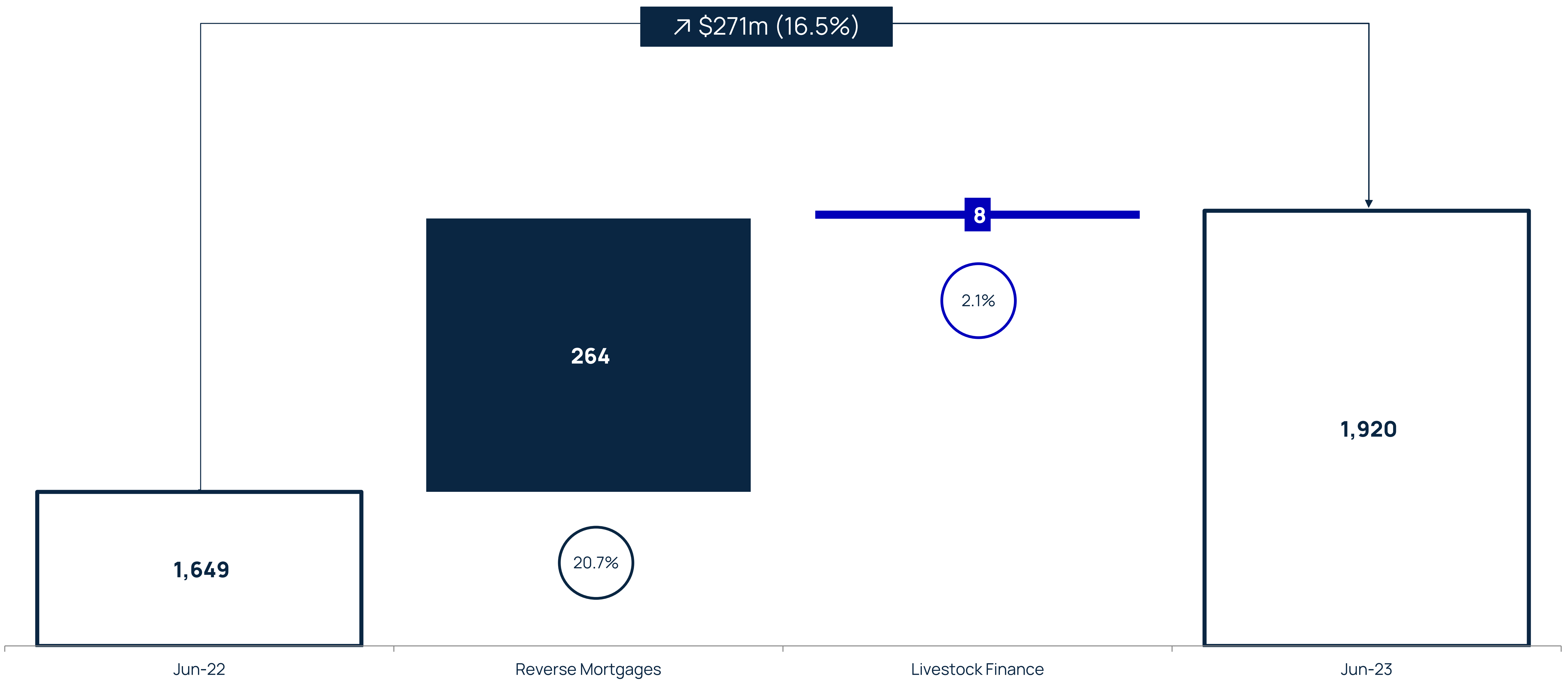
AU divisional summary





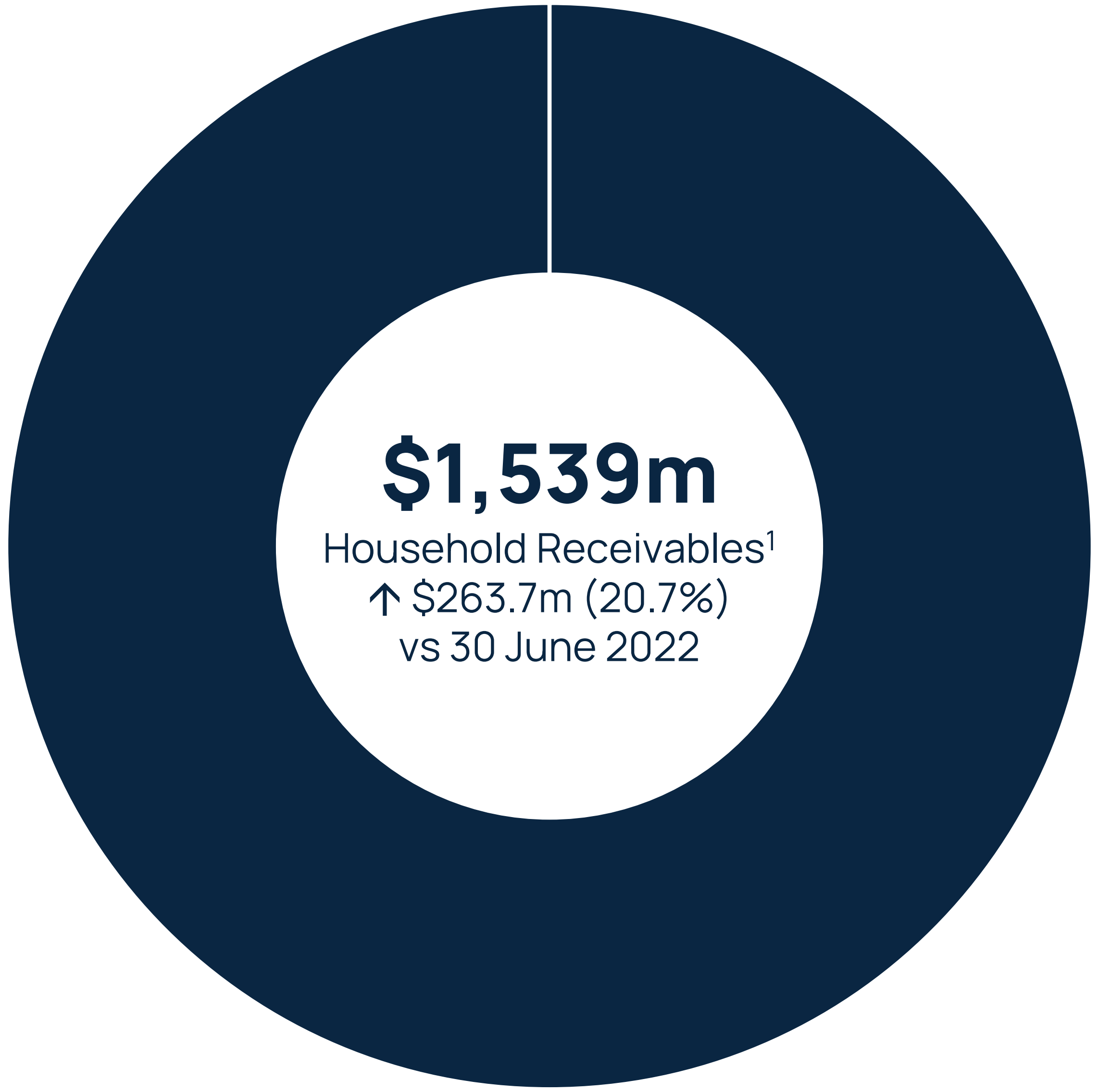
[1] Excluding the impact of changes in FX rates
[2] Includes full year contribution of StockcCo Australia since the completion of acquisition on 31 May 2022.

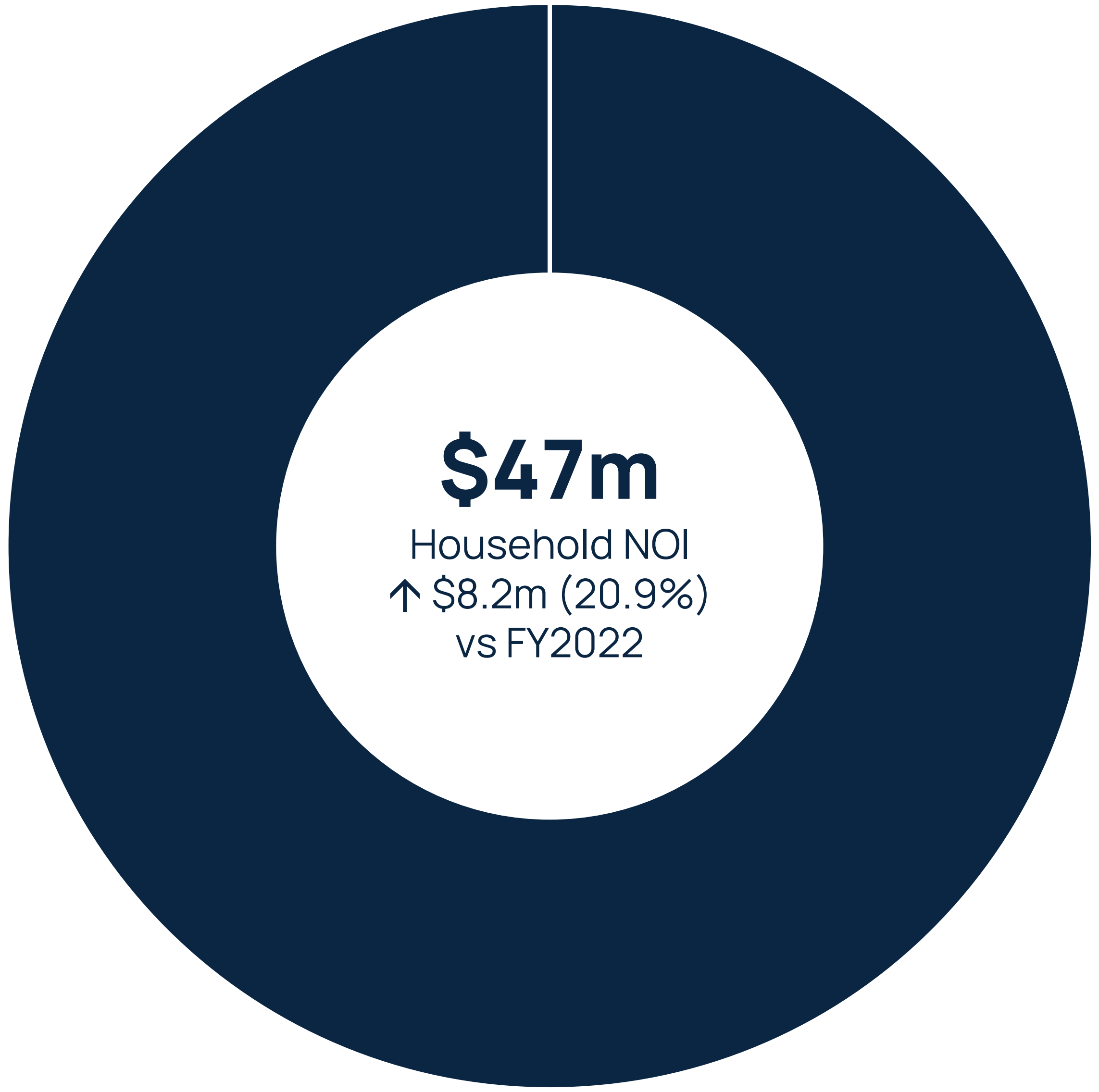
AU divisional summary



Note: The graph shows FY2023 growth in receivables by portfolio excluding the impact of changes in FX rates and intercompany balances. All figures in NZ$m.

AU Household





Reverse Mortgages[1]

- Growth was driven by increased debt consolidation and cost of living requests due to current economic environment, and customers seeking funds to age in place more comfortably.
- Growth is expected to remain strong in FY2024 as ongoing improvements and efficiencies are made to the loan application, approval and maintenance process.

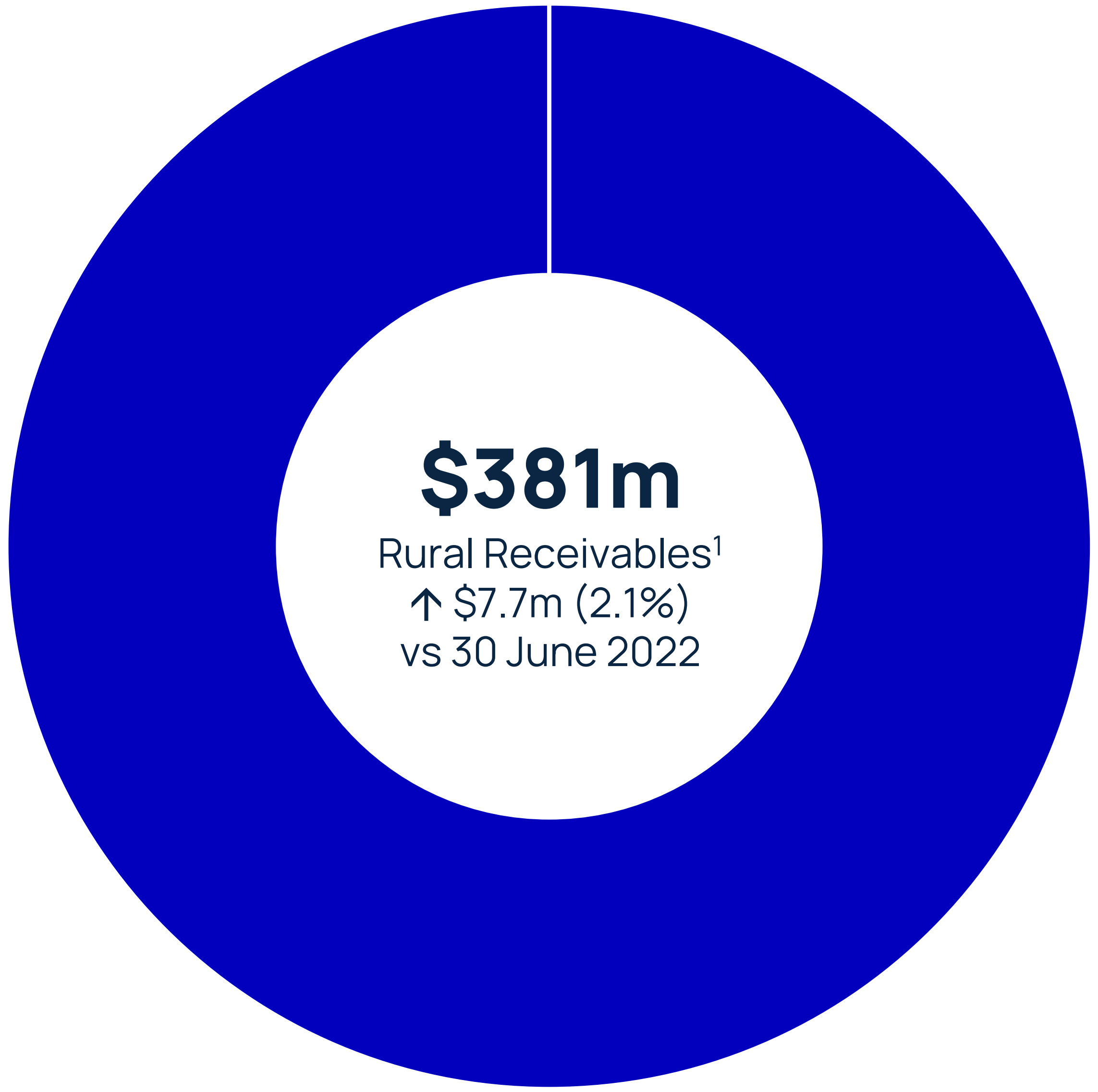
[1] Excluding the impact of changes in FX rates.

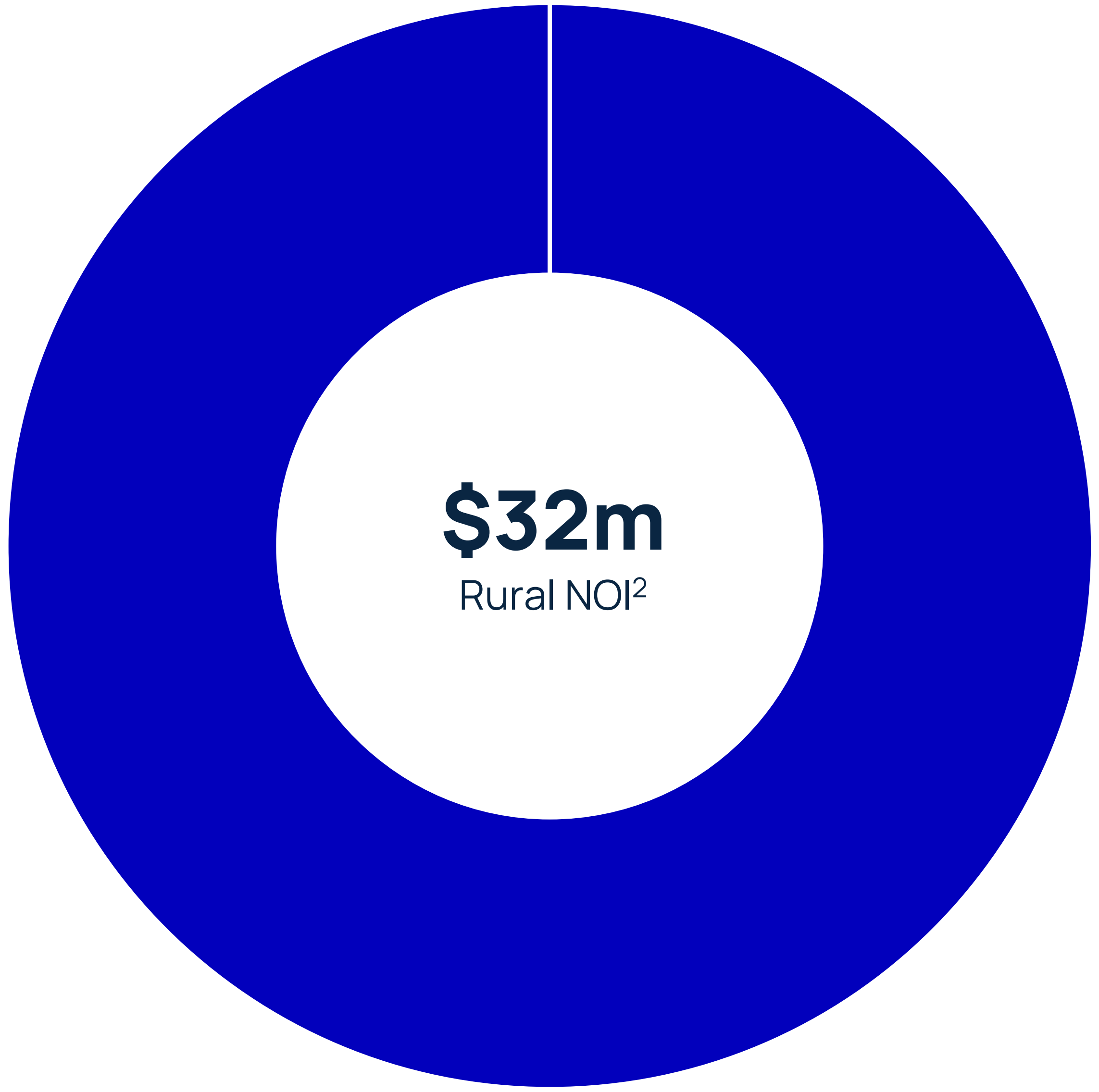
AU Reverse Mortgages portfolio analytics[1]

$1,539m AU Reverse Mortgages +$264m (20.7%) vs June 2022	**$180,432** Average loan size	**77** Weighted average borrowers' age	**22.8%** Compounded annual growth rate[2]
11.7% Average origination LVR	**21.5%** Weighted average LVR	**0.0%** Proportion of the loan book over 75% LVR	**1** Number of loans in the book over 75% LVR
$349m (+$78m vs FY2022) FY2023 origination	**$197m** (+$30m vs FY2022) Total repayments in FY2023	**16.0%** (vs 15.7% in FY2022) FY2023 repayment rate	**16.1%** (vs 19.0% in FY2022) Repayments from vintage loans (+11 years)

[1] All figures in NZD, excluding the impact of changes in FX rates (where applicable).
[2] Compounded annual growth rate for the period 1 July 2018 – 30 June 2023.

AU Rural





Livestock Finance

- Subdued growth was due to macroeconomic events affecting livestock prices and demand, including adverse weather conditions, the rising interest rate environment, and low export demand with the USA drought and China's COVID-19 response contributing to freezers being full around the world.
- Despite lower dollars per head, the volume of livestock financed increased. At 30 June 2023, cattle was up 25% compared with 30 June 2022. Sheep transactions were flat.
- Direct client growth of 11%.
- Processor capacity has been strained due to a lack of skilled workers, the ongoing impacts of COVID-19 and adverse weather conditions. Slaughter production in 2022 was down approximately 27% from 2021 volumes. This is expected to improve in the first half of FY2024 and have a positive effect on livestock demand and value, as processors work through their backlog.
- The outlook is positive with demand for protein expected to increase and have a positive effect on livestock value.

[1] Excluding the impact of changes in FX rates
[2] Includes full year contribution of StockcCo Australia since the completion of acquisition on 31 May 2022.

05

Outlook

Jeff Greenslade
Chief Executive Officer Heartland Group

Outlook

Business as usual growth

- Heartland's strength is its track record of strong growth in core lending portfolios.
- Growth focus will be on Reverse Mortgages, Motor Finance, Asset Finance and Livestock Finance.
- Supported by ongoing digitalisation and automation of lending platforms.
- Leverage demographic-driven demand in Reverse Mortgages.

NIM stabilisation

- NIM outlook is stable with repayment and replacement of legacy lower margin Motor Finance and Asset Finance loans.
- Growth mix will continue to influence margin, causing acceptable contraction offset by corresponding growth.

Ambition to double underlying NPAT within 5 years

- Since 2012, Heartland's NPAT has more than tripled.
- Ambition to continue track record of income growth by doubling underlying NPAT within 5 years.

Obtain an ADI licence

- Complete Challenger Bank acquisition, which remains subject to RBNZ and APRA approval. Heartland's desire is to complete the acquisition in the 2023 calendar year.
- Post-completion, Heartland's focus will be on integration and leveraging its common distribution channels in NZ to expand into AU.

Ambition to reduce underlying CTI ratio to <35% by FY2028

- Digitalisation initiatives underway to improve operational efficiency and increase customer self-service functionality, including One-Click Deferral, reducing telephony, and further automation.
- Revenue growth and careful management of costs critical pathways to a reduced CTI ratio.
- Stable CTI ratio expected while investment and delivery of initiatives continues .

FY2024 NPAT

- Heartland expects NPAT for FY2024 to be within the guidance range of $116 million to $122 million, excluding any impacts of fair value changes on equity investments held and the impact of the de-designation of derivatives, and any costs related to the acquisition of Challenger Bank, which remains subject to RBNZ and APRA approval.
- As the acquisition nears completion, guidance will be updated to reflect the impact of Challenger Bank becoming part of Heartland.

06

Disclaimer, glossary & appendices

Disclaimer

This presentation has been prepared by Heartland Group Holdings Limited (**NZX/ASX: HGH**) (the **Company** or **Heartland**) for the purpose of briefings in relation to its financial statements.

The presentation and the briefing (together the **Presentation**) contain summary information only, which should not be relied on in isolation from the full detail in the financial statements.

The information in the Presentation has been prepared with due care and attention, but its accuracy, correctness and completeness cannot be guaranteed. No person (including the Company and its directors, shareholders and employees) will be liable to any other person for any loss arising in connection with the Presentation.

The Presentation outlines a number of the Company's forward-looking plans and projections. Those plans and projections reflect current expectations, but are inherently subject to risk and uncertainty, and may change at any time. There is no assurance that those plans will be implemented or that projections will be realised. You are strongly cautioned not to place undue reliance on any forward-looking statements, particularly in light of the current economic climate.

No person is under any obligation to update this presentation at any time after its release or to provide further information about the Company.

The information in this presentation is of a general nature and does not constitute financial product advice, investment advice or any recommendation. Nothing in this presentation constitutes legal, financial, tax or other advice.

Non-GAAP measures

This presentation contains references to non-GAAP measures including underlying profit or loss, underlying ROE, underlying CTI ratios and underlying EPS. A reconciliation between reported and the non-GAAP measure of underlying financial information is included on page 42.

Because Heartland complies with accounting standards, investors know that comparisons can be made with confidence between reported profits and those of other companies, and there is integrity in Heartland's reporting approach. These non-GAAP figures are provided as a supplementary measure for readers to assess Heartland's performance alongside NZ GAAP reported measures, where one-offs, both positive and negative, can make it difficult to compare profits between years. However, these non-GAAP measures do not have standardised meanings prescribed by GAAP and should not be viewed in isolation nor considered a substitute for measures reported in accordance with NZ GAAP.

Non-GAAP financial information has not been subject to review by PricewaterhouseCoopers, Heartland's external auditor.

All amounts are in New Zealand dollars unless otherwise indicated. Financial data in this presentation is as at 30 June 2023 unless otherwise indicated. Any other financial information provided as at a date after 30 June 2023 has not been audited or reviewed by any independent registered public accounting firm.

Glossary

ABP	Australia Bank Programme	NII	Net interest income
ADI	Authorised deposit-taking institution	NIM	Net interest margin
ANZSIC	Australian and New Zealand Standard Industrial Classification	NOI	Net operating income
APRA	Australian Prudential Regulation Authority	NPAT	Net profit after tax
bps	Basis points	O4B	Open for Business
CCCFA	New Zealand Credit Contracts and Consumer Finance Act 2003	OOI	Other Operating Income
Challenger Bank	Challenger Bank Limited	OPEX	Operating expenses
cps	Cents per share	pps	Percentage points
CTI ratio	Cost to income ratio	RBNZ	Reserve Bank of New Zealand
DRP	Dividend Reinvestment Plan	Receivables	Gross Finance Receivables
EPS	Earnings per share	ROE	Return on Equity
FX	Foreign currency exchange	SME	Small-to-medium sized enterprise
Harmoney	Harmoney Corp Limited	TSR	Total shareholder return
Heartland	Heartland Group Holdings Limited or the **Company**	Q1	First quarter of FY2023 (1 July to 30 September 2022)
Heartland Australia Group	Heartland Australia Holdings Pty Ltd and its direct and indirect wholly-owned subsidiaries	Q2	Second quarter of FY2023 (1 October to 31 December 2022)
Heartland Bank, HBL	Heartland Bank Limited	Q4	Fourth quarter of FY2023 (1 April to 30 June 2023)
LVR	Loan-to-value ratio	1H2023	First half of FY2023 (1 July to 31 December 2022)
MTN	Medium Term Note	2H2023	Second half of FY2023 (1 January to 30 June 2023)

Appendix 1: Financial performance

	Reported				Underlying			
$m	FY2023	FY2022	Change ($)	Change (%)	FY2023	FY2022	Change ($)	Change (%)
NII	282.0	250.1	31.8	12.7%	283.9	248.3	35.6	14.3%
OOI[1]	3.3	17.5	(14.1)	(81.0%)	16.9	13.7	3.1	22.7%
NOI	**285.3**	**267.6**	**17.7**	**6.6%**	**300.7**	**262.0**	**38.7**	**14.8%**
OPEX	128.1	116.8	11.3	9.7%	126.2	111.4	14.9	13.4%
Impairment Expense	23.2	13.8	9.4	68.1%	23.2	15.7	7.5	47.9%
Profit Before Tax	134.0	137.0	(3.0)	(2.2%)	151.2	134.9	16.3	12.1%
Tax Expense	38.1	41.9	(3.8)	(9.0%)	41.1	38.8	2.3	5.8%
NPAT	95.9	95.1	0.7	0.8%	110.2	96.1	14.1	14.6%
NIM	3.97%	4.05%	(8 bps)		4.00%	4.16%	(16 bps)	
CTI	44.9%	43.6%	126 bps		42.0%	42.5%	(53 bps)	
Impairment Expense Ratio[2]	0.36%	0.25%	11 bps		0.36%	0.29%	7 bps	
ROE	10.4%	12.1%	(169 bps)		11.9%	12.6%	(68 bps)	
EPS	14.0 cps	16.1 cps	(2.1 cps)		16.0 cps	16.3 cps	(0.3 cps)	

[1] Includes fair value movements. [2] Impaired asset expense as a percentage of average Receivables.

Appendix 2: Financial position

$m	30 June 2023	30 June 2022	Movement ($m)	Movement (%)
Liquid Assets	627	585	42	7.1%
Gross Finance Receivables	6,791	6,196	596	9.6%
Provisions	(53)	(52)	(1)	(2.4%)
Other Assets	383	362	21	5.8%
Total Assets	**7,747**	**7,090**	**657**	**9.3%**
Retail Deposits	*4,131*	*3,593*	*539*	*15.0%*
Other Borrowings	*2,496*	*2,578*	*(82)*	*(3.2%)*
Total Funding	6,627	6,171	457	7.4%
Other Liabilities	89	111	(22)	(19.7%)
Equity	1,031	809	222	27.5%
Total Equity & Liabilities	**7,747**	**7,090**	**657**	**9.3%**

Appendix 3: Reconciliation of reported with underlying results

FY2023 one-offs included in the reported result:

- *Hedging*: a $9.1 million loss was recognised in relation to derivatives that were de-designated from prior hedge accounting relationships in FY2022.
- *Valuation of equity investments*: a $4.5 million fair value loss was recognised on investment in Harmoney shares.
- *Bridging loan:* a $1.9 million interest expense was recognised for a $174 million (A$158 million) bridging loan taken by Heartland to acquire StockCo Australia, which was fully repaid in September 2022.
- *Other provisions:* $0.7 million of unwarranted legacy provisions were released.
- *ABP costs*: $2.2 million of transaction and other costs in relation to becoming an ADI in Australia. In addition, $6.4 million of costs directly attributable to applying to become an ADI have been capitalised as an intangible asset.
- *Other non-recurring expenses:* $0.3 million.

FY2022 one-offs included in the reported result:

- *Hedging:* A $16.7 million gain was recognised in relation to derivatives that were de-designated from hedge accounting relationships.
- *Valuation of equity investments:* a $12.7 million fair value loss was recognised on investment in Harmoney shares, and a further $0.3 million fair value loss was recognised on Heartland Bank's rights over a profit-sharing arrangement with a customer.
- *Impairment provisions:* $9.6 million COVID-19 Overlay, originally raised in FY2020, remained entirely unutilised and was released in full. A new $8.0 million Economic Overlay was created.
- *Voluntary amortisation of intangibles:* $2.9 million expense was recognised for intangibles that are no longer expected to derive future economic benefits.
- *Other non-recurring expenses:* $1.0 million.
- *Aged items provisions and legacy accruals:* a combined $0.5 million of unwarranted accruals and provisions for aged legacy suspense account transactions were released.
- *Tax adjustments:* a $1.2 million release of tax provisions relating to prior periods and $0.2 million of other non-recurring tax benefits were recognised during the year.

$m	FY2023	FY2022	Movement ($)	Movement (%)
Reported NOI	**285.3**	**267.6**	**17.7**	**6.6%**
Less:				
StockCo Australia impacts	(1.9)	1.9	(3.8)	
Hedge accounting Impacts	(9.1)	16.7	(25.8)	
Net fair value gain/loss on investments	(4.5)	(13.0)	8.5	
Underlying NOI	**300.7**	**262.0**	**38.7**	**14.8%**
Reported OPEX	**128.1**	**116.8**	**11.3**	**9.7%**
Less:				
StockCo Australia impacts	-	1.9	(1.9)	
Voluntarily accelerated amortisation	-	2.9	(2.9)	
Legacy provisions and accruals	(0.7)	(0.5)	(0.2)	
ABP costs	2.2	-	2.2	
Other non-recurring items	0.3	1.0	(0.7)	
Underlying OPEX	**126.2**	**111.4**	**14.9**	**13.4%**
Reported impairment expense	**23.2**	**13.8**	**9.4**	**68.1%**
Less:				
StockCo Australia impacts	-	(0.3)	0.3	
COVID-19 overlay release	-	(9.6)	9.6	
Economic Overlay created	-	8.0	(8.0)	
Underlying impairment expense	**23.2**	**15.7**	**7.5**	**47.9%**
Reported NPAT	**95.9**	**95.1**	**0.7**	**0.8%**
Less:				
Post-tax impact of one-offs	(14.3)	(2.3)	(12.0)	
Tax adjustments relating to prior periods	-	1.4	(1.4)	
Underlying NPAT	**110.2**	**96.1**	**14.1**	**14.6%**
Reported NIM	3.97%	4.05%	(8 bps)	
Underlying NIM	**4.00%**	**4.16%**	**(16 bps)**	
Reported CTI	44.9%	43.6%	126 bps	
Underlying CTI	**42.0%**	**42.5%**	**(53 bps)**	
Reported ROE	10.4%	12.1%	(169 bps)	
Underlying ROE	**11.9%**	**12.6%**	**(68 bps)**	

Thank you

Investor & media relations

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Investor information

For more information
heartlandgroup.info/investor-information

HEARTLAND
GROUP

HEARTLAND GROUP

Results announcement

(for Equity Security issuer/Equity and Debt Security issuer)

Updated as at June 2023

Results for announcement to the market		
Name of issuer	Heartland Group Holdings Limited	
Reporting Period	12 months to 30 June 2023	
Previous Reporting Period	12 months to 30 June 2022	
Currency	NZD	
	Amount (000s)	**Percentage change**
Revenue from continuing operations	$285,315	6.6%
Total Revenue	$285,315	6.6%
Net profit/(loss) from continuing operations	$95,868	0.8%
Total net profit/(loss)	$95,868	0.8%
Interim/Final Dividend		
Amount per Quoted Equity Security	$0.06000000	
Imputed amount per Quoted Equity Security	$0.02333333	
Record Date	06/09/2023	
Dividend Payment Date	20/09/2023	
	Current period	**Prior comparable period**
Net tangible assets per Quoted Equity Security	$1.09	$0.96
A brief explanation of any of the figures above necessary to enable the figures to be understood	Please refer to the audited financial statements that accompany this announcement for a further explanation of these figures.	
Authority for this announcement		
Name of person authorised to make this announcement	Andrew Dixson, Chief Financial Officer	
Contact person for this announcement	Nicola Foley, Group Head of Communications	
Contact phone number	+64 27 3456 809	
Contact email address	nicola.foley@heartland.co.nz	
Date of release through MAP	29/08/2023	

Audited financial statements accompany this announcement.

HEARTLAND GROUP

Distribution Notice

Updated as at June 2023

Section 1: Issuer information				
Name of issuer	Heartland Group Holdings Limited			
Financial product name/description	Ordinary shares			
NZX ticker code	HGH			
ISIN (If unknown, check on NZX website)	NZHGHE0007S9			
Type of distribution (Please mark with an X in the relevant box/es)	Full Year	X	Quarterly	
	Half Year		Special	
	DRP applies	X		
Record date	6/09/2023			
Ex-Date (one business day before the Record Date)	5/09/2023			
Payment date (and allotment date for DRP)	20/09/2023			
Total monies associated with the distribution[1]	$ 42,579,492.00			
Source of distribution (for example, retained earnings)	Retained earnings			
Currency	NZD			
Section 2: Distribution amounts per financial product				
Gross distribution[2]	$ 0.08333333			
Gross taxable amount [3]	$ 0.08333333			
Total cash distribution[4]	$ 0.06000000			
Excluded amount (applicable to listed PIEs)	NIL			
Supplementary distribution amount	$ 0.01058824			
Section 3: Imputation credits and Resident Withholding Tax[5]				
Is the distribution imputed	Fully imputed – YES			
	~~Partial imputation~~			
	~~No imputation~~			

[1] Continuous issuers should indicate that this is based on the number of units on issue at the date of the form
[2] "Gross distribution" is the total cash distribution plus the amount of imputation credits, per financial product, before the deduction of Resident Withholding Tax (**RWT**).
[3] "Gross taxable amount" is the gross distribution minus any excluded income.
[4] "Total cash distribution" is the cash distribution excluding imputation credits, per financial product, before the deduction of RWT. This should *include* any excluded amounts, where applicable to listed PIEs.
[5] The imputation credits plus the RWT amount is 33% of the gross taxable amount for the purposes of this form. If the distribution is fully imputed the imputation credits will be 28% of the gross taxable amount with remaining 5% being RWT. This does not constitute advice as to whether or not RWT needs to be withheld.

If fully or partially imputed, please state imputation rate as % applied[6]	28%	
Imputation tax credits per financial product	$ 0.02333333	
Resident Withholding Tax per financial product	$ 0.00416667	
Section 4: Distribution re-investment plan (if applicable)		
DRP % discount (if any)	2.0%	
Start date and end date for determining market price for DRP	7/09/2023	13/09/2023
Date strike price to be announced (if not available at this time)	14/09/2023	
Specify source of financial products to be issued under DRP programme (new issue or to be bought on market)	New issue	
DRP strike price per financial product	$	
Last date to submit a participation notice for this distribution in accordance with DRP participation terms	07/09/2023	
Section 5: Authority for this announcement		
Name of person authorised to make this announcement	Andrew Dixson, Chief Financial Officer	
Contact person for this announcement	Nicola Foley, Group Head of Communications	
Contact phone number	+64 27 3456 809	
Contact email address	nicola.foley@heartland.co.nz	
Date of release through MAP	29/08/2023	

[6] Calculated as (imputation credits/gross taxable amount) x 100. Fully imputed dividends will be 28% as a % rate applied.

NZX/ASX release
29 August 2023

ASX Listing Rule 1.15.3 Statement

Heartland Group Holdings Limited's (**Heartland**) (NZX/ASX: HGH) (an ASX Foreign Exempt Listing) confirms, for the purposes of ASX Listing Rule 1.15.3, that it has complied with and continues to comply with the Listing Rules of NZX Limited, which is its overseas home exchange.

– ENDS –

The person(s) who authorised this announcement:

Jeff Greenslade
Chief Executive Officer

For further information, please contact:

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Financial Statements

For the year ended 30 June 2023

HEARTLAND GROUP

Contents

General Information

These financial statements are issued by Heartland Group Holdings Limited (**HGH**) and its subsidiaries (the **Group**) for the year ended 30 June 2023.

Name and address for service

The Group's address for service is Level 3, 35 Teed Street, Newmarket, Auckland 1023.

Details of incorporation

HGH was incorporated under the Companies Act 1993 on 19 July 2018.

Auditor

PricewaterhouseCoopers
PwC Tower, Level 27
15 Customs Street West
Auckland 1010

Other Material Matters

There are no material matters relating to the business or affairs of the Group that are not disclosed in these consolidated financial statements which, if disclosed, would materially affect the decision of a person to subscribe for debt or equity instruments of which the Group is the issuer.

Directors

All Directors of HGH reside in New Zealand with the exception of Ellen Frances Comerford and Geoffrey Edward Summerhayes who reside in Australia. Communications to the Directors can be sent to Heartland Group Holdings Limited, Level 3, 35 Teed Street, Newmarket, Auckland 1023.

On 20 February 2023, Geoffrey Ricketts stepped down as Chairperson of Heartland Group Holdings Limited and ceased directorship of Heartland Group Holdings Limited on 10 March 2023.

The Board resolved on 23 February 2023 for Greg Tomlinson to assume the role of Chairperson.

There have been no other changes to the composition of the Board of Directors of the Group for the year ended 30 June 2023.

The Directors of HGH and their details at the time these financial statements were signed were:

Chair – Board of Directors
Name: Gregory Raymond Tomlinson
Type of Director: Non-Independent Non-Executive Director
Qualifications: AME
Occupation: Company Director

External Directorships:
Alta Cable Holdings Limited, Chippies Vineyard Limited, Indevin Group Limited, Mountbatten Trustee Limited, Nearco Stud Limited, Oceania Healthcare Limited, Pelorus Finance Limited, St Leonards Limited, Tomlinson Group Argenta GP Limited, Tomlinson Group NZ Limited, Tomlinson Holdings Limited, Tomlinson Group Investments Limited, Tomlinson Ventures Limited, Terra Vitae Vineyards Limited, Villa Maria Estate Limited.

Name: Ellen Frances Comerford
Type of Director: Independent Non-Executive Director
Qualifications: BEc
Occupation: Company Director

External Directorships:
Airtasker Limited, Comerford Gohl Holdings Pty Limited, Lendi Group Pty Ltd, IVM InterSurer B.V, Hollard Investments B.V, Hollard Investments II BV, Greenstone Holdco Pty Ltd.

Name: Jeffrey Kenneth Greenslade
Type of Director: Non-Independent Executive Director
Qualifications: LLB
Occupation: Chief Executive Officer of Heartland Group Holdings

External Directorships:
Henley Family Investments Limited.

Name: Kathryn Mitchell
Type of Director: Independent Non-Executive Director
Qualifications: BA, CMInstD
Occupation: Company Director

External Directorships:
Chambers@151 Limited, Christchurch International Airport Limited, Farmright Limited, Firsttrax Limited, Helpings Hands Holdings Limited, Link Engine Management Limited, Morrison Horgan Limited, The New Zealand Merino Company Limited, The A2 Milk Company Limited

Name: Geoffrey Edward Summerhayes
Type of Director: Independent Non-Executive Director
Qualifications: BBA
Occupation: Company Director

External Directorships:
OnePath General Insurance Pty Limited, Zurich Australian Insurance Limited, Zurich Australia Limited, Zurich Financial Services Australia Limited, Zurich Investment Management Limited.

Directors' Statements

The consolidated financial statements are dated 28 August 2023 and have been signed by all Directors.

G R Tomlinson (Chair)

E F Comerford

J K Greenslade

G E Summerhayes

K Mitchell

Consolidated Statement of Comprehensive Income

For the year ended 30 June 2023

$000's	Note	June 2023	June 2022
Interest income	3	527,710	342,101
Interest expense	3	245,721	91,959
Net interest income		**281,989**	**250,142**
Operating lease income	4	5,631	5,284
Operating lease expenses	4	3,827	3,383
Net operating lease income		**1,804**	**1,901**
Lending and credit fee income		11,753	9,639
Other (expense)/income	5	(5,742)	18,933
Net operating income		**289,804**	**280,615**
Operating expenses	6	128,079	116,753
Profit before impaired asset expense and income tax		**161,725**	**163,862**
Fair value (loss) on investments		(4,488)	(12,998)
Impaired asset expense	8	23,244	13,823
Profit before income tax		**133,993**	**137,041**
Income tax expense	9	38,125	41,916
Profit for the year		**95,868**	**95,125**
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss, net of income tax:			
Effective portion of change in fair value of derivative financial instruments		7,116	7,041
Movement in fair value reserve		(533)	(712)
Movement in foreign currency translation reserve		(6,803)	2,340
Items that will not be reclassified to profit or loss, net of income tax:			
Movement in fair value of equity investments at fair value through other comprehensive income		(2,411)	-
Movement in defined benefit reserve		-	(171)
Net loss due to wind-up of superannuation scheme		-	(473)
Other comprehensive income for the year, net of income tax		**(2,631)**	**8,025**
Total comprehensive income for the year		**93,237**	**103,150**
Earnings per share			
Basic earnings per share	10	13.96c	16.13c
Diluted earnings per share	10	13.96c	16.13c

Total comprehensive income for the year is attributable to the owners of the Group.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 30 June 2023

		June 2023				June 2022			
$000's	**Note**	**Share Capital**	**Reserves**	**Retained Earnings**	**Total Equity**	**Share Capital**	**Reserves**	**Retained Earnings**	**Total Equity**
Balance at beginning of year		**599,185**	**9,936**	**199,586**	**808,707**	**583,781**	**(477)**	**178,388**	**761,692**
Total comprehensive income for the year									
Profit for the year		-	-	95,868	95,868	-	-	95,125	95,125
Other comprehensive (loss)/income, net of income tax	17	-	(2,631)	-	(2,631)	-	8,498	(473)	8,025
Total comprehensive income for the year		**-**	**(2,631)**	**95,868**	**93,237**	**-**	**8,498**	**94,652**	**103,150**
Contributions by and distributions to owners									
Dividends paid	16	-	-	(71,402)	(71,402)	-	-	(73,454)	(73,454)
Dividend reinvestment plan	16	7,100	-	-	7,100	15,404	-	-	15,404
Transaction costs associated with capital raising		(3,749)	-	-	(3,749)	-	-	-	-
Share based payments		-	105	-	105	-	1,915	-	1,915
Share issuance	16	197,006	-	-	197,006				
Vesting of share based payments		1,170	(1,170)	-	-	-	-	-	-
Total transactions with owners		**201,527**	**(1,065)**	**(71,402)**	**129,060**	**15,404**	**1,915**	**(73,454)**	**(56,135)**
Balance at end of the year		**800,712**	**6,240**	**224,052**	**1,031,004**	**599,185**	**9,936**	**199,586**	**808,707**

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Financial Position

As at 30 June 2023

$000's	Note	June 2023	June 2022
Assets			
Cash and cash equivalents		311,503	310,758
Investments	11	330,240	289,294
Derivative financial instruments	12	36,983	45,221
Finance receivables	13	4,334,214	4,146,821
Finance receivables - reverse mortgages	21	2,403,810	1,996,854
Investment properties		11,903	11,832
Operating lease vehicles	14	16,966	15,161
Right of use assets	18	12,318	14,145
Other assets	18	27,990	18,229
Current tax asset		1,960	-
Intangible assets	18	235,733	218,874
Deferred tax asset	9	21,105	23,074
Total assets		**7,744,725**	**7,090,263**
Liabilities			
Deposits	15	4,131,025	3,592,508
Other borrowings	15	2,496,375	2,578,213
Derivative financial instruments	12	7,624	6,341
Lease liabilities	18	14,287	16,240
Tax liabilities		6,112	22,044
Trade and other payables	18	58,298	66,210
Total liabilities		**6,713,721**	**6,281,556**
Net assets		**1,031,004**	**808,707**
Equity			
Share capital	16	800,712	599,185
Retained earnings and other reserves	17	230,292	209,522
Total equity		**1,031,004**	**808,707**

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 30 June 2023

$000's	Note	June 2023	June 2022
Cash flows from operating activities			
Interest received		333,874	222,894
Operating lease income received		4,571	3,913
Lending, credit fees and other income received		6,292	6,101
Operating inflows		**344,737**	**232,908**
Interest paid		(193,679)	(100,467)
Payments to suppliers and employees		(128,195)	(69,463)
Taxation paid		(54,629)	(32,987)
Operating outflows		**(376,503)**	**(202,917)**
Net cash flows (applied to)/from operating activities before changes in operating assets and liabilities		**(31,766)**	**29,991**
Proceeds from sale of operating lease vehicles		4,492	4,481
Purchase of operating lease vehicles		(8,766)	(10,758)
Net movement in finance receivables		(448,210)	(693,512)
Net movement in deposits		526,939	407,484
Net cash flows from/(applied to) operating activities[1]		**42,689**	**(262,314)**
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets		(24,669)	(9,809)
Proceeds from investment securities		55,443	82,945
Purchase of investment securities		(95,000)	-
Deposit paid for the conditional acquisition of Challenger Bank Limited		(3,936)	-
Purchase of equity investment		(6,952)	(7,414)
Purchase of investment property		(71)	-
Purchase of subsidiary, net of cash acquired		(3,047)	(159,919)
Net cash flows (applied to) investing activities		**(78,232)**	**(94,197)**
Cash flows from financing activities			
Proceeds from wholesale funding		1,264,359	1,103,510
Repayment of wholesale borrowings		(1,208,292)	(635,371)
Proceeds from issue of unsubordinated notes		87,589	77,243
Repayment of unsubordinated notes		(330,300)	-
Proceeds from issue of subordinated notes		97,934	-
Dividends paid		(64,303)	(58,050)
Payment of lease liabilities		(2,656)	(2,396)
Net issue of share capital	16	193,364	-
Total cash provided from financing activities		**37,695**	**484,936**
Net increase in cash held		**2,152**	**128,425**
Effect of exchange rates on cash and cash equivalents		(1,407)	-
Opening cash and cash equivalents		310,758	182,333
Closing cash and cash equivalents[2]		**311,503**	**310,758**

[1] Cash flows from operating activities do not include cash flows from wholesale funding which are included as part of financing activities.

[2] At 30 June 2023, the Group has $97.0 million (2022: $76.7 million) of cash held by the Trusts which may only be used for the purposes defined in the underlying Trust documents. Refer to Note 27 - Structured entities for definition of Trusts and further details.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows (continued)

For the year ended 30 June 2023

Reconciliation of profit after tax to net cash flows from operating activities

$000's	Note	June 2023	June 2022
Profit for the year		**95,868**	**95,125**
Add/(less) non-cash items:			
Depreciation and amortisation expense		10,124	10,691
Depreciation on lease vehicles	14	3,461	3,103
Capitalised net interest income and fee income		(154,706)	(113,368)
Impaired asset expense	8	23,244	13,823
Investment fair value movement		6,899	12,998
Deferred tax		1,969	(8,957)
Other non-cash items		2,097	(12,310)
Total non-cash items		**(106,912)**	**(94,020)**
Add/(less) movements in operating assets and liabilities:			
Finance receivables		(448,210)	(693,512)
Operating lease vehicles		(5,266)	(6,277)
Other assets		(2,856)	(207)
Current tax		(17,892)	14,604
Derivative financial instruments		9,521	(23,214)
Deposits		526,939	407,484
Other liabilities		(8,503)	37,703
Total movements in operating assets and liabilities		**53,733**	**(263,419)**
Net cash flows from/(applied to) operating activities[1]		**42,689**	**(262,314)**

[1]Cash flows from operating activities do not include cash flows from wholesale funding which are included as part of financing activities.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows (continued)

For the year ended 30 June 2023

Net debt reconciliation

The below table sets out net cash flow and non-cash changes in liabilities arising from financing activities.

$000's	Note	June 2023	June 2022
Balance as at beginning of year[1]		**2,594,453**	**1,693,299**
Proceeds from wholesale funding		1,264,359	1,103,510
Repayment of wholesale borrowings		(1,208,292)	(635,371)
Proceeds from issue of unsubordinated notes		87,589	77,243
Repayment of unsubordinated notes		(330,300)	-
Proceeds from issue of subordinated debt		97,934	-
Payment of lease liabilities		(2,656)	(2,396)
Total cash movements		**(91,366)**	**542,986**
Acquisition of debt from purchase of subsidiary		-	358,942
Capitalised interest and fee expense		34,809	12,630
Fair value movements		(473)	(11,534)
Foreign exchange and other movements		(26,761)	(1,870)
Total non-cash movements		**7,575**	**358,168**
Balance as at the end of year		**2,510,662**	**2,594,453**

[1]Includes lease liabilities and other borrowings.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Notes to the Financial Statements

For the year ended 30 June 2023

1 Financial statements preparation

Reporting entity

The financial statements presented are the consolidated financial statements comprising Heartland Group Holdings (**HGH**) and its subsidiaries (the **Group**). Refer to Note 26 – Significant subsidiaries for further details.

HGH is a company incorporated in New Zealand under the Companies Act 1993 and a Financial Market Conduct (**FMC**) reporting entity for the purposes of the Financial Markets Conduct Act 2013.

Basis of preparation

The consolidated financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (**NZ GAAP**), the New Zealand Exchange (**NZX**) Main Board Listing Rules and the Australian Securities Exchange (**ASX**) Listing Rules. The financial statements comply with New Zealand Equivalents to International Financial Reporting Standards (**NZ IFRS**) and other applicable Financial Reporting Standards as appropriate for profit-oriented entities. The financial statements also comply with International Financial Reporting Standards (**IFRS**) as issued by the International Accounting Standards Board.

The consolidated financial statements are presented in New Zealand dollars which is the Group's functional and presentation currency. Unless otherwise indicated, amounts are rounded to the nearest thousand dollars.

The consolidated financial statements have been prepared on a going concern basis after considering the Group's funding and liquidity position.

The accounting policies adopted have been applied consistently throughout the periods presented in these consolidated financial statements.

Certain comparative balances have been reclassified to align with the presentation used in the current financial year. These reclassifications have no impact on the overall financial performance or financial position for the comparative year.

Basis of measurement

The financial statements have been prepared on the basis of historical cost, except for certain financial instruments and investment properties, which are measured at their fair values as identified in the accounting policies set out in the accompanying notes to the financial statements.

Principles of consolidation

The consolidated financial statements of the Group incorporate the assets, liabilities and results of all controlled entities. Controlled entities are all entities in which the Group is exposed to, or has rights to, variable returns from its involvement with the entities and has the ability to affect those returns through its power over the entities. Intercompany transactions, balances and any unrealised income and expense (except for foreign currency transaction gains or losses) between controlled entities are eliminated.

Assets and liabilities in a transactional currency that is not the New Zealand dollar, are translated at the exchange rates ruling at balance date. Revenue and expense items are translated at the average rate at the balance date. Exchange differences are taken to the consolidated statement of comprehensive income.

1 Financial statements preparation (continued)

Changes in accounting standards

Accounting standards issued and effective

There have been no changes to accounting policies or new or amended standards that are issued and effective that are expected to have a material impact on the Group.

Accounting standards issued not yet effective

Disclosure of fees for audit firms' services (Amendments to FRS-44)

Amendments were issued to FRS-44 *New Zealand Additional Disclosures* (**Amendments to FRS-44**) that require an entity to describe the services provided by its audit or review firm and to disclose the fees incurred by the entity for those services using prescribed categories. These amendments apply to accounting periods beginning on or after 1 January 2024. Earlier application is permitted for accounting periods that begin before 1 January 2024 but have not ended or do not end before 15 June 2023.
The Group has early adopted the Amendments to FRS-44 from 1 July 2022. Refer to Note 7 - Compensation of auditor for further details.

Climate-related standards

Climate-related disclosure standards were issued in December 2022, and took effect on 1 January 2023. These include the Climate-related Disclosures (CS 1), Adoption of Aotearoa New Zealand Climate Standards (CS 2) and General Requirements for Climate-related Disclosures (CS 3). The Group is a designated climate reporting entity under the climate related disclosure regime and is required to meet its requirements effective from the financial reporting period commencing 1 July 2023.

Other new accounting standards, amendments to accounting standards and interpretations have been published that are not mandatory for the 30 June 2023 reporting periods and have not been early adopted by the Group. These standards, amendments or interpretations are not expected to have a material impact on the current or future reporting periods.

Critical accounting estimates and judgements

The preparation of the Group's consolidated financial statements requires the use of estimates and judgements. This note provides an overview of the areas that involve a higher degree of judgement or complexity. Detailed information about each of these estimates and judgements is included in the relevant notes together with the basis of calculation for each affected item in the financial statements.

- Provisions for impairment - The effect of credit risk is quantified based on the Group's best estimate of future cash repayments and proceeds from any security held or by reference to risk profile groupings, historical loss data and forward-looking information. Refer to Note 8 - Impaired asset expense and Note 13 - Finance receivables for further details.

- Recognition of Banking Licence intangible asset - The recognition of Banking Licence intangible asset required judgement in determining external and internal costs directly attributable to the Group's joint application for an Australian Authorised Deposit-Taking Institution Licence with Challenger Bank Limited (**CBL**). Judgement is also required to determine whether such costs fulfil the definition and recognition criteria of an intangible asset. Such costs include professional fees and costs of employee benefits arising directly from the application. Refer to Note 18 - Other balance sheet items for further details.

- Fair value of reverse mortgages - Fair value is quantified by the transaction price. Management judgement is applied in determining the appropriateness of the transaction price as fair value. Refer to Note 21 - Fair value for further details.

- Goodwill - The Group carries out impairment testing annually over the carrying value of goodwill of its cash generating units (**CGUs**). Uncertainty is involved in estimating fair value less cost to sell and judgement is applied in assumptions used to determine the recoverable amount of CGU for impairment testing. Refer to Note 18 – Other balance sheet items for further details.

1 Financial statements preparation (continued)

Critical accounting estimates and judgements (continued)

Assumptions made at each reporting date (e.g., the calculation of the provision for impairment and fair value adjustments) are based on best estimates as at that date. Although the Group has internal controls in place to ensure that estimates can be reliably measured, actual amounts may differ from these estimates. The estimates and judgements used in the preparation of the Group's financial statements are continually evaluated.

They are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity. Revisions to accounting estimates are recognised in the reporting period in which the estimates are revised and in any future periods affected.

Significant events

On 20 October 2022 Heartland Group Holdings Limited entered into a conditional share purchase agreement for the purchase of CBL from Challenger Limited for a consideration of approximately AU $36 million, subject to adjustments for net assets delivered at completion. The share purchase agreement is subject to obtaining the requisite regulatory approvals. A 10% deposit was paid to Challenger Limited on execution of the conditional share purchase agreement and is recorded within other assets in the consolidated statement of financial position.

Financial assets and liabilities

Financial Assets

Financial assets are classified based on:

- The business model within which the assets are managed; and
- Whether the contractual cash flows of the instrument represent solely payment of principal and interest (**SPPI**).

The Group determines the business model at the level that reflects how groups of financial assets are managed. When assessing the business model, the Group considers factors including how performance and risks are managed, evaluated and reported and the frequency and volume of, and reason for sales in previous periods.

Financial assets are classified into the following measurement categories:

Financial Assets	Measurement Category	Note
Bank bonds and floating rate notes	Fair value through other comprehensive income (**FVOCI**)	11
Public sector securities and corporate bonds	FVOCI	11
Equity investments	Fair value through profit or loss (**FVTPL**) and FVOCI	11
Finance receivables – Reverse mortgages	FVTPL	21
Finance receivables	Amortised cost	13
Derivative financial instruments	FVTPL	12

Financial assets measured at amortised cost
Financial assets are measured at amortised cost if they are held within a business model whose objective is achieved through holding the financial asset to collect contractual cash flows which represent SPPI.

Financial assets at amortised cost are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method.

1 Financial statements preparation (continued)

Financial assets and liabilities (continued)

Financial Assets (continued)

Financial assets measured at FVOCI

Financial assets are measured at FVOCI if they are held within a business model whose objective is achieved both through collecting contractual cash flows which represent SPPI or selling the financial asset.

Financial assets at FVOCI are measured at fair value with unrealised gains and losses recognised in other comprehensive income except for interest income, impairment charges and foreign exchange gains and losses, which are recognised in profit or loss.

Financial assets measured at FVTPL

Financial assets are measured at FVTPL if:

- they are held within a business model whose objective is achieved through selling or repurchasing the financial asset in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking; or
- the contractual cash flows of the financial asset do not represent SPPI on the principal balance outstanding; or
- they are designated at FVTPL upon initial recognition to eliminate or reduce an accounting mismatch.

Financial assets at FVTPL are measured at fair value with subsequent changes in fair value recognised in profit or loss.

Financial Liabilities

Financial liabilities are classified into the following measurement categories:

- those to be measured at amortised cost;
- those to be measured at FVTPL.

Financial liabilities measured at amortised cost
Financial liabilities are measured at amortised cost if they are not held for trading or designated at FVTPL.

Financial liabilities measured at amortised cost are accounted for using the effective interest rate method.

Financial liabilities measured at FVTPL
Financial liabilities are measured at FVTPL if:

- they are held for trading whose principal objective is achieved through selling or repurchasing the financial liability in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking; or
- they are designated at FVTPL upon initial recognition to eliminate or reduce an accounting mismatch.

Financial liabilities at FVTPL are measured at fair value with subsequent changes in fair value recognised in profit or loss.

Further details of the accounting policy for each category of financial asset or financial liability mentioned above is set out in the note for the relevant item.

The Group’s policies for determining the fair value of financial assets and financial liabilities are set out in Note 21 - Fair value.

1 Financial statements preparation (continued)

Financial assets and liabilities (continued)

Financial liabilities (continued)

Recognition

The Group initially recognises finance receivables and borrowings on the date that they are originated. All other financial assets and liabilities (including assets and liabilities designated at FVTPL) are initially recognised on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

Derecognition

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset.

The Group enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all risks or rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the consolidated statement of financial position. Transfers of assets with the retention of all or substantially all risks and rewards include, for example, securitised assets and repurchase transactions.

Financial liabilities are derecognised when the obligation is discharged, cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, the exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, with the difference in the respective carrying amounts recognised in profit or loss.

Performance

2 Segmental analysis

Segment information is presented in respect of the Group's operating segments which are consistent with those used for the Group's management and internal reporting structure.

An operating segment is a component of an entity engaging in business activities and whose operating results are regularly reviewed by the Group's chief operating decision maker (**CODM**). The CODM, who is responsible for allocating resources and assessing performance of the Group, has been identified as the Group’s Chief Executive Officer (**CEO**) and direct reports.

The Group operates within New Zealand and Australia and comprises the following main operating segments:

Operating segments – New Zealand

Motor	Motor vehicle finance.
Reverse mortgages	Reverse mortgage lending.
Personal lending	Transactional, home loans and personal loans to individuals.
Business	Term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium sized businesses.
Rural	Specialist financial services to the farming sector, primarily offering livestock finance, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers.

Operating segments - Australia

StockCo Australia	Specialising in livestock finance within Australia. This segment was acquired through the acquisition of StockCo Holdings 2 Pty Ltd and StockCo Australia Management Pty Ltd on 31 May 2022. One month of income and expenses are recognised in this segment for the year ended 30 June 2022.
Australia	Reverse mortgage lending and other financial services within Australia.

Certain operating expenses, such as premises, IT and support centre costs are not allocated to operating segments and are included in Other. Finance receivables are allocated across the operating segments. Other assets and liabilities are managed centrally and therefore are not allocated across the operating segments. The Group does not rely on any single major customer for its revenue base.

2 Segmental analysis (continued)

$000's	Motor	Reverse Mortgages	Personal Lending	Business	Rural	StockCo Australia	Australia	Other	Total
June 2023									
Net interest income	60,681	39,696	9,548	71,630	33,522	31,873	43,411	(8,372)	281,989
Lending and credit fee	2,034	2,671	447	2,278	292	-	4,031	-	11,753
Net other income/(expense)	1,485	-	935	991	398	2	(42)	(7,707)	(3,938)
Net operating income/(expense)	**64,200**	**42,367**	**10,930**	**74,899**	**34,212**	**31,875**	**47,400**	**(16,079)**	**289,804**
Operating expenses	4,140	4,929	6,461	9,387	3,068	8,909	13,043	78,142	128,079
Profit/(loss) before impaired asset expense and income tax	**60,060**	**37,438**	**4,469**	**65,512**	**31,144**	**22,966**	**34,357**	**(94,221)**	**161,725**
Fair value (loss) on investments	-	-	-	-	-	-	-	(4,488)	(4,488)
Impaired asset expense	10,911	-	3,195	8,156	630	103	249	-	23,244
Profit/(loss) before income tax	**49,149**	**37,438**	**1,274**	**57,356**	**30,514**	**22,863**	**34,108**	**(98,709)**	**133,993**
Income tax expense	-	-	-	-	-	-	-	38,125	38,125
Profit/(loss) for the year	**49,149**	**37,438**	**1,274**	**57,356**	**30,514**	**22,863**	**34,108**	**(136,834)**	**95,868**
Total assets	**1,563,939**	**888,600**	**358,572**	**1,356,913**	**712,596**	**374,193**	**1,520,437**	**969,475**	**7,744,725**
Total liabilities									**6,713,721**
June 2022									
Net interest income	69,730	29,957	10,287	70,602	29,460	1,889	38,662	(445)	250,142
Lending and credit fee income	1,582	2,583	364	2,145	269	-	2,583	113	9,639
Net other income	1,744	-	1,198	534	472	3	107	16,776	20,834
Net operating income	**73,056**	**32,540**	**11,849**	**73,281**	**30,201**	**1,892**	**41,352**	**16,444**	**280,615**
Operating expenses	3,792	4,485	6,419	9,358	3,038	1,692	11,286	76,683	116,753
Profit/(loss) before impaired asset expense and income tax	**69,264**	**28,055**	**5,430**	**63,923**	**27,163**	**200**	**30,066**	**(60,239)**	**163,862**
Fair value (loss) on investments	-	-	-	-	-	-	-	(12,998)	(12,998)
Impaired asset expense/(benefit)	1,481	-	(877)	11,831	2,256	(291)	(577)	-	13,823
Profit/(loss) before income tax	**67,783**	**28,055**	**6,307**	**52,092**	**24,907**	**491**	**30,643**	**(73,237)**	**137,041**
Income tax expense	-	-	-	-	-	-	-	41,916	41,916
Profit/(loss) for the year	**67,783**	**28,055**	**6,307**	**52,092**	**24,907**	**491**	**30,643**	**(115,153)**	**95,125**
Total assets	**1,382,367**	**721,264**	**332,783**	**1,387,352**	**687,232**	**372,172**	**1,288,494**	**918,599**	**7,090,263**
Total liabilities									**6,281,556**

3 Net interest income

Policy

Interest income and expense on financial instruments is measured using the effective interest rate method that discounts the financial instruments' future cash flows to their present value and allocates the interest income or expense over the life of the financial instrument. The effective interest rate is established on initial recognition of the financial assets or liabilities and is not subsequently revised. For financial instruments at amortised cost, the calculation of the effective interest rate includes all yield related fees and commissions paid or received that are an integral part of the underlying financial instrument.

Interest income is calculated based on the gross carrying amount of financial assets in stages 1 and 2 of the Group's expected credit losses (**ECL**) model and on the carrying amount net of the provision for ECL for financial assets in stage 3. For financial instruments measured at FVTPL, interest is not calculated under the effective interest rate method.

$000's	**June 2023**	**June 2022**
Interest income		
Cash and cash equivalents	10,906	811
Investments	5,081	5,156
Finance receivables	335,070	236,916
Finance receivables - reverse mortgages	176,653	99,218
Total interest income[1]	**527,710**	**342,101**
Interest expense		
Deposits	148,054	45,717
Other borrowings	117,774	46,110
Net interest (income)/expense on derivative financial instruments	(20,107)	132
Total interest expense[2]	**245,721**	**91,959**
Net interest income	**281,989**	**250,142**

[1] Cash and cash equivalents and Finance receivables are measured at amortised cost. Investments are measured at FVOCI. Total interest income derived from these financial assets is calculated using the effective interest rate method. Finance receivables - reverse mortgages are measured at FVTPL.

[2] Deposits and Other borrowings are measured at amortised cost, therefore interest expense incurred on these financial liabilities is calculated using the effective interest rate method. Net interest expense on derivative financial instruments is not calculated using the effective interest rate method as they are measured at FVTPL.

4 Net operating lease income

Policy
As a lessor, the Group retains substantially all the risks and rewards incidental to ownership of the assets and therefore, classifies the leases as operating leases. Rental income and expense from operating leases are recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term. Profits on the sale of operating lease assets are included as part of operating lease income. Current year depreciation and losses on the sale of operating lease assets are included as part of operating lease expenses. The leased assets are depreciated over their useful lives on a basis consistent with similar assets.

$000's	June 2023	June 2022
Operating lease income		
Lease income	4,639	4,161
Gain on disposal of lease assets	992	1,123
Total operating lease income	**5,631**	**5,284**
Operating lease expense		
Depreciation on lease assets	3,461	3,103
Direct lease costs	366	280
Total operating lease expense	**3,827**	**3,383**
Net operating lease income	**1,804**	**1,901**

5 Other income

Policy
Rental income from investment properties
Rental income from investment properties is recognised on a straight-line basis over the term of the relevant lease.

Insurance income
Insurance premium income and commission expense are recognised in profit or loss from the date of attachment of the risk over the period of the insurance contract. Claim expense is recognised in the profit or loss on an accrual basis once our liability to the policyholder has been confirmed under the terms of the contract.

Fair value gain or loss on derivative financial instruments
A fair value gain or loss associated with the effective portion of a derivative designated as a cash flow hedge is recognised initially in the hedging reserve. The ineffective portion of a fair value gain or loss and changes in the fair value of any derivatives not designated in a hedge relationship are recognised immediately in the consolidated statement of comprehensive income and disclosed within Other income. Refer to Note 12 - Derivative financial instruments for further details.

$000's	June 2023	June 2022
Rental income from investment properties	1,064	833
Insurance income[1]	756	664
Other income	624	703
Fair value (loss)/gain on derivative financial instruments	(8,237)	16,723
Foreign exchange gain	51	10
Total other income	**(5,742)**	**18,933**

[1]Insurance income includes net income from Marac Insurance Limited (**MIL**), a subsidiary of Heartland Bank Limited (**HBL**). MIL ceased writing insurance policies in 2020 with the periodic policies expected to expire in 2025.

6 Operating expenses

Policy
Operating expenses are recognised as the underlying service is rendered or over a period in which an asset is consumed or a liability is incurred.

$000's	**June 2023**	**June 2022**
Personnel expenses[1]	66,989	61,152
Directors' fees	1,451	1,149
Superannuation	1,772	1,530
Depreciation - property, plant and equipment	1,904	2,459
Legal and professional fees[2]	4,642	4,094
Advertising and public relations	3,089	4,510
Depreciation - right of use asset	2,539	2,310
Technology services	10,296	9,374
Telecommunications, stationery and postage	1,948	1,723
Customer administration costs	9,814	7,058
Customer onboarding costs	2,765	2,533
Occupancy costs	1,741	1,476
Amortisation of intangible assets	5,681	5,922
Other operating expenses	13,448	11,463
Total operating expenses	**128,079**	**116,753**

[1]Excludes certain personnel expenses directly incurred in acquiring and developing software and capitalised as part of specific application software.

[2]Legal and professional fees include compensation of auditor which is disclosed in Note 7 - Compensation of auditor.

7 Compensation of auditor

In accordance with the Amendments to FRS-44, adopted by the Group from 1 July 2022, the Group is required to disclose the fees incurred for services received from its audit or review firm, with a description of each service, including audit or review of the financial statements. Other services performed during the reporting period are required to be disclosed using the following categories:

- audit or review related services;
- other assurance services and other agreed-upon procedures engagements;
- taxation services and;
- other services.

In accordance with the Group's external auditor independence policy, it is prohibited for the external auditor's firm to perform tax compliance work. It is also the Group's policy to engage the external auditor's firm on assignments additional to its statutory audit duties only if they are not perceived to be in conflict with the role of external auditor. All services are pre-approved by the Board Audit and Risk Committee.

The fees payable to the current auditor, PricewaterhouseCoopers New Zealand (**PwC NZ**) and to the predecessor auditor, KPMG are outlined in the below table:

7 Compensation of auditor (continued)

$000's	June 2023	June 2022
Fees paid to current auditor - PwC NZ		
Audit and review of financial statements[1]	1,046	-
Other assurance and agreed-upon procedure services paid to auditor[2]	89	
Taxation services paid to auditor[3]	54	
Other services paid to auditor[4]	33	-
Total compensation paid to PwC NZ	**1,222**	**-**
Fees paid to predecessor auditor - KPMG		
Audit and review of financial statements[1]	40	879
Other assurance and agreed upon-procedure services paid to auditor[2]	-	103
Total compensation paid to KPMG	**40**	**982**
Total compensation of auditor	**1,262**	**982**

[1]Audit and review of the financial statements includes fees paid for both the audit of the annual financial statements and review of interim financial statements.

[2]Other assurance related services paid to the auditor comprise reasonable assurance engagement for insurance solvency return, trust deed reporting, supervisor and registry audits, Economic and Financial Statistics (**EFS**) regulatory reporting engagement, Australian Financial Service Licence (**AFSL**) assurance engagement and agreed-upon procedures.

[3]PwC Australia was engaged to carry out tax work in respect of Stockco Australia's 30 June 2022 tax returns prior to the appointment of PwC NZ.

[4]Other non-assurance services paid to PwC relates to actuarial services for reverse mortgages for HBL carried out by PwC NZ prior to the appointment as external auditors and fees for executive reward survey report.

8 Impaired asset expense

$000's	June 2023	June 2022
Individually impaired asset expense	13,010	10,783
Collectively impaired asset expense	12,794	6,396
Total impaired asset expense excluding recovery of amounts previously written off	**25,804**	**17,179**
Recovery of amounts previously written off to the income statement	(2,560)	(3,356)
Total impaired asset expense	**23,244**	**13,823**

Refer to Note – 13 Finance receivables for provision for impairment details.

9 Taxation

Policy
Income tax
Income tax expense for the year comprises current tax and movements in deferred tax balances, including any adjustment required for prior years' tax expense. Income tax expense is recognised in profit and loss except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in equity or other comprehensive income.

Current tax
Current tax is the expected tax payable or receivable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to the tax payable or receivable in respect of previous years. Current tax for current and prior years is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred tax
Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for taxation purposes. A deferred tax asset is recognised only to the extent that it is probable that a future taxable profit will be available to realise the asset.

Goods and services tax (GST)
Revenues, expenses and assets are recognised net of GST. As the Group is predominantly involved in providing financial services, only a proportion of GST paid on inputs is recoverable. The non-recoverable proportion of GST is treated as an expense or, if relevant, as part of the cost of acquisition of an asset.

Income tax expense

$000's	**June 2023**	**June 2022**
Income tax recognised in profit or loss		
Current tax		
Current year	37,159	46,239
Adjustments for prior year	(1,556)	(760)
Tax at other rates	554	486
Deferred tax		
Current year	1,457	(3,750)
Adjustments for prior year	304	(282)
Tax at other rates	207	(17)
Total income tax expense recognised in profit or loss	**38,125**	**41,916**
Income tax recognised in other comprehensive income		
Current tax		
Investment securities at fair value in fair value reserve	(246)	(5,271)
Fair value movements in derivatives held in cash flow hedge reserve	2,418	7,743
Total income tax expense recognised in other comprehensive income	**2,172**	**2,472**
Reconciliation of effective tax rate		
Profit before income tax	**133,993**	**137,041**
Tax at the local income tax rate (NZ: 28%, Australia: 30%)	38,175	38,841
Adjusted tax effect of items not deductible	1,202	4,117
Adjustments for prior year	(1,252)	(1,042)
Total income tax expense	**38,125**	**41,916**

9 Taxation (continued)

Deferred tax assets comprise the following temporary differences:

$000's	June 2023	June 2022
Employee expenses	2,516	2,169
Share Based payment	1,069	1,039
Provision for impairment	14,958	14,649
Intangibles and property plant and equipment	(1,529)	(2,968)
Deferred acquisition costs	(55)	(196)
Operating lease vehicles	451	680
Deferred income	(6,938)	(4,786)
Prior year tax loss	8,540	9,362
Deductible prior year expense	593	603
Other temporary differences	1,500	2,522
Total deferred tax assets	**21,105**	**23,074**
Opening balance of deferred tax assets	**23,074**	**14,117**
Movement recognised in profit or loss	(1,969)	4,084
Transfer on acquisition of business	-	4,873
Closing balance of deferred tax assets	**21,105**	**23,074**

Imputation credit account

$000's	June 2023	June 2022
Imputation credits available for use in subsequent reporting periods	37,785	19,114

10 Earnings Per Share

	June 2023			June 2022		
	Earnings Per Share Cents	Net Profit After Tax $000's	Weighted Average No. of Shares 000's	Earnings Per Share Cents	Net Profit After Tax $000's	Weighted Average No. of Shares 000's
Basic earnings	13.96	95,868	686,781	16.13	95,125	589,771
Diluted earnings	13.96	95,868	686,781	16.13	95,125	589,771

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Financial Position

11 Investments

Policy
Investments are classified into one of the following categories:

Fair value through profit or loss
Investments under this category include equity investments and are measured at fair value plus transaction costs. Changes in fair value of these investments are recognised in profit or loss in the period in which they occur.

Fair value through other comprehensive income
Investments under this category include bank bonds, floating rate notes, public securities, corporate bonds and equity investments where the Group have irrevocably elected at initial recognition to measure at FVOCI. These are initially measured at fair value, including transaction costs, and subsequently carried at fair value. Changes in fair value of these investments are recognised in other comprehensive income and presented within the fair value reserve.

Amortised cost
Investments under this category include bank deposits and are measured using effective interest rate method. They are held to collect contractual cash flows that are solely payments of principal and interest on the principal amount outstanding.

$000's	June 2023	June 2022
Bank deposits, bank bonds and floating rate notes	305,310	261,259
Public sector securities and corporate bonds	9,882	12,953
Equity investments	15,048	15,082
Total investments	**330,240**	**289,294**

Refer to Note 21 - Fair value for details of the split between investments measured at fair value through profit or loss, fair value through other comprehensive income and amortised cost.

12 Derivative financial instruments

Policy
The Group uses derivatives for risk management purposes. Derivatives held for risk management purposes are placed into hedges that either meet hedge accounting requirements, or economic hedges not placed into an accounting hedge relationship.

Derivatives are recognised at their fair value, with the derivatives being carried as assets when their fair value is positive and as liabilities when their fair value is negative.

A hedged item is an asset, liability, firm commitment or highly probable forecast transaction that exposes the Group to risk of changes in fair value or cash flows, and that is designated as being hedged. The Group applies fair value hedge accounting to hedge movements in the value of fixed interest rate assets and liabilities subject to interest rate risk. The Group applies cash flow hedge accounting to hedge the variability in highly probable forecast future cash flows attributable to interest rate risk on variable rate assets and liabilities.

Derivative instruments that do not qualify for hedge accounting are held as economic hedges. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the consolidated statement of comprehensive income and disclosed within Other income.

Fair value hedge accounting
The criteria that must be met for a relationship to qualify for hedge accounting include:

- the hedging relationship must be formally designated and documented at inception of the hedge,
- effectiveness testing must be carried out on an on-going basis to ensure the hedge is effective and consistent with the originally documented risk management strategy, and
- the instruments or counterparty must be a third party external to the Group.

The Group documents, at the inception of the transaction, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair value of hedged items.

Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify for fair value hedge accounting are recorded through profit or loss alongside any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

Where the hedged item is carried at amortised cost, the movement in fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to carrying amount of a hedged item carried at amortised cost is amortised to the consolidated statement of comprehensive income on an effective yield basis over the remaining period to maturity of the hedged item. Where a hedged item carried at amortised cost is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the consolidated statement of comprehensive income.

Cash flow hedge accounting
The criteria that must be met for a relationship to qualify for hedge accounting include:

- the hedging relationship must be formally designated and documented at inception of the hedge,
- effectiveness testing must be carried out on an on-going basis to ensure the hedge is effective and consistent with the originally documented risk management strategy, and
- the instruments or counterparty must be a third party external to the Group.

12 Derivative financial instruments (continued)

Cash flow hedge accounting (continued)

The Group documents, at the inception of the transaction, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

A fair value gain or loss associated with the effective portion of a derivative designated as a cash flow hedge is recognised initially in the hedging reserve. The ineffective portion of a fair value gain or loss is recognised immediately in the consolidated statement of comprehensive income.

When a hedging derivative expires or is sold, the hedge no longer meets the criteria for hedge accounting, or the Group elects to revoke the hedge designation, the cumulative gain or loss on the hedging derivative remains in the cash flow hedging reserve until the forecast transaction occurs and affects income, at which point it is transferred to the corresponding income or expense line. If a forecast transaction is no longer expected to occur, the cumulative gain or loss on the hedging derivative previously reported in the cash flow hedging reserve is immediately transferred to the consolidated statement of comprehensive income.

Net investment hedge

The Group held investments in foreign operations, where changes in net assets resulting from changes in foreign currency rate were recognised in the foreign currency translation reserve.

Where the Group hedges the currency translation risk arising from net investments in foreign operations, the gains and losses on the hedging instruments are also reflected in other comprehensive income to the extent the hedge is effective. When all or part of a foreign operation is disposed, the cumulative value of the exchange differences is recognised in profit or loss.

The Group actively manages interest rate risk by entering into derivative contracts to hedge against movements in interest rates. As permitted by NZ IFRS 9, the Group has elected to continue to apply the hedge accounting requirements of NZ IAS 39.

The Group's approach to managing market risk, including interest rate risk, is disclosed in Note 25 – Interest rate risk. The Group actively manages residual interest rate risk from the net exposure of its underlying assets and liabilities, associated with the mismatch of the interest rate repricing profiles of its interest earning assets and interest bearing liabilities, by entering into interest rate swaps to hedge against movements in interest rates.

Interest rate swaps are bilateral derivative contracts with commitments to exchange one set of cash flows for another resulting in an economic exchange of interest rates (for example, fixed rate for floating rate) without exchange of principal. Interest rate swap notional values indicate the volume of transactions outstanding at the end of the financial year and provide basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved, therefore don't indicate the Group's exposure to credit or market risks. The fair values of derivative instruments and their notional values are set out in the below table.

12 Derivative financial instruments (continued)

$000's	June 2023 Notional Principal	June 2023 Fair Value Assets	June 2023 Fair Value Liabilities	June 2022 Notional Principal	June 2022 Fair Value Assets	June 2022 Fair Value Liabilities
Interest rate related contracts						
Held as economic hedges	260,650	6,539	-	619,005	17,847	1,543
Designated as cash flow hedges	850,068	15,398	941	327,636	8,678	-
Designated as fair value hedges	543,200	15,045	6,683	549,200	18,696	4,798
Interest rate swaps	**1,653,918**	**36,982**	**7,624**	**1,495,841**	**45,221**	**6,341**
Foreign currency related contracts						
Held as economic hedges	168	1	-	786	-	-
FX Forwards	168	1	-	786	-	-
Total derivative financial instruments	**1,654,086**	**36,983**	**7,624**	**1,496,627**	**45,221**	**6,341**

Micro cash flow hedge accounting is applied to interest rate swaps designated as hedges of the Group's floating rate domestic borrowings and deposits by using 'receive floating / pay fixed' interest rate swaps to fix the cost of floating interest rate borrowings and deposits.

Micro fair value hedge accounting is applied to receive fixed interest rate swaps designated as hedges of interest rate risk arising from fixed-rate subordinated notes and retail bond, and to pay fixed interest rate swaps designated as hedges of interest rate risk arising from fixed-rate investment securities.

The Group determines whether an economic relationship between the hedged item and the hedging instrument exists based on an assessment of the qualitative characteristics of this hedged item and the hedged risk, supported by quantitative analysis. Close alignment of the critical terms of the hedged item and hedging instrument is also considered a strong indication of the presence of an economic relationship by the Group.

The Group establishes a hedge ratio by aligning the par amount of the exposure to be hedged and the notional amount of the interest rate swap designated as a hedging instrument.

Retrospective testing for each reporting period uses a regression model, which compares the change in the fair value of the hedged item and the change in the fair value of the hedging instrument. For a hedge to be deemed effective, the change in fair values should be within 80% and 125% of each other. Should the result fall outside this range the hedge would be deemed ineffective and recognised immediately through the income statement in line with each hedge relationship policy above.

12 Derivative financial instruments (continued)

The hedge relationship is reviewed on a monthly basis and the hedging instruments and hedged items are de-designated and re-designated, if necessary, based on the effectiveness test results and changes in the hedged exposure.

Hedge ineffectiveness may arise from timing difference on repricing between the hedged item and the hedging instrument, difference in timing of their cash flows, or due to changes in the counterparties' credit risk affecting the fair value of hedging instruments.

The following table shows the maturity and interest rate risk profiles of the interest rate swaps as hedging instruments in continuing fair value and cash flow hedge relationships.

$000's	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
June 2023						
Interest rate risk						
Cash flow hedge relationships						
Pay fixed						
Nominal amounts	-	20,000	295,000	535,068	-	850,068
Average interest rate	-	4.22%	3.78%	4.00%	-	
Fair value hedge relationships						
Pay fixed						
Nominal amounts	54,700	38,000	60,000	160,400	5,100	318,200
Average interest rate	1.17%	0.77%	0.88%	3.06%	1.51%	
Receive fixed						
Nominal amounts	-	125,000	-	100,000	-	225,000
Average interest rate	-	1.78%	-	4.30%	-	
Total interest rate risk nominal amount	**54,700**	**183,000**	**355,000**	**795,468**	**5,100**	**1,393,268**

12 Derivative financial instruments (continued)

$000's	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
June 2022						
Interest rate risk						
Cash flow hedge relationships						
Pay fixed						
Nominal amounts	-	8,845	5,528	313,263	-	327,636
Average interest rate	-	0.20%	0.37%	2.47%	-	
Fair value hedge relationships						
Pay fixed						
Nominal amounts	20,000	31,000	92,700	115,400	15,100	274,200
Average interest rate	1.20%	0.81%	1.00%	0.84%	1.45%	
Receive fixed						
Nominal amounts	150,000	-	125,000	-	-	275,000
Average interest rate	4.50%	-	1.78%	-	-	
Total interest rate risk nominal amount	**170,000**	**39,845**	**223,228**	**428,663**	**15,100**	**876,836**

The following table sets out the accumulated fair value adjustments arising from the corresponding fair value hedge relationships and the outcome of the changes in fair value of the hedged item as well as the hedging instruments used as the basis for recognising effectiveness.

	As at 30 June 2023		For the year ended 30 June 2023
$000's	Carrying value	Accumulated amount of fair value hedge adjustment	Hedge ineffectiveness gain/(loss) recognised in income statement
Interest rate risk			
Investments	290,723	(14,893)	2,620
Other borrowings	(219,959)	5,331	473
Total	**70,764**	**(9,562)**	**3,093**
Interest rate swaps	**8,362**	**8,362**	**(3,133)**
Hedge ineffectiveness of financial instruments recognised in other income			**(40)**

12 Derivative financial instruments (continued)

$000's	As at 30 June 2022 Carrying value	Accumulated amount of fair value hedge adjustment	For the year ended 30 June 2022 Hedge ineffectiveness gain/(loss) recognised in income statement
Interest rate risk			
Investments	262,314	(16,914)	(14,793)
Other borrowings	(272,983)	4,858	11,543
Total	**(10,669)**	**(12,056)**	**(3,250)**
Interest rate swaps	**13,898**	**13,898**	**3,295**
Hedge ineffectiveness of financial instruments recognised in other income			**45**

The accumulated amount of fair value hedge adjustments included in the carrying amount of hedged items that have ceased to be adjusted for hedging gains and losses is nil (2022: nil).

The balance of the cash flow hedge reserve, amounts recognised in the reserve, and amounts transferred out of the reserve are shown in the following table.

$000's	June 2023 Cash flow hedge reserve	FCTR[1]	June 2022 Cash flow hedge reserve	FCTR[1]
Cash flow hedges				
Balance at beginning of year	7,959	-	918	-
Transferred to the income statement	(1,771)	-	(641)	-
Net gains from change in fair value	11,305	-	10,743	-
Net movement before tax	**9,534**	**-**	**10,102**	**-**
Tax on net movement in cash flow hedge reserve	(2,418)	-	(3,061)	-
Balance at end of year	**15,075**	**-**	**7,959**	**-**
Net investment hedge	**-**	**2,537**	**-**	**-**

[1]Represents the accumulated effective amount of the hedging instrument deferred to Foreign currency translation reserve (**FCTR**) and is related to hedge relationship for which hedge accounting is no longer applied.

During the year ended 30 June 2023, a gain of $0.7 million was recognised in fair value gain on derivative financial instruments in the consolidated statement of comprehensive income related to hedge ineffectiveness from cash flow hedge relationships (2022: nil).

There were no transactions for which cash flow hedge accounting had to be ceased as a result of the highly probable cash flows no longer being expected to occur (2022: nil).

There are $10.1 million (2022: $1.6 million) of balances recognised in the cash flow hedge reserve for which hedge accounting is no longer applied on the basis that the associated variable cash flows are still expected to occur over the lifetime of the original hedge relationships. The associated cash flow hedge reserve is being released over the period of the original hedge relationship which has since been de-designated.

13 Finance receivables

Policy

Finance receivables are initially recognised at fair value plus incremental direct transaction costs and are subsequently measured at amortised cost using the effective interest method, less any impairment loss.

Fees and direct costs relating to loan origination, financing and loan commitments are deferred and amortised to interest income over the life of the loan using the effective interest rate method. Lending fees not directly related to the origination of a loan are recognised over the period of service.

$000's	**June 2023**	**June 2022**
Gross finance receivables at amortised cost	4,387,480	4,198,826
Less provision for impairment	(53,266)	(52,005)
Net finance receivables at amortised cost	**4,334,214**	**4,146,821**

13 Finance receivables (continued)

Policy

Impairment of finance receivables
At each reporting date, the Group applies a three-stage approach to measuring expected credit losses (**ECL**) of finance receivables not carried at fair value. The ECL model assesses whether there has been a significant increase in credit risk since initial recognition.

Exposures are assessed on a collective basis in each stage unless there is sufficient evidence that one or more events associated with an exposure could have a detrimental impact on estimated future cash flows. Where such evidence exists, the exposure is assessed on an individual basis.

For the purposes of a collective evaluation of impairment, finance receivables are grouped based on shared credit risk characteristics, credit risk ratings, contractual term, date of initial recognition, remaining term to maturity, customer type and other relevant factors.

The ECL model is a forward-looking model where impairment allowances are recognised before losses are actually incurred. On initial recognition, an impairment allowance is required, based on events that are possible in the next 12 months.

Assets may migrate between the following stages based on their change in credit quality:

Stage 1 - 12 months ECL (past due 30 days or less)

Where there has been no evidence of increased credit risk since initial recognition, and finance receivables are not credit impaired upon origination, the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months is recognised.

Stage 2 - Lifetime ECL not credit impaired (greater than 30 but less than 90 days past due)

Where there has been a significant increase in credit risk.

Stage 3 - Lifetime ECL credit impaired (90 days past due or more)

Objective evidence of impairment, are considered to be in default or otherwise credit impaired.

Credit quality of financial assets
The Group internally computes probability of default using historical default data, to assess the potential risk of default of the lending, or other financial services products, provided to counterparties or customers. The Group has defined counterparty probabilities of default across consumer, retail, business and rural portfolios.

The Group considers a receivable to be in default when contractual payments are 90 days or more past due, or when it is considered unlikely that the credit obligation to the Group will be paid in full without recourse to actions, such as realisation of security.

Finance receivables are written off against the related impairment allowance when there is no reasonable expectation of recovery. Any recoveries of amounts previously written off are credited to credit impairment expense in profit or loss.

In determining whether credit risk has increased all available information relevant to the assessment of economic conditions at the reporting date are taken into consideration. To do this the Group considers its historical loss experience and adjusts this for current observable data. In addition to this the Group uses reasonable and supportable forecasts of future economic conditions including experienced judgement to estimate the amount of an expected impairment loss. Future economic conditions consider macroeconomic factors such as unemployment, interest rate, gross domestic product, and inflation, and requires an evaluation of both the current and forecast direction of the economic cycle. The methodology and assumptions including any forecasts of future economic conditions are reviewed regularly as incorporating forward-looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the ECL.

13 Finance receivables (continued)

Policy (continued)
The calculation of expected credit loss is modelled for portfolios of like assets. For portfolios which are either new or too small to model, judgement is used to determine impairment provisions.
For assets that are individually assessed for ECL, the allowance for ECL is calculated directly as the difference between the defaulted assets carrying value and the recoverable amount (being the present value of expected future cash flows, including cashflows from the realisation of collateral or guarantees, where applicable).

Modification of contractual cash flows
The Group sometimes modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximising recovery.

Such restructuring activities include extended payment term arrangements, payment holidays and payment forgiveness. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Restructuring is most commonly applied to term loans.

Information is not presented in respect of other financial assets or credit related contingent liabilities as the related allowances for ECL are not material to the Group.

The Group's models for estimating ECL for each of its portfolios are based on the historic credit experience of those portfolios. The models assume that economic conditions remain static over time. If the Group forecasts that economic conditions may change in the foreseeable future, the Group applies judgement to determine whether the modelled output should be subject to an economic overlay. Judgement is required to establish clear correlation between key economic indicators and the credit performance of the Group's unique portfolios.

The most significant and judgemental provision for impairment is on motor vehicle lending with a collective ECL of $15.1 million at 30 June 2023 (2022: $9.5 million). There are fewer judgements on the other remaining lending portfolios.

The motor vehicle lending impairment allowance is sensitive to changes in the level of unemployment. The modelled provision for motor vehicle lending is a probability weighted estimate based on three scenarios. The forecast of unemployment across all three scenarios uses consensus external data obtained from external economic experts.

The forecast assumes the following for unemployment for all three scenarios:

	2024	2025	2026
Upside	4.00%	4.80%	4.40%
Central	4.60%	5.20%	5.00%
Downside	5.96%	6.13%	5.70%

The probability weights assigned to each scenario are based on management's estimate of their relative likelihood. The following table indicates the weightings applied by the Group as at 30 June 2023:

Upside	15%
Central	50%
Downside	35%

The following sensitivity table shows the provision for impairment based on the probability weighted scenarios and what the impairment allowance for motor vehicle lending would be assuming a 100% weighting is applied to the three scenarios with all other assumptions held constant.

Reported probability weighted impairment allowance	$ 15.1 million
100% Upside	$ 9.7 million
100% Central	$ 12.4 million
100% Downside	$ 21.2 million

13 Finance receivables (continued)

The following table details the movement from the opening balance to the closing balance of the provision for impairment losses by class.

$000's	Collectively Assessed Stage 1	Collectively Assessed Stage 2	Collectively Assessed Stage 3	Individually Assessed	Total
June 2023					
Impairment allowance as at 30 June 2022	**20,256**	**1,958**	**14,602**	**15,189**	**52,005**
Changes in loss allowance					
Transfer between stages[1]	(8,226)	(3,864)	3,758	8,332	-
New and increased provision (net of provision releases)[1]	983	4,369	15,774	4,678	25,804
Credit impairment charge	**(7,243)**	**505**	**19,532**	**13,010**	**25,804**
Write-offs	-	-	(12,612)	(11,904)	(24,516)
Effect of changes in foreign exchange rate	(4)	-	(23)	-	(27)
Impairment allowance as at 30 June 2023	**13,009**	**2,463**	**21,499**	**16,295**	**53,266**
June 2022					
Impairment allowance as at 30 June 2021	**26,807**	**2,427**	**16,824**	**7,629**	**53,687**
Changes in loss allowance					
Transfer between stages[1]	(3,909)	(2,556)	1,189	5,276	-
New and increased provision (net of provision releases)[1]	(3,666)	2,083	13,255	5,507	17,179
Credit impairment charge	**(7,575)**	**(473)**	**14,444**	**10,783**	**17,179**
Write-offs	-	-	(16,666)	(3,411)	(20,077)
Effect of changes in foreign exchange rate	32	4	-	-	36
Acquisition of portfolio	992	-	-	188	1,180
Impairment allowance as at 30 June 2022	**20,256**	**1,958**	**14,602**	**15,189**	**52,005**

[1] The increase in provision when a loan moves to a higher stage is included in New and increased provision (net of provision releases) in the higher stage to which the loan moved. The decrease in provision when a loan moves to a lower stage is included in New and increased provision (net of provision releases) in the higher stage from which the loan moved.

13 Finance receivables (continued)

Impact of changes in gross finance receivables held at amortised cost on allowance for ECL

	Collectively Assessed			Individually	
$000's	**Stage 1**	**Stage 2**	**Stage 3**	**Assessed**	**Total**
30 June 2023					
Gross finance receivables as at 30 June 2022	3,967,917	118,424	46,114	66,371	4,198,826
Transfer between stages	(237,955)	161,605	64,627	11,723	-
Additions	1,412,648	-	-	9,326	1,421,974
Deletions	(1,072,012)	(97,559)	(17,068)	(15,194)	(1,201,833)
Write-offs	-	-	(12,379)	(19,108)	(31,487)
Gross finance receivables as at 30 June 2023	**4,070,598**	**182,470**	**81,294**	**53,118**	**4,387,480**
30 June 2022					
Gross finance receivables as at 30 June 2021	3,092,653	165,793	45,564	38,143	3,342,153
Transfer between stages	(112,179)	25,532	31,253	55,394	-
Additions	2,433,553	-	-	3,190	2,436,743
Deletions	(1,446,110)	(72,901)	(12,782)	(26,945)	(1,558,738)
Write-offs	-	-	(17,921)	(3,411)	(21,332)
Gross finance receivables as at 30 June 2022	**3,967,917**	**118,424**	**46,114**	**66,371**	**4,198,826**

Impact of changes in gross exposures on loss allowances

Overall credit impairment provisions increased by $1.3 million (2.4%) for the year ended 30 June 2023, mainly due to increase in gross receivables of $188.7 million (4.5%) and movement of exposures into more advanced stages. This is offset by the release of provisions previously held against assets written off during the year as well as reduction in loss given default from more effective arrears management.

As at 30 June 2023, there were nil undrawn lending commitments available to counterparties for whom drawn balances are classified as individually impaired (2022: $0.003 million).

(a) Assets under administration

As at 30 June 2023, the contractual amount outstanding on loans to customers written off during the year and are still subject to enforcement activity was nil (2022: nil).

14 Operating lease vehicles

Policy
Operating lease vehicles are stated at cost less accumulated depreciation.

Operating lease vehicles are depreciated on a straight-line basis over their expected useful life after allowing for any residual values. The estimated lives of these vehicles vary up to five years. Vehicles held for sale are not depreciated but are tested for impairment.

$000's	June 2023	June 2022
Cost		
Opening balance	20,450	16,114
Additions	8,766	10,758
Disposals	(6,303)	(6,422)
Closing balance	**22,913**	**20,450**
Accumulated depreciation		
Opening balance	5,289	5,249
Depreciation charge for the year	3,461	3,103
Disposals	(2,803)	(3,063)
Closing balance	**5,947**	**5,289**
Opening net book value	15,161	10,865
Closing net book value	**16,966**	**15,161**

The future minimum lease payments receivable under operating leases not later than one year is $4.086 million (2022: $3.057 million), within one to five years is $7.598 million (2022: $6.465 million) and over five years is nil (2022: nil).

15 Borrowings

Policy
Borrowings and deposits are initially recognised at fair value including incremental direct transaction costs. They are subsequently measured at amortised cost using the effective interest method.

The Group hedges interest rate risk on certain debt issues. When fair value hedge accounting is applied to fixed rate debt issues, the carrying values are adjusted for changes in fair value related to the hedged risks.

$000's	June 2023	June 2022
Deposits	4,131,025	3,592,508
Total borrowings related to deposits	**4,131,025**	**3,592,508**
Unsubordinated notes	385,482	636,407
Subordinated notes	97,794	-
Securitised borrowings	1,713,737	1,559,108
Certificate of deposit	148,110	198,715
Bank borrowings	131,248	173,982
Money market borrowings	20,004	10,001
Total other borrowings	**2,496,375**	**2,578,213**
Total deposits and other borrowings	**6,627,400**	**6,170,721**
Due within one year	4,731,388	4,174,630
Due more than one year	1,896,012	1,996,091
Total deposits and other borrowings	**6,627,400**	**6,170,721**

Deposits and unsubordinated notes rank equally and are unsecured.

15 Borrowings (continued)

Unsubordinated notes

Unsubordinated notes include short and long-term retail bonds and medium term notes. Medium term notes are issued pursuant to the terms of the Guarantee Deed Poll dated 15 February 2019. Medium term notes are issued in Australian dollars to eligible non-retail investors in compliance with applicable law.

The Group has the following unsubordinated notes on issue at balance sheet date.

Retail bonds and medium term notes $000's	Frequency of interest repayment	June 2023	June 2022	Maturity Date
NZ$150 million	Semi-annually	-	145,142	21 September 2022
AU $47 million	Monthly	-	52,362	6 October 2022
AU $45 million	Quarterly	-	49,976	21 April 2023
AU $75 million	Quarterly	-	83,318	22 April 2023
NZ $125 million	Semi-annually	122,165	127,841	12 April 2024
AU $45 million	Quarterly	49,471	50,003	9 July 2024
AU $30 million	Quarterly	32,585	-	9 July 2024
AU $115 million	Quarterly	125,925	127,765	13 May 2025
AU $50 million	Quarterly	55,336	-	5 October 2027
Total retail bonds and medium term notes		**385,482**	**636,407**	

Subordinated notes

On 28 April 2023, HBL, a subsidiary of the Group, issued $100 million of subordinated unsecured notes (**Subordinated notes**) to New Zealand investors and certain overseas institutional investors pursuant to the terms of the Subordinated Unsecured Notes Deed Poll in accordance with the laws of New Zealand. Subordinated notes are treated as Tier 2 capital under HBL regulatory capital requirements and will mature on 28 April 2033.

Interest payable
The interest rate is a fixed rate of 7.51% for a period of 5 years until 28 April 2028, after which it will reset to quarterly floating rate equal to the sum of the applicable 3-month Bank Bill Rate plus 3.2% Issue Margin. The quarterly payment of interest in respect of the subordinated notes are subject to HBL being solvent at the time of, and immediately following the interest payment.

Early Redemption
HBL may choose to repay all or some of the subordinated notes for their face value together with accrued interest (if any) on 28 April 2028 or any interest payment date thereafter. Early redemption of all the subordinated notes for certain tax or regulatory events is permitted on an interest payment date. Early redemption is subject to certain conditions, including HBL obtaining the Reserve Bank of New Zealand (**RBNZ**) prior written approval and HBL being solvent at the time.

Ranking
The claims of the holders of the subordinated notes will rank:
- Behind the claims of all depositors and other creditors of HBL;
- equally with the claims of other holders of any other securities and obligations that rank equally with the subordinated notes and;
- ahead of the rights of the HBL's shareholders and holders of any other securities and obligations of HBL that rank behind the subordinated notes.

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15 Borrowings (continued)

Securitised Borrowings

The Group had the following securitised borrowings outstanding as at 30 June 2023:

Securitisation facility $000's	Currency	June 2023 Limit	 Drawn[1]	June 2022 Limit	 Drawn[1]	 Maturity Date
StockCo Securitisation Trust 2021-1 (**StockCo**)	AU	300,000	271,739	300,000	275,420	27 May 2024
Seniors Warehouse Trust No. 2 (**SWT2**)	AU	450,000	457,657	350,000	232,982	1 July 2024
Heartland Auto Receivable Warehouse (**HARWT**)	NZD	400,000	227,054	400,000	267,779	26 August 2024
Seniors Warehouse Trust (**SWT**)	AU	600,000	622,344	600,000	646,744	30 September 2025
Atlas 2020-1 Trust (**Atlas**)	AU	127,462	134,943	127,462	136,183	24 September 2050
Total securitised borrowings			**1,713,737**		**1,559,108**	

[1]Facility limit is stated in functional currency, drawn balance is stated in NZD.

- HARWT notes issued to investors are secured over motor vehicle loans.
- StockCo notes issued to investors are secured over livestock loans.
- SWT, SWT2 and Atlas notes issued to investors are secured over reverse mortgage loans.

The Group actively engages facility providers in commercial negotiations including tenor extensions, increase in facility limits, refinancing arrangements, and other commercial terms. The Group has a track record of extending or refinancing funding arrangements as they fall due and does not anticipate any difficultly in doing so when the facilities above expire.

16 Share capital and dividends

Policy
Ordinary shares are classified as equity, incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effect.

	June 2023 Number of Shares	June 2022 Number of Shares
Issued shares		
Opening balance	592,904	585,904
Shares issued during the year	112,417	-
Shares issued - dividend reinvestment plan	4,337	7,000
Closing balance	**709,658**	**592,904**

HGH completed a capital raise during the year which comprised a share placement (**Placement**) and a Share Purchase Plan (**SPP**). HGH issued 72,222,222 shares at $1.8000 per share on 26 August 2022 under the Placement and 38,822,458 new shares at $1.7674 per share on 9 September 2022 under the SPP. The total value of shares issued was $198.6 million with $3.7 million of transaction costs recognised in relation to this share issuance.

On 19 September 2022, HGH issued a further 2,250,625 shares at $0.5200 per share ($1.2 million) under the Long Term Incentive Scheme of HGH (**LTI Scheme**), of which 877,777 shares at $1.8329 per share ($1.6 million) were acquired by HGH pursuant to the buyback offer to the participants to fund the tax liability arising for those participants upon receipt of shares under the LTI Scheme.

The Group issued 4,336,812 new shares at $1.6370 per share ($7.1 million) on 23 March 2023 under a dividend reinvestment plan (**DRP**) for the period (2022: 3,930,116 new shares at $2.2713 per share ($8.9 million) on 15 September 2021 and 3,069,339 new shares at $2.1105 per share ($6.5 million) on 16 March 2022 under the DRP for the period).

The ordinary shares have no par value. Each ordinary share of HGH carries the right to vote on a poll at meetings of shareholders, the right to an equal share in dividends and the right to an equal share in the distribution of the surplus assets of HGH in the event of liquidation.

16 Share capital and dividends (continued)

Dividends paid

	June 2023 Date Declared	June 2023 Cents Per Share	June 2023 $000's	June 2022 Date Declared	June 2022 Cents Per Share	June 2022 $000's
Final dividend	24 August 2022	5.5	32,609	24 August 2021	7.0	41,013
Interim dividend	28 February 2023	5.5	38,793	22 February 2022	5.5	32,441
Total dividends paid			**71,402**			**73,454**

17 Other reserves

$000's	Employee Benefit Reserve	Foreign Currency Translation Reserve (FCTR)	Fair Value Reserve	Defined Benefit Reserve	Cash Flow Hedge Reserve	Total
June 2023						
Balance as at 30 June 2022	4,646	(1,635)	(1,034)	-	7,959	9,936
Movements attributable to net investments in foreign operations and net investment hedges	-	(6,803)	-	-	-	(6,803)
Movements attributable to fair value hedges	-	-	(779)	-	-	(779)
Movements attributable to cash flow hedges	-	-	-	-	9,534	9,534
Equity securities at FVOCI	-	-	(2,411)	-	-	(2,411)
Share based payments	105	-	-	-	-	105
Vesting of share based payments	(1,170)	-	-	-	-	(1,170)
Income tax effect	-	-	246	-	(2,418)	(2,172)
Balance as at 30 June 2023	**3,581**	**(8,438)**	**(3,978)**	**-**	**15,075**	**6,240**
June 2022						
Balance as at 30 June 2021	2,731	(3,975)	(322)	171	918	(477)
Movements attributable to net investments in foreign operations	-	2,340	-	-	-	2,340
Movements attributable to fair value hedges	-	-	(1,301)	-	-	(1,301)
Movements attributable to cash flow hedges	-	-	-	-	10,102	10,102
Equity securities at FVOCI	-	-	-	(171)	-	(171)
Share based payments	1,915	-	-	-	-	1,915
Income tax effect	-	-	589	-	(3,061)	(2,472)
Balance as at 30 June 2022	**4,646**	**(1,635)**	**(1,034)**	**-**	**7,959**	**9,936**

Employee benefit reserve

Includes amounts which arise on the recognition of the Group’s fair value estimate of equity instruments expected to vest under share-based compensation plan.

FCTR

Exchange differences arising on translation of the Group's foreign operations are accumulated in the Foreign currency translation reserve and recognised in other comprehensive income. The cumulative amount is reclassified to profit or loss when a foreign operation is disposed of.

17 Other reserves (continued)

Fair value reserve
Includes changes in the fair value of investment securities measured at fair value through other comprehensive income, net of tax. For debt securities, these changes are reclassified to the profit or loss when the asset is disposed. For equity securities, these changes are not reclassified to the profit or loss when the asset is disposed.

Defined benefit reserve
Includes predetermined retirement benefits calculated for employees of a historical amalgamated entity which was wound up during the prior financial year.

Cash flow hedge reserve
This includes fair value gains and losses associated with the effective portion of the designated cash flow hedging instruments, net of tax.

18 Other balance sheet items

Policy
Property, plant and equipment are stated at cost less accumulated depreciation and impairment (if any). Depreciation is calculated on a straight line basis to write off the net cost or revalued amount of each asset over its expected life to its estimated residual value.

$000's	June 2023	June 2022
Other assets		
Trade receivables	430	-
GST receivables	562	2,946
Prepayments[1]	11,931	7,674
Property, plant and equipment[2]	14,241	7,336
Other receivables	826	273
Total other assets	**27,990**	**18,229**

[1]Prepayments include deposit paid for the conditional acquisition of CBL of $3.9 million.

[2]Property, plant and equipment include rural property worth $7.8 million acquired during the year.

Policy
Intangible assets
Intangible assets with finite useful lives
Software acquired or internally developed by the Group is stated at cost less accumulated amortisation and any accumulated impairment losses. Expenditure on software assets is capitalised only when it increases the future economic value of that asset. Certain internal and external costs directly incurred in acquiring and developing software are capitalised when specific criteria are met. Costs incurred on planning or evaluating software proposals during the research phase or on maintaining systems after implementation are not capitalised. Amortisation of software is on a straight line basis, at rates which will write off the cost over the assets' estimated useful lives. The expected useful life of the software has been determined to be ten years.

Software-as-a-Service (SaaS) arrangements
SaaS arrangements are service agreements that grant the Group the right to access the cloud provider's application software over the contract period. Costs associated with configuring or customising the software, along with ongoing fees for accessing the cloud provider's application, are recognised as operating expenses when the services are received.

Some of these costs pertain to developing software code that enhances or modifies, or creates additional capability to, existing on-premise systems and qualifies as an intangible asset based on its definition and recognition criteria.

18 Other balance sheet items (continued)

Policy (continued)
Intangible assets (continued)
Software-as-a-Service (SaaS) arrangements (continued)
The Group capitalises costs incurred in configuring or customising certain suppliers' application software within specific cloud computing arrangements as intangible assets as the Group considers that it would benefit from those costs to implement the cloud-based software over the expected terms of the cloud computing arrangements. However, such capitalisation occurs only if the activities result in creating an intangible asset that the Group has control over and meets the necessary recognition criteria. Costs that do not meet the criteria for capitalisation as intangible assets are expensed as incurred unless they are paid to the suppliers (or subcontractors of the supplier) of the cloud-based software to significantly customise the cloud-based software for the Group (i.e., such services are not distinct from the Group's right to receive access to the supplier's cloud-based software). In the latter case, the upfront costs are recorded as prepayments for services and amortised over the expected terms of the cloud computing arrangements.

Goodwill
Goodwill arising on acquisition represents the excess of the cost of the acquisition over the Group's interest in the fair value of the identifiable net assets acquired. Goodwill that has an indefinite useful life is not subject to amortisation and is tested for impairment annually. Goodwill is carried at cost less accumulated impairment losses.

$000's	**June 2023**	**June 2022**
Computer software		
Software - cost	48,513	45,091
Software under development	28,391	16,196
Accumulated amortisation	31,944	26,275
Net carrying value of computer software	**44,960**	**35,012**
Goodwill	184,422	183,235
Net carrying value of goodwill	**184,422**	**183,235**
Other intangible assets[1]	6,351	627
Total intangible assets	**235,733**	**218,874**

[1]Other intangible assets include capitalised banking licence costs of $6.4 million (2022: $0.6 million)

Banking Licence

On 20 October 2022 Heartland Group Holdings Limited entered into a conditional share sale agreement with Challenger Limited to acquire 100% of the shares of CBL, holder of a full Australian Authorised Deposit-Taking Institution (**ADI**) Licence. HGH and CBL have jointly applied to the Australian Prudential Regulatory Authority (**APRA**) for approval to expand the range of products CBL offers and to amend CBL's APRA approved business plan to integrate with HGH's existing Australian based financial services business.

Costs directly attributable to the application are recognised as Banking licence intangible asset. On completion the Banking Licence is expected to have an indefinite life as there is no foreseeable limit to the period over which the asset is expected to generate benefits for the business.

Goodwill

For the purposes of impairment testing, goodwill is allocated to cash generating units. A Cash Generating Unit (**CGU**) is the smallest identifiable group of assets that generate independent cash inflows. Group has assessed that goodwill should be allocated to the smallest identifiable CGU:

- Heartland Australia Holdings Pty Limited: $15.3 million (2022: $15.3 million).
- Heartland Bank Limited: $29.8 million (2022: $29.8 million).
- StockCo AU Group: $139.3 million (2022: $138.1 million).

18 Other balance sheet items (continued)

Impairment testing of goodwill

The Group has performed impairment tests for CGUs with goodwill. Further information about impairment tests performed for CGUs with goodwill is provided below.

Heartland Bank Limited (**HBL**) and Heartland Australia Holdings Pty Limited (**HAH**)

The recoverable amount of the businesses was determined on a value in use basis using a discounted cash flow methodology. The model uses a five-year cash flow forecast based on the latest budget approved by the Board and extended out based on long term growth rates. The long-term growth rate applied to the future cash flows after year five of the forecast was 2.0% and 2.5% for HBL and HAH respectively (2022: 2.0% and 2.0%), and a discount rate of 10.0% (2022: 10.0%) was applied which reflect both past experience and external sources of information. The goodwill impairment assessment indicates significant headroom, and that no foreseeable adjustments to key assumptions such as growth rate or discount rate would lead to impairment.

There was no indication of impairment and no impairment losses have been recognised against the carrying amount of goodwill for the year ended 30 June 2023 (2022: nil).

StockCo AU Group

The recoverable amount of the business was determined on a fair value less cost to sell basis using a discounted cash flow methodology. The model uses a four-year cash flow forecast based on the latest growth target approved by the Board and extended out based on growth expectations for the business. This valuation methodology uses level three inputs in terms of the fair value hierarchy in NZ IFRS 13. The following drivers and key assumptions are used in the model:

- Annual lending growth which has been forecasted based on management's current expectations of growth in the specialist livestock financing portfolio. In forming these expectations management has referenced the current and expected outlook in the overall Australian cattle and lamb markets and factored in pricing and growth strategies relative to market outlook. This includes targeting new customer segments and distribution channels to broaden reach.

- Gross interest income (including interest yield) which represents the pricing of the products which factors in market outlook and new customer segments and are estimated based on management's past experience.

- Cost of funds which was projected based on the forward curve for bank bill rate plus a margin at the date of assessment, representing the expected funding structure of an analogous Australian ADI noting that the Group is working towards obtaining an Australian ADI licence.

- Terminal growth rate of 2.4% after year five of the forecast and discount rate of 12.0%, which reflects external sources of information.

The recoverable amount of the business exceeds its carrying amount by $30.4 million (A$28.0 million). The discount rate would need to rise above 13.5% and the terminal growth rate will need to be below 2.0% in combination to result in an impairment.

The forecast cash flow drivers are outlined in the following table. For each driver management has identified what a reasonable possible change, based on the expected range which would impact the recoverable amount. The expected impact on the CGU recoverable amount from the sensitivities below do not capture any interrelationships between funding costs, gross interest income and annual lending growth.

Sensitivity of key driver	**Expected impact on CGU recoverable amount**	
$000's	**Upside**	**Downside**
+/- 10% in annual lending growth	2,639	(2,687)
+/- 3% in gross interest income (including interest yield)	15,741	(14,731)
+/- 3% in funding cost	4,771	(4,708)

18 Other balance sheet items (continued)

Policy
Employee benefits
Annual leave entitlements are accrued at amounts expected to be paid. Long service leave is accrued by calculating the probable future value of the entitlements and discounting back to present value. Obligations to defined contribution superannuation schemes are recognised as an expense when the contribution is paid.

$000's	June 2023	June 2022
Trade and other payables		
Trade payables	14,731	21,358
Insurance liability	914	1,838
Employee benefits	11,224	9,548
Other tax payables	3,820	1,124
Collateral received on derivatives[1]	27,609	32,342
Total trade and other payables	**58,298**	**66,210**

[1]The Group has accepted collateral arising from derivative transactions, included in Cash and cash equivalents.

Policy
Leases
The Group leases office space, car parks, equipment and cars. Rental contracts are typically made for fixed periods but may have extension options. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions.

In determining the lease term, all facts and circumstances that create an economic incentive to exercise an extension option are considered. Extension options are only included in the lease term if the lease is reasonably certain to be extended.

Lease liabilities are measured at the present value of the remaining lease payments and discounted using the Group's incremental borrowing rate (**IBR**). Lease liabilities are measured using the effective interest method. Carrying amounts are remeasured only upon reassessments and lease modifications.

Right of use assets are depreciated at the shorter of lease term or the Group’s depreciation policy for that asset class.

$000's	June 2023	June 2022
Right of use assets		
Balance at beginning of year	14,145	15,985
Depreciation charge for the year, included within depreciation expense in the income statement	(2,539)	(2,310)
Additions to right of use assets	712	470
Total right of use assets	**12,318**	**14,145**
Lease liability		
Current	3,166	3,674
Non-current	11,121	12,566
Total lease liability	**14,287**	**16,240**
Interest expense relating to lease liability	**488**	**479**

19 Acquisition

Policy

Business combination

The Group accounts for business combinations using the acquisition method when the acquired set of activities and assets meets the definition of a business and control is transferred to the Group. In determining whether a particular set of activities and assets is a business, the Group assesses whether the set of assets and activities consists of inputs and processes applied to those inputs that have the ability to contribute to the creation of outputs.

The consideration transferred in the acquisition and any contingent consideration to be transferred are generally measured at fair value, as are the identifiable net assets acquired. Goodwill is initially measured at cost (being the excess of the aggregate of the consideration transferred over the fair value of the net assets acquired) and is tested annually for impairment. Any gain on a bargain purchase is recognised in profit or loss immediately. If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period (see below), or additional assets or liabilities are recognised, to reflect new information obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the amounts recognised as of that date. The measurement period is the period from the date of acquisition to the date the Group obtains complete information about facts and circumstances that existed as of the acquisition date, and does not exceed twelve months. Transaction cost related to the acquisition is recognised as an expense in profit or loss when incurred with the exception of costs to issue debt or equity securities.

On 31 May 2022, the Group acquired 100% of the shares in StockCo Holdings 2 Pty Ltd and StockCo Australia Management Pty Ltd (collectively **StockCo Australia**). The consideration paid was subject to a completion adjustment based on the net asset movements since the determination date. The final purchase consideration with respect to this acquisition was A$157.40 million or NZ$173.31 million at exchange rate of the dates of the acquisition and the completion adjustment.

During the year ended 30 June 2023, the purchase price adjustments were finalised and an adjustment of NZ$1.73 million was made to the final purchase consideration. The fair value of consideration increased from NZ$171.58 million to NZ$173.31 million. There was new information relating to the facts and circumstances prevailing at completion date that resulted in fair value adjustments to livestock receivables and trade and other payables. Goodwill increased from NZ$137.58 million to NZ$141.16 million.

19 Acquisition (continued)

Details of the fair value of the assets and liabilities acquired and the final goodwill arising from the acquisition of StockCo Australia are set out as follows:

$000's	Fair value recognised on acquisition
Assets	
Cash and cash equivalents	9,564
Livestock receivables	372,991
Right of use assets	354
Deferred tax asset	5,285
Other assets	4,713
Total assets	**392,907**
Liabilities	
Other borrowings	358,942
Lease liabilities	354
Trade and other payables	1,456
Total liabilities	**360,752**
Net assets acquired	**32,155**
Final goodwill arising on acquisition	141,155
Fair value of consideration	**171,578**
Purchase price adjustment	1,732
Total cash consideration transferred	**173,310**

20 Related party transactions and balances

Policy

A person or entity is a related party under the following circumstances:

a) A person or a close member of that person's family if that person:
   i) has control or joint control over HGH;
   ii) has significant influence over HGH; or
   iii) is a member of the key management personnel of HGH.

b) An entity is related to HGH if any of the following conditions applies:
   i) the entity and HGH are members of the same group;
   ii) one entity is an associate or joint venture of the other entity;
   iii) both entities are joint ventures of the same third party;
   iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;
   v) the entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to HGH
   vi) the entity is controlled, or jointly controlled by a person identified in (a); and
   vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(a) Transactions with key management personnel

Key management personnel (**KMP**), are those who, directly or indirectly, have authority and responsibility for planning, directing and controlling the activities of the Group. This includes all executive staff and Directors.

KMP receive personal banking and financial investment services from the Group in the ordinary course of business. The terms and conditions, for example interest rates and collateral, and the risks to the Group are comparable to transactions with other employees and did not involve more than the normal risk of repayment or present other unfavourable features.

All other transactions with KMPs and their related parties are conducted in the ordinary course of business on commercial terms and conditions.

$000's	**June 2023**	**June 2022**
Transactions with key management personnel		
Interest income	123	26
Interest expense	(43)	(24)
Key management personnel compensation		
Short-term employee benefits	(8,083)	(8,790)
Share-based plan benefit/(expense)	14	(1,915)
Total transactions with key management personnel	**(7,989)**	**(10,703)**
Due from/(to) key management personnel		
Lending	4,428	229
Borrowings - deposits	(855)	(508)
Total due from/(to) key management personnel	**3,573**	**(279)**

20 Related party transactions and balances (continued)

(b) Transactions with related parties

HGH is the ultimate parent company of the Group.

Entities within the Group have regular transactions with each other on agreed terms. The transactions include the provision of tax and administrative services and customer operations. Banking facilities are provided by HBL to other Group entities on normal commercial terms as with other customers. There is no lending from subsidiaries within the Group to HGH.

Related party transactions between the Group eliminate on consolidation. Related party transactions outside of the Group are as follows:

$000's	**June 2023**	**June 2022**
ASF Custodians Pty Limited		
Audit fees	4	7
Heartland Trust (HT)		
Dividends paid	714	809

HT held 6,504,266 shares in HGH (2022: 6,475,976 shares).

The Trustees of HT and certain employees of the Group provided their time and skills to the oversight and operation of HT at no charge.

21 Fair value

Policy
Fair value is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

On initial recognition, the transaction price generally represents the fair value of the financial instrument, unless there is observable information from an active market that provides a more appropriate fair value.

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Group determines fair value using other valuation techniques.

The Group measures fair values using the following fair value hierarchy, which reflects the observability of the inputs used in measuring fair value:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (derived from prices).

Level 3 - Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Group recognises transfers between levels of the fair value hierarchy as at the end of the reporting period during which the change has occurred.

(a) Financial instruments measured at fair value

The following methods and assumptions were used to estimate the fair value of each class of financial asset and liability measured at fair value on a recurring basis in the consolidated statement of financial position.

The Group has an established framework in performing valuations required for financial reporting purposes including Level 3 fair values. The Group regularly reviews and calibrates significant unobservable inputs and valuation adjustments in accordance with market participants' views. If external valuation specialists are engaged to measure fair values, the Group assesses the evidence obtained from these specialists to support the conclusion of these valuations. All significant valuations are reported to the Group's Board Audit and Risk Committee for approval prior to its adoption in the financial statements.

Investment in debt securities

Investments in public sector securities and corporate bonds are stated at FVOCI, with the fair value being based on quoted market prices (Level 1 under the fair value hierarchy) or modelled using observable market inputs (Level 2 under the fair value hierarchy).

Investments valued under Level 2 of the fair value hierarchy are valued either based on quoted market prices or dealer quotes for similar instruments, or discounted cash flows analysis.

Investments in equity securities

Investments in equity securities are classified as FVTPL unless an irrevocable election is made by the Group to measure at FVOCI. Investment in listed securities traded in liquid, active markets where prices are readily observable are measured under Level 1 of the fair value hierarchy with no modelling or assumptions used in the valuation.

21 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

Investments in equity securities (continued)

Equity securities are measured at FVOCI where they are not held for trading, the Group doesn't have control or significant influence over the investee and where an irrevocable election is made to measure them at FVOCI. These securities are measured at fair value with unrealised gains and losses recognised in other comprehensive income except for dividend income which is recognised in profit or loss. Investments in unlisted equity securities are measured under Level 3 of the fair value hierarchy with the fair value being based on unobservable inputs using market accepted valuation techniques.

Where appropriate, the Group may apply adjustments to the above-mentioned techniques to determine fair value of an equity security to reflect the underlying characteristics. These adjustments are reflective of market participant considerations in valuing the said security.

The Group has irrevocably elected to account for certain equity investments at fair value through other comprehensive income. These are Level 3 investments and were valued using outcomes from capital raises completed most recently, calibrated against market multiples as at 30 June 2023.

Finance receivables - reverse mortgages

The reverse mortgage portfolio is classified and measured at FVTPL under NZ IFRS 9 Financial instruments (**NZ IFRS 9**). NZ IFRS 4 Insurance contracts (**NZ IFRS 4**) requires entities to account for insurance components of lifetime mortgage contracts. The review of the reverse mortgage portfolio valuation determined that the terms and conditions of these loan contracts do not contain a component of significant insurance risk, therefore they continue to be treated under NZ IFRS 9 Financial Instruments classified at FVTPL under NZ IFRS. Application of NZ IFRS 17 going forward will have a policy choice to continue applying NZ IFRS 9 for these instruments.

On initial recognition the Group considers the transaction price to represent the fair value of the loan, on the basis that no reliable fair value can be estimated as there is no relevant active market and fair value cannot be reliably measured using other valuation techniques under NZ IFRS 13 Fair value measurement.

For subsequent measurement, and at balance date, the Group considered whether the fair value can be determined by reference to a relevant active market or using a valuation technique that incorporates observable inputs but has concluded relevant support is not currently available. In the absence of such market evidence the Group has used an actuarial valuation to determine a proxy for the fair value that incorporates changes in the portfolio risk and expectations of the portfolio performance. The actuarial valuation includes inputs such as mortality and potential move into care, voluntary exits, house price changes, interest rate margin and the no equity guarantee. This estimate is highly subjective and a wide range of plausible values are possible. The estimate provides an indication of whether the transaction value is overstated.

The Group does not consider that the actuarial estimate has moved outside of the original expectation range on initial recognition. There has been no fair value movement recognised in profit or loss during the period (2022: nil). Fair value is not sensitive to the above assumptions due to the nature of reverse mortgage loans. In particular, given conservative origination loan-to-value ratio and security criteria, a material deterioration in house prices combined with a material increase in interest rates over a sustained period of time would likely need to occur before any potential impact to fair value.

The Group will continue to reassess the existence of a relevant active market and movements in expectations on an on-going basis.

21 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

Derivative financial instruments

Interest rate and foreign currency related contracts are recognised in the financial statements at fair value. Fair values are determined from observable market prices as at the reporting date, discounted cash flow models or option pricing models as appropriate (Level 2 under the fair value hierarchy).

The following table analyses financial instruments measured at fair value at the reporting date by the level in the fair value hierarchy into which each fair value measurement is categorised. The amounts are based on the values recognised in the consolidated statement of financial position.

$000's	Level 1	Level 2	Level 3	Total
June 2023				
Assets				
Investments	318,756	-	11,484	330,240
Derivative financial instruments	-	36,983	-	36,983
Finance receivables - reverse mortgages	-	-	2,403,810	2,403,810
Total financial assets measured at fair value	**318,756**	**36,983**	**2,415,294**	**2,771,033**
Liabilities				
Derivative financial instruments	-	7,624	-	7,624
Total financial liabilities measured at fair value	**-**	**7,624**	**-**	**7,624**
June 2022				
Assets				
Investments	279,841	-	7,032	286,873
Derivative financial instruments	-	45,221	-	45,221
Finance receivables - reverse mortgages	-	-	1,996,854	1,996,854
Total financial assets measured at fair value	**279,841**	**45,221**	**2,003,886**	**2,328,948**
Liabilities				
Derivative financial instruments	-	6,341	-	6,341
Total financial liabilities measured at fair value	**-**	**6,341**	**-**	**6,341**

There were no transfers between levels in the fair value hierarchy in the year ended 30 June 2023 (2022: $8.1 million of equity investments transferred out of Level 3 to Level 1).

21 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

The movement in Level 3 assets measured at fair value are below:

$000's	Finance Receivables - Reverse Mortgage	Investments	Total
June 2023			
As at 30 June 2022	1,996,854	7,032	2,003,886
New loans	543,248	-	543,248
Repayments	(297,066)	-	(297,066)
Capitalised Interest and fees	183,458	-	183,458
Purchase of investments	-	6,952	6,952
Fair value (loss) on investment	-	(2,411)	(2,411)
Other[1]	(22,684)	(89)	(22,773)
As at 30 June 2023	**2,403,810**	**11,484**	**2,415,294**
June 2022			
As at 30 June 2021	1,676,073	20,667	1,696,740
New loans	439,110	-	439,110
Repayments	(257,319)	-	(257,319)
Capitalised Interest and fees	106,966	-	106,966
Purchase of investments	-	7,414	7,414
Fair value (loss) on investment	-	(12,998)	(12,998)
Other[1]	32,024	-	32,024
Transfer out of level 3	-	(8,051)	(8,051)
As at 30 June 2022	**1,996,854**	**7,032**	**2,003,886**

[1] This relates to foreign currency translation differences for the assets.

(b) Financial instruments not measured at fair value

The following assets and liabilities of the Group are not measured at fair value in the consolidated statement of financial position.

Cash and cash equivalents

Cash and cash equivalents are measured at amortised cost and their carrying value is considered equivalent to their fair value due to their short term nature.

Finance receivables

The fair value of the Group's finance receivables is calculated using a valuation technique which assumes the Group's current weighted average lending rates for loans of a similar nature and term.

The current weighted average lending rate used to fair value finance receivables with a fixed interest rate was 10.25% (2022: 7.77%). Finance receivables with a floating interest rate are deemed to be at current market rates. The current amount of credit provisioning has been deducted from the fair value calculation of finance receivables as a proxy for future losses.

21 Fair value (continued)

(b) Financial instruments not measured at fair value (continued)

Borrowings

The fair value of deposits, bank borrowings and other borrowings is the present value of future cash flows and is based on the current market interest rates payable by the Group for debt of similar maturities. The average current market rate used to fair value other borrowings was 6.66% (2022: 3.57%).

Other financial assets and financial liabilities

The fair value of financial instruments such as short-term trade receivables and payables is considered equivalent to their carrying value due to their short-term nature.

The following table sets out financial instruments not measured at fair value where the carrying value does not approximate fair value, compares their carrying value against their fair value and analyses them by level in the fair value hierarchy.

	June 2023			June 2022		
$000's	**Fair Value Hierarchy**	**Total Fair Value**	**Total Carrying Value**	**Fair Value Hierarchy**	**Total Fair Value**	**Total Carrying Value**
Assets						
Investments[1]	Level 2	-	-	Level 2	2,418	2,421
Finance receivables	Level 3	4,102,591	4,334,214	Level 3	4,073,977	4,146,821
Total financial assets		**4,102,591**	**4,334,214**		**4,076,395**	**4,149,242**
Liabilities						
Deposits	Level 2	4,130,326	4,131,025	Level 2	3,590,918	3,592,508
Other borrowings	Level 2	2,496,310	2,496,375	Level 2	2,578,213	2,578,213
Total financial liabilities		**6,626,636**	**6,627,400**		**6,169,131**	**6,170,721**

[1]Included within Investments are bank deposits which are held to support the Group's contractual cash flows. Such investments are measured at amortised cost.

21 Fair value (continued)

(c) Classification of financial instruments

The following tables summarise the categories of financial instruments and the carrying value and fair value of all financial instruments of the Group:

$000's	FVOCI Equity	FVOCI Debt Securities	FVTPL	Amortised Cost	Total Carrying Value
June 2023					
Assets					
Cash and cash equivalents	-	-	-	311,503	311,503
Investments	9,665	315,192	5,383	-	330,240
Finance receivables	-	-	-	4,334,214	4,334,214
Finance receivables - reverse mortgages	-	-	2,403,810	-	2,403,810
Derivative financial instruments	-	-	36,983	-	36,983
Other financial assets	-	-	-	1,256	1,256
Total financial assets	**9,665**	**315,192**	**2,446,176**	**4,646,973**	**7,418,006**
Liabilities					
Deposits	-	-	-	4,131,025	4,131,025
Other borrowings	-	-	-	2,496,375	2,496,375
Derivative financial instruments	-	-	7,624	-	7,624
Other financial liabilities	-	-	-	43,254	43,254
Total financial liabilities		**-**	**7,624**	**6,670,654**	**6,678,278**
June 2022					
Assets					
Cash and cash equivalents	-	-	-	310,758	310,758
Investments	5,528	271,790	9,555	2,421	289,294
Finance receivables	-	-	-	4,146,821	4,146,821
Finance receivables - reverse mortgages	-	-	1,996,854	-	1,996,854
Derivative financial instruments	-	-	45,221	-	45,221
Other financial assets	-	-	-	273	273
Total financial assets	**5,528**	**271,790**	**2,051,630**	**4,460,273**	**6,789,221**
Liabilities					
Deposits	-	-	-	3,592,508	3,592,508
Other borrowings	-	-	-	2,578,213	2,578,213
Derivative financial instruments	-	-	6,341	-	6,341
Other financial liabilities	-	-	-	55,538	55,538
Total financial liabilities	**-**	**-**	**6,341**	**6,226,259**	**6,232,600**

Risk Management

22 Enterprise risk management program

The board of directors (the **Board**) sets and monitors the Group's risk appetite across the primary risk domains of credit, capital, liquidity, market (including interest rate), operational and compliance and general business risk. Management is, in turn, responsible for ensuring appropriate structures, policies, procedures and information systems are in place to actively manage these risk domains, as outlined within the Enterprise Risk Management Framework (**ERMF**). Collectively, these processes are known as the Group's Enterprise Risk Management Program (**RMP**).

Role of the Board and the Board Audit and Risk Committee

The Board, through its Board Audit and Risk Committee (**BARC**) is responsible for oversight and governance of the development of the RMP. The role of the BARC includes assisting the Board to formulate its risk appetite and monitoring the effectiveness of the RMP. BARC's responsibilities also include:

- Reviewing financial reporting and application of accounting policies as part of the internal control and risk assessment framework.
- Monitoring the identification, evaluation and management of all significant risks through the Group. This work is supported by an internal audit programme, which provides an independent assessment of the design, adequacy and effectiveness of internal controls. The BARC receives regular reports from internal audit.
- Advising the Board on the formulation of the Board's Risk Appetite Statement.
- Reviewing any reports, policies, standards, other risk documents or matters, or minutes which have been prepared by or in respect of the HGH's Board.
- Monitor material, emerging and strategic risks for the Group and its subsidiaries.

The BARC consists of three non-executive directors. The Chair of the Heartland Bank Limited (**HBL**) Audit Committee and the Chair of the HBL Risk Committee, as well as the HGH CEO, the HBL CEO, the Head of Internal Audit and the HGH CFO, each attend BARC meetings. The BARC undertakes its responsibilities with the assistance of subsidiary Boards and subsidiary Board Committees.

Internal Audit

The Group has an Internal Audit function, the objective of which is to provide independent, objective assurance over the internal control environment. In certain circumstances, Internal Audit will provide risk and control advice to Management provided the work does not impede the independence of the Internal Audit function. The function assists the Group in accomplishing its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Internal Audit is allowed full, free and unfettered access to any and all of the organisation's records, personnel and physical properties deemed necessary to accomplish its activities.

A regular cycle of review has been implemented to cover all areas of the business, focused on assessment, management and control of risks identified. The audit plan takes into account cyclical review of various business units and operational areas, as well as identified areas of higher identified risk. The audit methodology is designed to meet the International Standards for the Professional Practice of Internal Auditing of The Institute of Internal Auditors.

Each audit has specific audit procedures tailored to the area of business that is being reviewed. The audit procedures are updated during each audit to reflect any process changes. Audit work papers are completed to evidence the testing performed in accordance with the audit procedures.

22 Enterprise risk management program (continued)

Internal Audit (continued)

The Head of Internal Audit has a direct reporting line to the Chair of the BARC. Internal audit has accountability to the BARC. A schedule of all outstanding internal control issues is maintained and presented to the BARC to assist and track the resolution of previously identified issues. Any issues raised that are categorised as high risk are specifically reviewed by internal audit during a follow up review once the issue is considered closed by management. The follow up review is performed with a view to formally close out the issue.

Executive Risk Committee (ERC)

The ERC comprises the CEO of HBL, CRO of HBL, CFO of HGH, Financial Controller of HBL and Head of Internal Audit. The ERC has responsibility for overseeing risk aspects including internal control environment to ensure that residual risk is consistent with the Group's risk appetite. The ERC generally meets monthly and minutes are made available to the BARC. ERC's specific responsibilities include decision making and oversight of operational risk, compliance risk and credit risk.

Asset and Liability Committee (ALCO)

The ALCO is a group management committee comprising the CEO of HBL, CFO of HGH, CRO of HBL, Head of Retail and Financial Controller of HBL. The ALCO generally meets monthly, and provides reports made available to HBL Audit and Risk Committees and to the BARC. ALCO's specific responsibilities include decision making and oversight of risk matters in relation to:

- Market risk covering Foreign Exchange Risk and Interest Rate risk (including non-traded interest rate risk and the investment of capital).
- Liquidity risk (including funding).
- Balance sheet structure.
- Capital management.

Climate-related risks

Climate change risks are managed in accordance with the Group's RMP and supported by the environmental sustainability framework.

The Group considers the impact of climate-related risks on its financial position and performance (and in this regard, the Board is currently in the process of establishing a new Board Committee to assist it in managing its climate related risks). While the effects of climate change represent a source of uncertainty, the Group has concluded that climate-related risks do not have a material impact on the judgements, assumptions and estimates for the year ended 30 June 2023.

22 Enterprise risk management program (continued)

Operational and compliance risk

Operational and compliance risk is the risk arising from day-to-day operational activities in the execution of the Group's strategy which may result in direct or indirect loss. Operational and compliance risk losses can occur as a result of fraud, human error, missing or inadequately designed processes, failed systems, damage to physical assets, improper behaviour or from external events. The losses range from direct financial losses, to reputational damage, unfavourable media attention, injury to or loss of staff or clients or as a breach of laws or banking regulations. Where appropriate, risks are mitigated by insurance.

To ensure appropriate responsibility is allocated for the management, reporting and escalation of operational and compliance risk, the Group operates a “three lines of defence” model which outlines principles for the roles, responsibilities and accountabilities for operational and compliance risk management:

- The first line of defence is the business line management of the identification, management and mitigation of the risks associated with the products and processes of the business. This accountability includes regular testing and attestation of the adequacy and effectiveness of controls and compliance with the Group's policies.

- The second line of defence is the Risk and Compliance function, responsible for the design and ownership of the Operational Risk Management Framework. It incorporates key processes including Risk and Control Self-Assessment (**RCSA**), incident management, independent evaluation of the adequacy and effectiveness of the internal control framework, and the attestation process.

- The third line of defence is Internal Audit which is responsible for independently assessing how effectively the Group is managing its risk according to its stated risk appetite.

Market risk

Market risk is the possibility of experiencing losses or gains due to factors affecting the overall performance of financial markets in which the Group is exposed. The primary market risk exposures for the Group are interest rate risk and foreign exchange risk. The risk being that market interest rates or foreign exchange rates will change and adversely impact on the Group’s earnings due to either adverse moves in foreign exchange market rates or in the case of interest rate risks mismatches between repricing dates of interest-bearing assets and liabilities and/or differences between customer pricing and wholesale rates.

Interest rate risk

Interest rate risk refers to exposure of an entity’s earnings and/or capital because of a mismatch between the interest rate exposures of its assets and liabilities. Interest rate risk for the Group arises from the provision of non-traded retail banking products and services and from traded wholesale transactions entered into to reduce aggregate interest rate risk (known as hedges). This risk arises from four key sources:

- Mismatches between the repricing dates of interest-bearing assets and liabilities (yield curve and repricing risk);

- Banking products repricing differently to changes in wholesale market rates (basis risk);

- Loan prepayment or deposit early withdrawal behaviour from customers that deviates from the expected or contractually agreed behaviour (optionality risk); and

- The effect of internal or market forces on a bank’s net interest margin where, for example, in a low-rate environment any fall in rates will further decrease interest income earned on the assets whereas funding cost cannot be reduced as it is already at the minimum level (margin compression risk).

Refer to Note 25 - Interest rate risk for further details regarding interest rate risk.

22 Enterprise risk management program (continued)

Foreign exchange risk

Foreign exchange risk is the risk that the Group's earnings and shareholder equity position are adversely impacted from changes in foreign exchange rates. The Group has exposure to foreign exchange translation risks through its Australian subsidiaries (which have a functional currency of Australian dollars (**AUD**)), in the forms of profit translation risk and balance sheet translation risk.

Profit translation risk is the risk that deviations in exchange rates have a significant impact on the reported profit. Balance sheet translation risk is the risk that whilst the foreign currency value of the net investment in a subsidiary may not have changed, when translated back to the New Zealand dollars (**NZD**), the NZD value has changed materially due to movements in the exchange rates. Foreign exchange revaluation gains and losses are booked to the foreign currency translation reserve. Foreign exchange rate movements in any given year may have an impact on other comprehensive income. The Group manages this risk by setting and approving the foreign exchange rate for the upcoming financial year and entering into hedging contracts to manage the foreign exchange translation risks.

Counterparty Credit Risk

The Group has on-going credit exposure associated with:

- Cash and cash equivalents;
- Finance receivables;
- Holding of investment securities; and
- Payments owed to the Group from risk management instruments.

Counterparty credit risk is managed against limits set in the Market Risk Policy including credit exposure on derivative contracts, bilateral set-off arrangements, cash and cash equivalents and investment securities.

23 Credit risk exposure

Credit risk is the risk that a borrower will default on any type of debt by failing to make payments which it is obligated to make. The risk is primarily that of the lender and includes loss of principal and interest, disruption to cash flows and increased collection costs.

Credit risk is managed to achieve sustainable risk-reward performance whilst maintaining exposures within acceptable risk "appetite" parameters. This is achieved through the combination of governance, policies, systems and controls, underpinned by commercial judgement as described below.

To manage this risk the ERC oversees the formal credit risk management strategy. The ERC reviews the Group's credit risk exposures typically on a monthly basis. The credit risk management strategies aim to ensure that:

- Credit origination meets agreed levels of credit quality at point of approval;
- Sector concentrations are monitored;
- Maximum total exposure to any one debtor is actively managed;
- Changes to credit risk are actively monitored with regular credit reviews.

The BARC (with the assistance of the HBL Board Risk Committee for New Zealand and the Heartland Australia Group Board for Australia) also oversees the Group's credit risk exposures to monitor overall risk metrics having regard to risk appetite set by the Board.

HBL's Board Risk Committee (**BRC**) has authority for approval of all credit exposures for New Zealand. Lending authority has been provided by the BRC to HBL's Credit Committee, and to the business units under a detailed Delegated Lending Authority framework. Application of credit discretions in the business operation are monitored through a defined review and hindsight structure as outlined in the Credit Risk Oversight Policy. Delegated Lending Authorities are provided to individual officers with due cognisance of their experience and ability. Larger and higher risk exposures require approval of senior management, the Credit Committee and ultimately through to HBL's BRC

Heartland Australia Group Board has authority for approval for all credit exposures for Australia.

Reverse mortgage loans and negative equity risk

Reverse mortgage loans are a form of mortgage lending designed for the needs of people over 60 years of age. These loans differ to conventional mortgages in that they typically are not repaid until the borrower ceases to reside in the property. Further, interest is not required to be paid, it is capitalised into the loan balance and is repayable on termination of the loan. As such, there are no incoming cash flows and therefore no default risk to manage during the term of the loan. Negative equity risk arises from the promise by the Group that the maximum repayment amount is limited to the net sale proceeds of the borrowers' property.

The Group's exposure to negative equity risk is managed via lending standards specific for this product. In addition to usual criteria regarding the type, and location, of security property that the Group will accept for reverse mortgage lending, a key aspect of the Group's policy is that a borrower's age on origination of the reverse mortgage loan will dictate the loan-to-value ratio of the reverse mortgage on origination. New Zealand and Australia reverse mortgage lending standards and operations are well aligned.

23 Credit risk exposure (continued)

Business Finance Guarantee Scheme

In April 2020, HBL along with other registered banks in New Zealand, entered into a Deed of Indemnity with the New Zealand Government to implement the New Zealand Government's Business Finance Guarantee Scheme (the "**Scheme**"). The purpose of the Scheme was to provide short term credit to eligible small and medium size businesses, who had been impacted by the economic effects of COVID-19. The Scheme allowed banks to lend to a maximum of $5 million for a five-year term. The New Zealand Government guaranteed 80% of any loss incurred (credit risk) with the Bank holding the remaining 20%. The Scheme concluded on 30 June 2021. As at 30 June 2023 the Bank had a total exposure of $54.8 million (2022: $64.8 million) to its customers under this Scheme.

Maximum exposure to credit risk at the relevant reporting dates

The following table represents the maximum credit risk exposure, without taking into account any collateral held. The on balance sheet exposures set out below are based on net carrying amounts as reported in the consolidated statement of financial position.

$000's	June 2023	June 2022
On balance sheet:		
Cash and cash equivalents	311,503	310,758
Investments	315,192	274,212
Finance receivables	4,334,214	4,146,821
Finance receivables - reverse mortgages	2,403,810	1,996,854
Derivative financial assets	36,983	45,221
Other financial assets	1,256	273
Total on balance sheet credit exposures	**7,402,958**	**6,774,139**
Off balance sheet:		
Letters of credit, guarantee commitments and performance bonds	7,378	8,969
Undrawn facilities available to customers	435,314	416,561
Conditional commitments to fund at future dates	24,873	34,791
Total off balance sheet credit exposures	**467,565**	**460,321**
Total credit exposures	**7,870,523**	**7,234,460**

Concentration of credit risk by geographic region

$000's	June 2023	June 2022
New Zealand	5,540,453	5,264,609
Australia	2,115,332	1,809,104
Rest of the world [1]	268,004	212,752
	7,923,789	**7,286,465**
Provision for impairment	(53,266)	(52,005)
Total credit exposures	**7,870,523**	**7,234,460**

[1]These overseas assets are primarily NZD-denominated investments in AA+ (Standard & Poor's) and higher rated securities issued by offshore supranational agencies ("Kauri Bonds").

23 Credit risk exposure (continued)

Concentration of credit risk by industry sector

The Australian and New Zealand Standard Industrial Classification (**ANZSIC**) codes have been used as the basis for categorising customer and investee industry sectors.

$000's	June 2023	June 2022
Agriculture	1,156,042	1,120,678
Forestry and fishing	130,055	148,797
Mining	8,266	12,524
Manufacturing	80,729	78,432
Finance and insurance	817,864	784,948
Wholesale trade	46,053	41,986
Retail trade and accommodation	402,146	423,975
Households	4,078,270	3,555,566
Other business services	198,377	189,860
Construction	336,333	291,971
Rental, hiring and real estate services	205,079	199,388
Transport and storage	359,865	323,732
Other	104,710	114,608
	7,923,789	**7,286,465**
Provision for impairment	(53,266)	(52,005)
Total credit exposures	**7,870,523**	**7,234,460**

Credit risk grading

The Group's finance receivables are monitored either by account behaviour (**Behavioural portfolio**) or a regular assessment of their credit risk grade based on an objective review of defined risk characteristics (**Judgemental portfolio**).

Finance receivables - reverse mortgages have no arrears characteristics and are assessed on origination against a pre-determined criteria.

The Judgemental portfolio consists mainly of business and rural lending where an on-going and detailed working relationship with the customer has been developed while the Behavioural portfolio consists of consumer, retail and smaller business receivables.

Judgemental loans are individually risk graded based on loan status, financial information, security and debt servicing ability. Exposures in the Judgemental portfolio are credit risk graded by an internal risk grading mechanism where grade 1 is the strongest risk. Grade 8 and grade 9 are the weakest risk grades where a loss is probable. Behavioural loans are managed based on their arrears status.

All loans past due but not impaired have been categorised into three impairments stages (see Note 13 – Finance receivables) which are in most cases based on arrears status. If a Judgemental loan is risk graded 6 or above it will be classified as stage 2 as a minimum and carry a provision based on lifetime ECL.

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23 Credit risk exposure (continued)

Credit risk grading (continued)

$000's	Collectively Assessed Stage 1	Stage 2	Stage 3	Individually Assessed	Total
June 2023					
Judgemental portfolio					
Grade 1 - Very Strong	25	-	-	-	25
Grade 2 - Strong	3,658	-	-	-	3,658
Grade 3 - Sound	41,887	477	-	-	42,364
Grade 4 - Adequate	637,993	9,975	3,477	-	651,445
Grade 5 - Acceptable	1,390,926	5,492	602	-	1,397,020
Grade 6 - Monitor	-	64,946	6,763	-	71,709
Grade 7 - Substandard	-	76,955	13,725	-	90,680
Grade 8 - Doubtful	-	-	-	51,447	51,447
Grade 9 - At risk of loss	-	-	-	1,671	1,671
Total Judgemental portfolio	2,074,489	157,845	24,567	53,118	2,310,019
Total Behavioural portfolio	1,996,109	24,625	56,727	-	2,077,461
Gross finance receivables	**4,070,598**	**182,470**	**81,294**	**53,118**	**4,387,480**
Provision for impairment	(13,009)	(2,463)	(21,499)	(16,295)	(53,266)
Total finance receivables	**4,057,589**	**180,007**	**59,795**	**36,823**	**4,334,214**
Undrawn facilities available to customers	57,471	77,150	123,248	-	257,869
June 2022					
Judgemental portfolio					
Grade 1 - Very Strong	26	-	-	-	26
Grade 2 - Strong	10,859	-	-	-	10,859
Grade 3 - Sound	53,756	-	-	-	53,756
Grade 4 - Adequate	697,590	5,382	1,052	-	704,024
Grade 5 - Acceptable	1,366,680	1,823	53	-	1,368,556
Grade 6 - Monitor	-	25,106	2,308	-	27,414
Grade 7 - Substandard	-	64,203	4,998	-	69,201
Grade 8 - Doubtful	-	-	-	62,860	62,860
Grade 9 - At risk of loss	-	-	-	3,511	3,511
Total Judgemental portfolio	2,128,911	96,514	8,411	66,371	2,300,207
Total Behavioural portfolio	1,839,006	21,910	37,703	-	1,898,619
Gross finance receivables	**3,967,917**	**118,424**	**46,114**	**66,371**	**4,198,826**
Provision for impairment	(20,256)	(1,958)	(14,602)	(15,189)	(52,005)
Total finance receivables	**3,947,661**	**116,466**	**31,512**	**51,182**	**4,146,821**
Undrawn facilities available to customers	63,475	73,175	110,495	-	247,145

23 Credit risk exposure (continued)

Collateral held

The Group employs a range of policies and practices to mitigate credit risk and has internal policies on the acceptability of specific classes of collateral. Collateral is held as security to support credit risk on finance receivables and enforced in satisfying the debt in the event contractual repayment obligations are not met. The collateral held for mitigating credit risk for the Group's lending portfolios is outlined below.

Reverse mortgage and Residential mortgage loans
Reverse mortgage loans are secured by a first mortgage over a residential property which is typically a customer's primary residential dwelling, residential investment property or holiday home. Residential mortgage loans are secured by a residential mortgage over an owner-occupied property located in an approved urban area.

Corporate lending
Business lending including rural lending is typically secured by way of a charge over property and/or specific security agreement over relevant business assets, and, where considered appropriate, a general security agreement to provide the ability to control cash flows.

Other lending
Other lending comprises personal loans, primarily motor loans, which are secured by a motor vehicle or a boat; and other shorter term smaller personal loans which are predominantly unsecured.

The Group analyses the coverage of the loan portfolio which is secured by the collateral it holds.

Coverage is measured by the value of security as a proportion of loan balance outstanding and classified as follows:

Fully secured	Greater or equal to 100%
Partially secured	1% - 99.9%
Unsecured	No security held

The Group's loan portfolio have the following coverage from collateral held:

	Corporate	Residential	All other
June 2023			
Fully secured	91%	100%	73%
Partially secured	4%	-	12%
Unsecured	5%	-	15%
Total	**100%**	**100%**	**100%**
June 2022			
Fully secured	92%	100%	71%
Partially secured	6%	-	14%
Unsecured	2%	-	15%
Total	**100%**	**100%**	**100%**

24 Liquidity risk

Liquidity risk is the risk that the Group is unable to meet its payment obligations as they fall due. The timing mismatch of cash flows and the related liquidity risk in all banking operations are closely monitored by the Group.

Measurement of liquidity risk is designed to ensure that the Group has the ability to generate or obtain sufficient cash in a timely manner and at a reasonable price to meet its financial commitments on a daily basis.

The Group's exposure to liquidity risk is governed by a policy approved by the Board and managed by ALCO. This policy sets out the nature of the risk which may be taken and aggregate risk limits, which ALCO must observe. Within this, the objective of the ALCO is to derive the most appropriate strategy for the Group in terms of a mix of assets and liabilities given its expectations of future cash flows, liquidity constraints and capital adequacy. The ALCO employs asset and liability cash flow modelling to determine appropriate liquidity and funding strategies.

RBNZ facilities

In March 2020, HBL was onboarded by the RBNZ as an approved counterparty and executed a 2011 Global Master Repo Agreement providing an additional source for intra-day liquidity for the Group if required.

The Group holds the following liquid assets and committed funding sources for the purpose of managing liquidity risk:

$000's	June 2023	June 2022
Cash and cash equivalents	311,503	310,758
Investments in debt securities	315,192	274,212
Total liquid assets	**626,695**	**584,970**
Undrawn committed bank facilities	294,042	360,859
Total liquid assets and committed undrawn funding	**920,737**	**945,829**

24 Liquidity risk (continued)

Contractual liquidity profile of financial liabilities

The following tables present the Group's financial liabilities by relevant maturity groupings based upon contractual maturity date. The amounts disclosed in the tables represent undiscounted future principal and interest cash flows. As a result, the amounts in the tables below may differ to the amounts reported on the consolidated statement of financial position.

The contractual cash flows presented below may differ significantly from actual cash flows. This occurs as a result of future actions by the Group and its counterparties, such as early repayments or refinancing of term loans and borrowings. Deposits and other public borrowings include customer savings deposits and transactional accounts, which are at call. These accounts provide a stable source of long term funding for the Group.

$000's	On Demand	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
June 2023							
Non-derivative financial liabilities							
Deposits	782,771	2,313,983	1,015,525	62,618	42,186	-	4,217,083
Other borrowings	-	220,675	575,087	918,506	822,614	330,353	2,867,235
Lease liabilities	-	1,489	1,501	2,875	7,046	2,731	15,642
Other financial liabilities	-	43,254	-	-	-	-	43,254
Total non-derivative financial liabilities	**782,771**	**2,579,401**	**1,592,113**	**983,999**	**871,846**	**333,084**	**7,143,214**
Derivative financial liabilities							
Inflows from derivatives	-	3,583	3,552	4,799	13,469	-	25,403
Outflows from derivatives	-	6,644	6,796	5,773	13,125	-	32,338
Total derivative financial liabilities	**-**	**3,061**	**3,244**	**974**	**(344)**	**-**	**6,935**
Undrawn facilities available to customers	435,314	-	-	-	-	-	435,314
June 2022							
Non-derivative financial liabilities							
Deposits	887,976	2,028,225	561,468	103,192	41,655	-	3,622,516
Other borrowings	-	505,191	268,653	702,349	1,160,157	210,428	2,846,778
Lease liabilities	-	1,575	1,525	2,616	6,985	4,911	17,612
Other financial liabilities	-	55,538	-	-	-	-	55,538
Total non-derivative financial liabilities	**887,976**	**2,590,529**	**831,646**	**808,157**	**1,208,797**	**215,339**	**6,542,444**
Derivative financial liabilities							
Inflows from derivatives	-	15,681	1,759	3,505	813	-	21,758
Outflows from derivatives	-	14,800	3,227	6,621	839	-	25,487
Total derivative financial liabilities	**-**	**(881)**	**1,468**	**3,116**	**26**	**-**	**3,729**
Undrawn facilities available to customers	416,561	-	-	-	-	-	416,561

25 Interest rate risk

The Group's market risk is derived primarily of exposure to interest rate risk, predominantly from raising funds through the retail and wholesale deposit market, the debt capital markets and committed and uncommitted bank funding, securitisation of receivables and offering loan finance products to the commercial and consumer market in New Zealand and Australia.

The Group's exposure to market risk is governed by a policy approved by the Board and managed by the ALCO. This policy sets out the nature of risk which may be taken and aggregate risk limits, and the ALCO must conform to this. The objective of the ALCO is to derive the most appropriate strategy for the Group in terms of the mix of assets and liabilities given its expectations of the future and the potential consequences of interest rate movements, liquidity constraints and capital adequacy.

The objective of the Group's interest rate risk policies is to limit underlying net profit after tax (**NPAT**) volatility. The measurement comprises net interest income the Group generates from its interest earning assets and interest bearing liabilities.

The exposure to net interest income comes from a reduction in margins on interest earning assets or interest bearing liabilities and is managed when setting rates by taking into consideration wholesale rates, liquidity premiums, as well as appropriate lending credit margins.

An analysis of the Group's sensitivity to an increase (+) or decrease (-) in market interest rates by 100 basis points (**BP**) is as follows.

An (+)/(-) to market interest rates of 100 BP would result in a $0.12 million (+)/(-) to NPAT (2022: $0.67 million (+)/(-)) with a corresponding impact to equity.

The Group also manages interest rate risk by:

- Monitoring maturity profiles and seeking to match the re-pricing of assets and liabilities;
- Monitoring interest rates daily and regularly (at least monthly) reviewing interest rate exposures; and
- Entering into derivatives to hedge against movements in interest rates.

25 Interest rate risk (continued)

Contractual repricing analysis

The interest rate risk profile of financial assets and liabilities that follows has been prepared on the basis of maturity or next repricing date, whichever is earlier.

$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non-Interest Bearing	Total
June 2023							
Financial assets							
Cash and cash equivalents	303,811	-	7,688	-	-	4	311,503
Investments	29,828	24,963	37,767	55,460	167,174	15,048	330,240
Derivative financial assets	-	-	-	-	-	36,983	36,983
Finance receivables	1,891,666	382,923	601,344	767,933	690,348	-	4,334,214
Finance receivables - reverse mortgages	2,403,810	-	-	-	-	-	2,403,810
Other financial assets	-	-	-	-	-	1,256	1,256
Total financial assets	**4,629,115**	**407,886**	**646,799**	**823,393**	**857,522**	**53,291**	**7,418,006**
Financial liabilities							
Deposits	2,259,254	795,536	962,205	59,026	35,216	19,788	4,131,025
Other borrowings	1,918,311	49,598	393,072	-	135,394	-	2,496,375
Derivative financial liabilities	-	-	-	-	-	7,624	7,624
Lease liabilities	-	-	-	-	-	14,287	14,287
Other financial liabilities	-	-	-	-	-	43,254	43,254
Total financial liabilities	**4,177,565**	**845,134**	**1,355,277**	**59,026**	**170,610**	**84,953**	**6,692,565**
Effect of derivatives held for risk management	1,084,971	(66,798)	(41,181)	(556,676)	(420,316)	-	-
Net financial assets/(liabilities)	**1,536,521**	**(504,046)**	**(749,659)**	**207,691**	**266,596**	**(31,662)**	**725,441**

25 Interest rate risk (continued)

Contractual repricing analysis (continued)

$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non-Interest Bearing	Total
June 2022							
Financial assets							
Cash and cash equivalents	310,749	-	-	-	-	9	310,758
Investments	1,568	854	51,144	91,974	128,672	15,082	289,294
Derivative financial assets	-	-	-	-	-	45,221	45,221
Finance receivables	1,913,425	284,993	437,200	579,417	931,786	-	4,146,821
Finance receivables - reverse mortgages	1,996,854	-	-	-	-	-	1,996,854
Other financial assets	-	-	-	-	-	273	273
Total financial assets	**4,222,596**	**285,847**	**488,344**	**671,391**	**1,060,458**	**60,585**	**6,789,221**
Financial liabilities							
Deposits	2,197,104	684,378	546,718	99,196	38,325	26,787	3,592,508
Other borrowings	2,325,261	130,873	-	121,191	-	888	2,578,213
Derivative financial liabilities	-	-	-	-	-	6,341	6,341
Lease liabilities	-	-	-	-	-	16,240	16,240
Other financial liabilities	-	-	-	-	-	55,538	55,538
Total financial liabilities	**4,522,365**	**815,251**	**546,718**	**220,387**	**38,325**	**105,794**	**6,248,840**
Effect of derivatives held for risk management	986,194	(76,349)	(127,004)	(309,781)	(473,060)	-	-
Net financial assets/(liabilities)	**686,425**	**(605,753)**	**(185,378)**	**141,223**	**549,073**	**(45,209)**	**540,381**

The tables above illustrate the periods in which the cash flows from interest rate swaps are expected to occur and affect profit or loss.

Other Disclosures

26 Significant subsidiaries

Significant Subsidiaries	Country of incorporation and place of business	Nature of business	Proportion of ownership and voting power held June 2023	June 2022
Heartland Bank Limited	New Zealand	Bank	100%	100%
VPS Properties Limited	New Zealand	Investment property holding company	100%	100%
Marac Insurance Limited	New Zealand	Insurance services	100%	100%
Heartland Australia Holdings Pty Limited	Australia	Financial services	100%	100%
Heartland Australia Group Pty Limited	Australia	Financial services	100%	100%
Australian Seniors Finance Pty Limited	Australia	Management services	100%	100%
StockCo Holdings 2 Pty Limited	Australia	Financial services	100%	100%
StockCo Australia Management Pty Limited	Australia	Management services	100%	100%

27 Structured entities

A structured entity is one which has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity. Structured entities are created to accomplish a narrow and well-defined objective such as the securitisation or holding of particular assets, or the execution of a specific borrowing or lending transaction. Structured entities are consolidated where the substance of the relationship is that the Group controls the structured entity.

(a) Heartland Cash and Term PIE Fund (Heartland PIE Fund)

The Group controls the operations of the Heartland PIE Fund which is a portfolio investment entity that invests in the Group's deposits. Investments of Heartland PIE Fund are represented as follows:

$000's	June 2023	June 2022
Deposits	244,258	149,824

(b) Heartland Auto Receivable Warehouse Trust 2018-1 (HARWT)

HARWT securitises motor vehicle loan receivables as a source of funding.

The Group continues to recognise the securitised assets and associated borrowings in the consolidated statement of financial position as the Group remains exposed to and has the ability to affect variable returns from those assets and liabilities. Although the Group recognises those interests in HARWT, the loans sold to HARWT are set aside for the benefit of investors in HARWT. Other depositors and lenders to the Group have no recourse to those assets.

$000's	June 2023	June 2022
Cash and cash equivalents	16,874	20,197
Finance receivables	254,735	312,239
Other borrowings	(258,256)	(315,308)

27 Structured entities (continued)

(c) Seniors Warehouse Trust, Seniors Warehouse Trust No.2 (together the SW Trusts) and Australian Seniors Finance Settlement Trust (ASF Trust)

SW Trusts and ASF Trust (collectively the Trusts) form part of Australian Seniors Finance Pty Limited (**ASF**) reverse mortgage business and were set up by ASF as asset holding entities. The Trustee for the Trusts is ASF Custodians Pty Limited, and the Trust Manager is ASF. The reverse mortgage loans held by the Trusts are set aside for the benefit of the investors in the Trusts. The balances of SW Trusts and ASF Trust are represented as follows:

$000's	June 2023	June 2022
Cash and cash equivalents	29,392	26,003
Finance receivables - reverse mortgages	1,371,110	1,136,644
Other borrowings	(1,124,835)	(902,155)

(d) Atlas 2020-1 Trust (Atlas Trust)

Atlas Trust was set up on 11 September 2020 as part of ASF's reverse mortgage business similar to the existing SW Trusts and ASF Trust. The Trustee for the Trust is BNY Trust Company of Australia Limited and the Trust Manager is ASF. The balances of Atlas Trust are represented as follows:

$000's	June 2023	June 2022
Cash and cash equivalents	11,684	15,774
Finance receivables - reverse mortgages	144,099	138,950
Other borrowings	(143,353)	(145,219)

(e) StockCo Securitisation Trust 2022-1

StockCo Securitisation Trust 2022-1 was set up on 31 May 2022 as part of StockCo Australia's livestock business. The Trustee for the Trust is AMAL Trustees Pty Limited and the Trust Manager is AMAL Management Services Pty Limited. The balances of StockCo Securitisation Trust 2022-1 are represented as follows:

$000's	June 2023	June 2022
Cash and cash equivalents	39,089	15,007
Finance receivables	365,130	354,901
Other borrowings	(365,823)	(311,415)

28 Staff share ownership arrangements

The Group operates a number of share-based compensation plans that are equity settled. The fair value determined at the grant date is expensed on a straight-line basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest, with a corresponding increase in equity. At the end of each reporting period the Group revises its estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the employee benefits reserve.

(a) Share-based compensation plan details

Heartland performance rights plan (PR plan)

The PR plan was established to enhance the alignment of participants' interests with those of the Group's shareholders. Under the PR plan participants are issued performance rights which will entitle them to receive shares in the Group. As at June 2023, there were 5 active tranches being 2023, 2024 (CEOs), 2024 (non-CEOs), 2025 (CEOs) and 2025 (non-CEOs). All tranches are subject to the existing rules of the PR plan.

PR Plan 2017 Tranche and PR Plan 2018 Tranche (collectively the Legacy Tranches) and PR Plan 2022 Tranche (PR plan 2022) fully vested in September 2022 as per the original expectation and on the basis that the Group achieved its financial measures, strategic objectives and culture and conduct objectives over the period commencing 1 July 2019 and ending on 30 June 2022. On vesting, 2,250,625 performance rights were converted into ordinary shares, contributing a $1,170,325 decrease in the Employee benefits reserve.

PR Plan 2023 Tranche (PR plan 2023) and PR Plan 2024 (CEOs) Tranche (PR plan 2024 (CEOs))

The performance rights were issued subject to the participants' continued employment with the Group until the measurement date and the Group achieving its financial measures, strategic objectives and culture and conduct objectives, over the period commencing 1 July 2020 and ending on 30 June 2023. The targets are dynamic and may be adjusted by the Board from time to time in order to account for unanticipated capital changes during the performance period. The measurement date is the business day following the date on which the Group announces its full year results for the financial year ended 2023.

PR plan 2024 (CEOs) includes the performance rights originally issued to the CEOs under the PR plan 2023 but whose measurement period was subsequently modified to be from 1 July 2020 to 30 June 2024. There have been no other changes in plan terms or rules.

PR Plan 2024 (non-CEOs) Tranche (PR plan 2024 (non-CEOs)) and PR Plan 2025 (CEOs) Tranche (PR plan 2025 (CEOs))

PR plan 2024 (non-CEOs) and PR plan 2025 (CEOs) were issued for period commencing 1 July 2021 and ending on 30 June 2024 and 30 June 2025 respectively. The tranche rules have been aligned with PR plan 2023 and PR plan 2024 (CEOs). Measures are tested on the business day after the announcement of full year results for the financial years ended 30 June 2024 and 30 June 2025 respectively.

PR Plan 2025 (non-CEOs) Tranche (PR plan 2025 (non-CEOs))

PR plan 2025 (non-CEOs) was issued for the period commencing 1 July 2022 and ending on 30 June 2025. The tranche rules have been aligned with PR plan 2023 and PR plan 2024 (non-CEOs). Measures are tested on the business day after the announcement of full year results for the financial year ended 30 June 2025.

28 Staff share ownership arrangements (continued)

(a) Share-based compensation plan details (continued)

	June 2023 PR Plan Number of Rights	June 2022 PR Plan Number of Rights
Opening balance	8,801,096	7,742,276
Vested	(2,250,625)	-
Issued	1,717,909	2,454,395
Forfeited	(414,740)	(1,395,575)
Closing balance	**7,853,640**	**8,801,096**

(b) Effect of share-based payment transactions

$000's	**June 2023**	**June 2022**
Award of Shares		
PR Plan	105	1,915
Total expense recognised	**105**	**1,915**

As at 30 June 2023, $2.2 million of the share scheme awards remain unvested and not expensed (2022: $3.1 million). This expense will be recognised over the performance period of the awards.

(c) Number of rights outstanding

	June 2023		June 2022	
	Rights Outstanding	Remaining Years	Rights Outstanding	Remaining Years
PR Plan - 2017	-	-	1,543	-
PR Plan - 2018	-	-	139	-
PR Plan - 2022	-	-	568	-
PR Plan - 2023	1,275	-	4,096	1
PR Plan - 2024	3,548	1	922	2
PR Plan - 2025	3,031	2	1,533	3
Total	**7,854**		**8,801**	

29 Securitisation, funds management and other fiduciary activities

Funds management and other fiduciary activities

The Group, through Heartland PIE Fund Limited, controls, manages and administers the Heartland PIE Fund and its products (Heartland Call PIE and Heartland Term Deposit PIE). Refer to Note 27 - Structured entities has further details. The Heartland PIE Fund deals with HBL in the normal course of business, in the HBL's capacity as Registrar of the Fund and also invests in HBL's deposits. The Group is considered to control the Heartland PIE Fund, and as such the Heartland PIE Fund is consolidated within the financial statements of the Group.

30 Concentrations of funding

(a) Concentration of funding by industry

The Australian and New Zealand Standard Industrial Classification (**ANZSIC**) codes have been used as the basis for categorising customer and investee industry sectors.

$000's	June 2023	June 2022
Agriculture	113,341	113,848
Forestry and fishing	21,944	14,391
Mining	291	1,524
Manufacturing	19,185	18,643
Finance and insurance	2,627,218	2,420,850
Wholesale trade	7,634	5,854
Retail trade and accommodation	25,136	19,491
Households	3,215,828	2,754,452
Rental, hiring and real estate services	59,720	43,797
Construction	36,868	28,449
Other business services	66,763	66,731
Transport and storage	7,807	4,598
Other	40,183	41,686
Total	**6,241,918**	**5,534,314**
Unsubordinated notes	385,482	636,407
Total borrowings	**6,627,400**	**6,170,721**

(b) Concentration of funding by geographical area

$000's	June 2023	June 2022
New Zealand	4,634,934	4,410,372
Overseas	1,992,466	1,760,349
Total borrowings	**6,627,400**	**6,170,721**

31 Offsetting financial instruments

The Group offsets financial assets and financial liabilities and reports the net balance in the balance sheet where there is currently a legally enforceable right to set off and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Group enters into contractual arrangements with counterparties to manage the credit risks associated primarily with over-the-counter derivatives. The Group has entered into credit support annexes (**CSAs**) which form a part of International Swaps and Derivatives Association (**ISDA**) Master Agreement, in respect of certain exposures relating to derivative transactions. As per these CSAs, the Group or the counterparty needs to collateralise the market value of outstanding derivative transactions. As at 30 June 2023, the Group has received $27.61 million of cash collateral (2022: $32.34 million) against derivative assets. Cash collateral includes amounts of cash obtained to cover the net exposure between the counterparty in the event of default or insolvency. The cash collateral received is not netted off against the balance of derivative assets disclosed in the consolidated statement of financial position; and is disclosed within trade and other payables.

The following table sets out financial assets and financial liabilities which have not been offset but are subject to enforceable master netting agreements (or similar arrangements) and the related amounts not offset in the balance sheet. Financial instruments refer to amounts that are subject to relevant close out netting arrangements under a relevant ISDA agreement. ISDA and similar master netting arrangements do not meet the criteria for offsetting in the statement of financial position because under such agreements the counterparties typically have the right to offset only following an event of default, insolvency or bankruptcy or following other pre-determined events.

	Effects of offsetting on the balance sheet			Related amounts not offset		
$000's	**Gross amounts**	**Gross amount set off in balance sheet**	**Net amounts reported in the balance sheet**	**Financial instruments**	**Cash collateral received**	**Net amount**
June 2023						
Derivative financial assets	36,983	-	36,983	(7,624)	(27,609)	1,750
Total financial assets	**36,983**	-	**36,983**	**(7,624)**	**(27,609)**	**1,750**
Derivative financial liabilities	7,624	-	7,624	(7,624)	-	-
Total financial liabilities	**7,624**	-	**7,624**	**(7,624)**	-	**-**
June 2022						
Derivative financial assets	45,221	-	45,221	(6,341)	(32,342)	6,538
Total financial assets	**45,221**	**-**	**45,221**	**(6,341)**	**(32,342)**	**6,538**
Derivative financial liabilities	6,341	-	6,341	(6,341)	-	-
Total financial liabilities	**6,341**	**-**	**6,341**	**(6,341)**	**-**	**-**

32 Contingent liabilities and commitments

The Group in the ordinary course of business will be subject to claims and proceedings against it whereby the validity of the claim will only be confirmed by uncertain future events. In such circumstances the contingent liabilities are possible obligations, or present obligations if known, where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised, but are disclosed, unless they are remote. Where some loss is probable, provisions have been made on a case by case basis.

Contingent liabilities and credit related commitments arising in respect of the Group's operations were:

$000's	**June 2023**	**June 2022**
Letters of credit, guarantee commitments and performance bonds	7,378	8,969
Total contingent liabilities	**7,378**	**8,969**
Undrawn facilities available to customers	435,314	416,561
Conditional commitments to fund at future dates	24,873	34,791
Total commitments	**460,187**	**451,352**

33 Events after reporting date

The Group approved a fully imputed final dividend of 6 cents per share on 28 August 2023.

There were no other events subsequent to the reporting period which would materially affect the consolidated financial statements.

Independent auditor's report

To the shareholders of Heartland Group Holdings Limited

Our opinion

In our opinion, the accompanying financial statements of Heartland Group Holdings Limited (the Company), including its subsidiaries (the Group), present fairly, in all material respects, the financial position of the Group as at 30 June 2023, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

What we have audited

The Group's financial statements comprise:

- the consolidated statement of financial position as at 30 June 2023;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with Professional and Ethical Standard 1 *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the *International Code of Ethics for Professional Accountants (including International Independence Standards)* issued by the International Ethics Standards Board for Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our firm carries out other services for the Group. These services are audit and assurance related services comprising: assurance over financial service license compliance, insurance solvency, trust deed reporting, supervisor reporting and registry audits, regulatory reporting, agreed upon procedures and other services. Other services are actuarial services for reverse mortgages for the Group (completed prior to our appointment as auditor), tax compliance services for a subsidiary of the Group and the provision of an executive reward survey report. In addition, certain partners and employees of our firm may deal with the Group on normal terms within the ordinary course of trading activities of the Group. The provision of these other services and relationships have not impaired our independence as auditor of the Group.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Description of the key audit matter	How our audit addressed the key audit matter
Provision for impairment of finance receivables As disclosed in note 13 of the financial statements, the impairment allowance totalled $53.3 million at 30 June 2023. For the determination of the collectively assessed impairment allowance, this requires the use of credit risk methodologies that are applied in models using the Group's historical experience of the correlations between defaults and losses, borrower creditworthiness, segmentation of customers or portfolios and economic conditions. The assumptions we focused our audit on included those with greater levels of management judgement and for which variations have the most significant impact on the impairment allowance. For finance receivables that meet specific risk based criteria, the impairment allowance is individually assessed by the Group. These allowances are measured using probability weighted scenarios which are intended to reflect a range of reasonably possible outcomes, and incorporate assumptions such as estimated future cash proceeds expected to be recovered from the realisation of security held as collateral by the Group. We considered this a key audit matter due to the significant audit effort required and the inherent estimation uncertainty present in its determination, which is due to the subjectivity and extent of judgement used by the Group in the impairment allowance recognition and measurement.	We obtained an understanding of control activities over the Group's impairment allowance, and for relevant control activities assessed whether they are appropriately designed. For controls relevant to our planned audit approach we tested, on a sample basis, whether they operated effectively, throughout the financial year. In addition, we, along with our credit risk modelling expert, performed the following procedures, amongst others, on a targeted or sample basis, to assess the reasonableness of the Group's collective allowance for impairment: ● Assessed the appropriateness of the methodology inherent in the models used against the requirements of NZ IFRS 9 *Financial Instruments*; ● Challenged and assessed the appropriateness of the collective allowance for impairment inclusive of the impacts of any post model adjustments; ● We challenged management's modelling outcomes using a range of what we consider reasonably possible assumptions to assess the collective impairment allowance; and ● Tested the completeness and accuracy of critical data elements used in the calculations. With respect to individually assessed allowances we: ● For a sample of business and rural loans not identified as impaired, considered the borrowers latest financial information provided to the Group to assess the credit risk grade rating allocated to the borrower to assess whether the borrower has had a significant increase in credit risk, a critical data element which involves significant management judgement; ● For loans where an impairment was individually assessed, we considered the borrower's latest financial information, value of security held as collateral and probability weighted scenario outcomes (where applicable) to test the basis of measuring the impairment allowance. We also considered the impacts of events occurring subsequent to balance date on the impairment allowances. Where applicable, we considered the competency, capabilities, objectivity and nature of the work of certain experts used by the Group to assist in determining the individual impairment allowance.

Description of the key audit matter	How our audit addressed the key audit matter
	We also assessed the reasonableness of the disclosures against the requirements of the accounting standards.
Fair value of finance receivables - reverse mortgages The Group's fair value of finance receivables – reverse mortgages ("Reverse mortgages") totalled $2.4 billion at 30 June 2023 as disclosed in note 21 of the financial statements. Reverse mortgages are held at fair value through profit or loss. The fair value of reverse mortgages is subject to significant judgement and is highly complex. In addition, the current impacts of rising interest rates and declining house prices, combined with the economic outlook, increases the possibility of increasing outflows under the no negative equity guarantee provided by the Group to the borrower. Accordingly, we consider this to be a key audit matter. The Group records the estimated fair value of the reverse mortgages at transaction price on the basis no reliable fair value can be estimated as there is no relevant active market and fair value cannot be reliably estimated using other valuation techniques under NZ IFRS 13 *Fair Value Measurement (NZ IFRS 13)*. To assess whether the transaction price remains an appropriate proxy for fair value, the Group considers the impact on future discounted cash flows of changes in the risk profile and expectations of performance since loan origination. Specifically considering changes in mortality and potential move into care, voluntary exits, house prices, likelihood of cash outflows under the no negative equity guarantee and interest rate margins.	Our audit procedures included assessing the design and implementation of controls relating to the Group's assessment of the fair value of reverse mortgages. In addition, our audit procedures included: • Assessing the reasonableness of the Group's approach to estimating the fair value based on the transaction cost against the requirements of NZ IFRS 13; • Assessing whether there was evidence of a relevant active market or observable inputs in which to establish fair value using a market approach; • Engaging our internal actuarial experts to independently estimate the value of discounted future cash flows from the reverse mortgages, including any expected outflows under the no negative equity guarantee and comparing this to the transaction cost of reverse mortgages (carrying value) to assess any potential shortfall (a shortfall would indicate the transaction value was overstated); • Tested the completeness and accuracy of a sample of critical data elements used as inputs to our internal actuarial expert assessment of the value of discounted future cash flows; • Assessed the reasonableness of key assumptions (such as future house prices, voluntary exits, interest rate margins, future interest rates) used by our internal actuarial expert in their assessment of the value of discounted future cash flows; and • Considered the appropriateness of the disclosures in note 21 of the financial statements against the requirements of the accounting standards.

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Description of the key audit matter	How our audit addressed the key audit matter
StockCo AU Group goodwill impairment assessment The carrying amount of the StockCo AU Group cash generating unit goodwill as at 30 June 2023 as disclosed in note 18 of the financial statements amounted to $139.3 million. The carrying value of goodwill is a key audit matter as it is a significant amount in the Group's consolidated statement of financial position and the estimate of the recoverable amount is dependent on future cash flows. The Group used the Fair Value Less Costs of Disposal (FVLCD) methodology to determine the recoverable amount of the StockCo AU Group cash generating unit. The forecasts in the impairment model prepared by the Group are based on the Group's strategy, some elements of which would be excluded under a Value In Use (VIU) methodology under NZ IAS 36 *Impairment of assets (NZ IAS 36).* The future cash flows in the FVLCD model were prepared based on the Board approved four year forecast cash flows. The key drivers and assumptions used in the impairment model are the following: • Annual lending growth; • Gross interest income (including interest yield); • Cost of funds; • Discount rate; and • Terminal growth rate. Reasonably possible changes in key assumptions that could result in an impairment are disclosed in note 18 of the financial statements.	We obtained the impairment assessment prepared by management which had been independently reviewed by management's external experts. We held discussions with management to understand the assumptions used in the goodwill impairment assessment. We gained an understanding of the current and forecast outlook and the strategic direction of the business. Our audit procedures also included the following: • Obtaining an understanding of the business processes and controls applied by management in performing the impairment assessment; • Assessing the appropriateness of using a FVLCD approach against the requirements of NZ IAS 36; • Understanding key changes in the forecasts used in the impairment assessment compared to the forecasts used in the acquisition model when the business was acquired in the prior year; • Challenging management on the reasonableness of key cash flow assumptions, including movements in annual lending growth, gross interest income (including interest yield) and cost of funds; • Testing the mathematical accuracy of the impairment assessment; • Engaging our internal valuation expert to assess management's valuation methodology and key assumptions, including the discount rate, terminal growth rate and reasonableness of the costs of disposal; • Obtained and evaluated management's sensitivity analyses to ascertain the impact of reasonably possible changes; and • Considered the appropriateness of the disclosures in note 18 of the financial statements against the requirements of the accounting standards.

pwc

Description of the key audit matter	How our audit addressed the key audit matter
Operation of financial reporting information technology (IT) systems and controls The Group's operations and financial reporting processes are heavily dependent on IT systems for the capture, processing, storage and extraction of significant volumes of transactions which is critical to the recording of financial information and the preparation of the Group's financial statements. Accordingly, we consider this to be a key audit matter. In common with all other groups with a banking subsidiary, access management controls are important to ensure both access and changes made to applications and data are appropriate. Ensuring that only appropriate staff have access to IT systems, that the level of access itself is appropriate, and that access is periodically monitored, are key controls in mitigating the potential for fraud or error as a result of a change to an application or underlying data. The Group's controls over IT systems are intended to ensure that: • changes to existing systems operate as intended and are authorised; • access to process transactions or change data is appropriate and maintains an intended segregation of duties; • the use of privileged access to systems and data is restricted and monitored; and • IT processing is approved and where issues arise they are resolved.	For material financial statement transactions and balances, our procedures included obtaining an understanding of the business processes, IT systems used to generate and support those transactions and balances, associated IT application controls, and IT dependencies in manual controls. This involved assessing, where relevant to the audit: • change management: the processes and controls used to develop, test and authorise changes to the functionality and configurations within systems; • security: the access controls designed to enforce segregation of duties, govern the use of generic and privileged accounts, or ensure that data is only changed through authorised means; and • IT operations: the controls over certain IT batch processes used to ensure that any issues that arise are managed appropriately. Where relevant to our planned audit approach, we, along with our IT specialists, evaluated and tested the design and operating effectiveness of certain controls over the continued integrity of IT systems that are relevant to financial reporting. We also carried out tests, on a sample basis, of IT application controls that were key to our audit testing strategy in order to assess the accuracy of relevant system calculations, automated controls and the operation of certain system enforced access controls. Where we identified design or operating effectiveness matters relating to IT systems and application controls relevant to our audit, we performed alternative or additional audit procedures.

Our audit approach

Overview

Overall group materiality: $6.6 million, which represents approximately 5% of profit before tax.

We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark.

Following our assessment of the risk of material misstatement, full scope audits were conducted over the most financially significant operations, being the Heartland Bank Limited Banking Group and Heartland Australia Holdings Pty Limited. Specified audit and analytical review procedures were performed over the remaining operations.

As reported above, we have four key audit matters, being:

- Provision for impairment of finance receivables
- Fair value of finance receivables - reverse mortgages
- StockCo AU Group goodwill impairment assessment
- Operation of financial reporting information technology (IT) systems and controls

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance about whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group materiality for the financial statements as a whole as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate, on the financial statements as a whole.

How we tailored our group audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

The scope of our audit and the nature, timing and extent of audit procedures performed were determined by our risk assessment, the financial significance of components and other qualitative factors (including history of misstatement through fraud or error).

We performed audit procedures over components considered financially significant in the context of the Group (full scope audit) or in the context of individual primary statement account balances (audit of specific account balances). We performed other procedures including testing entity level controls, audit of specific financially significant financial statement line items and analytical review procedures to address the risk of material misstatement in the residual components.

Other information

The Directors are responsible for the other information. The other information comprises the information included in the Annual Report, but does not include the financial statements and our auditor's report thereon. The Annual Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we will not express any form of audit opinion or assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

When we read the other information not yet received, if we conclude that there is a material misstatement therein, we are required to communicate the matter to the Directors and use our professional judgement to determine the appropriate action to take.

Responsibilities of the Directors for the financial statements

The Directors are responsible, on behalf of the Company, for the preparation and fair presentation of the financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (NZ) and ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board's website at:

https://www.xrb.govt.nz/assurance-standards/auditors-responsibilities/audit-report-1/

This description forms part of our auditor's report.

Who we report to

This report is made solely to the Company's shareholders, as a body. Our audit work has been undertaken so that we might state those matters which we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

The engagement partner on the audit resulting in this independent auditor's report is Karen Shires.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
28 August 2023

Auckland

Disclosure Statement

For the year ended 30 June 2023

HEARTLAND
BANK

Contents

General Information

This Disclosure Statement has been issued by Heartland Bank Limited (**HBL** or the **Bank**) and its subsidiaries (the **Banking Group**) for the year ended 30 June 2023 in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the **Order**). The financial statements of the Banking Group for the year ended 30 June 2023 form part of, and should be read in conjunction with, this Disclosure Statement.

Words and phrases defined by the Order have the same meanings when used in this Disclosure Statement.

Name and address for service

The name of the Registered Bank is Heartland Bank Limited.

The Banking Group consists of the Bank and all of its subsidiaries.

The Bank's address for service is Level 3, 35 Teed Street, Newmarket, Auckland 1023.

The address for service of the ultimate parent, Heartland Group Holdings Limited (**HGH**), is Level 3, 35 Teed Street, Newmarket, Auckland 1023.

Details of incorporation

The Bank was incorporated under the Companies Act 1993 on 30 September 2010.

Interests in 5% or more of voting securities of the Bank

Name	Percentage held
Heartland Group Holdings Limited	100%

Heartland Group Holdings Limited has the ability to appoint 100% of Directors, subject to Reserve Bank of New Zealand (**RBNZ**) restrictions and RBNZ Director approval.

Priority of Creditors' Claims

In the event of the Bank becoming insolvent or ceasing business, certain claims set out in legislation are paid in priority to others. These claims include secured creditors, taxes, certain payments to employees and any liquidator's costs. After payment of those creditors, the claims of all other creditors are unsecured and would rank equally, with the exception of holders of subordinated bonds and notes which rank below all other claims.

Guarantee Arrangements

As at the date this Disclosure Statement was signed, no material obligations of the Bank were guaranteed.

Auditor

PricewaterhouseCoopers
PwC Tower, Level 27
15 Customs Street West
Auckland 1010

Directors

All Directors of the Bank reside in New Zealand. Communications to the Directors can be sent to Heartland Bank Limited, Level 3, 35 Teed Street, Newmarket, Auckland 1023.

On 8 November 2022, Simon Tyler was appointed as Director. Geoffrey Ricketts ceased directorship on 13 March 2023.

There have been no other changes in the composition of the Board of Directors of the Bank for the year ended 30 June 2023.

The Directors of the Bank and their details at the time this Disclosure Statement was signed were:

Chairman – Board of Directors
Name: Bruce Robertson Irvine
Qualifications: BCom, LLB, FCA, CFInstD
Type of Director: Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Air Rarotonga Limited, Amaia Day Spa (Tonga) Limited, Amaia Luxury Spa Limited, B R Irvine Limited, Blackbyre Horticulture Limited, Bowdens Mart Limited, MG Sustainable Operations Limited, Chambers @151 Limited, Clipper Investments (2002) Limited, Cockerill and Campbell (2007) Limited, Embassy Hotels Limited, GZ Capital Limited, GZ NZ Limited, GZ RES Limited, Hansons Lane International Holdings Limited, Hawling Holdings Limited, House of Travel Holdings Limited, J.S. Ewers Limited, Kaipaki Holdings Limited, Kaipaki Properties Limited, Lake Angelus Holdings Limited, Lamanna Bananas (NZ) Limited, Lamanna Premier Group Pty Limited, Lamanna Limited, Market Fresh Wholesale Limited, Market Gardeners Limited, MG Group Holdings Limited, MG Marketing Limited, MG New Zealand Limited, Monarch Hotels Limited, Noblesse Oblige Limited, Paradise Islands Limited, Phimai Holdings Limited, Quitachi Limited, Scenic Hotels (Karapiro) Limited, Scenic Hotels (Hamilton) Limited, Scenic Circle Convention Services Limited, Scenic Hotel (Haast) Limited, Scenic Circle (Napier) Limited, Scenic Hotel Group Limited, Scenic Hotels (Ashburton) Limited, Scenic Hotels (International) Limited, Scenic Circle MLC Café & Bar Limited, Skope Industries Limited, Southland Produce Markets Limited, Stark Holdings (NZ) Limited, Wavell Resources Limited, Scenic Circle (Rotorua) Limited, Scenic Circle (Queenstown) Limited, Scenic Hotels Limited, Abalon Investments Limited, Airedale Developments (Auckland) Limited, Scenic Hotels (Tonga) Limited, Waiho Investments Limited, Scenic Circle Hotels Management Services Limited, Scenic Hotel Collection New Zealand Limited, Scenic Hotels (Auckland) Limited, Scenic Hotels (Niue) Limited, Scenic Hotels (Kaikoura) Limited, Heartland Hotels Limited, Scenic (Franz Josef) Limited, Scenic Circle (Airedale) Limited, Scenic Circle (Bay Of Islands) Limited, Platinum Hotels Limited, Scenic Aviation Limited, Scenic Circle (Bay Of Plenty) Limited, Scenic Circle (Blenheim) Limited, Karma Finance Limited, Scenic Circle Hotels (Dunedin) Limited, Refined Hotels Limited, Scenic Hospitality Services Limited, Scenic Circle Glacier Country Hotel Limited, Scenic Circle (North Island) Limited, Scenic Hotels Technology Limited, Scenic Circle (Rotorua Lakes) Limited, Ezibed (2022) Limited, Mainstay International Hotels (NZ)(2022) Limited, Mainstay International Hotels (2022) Limited, Mitchell Corp New Zealand (2022) Limited, Te Kaikoura Investments Limited, MLC Scenic Limited, Wagstaff Holdings Limited, Heartland PIE Fund Limited, Scenic Hotel Punakaiki Limited, Golden Chain (NZ) (2022) Limited, Sproule Ft Leinster Limited, Sproule Ft Prestons Limited, Southern Paprika Limited, Premier Fresh Australia Pty Ltd.

Name: Jeffrey Kenneth Greenslade
Qualifications: LLB
Type of Director: Non-Independent Non-Executive Director
Occupation: Chief Executive Officer of Heartland Group Holdings
External Directorships:
Heartland Australia Group Pty Limited, Heartland Australia Holdings Pty Limited, Australian Seniors Finance Pty Limited, ASF Custodians Pty Limited, Heartland Group Holdings Limited, Henley Family Investments Limited, StockCo Holdings 2 Pty Limited, StockCo Australia Management Pty Limited.

Name: Edward John Harvey
Qualifications: BCom, CA, CFInstD
Type of Director: Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Napier Port Holdings Limited, Pomare Investments Limited, Port of Napier Limited.

Name: Kathryn Mitchell
Qualifications: BA, CMInstD
Type of Director: Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Chambers@151 Limited, Christchurch International Airport Limited, Farmright Limited, Firsttrax Limited, Helpings Hands Holdings Limited, Link Engine Management Limited, Morrison Horgan Limited, The New Zealand Merino Company Limited, Heartland Group Holdings Limited, The A2 Milk Company Limited.

Directors (continued)

Name: Shelley Maree Ruha
Qualifications: BCom, DipBank
Type of Director: Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Analey Holdings Limited, Analey Investments Limited, IT & Business Consulting Limited, New Zealand Rural Land Management GP Limited, Partners Group Holdings Limited, Partners Life Limited, 9 Spokes International Limited, Taxgift Limited, Hobson Wealth Holdings Limited, Hobson Wealth Partner's Limited, Paysauce Limited, 9 Spokes Knowledge Limited, 9 Spokes Operations Limited, 9 Spokes Trustee Limited, 9 Spokes US Holdings Limited, Allied Farmers Limited, Iris Group Holdings Limited, Iris Life Limited, Iris Services Limtied, 5M No.2 Limited, Alf Nominees Limited, Allied Farmers Rural Limited, Clearwater Hotel 2004 Limited, Lifestyles of New Zealand Queenstown Limited, Lonz 2008 Holdings Limited, Lonz 2008 Limited, NZ Farmers Livestock Finance Limited, QWF Holdings Limited, Rural Funding Solutionz Limited, UFL Lakeview Limited.

Name: Simon Ross Tyler
Qualifications: MSc, BSc (hons)
Type of Director: Independent Non-Executive Director
Occupation: Company Director
External Directorships:
Nutrition for Health Limited, Global Horticulture Limited, Palliser Estate Wines of Martinborough Limited.

Conflicts of interest policy

All Directors are required to disclose to the Board any actual or potential conflicts of interest which may exist or is thought to exist upon appointment and are required to keep these disclosures up to date. The details of each disclosure made by a Director to the Board must be entered in the Interests Register.

Directors are required to take any necessary and reasonable measures to try to resolve the conflict and comply with the Companies Act 1993 by disclosing interests and restrictions on voting. Any Director with a material personal, professional or business interest in a matter being considered by the Board must declare their interest and, unless the Board resolves otherwise, may not be present during the boardroom discussions or vote on the relevant matter.

Interested transactions

There have been no transactions between the Bank or any member of the Banking Group and any Director or immediate relative or close business associate of any Director which either has been entered into on terms other than those which would in the ordinary course of business of the Bank or any member of the Banking Group be given to any other person of like circumstances or means, or could be reasonably likely to influence materially the exercise of the Directors' duties.

Audit committee composition

Members of the Bank's Audit Committee as at the date of this Disclosure Statement are as follows:

Edward John Harvey (Chairperson)	Independent Non-Executive Director
Bruce Robertson Irvine	Independent Non-Executive Director
Shelley Maree Ruha	Independent Non-Executive Director
Simon Ross Tyler	Independent Non-Executive Director

Directors' Statements

Each Director of the Bank states that he or she believes, after due enquiry, that:

1. As at the date on which this Disclosure Statement is signed:

   (a) the Disclosure Statement contains all the information that is required by the Order; and

   (b) the Disclosure Statement is not false or misleading.

2. During the year ended 30 June 2023:

   (a) the Bank complied in all material respects with each Condition of Registration that applied during the period;

   (b) credit exposures to connected persons were not contrary to the interests of the Banking Group; and

   (c) the Bank had systems in place to monitor and control adequately material risks of the Banking Group, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk and other business risks, and that those systems were being properly applied.

This Disclosure Statement is dated 28 August 2023 and has been signed by all the Directors.

B. R. Irvine (Chair)

K. Mitchell

J. K. Greenslade

S. M. Ruha

E. J. Harvey

S. Tyler

Consolidated Statement of Comprehensive Income

For the year ended 30 June 2023

$000's	Note	June 2023	June 2022
Interest income	3	372,688	275,770
Interest expense	3	158,027	66,205
Net interest income		**214,661**	**209,565**
Operating lease income	4	5,631	5,284
Operating lease expense	4	3,827	3,383
Net operating lease income		**1,804**	**1,901**
Lending and credit fee income		7,722	6,943
Other income	5	2,932	24,860
Net operating income		**227,119**	**243,269**
Operating expenses	6	101,337	96,203
Profit before impaired asset expense and income tax		**125,782**	**147,066**
Fair value (loss) on investments		-	(315)
Impaired asset expense	8	22,891	14,692
Profit before income tax		**102,891**	**132,059**
Income tax expense	9	28,389	36,068
Profit for the year		**74,502**	**95,991**
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss, net of income tax:			
Effective portion of change in fair value of derivative financial instruments		7,264	6,540
Movement in fair value reserve		(533)	(712)
Items that will not be reclassified to profit or loss, net of income tax:			
Movement in defined benefit reserve		-	(171)
Net loss due to wind-up of superannuation scheme		-	(473)
Other comprehensive income for the year, net of income tax		**6,731**	**5,184**
Total comprehensive income for the year		**81,233**	**101,175**

Total comprehensive income for the year is attributable to the owner of the Bank.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 30 June 2023

		June 2023				June 2022			
$000's	**Note**	**Share Capital**	**Reserves**	**Retained Earnings**	**Total Equity**	**Share Capital**	**Reserves**	**Retained Earnings**	**Total Equity**
Balance at beginning of year		**553,239**	**6,412**	**147,852**	**707,503**	**553,239**	**755**	**87,834**	**641,828**
Total comprehensive income for the year									
Profit for the year		-	-	74,502	74,502	-	-	95,991	95,991
Other comprehensive income, net of income tax	16	-	6,731		6,731	-	5,657	(473)	5,184
Total comprehensive income for the year		**-**	**6,731**	**74,502**	**81,233**	**-**	**5,657**	**95,518**	**101,175**
Contributions by and distributions to owner									
Dividend to Heartland Group Holdings Limited	15	-	-	(60,000)	(60,000)	-	-	(35,500)	(35,500)
Total transactions with owner		**-**	**-**	**(60,000)**	**(60,000)**	**-**	**-**	**(35,500)**	**(35,500)**
Balance at end of the year		**553,239**	**13,143**	**162,354**	**728,736**	**553,239**	**6,412**	**147,852**	**707,503**

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Financial Position

As at 30 June 2023

$000's	Note	June 2023	June 2022
Assets			
Cash and cash equivalents		216,044	221,469
Investments	10	317,011	275,714
Derivative financial instruments	11	36,982	44,487
Due from related parties	18	-	1,540
Finance receivables	12	3,954,800	3,762,231
Finance receivables - reverse mortgages	19	888,600	721,264
Investment properties		11,903	11,832
Operating lease vehicles	13	16,966	15,161
Right of use assets	17	11,510	13,660
Other assets	17	19,597	13,338
Intangible assets	17	71,635	58,418
Deferred tax asset	9	16,760	15,538
Total assets		**5,561,808**	**5,154,652**
Liabilities			
Deposits	14	4,131,029	3,597,144
Other borrowings	14	615,126	749,478
Derivative financial instruments	11	7,624	6,335
Due to related parties	18	7,173	1,535
Lease liabilities	17	13,478	15,726
Tax liabilities		7,692	22,479
Trade and other payables	17	50,950	54,452
Total liabilities		**4,833,072**	**4,447,149**
Net assets		**728,736**	**707,503**
Equity			
Share capital	15	553,239	553,239
Retained earnings and other reserves	16	175,497	154,264
Total equity		**728,736**	**707,503**
Total interest earning and discount bearing assets		5,374,632	4,979,167
Total interest and discount bearing liabilities		4,726,367	4,318,947

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 30 June 2023

$000's	Note	June 2023	June 2022
Cash flows from operating activities			
Interest received		293,872	232,601
Operating lease income received		4,571	3,913
Lending, credit fees and other income received		12,236	11,740
Operating inflows		**310,679**	**248,254**
Interest paid		(138,332)	(87,131)
Payments to suppliers and employees		(93,333)	(47,169)
Taxation paid		(44,055)	(26,616)
Operating outflows		**(275,720)**	**(160,916)**
Net cash flows from operating activities before changes in operating assets and liabilities		**34,959**	**87,338**
Proceeds from sale of operating lease vehicles		4,492	4,482
Purchase of operating lease vehicles		(8,766)	(10,758)
Net movement in finance receivables		(301,687)	(636,981)
Net movement in deposits		522,307	376,052
Net movement in related party balances		3,202	(3,069)
Net cash flows from/(applied to) operating activities[1]		**254,507**	**(182,936)**
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets		(23,423)	(11,889)
Proceeds from investment securities		55,443	82,946
Purchase of investment securities		(95,000)	-
Purchase of investment property		(71)	-
Net cash flows (applied to)/from investing activities		**(63,051)**	**71,057**
Cash flows from financing activities			
Proceeds from wholesale funding		671,271	779,668
Repayment of wholesale borrowings		(753,838)	(521,541)
Repayment of unsubordinated notes		(150,000)	-
Proceeds from issue of subordinated debt		97,934	-
Dividends paid	15	(60,000)	(35,500)
Payment of lease liabilities		(2,248)	(2,182)
Net cashflows (applied to)/from financing activities		**(196,881)**	**220,445**
Net (decrease)/increase in cash held		**(5,425)**	**108,566**
Opening cash and cash equivalents		221,469	112,903
Closing cash and cash equivalents[2]		**216,044**	**221,469**

[1]Cash flows from operating activities do not include cash flows from wholesale funding which are included as part of financing activities.

[2]At 30 June 2023, the Banking Group has $16.9 million (2022: $20.2 million) of cash held by the Trust which may only be used for the purposes defined in the underlying Trust documents. Refer to Note 27 - Structured entities for definition of the Trust and further details.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows (continued)

For the year ended 30 June 2023

Reconciliation of profit after tax to net cash flows from operating activities

$000's	**Note**	**June 2023**	**June 2022**
Profit for the year		**74,502**	**95,991**
Add/(less) non-cash items:			
Depreciation and amortisation expense		9,299	10,294
Depreciation on lease vehicles	13	3,461	3,103
Capitalised net interest income and fee income		(69,249)	(46,108)
Impaired asset expense	8	22,891	14,692
Investment fair value movement		-	315
Deferred tax		(1,222)	(3,287)
Other non-cash items		1,015	(13,245)
Total non-cash items		**(33,805)**	**(34,236)**
Add/(less) movements in operating assets and liabilities:			
Finance receivables		(301,687)	(636,981)
Operating lease vehicles		(5,266)	(6,276)
Other assets		2,313	(1,780)
Current tax		(14,787)	14,923
Derivative financial instruments		8,794	(23,002)
Deposits		522,307	376,052
Other liabilities		2,136	32,373
Total movements in operating assets and liabilities		**213,810**	**(244,691)**
Net cash flows from/(applied to) operating activities[1]		**254,507**	**(182,936)**

[1]Cash flows from operating activities do not include cash flows from wholesale funding which are included as part of financing activities.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Consolidated Statement of Cash Flows (continued)

For the year ended 30 June 2023

Net debt reconciliation

The below table sets out net cash flow and non-cash changes in liabilities arising from financing activities.

$000's	Note	June 2023	June 2022
Balance as at beginning of year[1]		**765,204**	**520,665**
Proceeds from wholesale funding		671,271	779,668
Repayment of wholesale borrowings		(753,838)	(521,541)
Repayment of unsubordinated notes		(150,000)	-
Proceeds from issue of subordinated debt		97,934	-
Payment of lease liabilities		(2,248)	(2,182)
Total cash movements		**(136,881)**	**255,945**
Capitalised interest and fee expense		755	-
Fair value movements		(473)	(11,534)
Other movements		-	128
Total non-cash movements		**282**	**(11,406)**
Balances as at end of year		**628,605**	**765,204**

[1]Includes lease liabilities and other borrowings.

The notes to the financial statements form an integral part of, and should be read in conjunction with, these consolidated financial statements.

Notes to the Financial Statements

For the year ended 30 June 2023

1 Financial statements preparation

Reporting entity

The financial statements presented are the consolidated financial statements comprising Heartland Bank Limited (**HBL** or the **Bank**) and the Banking Group. Refer to Note 26 – Significant subsidiaries for further details.

The Bank is a company incorporated in New Zealand under the Companies Act 1993, a registered bank under the Banking (Prudential Supervision) Act 1989 and a Financial Market Conduct (**FMC**) reporting entity for the purposes of the Financial Markets Conduct Act 2013.

Basis of preparation

The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (**NZ GAAP)** and with the requirements of the Financial Markets Conduct Act 2013. The financial statements comply with New Zealand Equivalents to International Financial Reporting Standards (**NZ IFRS**) and other applicable Financial Reporting Standards as appropriate for profit-oriented entities, and the Registered Bank Disclosure Statement (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the **Order**). The financial statements also comply with International Financial Reporting Standards (**IFRS**) as issued by the International Accounting Standards Board.

The financial statements are presented in New Zealand dollars which is the Banking Group's functional and presentation currency. Unless otherwise indicated, amounts are rounded to the nearest thousand dollars.

The financial statements have been prepared on a going concern basis after considering the Banking Group's funding and liquidity position.

The accounting policies adopted have been applied consistently throughout the periods presented in these financial statements.

Certain comparative balances have been reclassified to align with the presentation used in the current financial year. These reclassifications have no impact on the overall financial performance or financial position for the comparative year.

Basis of measurement

The financial statements have been prepared on the basis of historical cost, except for certain financial instruments and investment properties, which are measured at their fair values as identified in the accounting policies set out in the accompanying notes to the financial statements.

Principles of consolidation

The consolidated financial statements of the Banking Group incorporate the assets, liabilities and results of all controlled entities. Controlled entities are all entities in which the Bank is exposed to, or has rights to, variable returns from its involvement with the entities and has the ability to affect those returns through its power over the entities. Intercompany transactions, balances and any unrealised income and expense (except for foreign currency transaction gains or losses) between controlled entities are eliminated.

Assets and liabilities in a transactional currency that is not the New Zealand dollar, are translated at the exchange rates ruling at balance date. Revenue and expense items are translated at the average rate at the balance date. Exchange differences are taken to the consolidated statement of comprehensive income.

1 Financial statements preparation (continued)

Changes in accounting standards

Accounting standards issued and effective

There have been no changes to accounting policies or new or amended standards that are issued and effective that are expected to have a material impact on the Banking Group.

Accounting standards issued not yet effective

Disclosure of fees for audit firms' services (Amendments to FRS-44)

Amendments were issued to FRS-44 New Zealand Additional Disclosures (Amendments to FRS-44) that require an entity to describe the services provided by its audit or review firm and to disclose the fees incurred by the entity for those services using prescribed categories. These amendments apply to accounting periods beginning on or after 1 January 2024. Earlier application is permitted for accounting periods that begin before 1 January 2024 but have not ended or do not end before 15 June 2023.

The Banking Group has early adopted the Amendments to FRS-44 from 1 July 2022. Refer to Note 7 - Compensation of auditor for further details.

Climate-related standards

Climate-related disclosure standards were issued in December 2022, and took effect on 1 January 2023. These include the Climate-related Disclosures (CS 1), Adoption of Aotearoa New Zealand Climate Standards (CS 2) and General Requirements for Climate-related Disclosures (CS 3). The Banking Group is a designated climate reporting entity under the climate related disclosure regime and is required to meet its requirements effective from the financial reporting period commencing 1 July 2023.

Other new accounting standards, amendments to accounting standards and interpretations have been published that are not mandatory for the 30 June 2023 reporting periods and have not been early adopted by the Banking Group. These standards, amendments or interpretations are not expected to have a material impact on the current or future reporting periods.

Critical accounting estimates and judgements

The preparation of the Banking Group's consolidated financial statements requires the use of estimates and judgements. This note provides an overview of the areas that involve a higher degree of judgement or complexity. Detailed information about each of these estimates and judgements is included in the relevant notes together with the basis of calculation for each affected item in the financial statements.

- Provisions for impairment - The effect of credit risk is quantified based on the Banking Group's best estimate of future cash repayments and proceeds from any security held or by reference to risk profile groupings, historical loss data and forward-looking information. Refer to Note 8 - Impaired asset expense and Note 12 - Finance receivables for further details.

- Fair value of reverse mortgages - Fair value is quantified by the transaction price. Management judgement is applied in determining the appropriateness of the transaction price as fair value. Refer to Note 19 - Fair value for further details.

Assumptions made at each reporting date (e.g., the calculation of the provision for impairment and fair value adjustments) are based on best estimates as at that date. Although the Banking Group has internal controls in place to ensure that estimates can be reliably measured, actual amounts may differ from these estimates. The estimates and judgements used in the preparation of the Banking Group's financial statements are continually evaluated. They are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity. Revisions to accounting estimates are recognised in the reporting period in which the estimates are revised and in any future periods affected.

1 Financial statements preparation (continued)

Financial assets and liabilities

Financial Assets

Financial assets are classified based on:

- The business model within which the assets are managed; and
- Whether the contractual cash flows of the instrument represent solely payment of principal and interest (**SPPI**).

The Banking Group determines the business model at the level that reflects how groups of financial assets are managed. When assessing the business model, the Banking Group considers factors including how performance and risks are managed, evaluated and reported and the frequency and volume of, and reason for sales in previous periods.

Financial assets are classified into the following measurement categories:

Financial Assets	Measurement Category	Note
Bank bonds and floating rate notes	Fair value through other comprehensive income (**FVOCI**)	10
Public sector securities and corporate bonds	FVOCI	10
Equity investments	Fair value through profit or loss (**FVTPL**)	10
Finance receivables – reverse mortgages	FVTPL	19
Finance receivables	Amortised cost	12
Derivative financial instruments	FVTPL	11

Financial assets measured at amortised cost
Financial assets are measured at amortised cost if they are held within a business model whose objective is achieved through holding the financial asset to collect contractual cash flows which represent SPPI.

Financial assets at amortised cost are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method.

Financial assets measured at FVOCI
Financial assets are measured at FVOCI if they are held within a business model whose objective is achieved both through collecting contractual cash flows which represent SPPI or selling the financial asset.

Financial assets at FVOCI are measured at fair value with unrealised gains and losses recognised in other comprehensive income except for interest income, impairment charges and foreign exchange gains and losses, which are recognised in profit or loss.

1 Financial statements preparation (continued)

Financial assets and liabilities (continued)

Financial Assets (continued)

Financial assets measured at FVTPL
Financial assets are measured at FVTPL if:

- they are held within a business model whose objective is achieved through selling or repurchasing the financial asset in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking; or

- the contractual cash flows of the financial asset do not represent SPPI on the principal balance outstanding; or

- they are designated at FVTPL upon initial recognition to eliminate or reduce an accounting mismatch.

Financial assets at FVTPL are measured at fair value with subsequent changes in fair value recognised in profit or loss.

Financial Liabilities

Financial liabilities are classified into the following measurement categories:

- Those to be measured at amortised cost;

- Those to be measured at FVTPL.

Financial liabilities measured at amortised cost
Financial liabilities are measured at amortised cost if they are not held for trading or designated at FVTPL.

Financial liabilities measured at amortised cost are accounted for using the effective interest rate method.

Financial liabilities measured at FVTPL
Financial liabilities are measured at FVTPL if:

- They are held for trading whose principal objective is achieved through selling or repurchasing the financial liability in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking; or

- They are designated at FVTPL upon initial recognition to eliminate or reduce an accounting mismatch.

Financial liabilities at FVTPL are measured at fair value with subsequent changes in fair value recognised in profit or loss.

Further details of the accounting policy for each category of financial asset or financial liability mentioned above is set out in the note for the relevant item.

The Banking Group's policies for determining the fair value of financial assets and financial liabilities are set out in Note 19 - Fair value.

Recognition

The Banking Group initially recognises finance receivables and borrowings on the date that they are originated. All other financial assets and liabilities (including assets and liabilities designated at FVTPL) are initially recognised on the trade date at which the Banking Group becomes a party to the contractual provisions of the instrument.

1 Financial statements preparation (continued)

Derecognition

The Banking Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Banking Group is recognised as a separate asset.

The Banking Group enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position but retains either all risks or rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the consolidated statement of financial position. Transfers of assets with the retention of all or substantially all risks and rewards include, for example, securitised assets and repurchase transactions.

Financial liabilities are derecognised when the obligation is discharged, cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, the exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, with the difference in the respective carrying amounts recognised in profit or loss.

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Performance

2 Segmental analysis

Segment information is presented in respect of the Banking Group's operating segments which are consistent with those used for the Banking Group's management and internal reporting structure.

An operating segment is a component of an entity engaging in business activities and whose operating results are regularly reviewed by the Banking Group's chief operating decision maker (**CODM**). The CODM, who is responsible for allocating resources and assessing business performance of the Banking Group, has been identified as the Bank's Chief Executive Officer (**CEO**) and direct reports.

Operating segments

The Banking Group operates within New Zealand and comprises the following main operating segments:

Motor	Motor vehicle finance.
Reverse mortgages	Reverse mortgage lending.
Personal lending	Transactional, home loans and personal loans to individuals.
Business	Term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium sized businesses.
Rural	Specialist financial services to the farming sector primarily offering livestock finance, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers.

Certain operating expenses, such as premises, IT and support centre costs are not allocated to operating segments and are included in Other. Finance receivables are allocated across the operating segments as assets. Liabilities are managed centrally and therefore are not allocated across the operating segments. The Banking Group does not rely on any single major customer for its revenue base.

$000's	Motor	Reverse Mortgages	Personal Lending	Business	Rural	Other	Total
June 2023							
Net interest income	60,681	39,696	9,426	71,630	33,522	(294)	214,661
Lending and credit fee income	2,034	2,671	447	2,278	292	-	7,722
Net other income	1,485	-	935	991	398	927	4,736
Net operating income	**64,200**	**42,367**	**10,808**	**74,899**	**34,212**	**633**	**227,119**
Operating expenses	4,140	4,928	6,459	9,387	3,068	73,355	101,337
Profit/(loss) before impaired asset expense and income tax	**60,060**	**37,439**	**4,349**	**65,512**	**31,144**	**(72,722)**	**125,782**
Impaired asset expense	10,911	-	3,195	8,155	630	-	22,891
Profit before income tax	**49,149**	**37,439**	**1,154**	**57,357**	**30,514**	**(72,722)**	**102,891**
Income tax expense	-	-	-	-	-	28,389	28,389
Profit/(loss) for the year	**49,149**	**37,439**	**1,154**	**57,357**	**30,514**	**(101,111)**	**74,502**
Total assets	**1,563,939**	**888,600**	**358,572**	**1,356,913**	**712,596**	**681,188**	**5,561,808**
Total liabilities							**4,833,072**

2 Segmental analysis (continued)

$000's	Motor	Reverse Mortgages	Personal Lending	Business	Rural	Other	Total
June 2022							
Net interest income	69,730	29,957	10,218	70,602	29,460	(402)	209,565
Lending and credit fee income	1,582	2,583	364	2,145	269	-	6,943
Net other income	1,744	-	1,198	534	470	22,815	26,761
Net operating income	**73,056**	**32,540**	**11,780**	**73,281**	**30,199**	**22,413**	**243,269**
Operating expenses	3,792	4,485	6,417	9,358	3,038	69,113	96,203
Profit/(loss) before impaired asset expense and income tax	**69,264**	**28,055**	**5,363**	**63,923**	**27,161**	**(46,700)**	**147,066**
Fair value (loss) on investments	-	-	-	-	-	(315)	(315)
Impaired asset expense/(benefit)	1,481	-	(877)	11,831	2,257	-	14,692
Profit/(loss) before income tax	**67,783**	**28,055**	**6,240**	**52,092**	**24,904**	**(47,015)**	**132,059**
Income tax expense	-	-	-	-	-	36,068	36,068
Profit/(loss) for the year	**67,783**	**28,055**	**6,240**	**52,092**	**24,904**	**(83,083)**	**95,991**
Total assets	**1,382,367**	**721,264**	**332,783**	**1,387,352**	**687,232**	**643,654**	**5,154,652**
Total liabilities							**4,447,149**

3 Net interest income

Policy

Interest income and expense on financial instruments is measured using the effective interest rate method that discounts the financial instruments' future cash flows to their present value and allocates the interest income or expense over the life of the financial instrument. The effective interest rate is established on initial recognition of the financial assets or liabilities and is not subsequently revised. For financial instruments at amortised cost, the calculation of the effective interest rate includes all yield related fees and commissions paid or received that are an integral part of the underlying financial instrument.

Interest income is calculated based on the gross carrying amount of financial assets in stages 1 and 2 of the Banking Group's expected credit losses (**ECL**) model and on the carrying amount net of the provision for ECL for financial assets in stage 3. For financial instruments measured at FVTPL, interest is not calculated under the effective interest rate method.

$000's	June 2023	June 2022
Interest income		
Cash and cash equivalents	9,585	805
Investments	5,081	5,156
Finance receivables	290,487	230,514
Finance receivables - reverse mortgages	67,535	39,295
Total interest income [1]	**372,688**	**275,770**

3 Net interest income (continued)

$000's	June 2023	June 2022
Interest expense		
Retail deposits	146,301	45,387
Other borrowings	31,490	20,727
Net interest (income)/expense on derivative financial instruments	(19,764)	91
Total interest expense [2]	**158,027**	**66,205**
Net interest income	**214,661**	**209,565**

[1] Cash and cash equivalents and Finance receivables are measured at amortised cost. Investments are measured at FVOCI. Total interest income derived from these financial assets is calculated using the effective interest rate method. Finance receivables - reverse mortgages are measured at FVTPL.

[2] Deposits and Other borrowings are measured at amortised cost, therefore interest expense incurred on these financial liabilities is calculated using the effective interest rate method. Net interest expense on derivative financial instruments is not calculated using the effective interest rate method as they are measured at FVTPL.

4 Net operating lease income

Policy

As a lessor, the Banking Group retains substantially all the risks and rewards incidental to ownership of the assets and therefore classifies the leases as operating leases. Rental income and expense from operating leases are recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term. Profits on the sale of operating lease assets are included as part of operating lease income. Current year depreciation and losses on the sale of operating lease assets are included as part of operating lease expenses. The leased assets are depreciated over their useful lives on a basis consistent with similar assets.

$000's	June 2023	June 2022
Operating lease income		
Lease income	4,639	4,161
Gain on disposal of lease assets	992	1,123
Total operating lease income	**5,631**	**5,284**
Operating lease expense		
Depreciation on lease assets	3,461	3,103
Direct lease costs	366	280
Total operating lease expense	**3,827**	**3,383**
Net operating lease income	**1,804**	**1,901**

5 Other income

Policy
Rental income from investment properties
Rental income from investment properties is recognised on a straight-line basis over the term of the relevant lease.

Insurance income
Insurance premium income and commission expense are recognised in profit or loss from the date of attachment of the risk over the period of the insurance contract. Claim expense is recognised in the profit or loss on an accrual basis once our liability to the policyholder has been confirmed under the terms of the contract.

Fair value gain or loss on derivative financial instruments
A fair value gain or loss associated with the effective portion of a derivative designated as a cash flow hedge is recognised initially in the hedging reserve. The ineffective portion of a fair value gain or loss and changes in the fair value of any derivatives not designated in a hedge relationship are recognised immediately in the consolidated statement of comprehensive income and disclosed within Other income. Refer to Note 11 - Derivative financial instruments for further details.

$000's	**June 2023**	**June 2022**
Rental income from investment properties	1,063	833
Insurance income[1]	756	664
Management fee income[2]	9,113	5,918
Other income	243	706
Fair value (loss)/gain on derivative financial instruments	(8,237)	16,723
Foreign exchange (loss)/gain	(6)	16
Total other income	**2,932**	**24,860**

[1] Insurance income includes net income from Marac Insurance Limited (**MIL**), a subsidiary of HBL. MIL ceased writing insurance policies in 2020 with the periodic policies expected to expire in 2025.

[2] Refer to Note 18 - Related party transactions and balances for further details.

6 Operating expenses

Policy
Operating expenses are recognised as the underlying service is rendered or over a period in which an asset is consumed or a liability is incurred.

$000's	June 2023	June 2022
Personnel expenses[1]	60,213	53,826
Directors' fees	574	542
Superannuation	1,171	1,045
Depreciation - property, plant and equipment	1,756	2,342
Legal and professional fees[2]	2,838	2,310
Advertising and public relations	1,803	2,814
Depreciation - right of use asset	2,150	2,122
Technology services	9,720	9,014
Telecommunications, stationery and postage	1,694	1,492
Customer administration costs	2,497	2,419
Customer onboarding costs	2,469	2,341
Occupancy costs	1,408	1,345
Amortisation of intangible assets	5,393	5,830
Other operating expenses	7,651	8,761
Total operating expenses	**101,337**	**96,203**

[1] Excludes certain personnel expenses directly incurred in acquiring and developing software and capitalised as part of specific application software.

[2] Legal and professional fees include compensation of auditor which is disclosed in Note 7 - Compensation of auditor.

7 Compensation of auditor

In accordance with the Amendments to FRS-44, adopted by the Banking Group from 1 July 2022, the Banking Group is required to disclose the fees incurred for services received from its audit or review firm, with a description of each service, including audit or review of the financial statements. Other services performed during the reporting period are required to be disclosed using the following categories:

- audit or review related services;
- other assurance services and other agreed-upon procedures engagements;
- taxation services and;
- other services.

In accordance with HGH's external auditor independence policy, it is prohibited for the external auditor's firm to perform tax compliance work. It is also the Banking Group's policy to engage the external auditor's firm on assignments additional to its statutory audit duties only if they are not perceived to be in conflict with the role of external auditor. All services are approved by the Board Audit and Risk Committee.

The fees payable to the current auditor, PricewaterhouseCoopers New Zealand (**PwC**) and to the predecessor auditor, KPMG are outlined in the below table:

$000's	**June 2023**	**June 2022**
Fees paid to current auditor - PwC		
Audit and review of financial statements[1]	660	-
Other assurance and agreed-upon procedure services paid to auditor[2]	17	
Other services paid to auditor[3]	17	-
Total compensation to PwC	**694**	**-**
Fees paid to predecessor auditor - KPMG		
Audit and review of financial statements[1]	-	593
Other assurance and agreed-upon procedure services paid to auditor[2]	-	20
Total compensation to KPMG	-	**613**
Total compensation of auditor	**694**	**613**

[1]Audit and review of the financial statements includes fees paid for both the audit of the annual financial statements and review of interim financial statements.

[2]Other assurance related services paid to the auditor comprise reasonable assurance engagement services for insurance solvency return, trust deed reporting, supervisor and registry audits.

[3]Other non-assurance services paid to PwC relates to actuarial services for reverse mortgages for the Banking Group carried out by PwC prior to the appointment as external auditors and fees for executive reward survey report.

8 Impaired asset expense

$000's	June 2023	June 2022
Individually impaired asset expense	13,033	10,782
Collectively impaired asset expense	11,757	6,665
Total impaired asset expense excluding recovery of amounts previously written off	**24,790**	**17,447**
Recovery of amounts previously written off to the income statement	(1,899)	(2,755)
Total impaired asset expense	**22,891**	**14,692**

Refer to Note 22 – Asset quality for provision for impairment details.

9 Taxation

Policy

Income tax

Income tax expense for the year comprises current tax and movements in deferred tax balances, including any adjustment required for prior years' tax expense. Income tax expense is recognised in profit and loss except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in equity or other comprehensive income.

Current tax

Current tax is the expected tax payable or receivable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to the tax payable or receivable in respect of previous years. Current tax for current and prior years is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred tax

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for taxation purposes. As required by NZ IAS 12 Income Taxes, a deferred tax asset is recognised only to the extent that it is probable that a future taxable profit will be available to realise the asset.

Goods and services tax (GST)

Revenues, expenses and assets are recognised net of GST. As the Banking Group is predominantly involved in providing financial services, only a proportion of GST paid on inputs is recoverable. The non-recoverable proportion of GST is treated as an expense or, if relevant, as part of the cost of acquisition of an asset.

9 Taxation (continued)

Income tax expense

$000's	June 2023	June 2022
Income tax recognised in profit or loss		
Current tax		
Current year	30,353	40,104
Adjustments for prior year	(742)	(748)
Deferred tax		
Current year	(1,447)	(2,895)
Adjustments for prior year	225	(393)
Total income tax expense recognised in profit or loss	**28,389**	**36,068**
Income tax recognised in other comprehensive income		
Current tax		
Investment securities at fair value in fair value reserve	(246)	(5,271)
Fair value movements in derivatives held in cash flow hedge reserve	2,418	7,537
Total income tax expense recognised in other comprehensive income	**2,172**	**2,266**

Reconciliation of effective tax rate

Profit before income tax	**102,891**	**132,059**
Prima facie tax @ 28%	28,810	36,976
Adjusted tax effect of items not deductible	97	232
Adjustments for prior year	(518)	(1,140)
Total income tax expense	**28,389**	**36,068**

Deferred tax assets comprise the following temporary differences:

$000's	June 2023	June 2022
Employee entitlements	1,370	1,234
Share based payment	616	501
Provision for impairment	14,622	14,176
Intangibles and property, plant and equipment	(1,530)	(2,972)
Deferred acquisition costs	(55)	(196)
Operating lease vehicles	451	680
Other temporary differences	1,286	2,116
Total deferred tax assets	**16,760**	**15,538**
Opening balance of deferred tax assets	**15,538**	**12,251**
Movement recognised in profit or loss	1,222	3,287
Closing balance of deferred tax assets	**16,760**	**15,538**

Financial Position

10 Investments

Policy
Investments are classified into one of the following categories:

Fair value through profit or loss
Investments under this category include equity investments and are measured at fair value plus transaction costs. Changes in fair value of these investments are recognised in profit or loss in the period in which they occur.

Fair value through other comprehensive income
Investments under this category include bank bonds, floating rate notes, public securities and corporate bonds. These are initially measured at fair value, including transaction costs, and subsequently carried at fair value. Changes in fair value of these investments are recognised in other comprehensive income and presented within the fair value reserve.

Amortised cost
Investments under this category include bank deposits and are measured using effective interest rate method. They are held to collect contractual cash flows that are solely payments of principal and interest on the principal amount outstanding.

$000's	**June 2023**	**June 2022**
Bank deposits, bank bonds and floating rate notes	305,310	261,258
Public sector securities and corporate bonds	9,882	12,953
Equity investments	1,819	1,503
Total investments	**317,011**	**275,714**

Refer to Note 19 - Fair value for details of the split between investments measured at fair value through profit or loss, fair value through other comprehensive income and amortised cost.

11 Derivative financial instruments

Policy
The Banking Group uses derivatives for risk management purposes. Derivatives held for risk management purposes are placed into hedges that either meet hedge accounting requirements, or economic hedges not placed into an accounting hedge relationship.

Derivatives are recognised at their fair value, with the derivatives being carried as assets when their fair value is positive and as liabilities when their fair value is negative.

A hedged item is an asset, liability, firm commitment or highly probable forecast transaction that exposes the Banking Group to risk of changes in fair value or cash flows, and that is designated as being hedged. The Banking Group applies fair value hedge accounting to hedge movements in the value of fixed interest rate assets and liabilities subject to interest rate risk. The Banking Group applies cash flow hedge accounting to hedge the variability in highly probable forecast future cash flows attributable to interest rate risk on variable rate assets and liabilities.

Derivative instruments that do not qualify for hedge accounting are held as economic hedges. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the consolidated statement of comprehensive income and disclosed within Other income.

Fair value hedge accounting
The criteria that must be met for a relationship to qualify for hedge accounting include:

- the hedging relationship must be formally designated and documented at inception of the hedge,
- effectiveness testing must be carried out on an on-going basis to ensure the hedge is effective, consistent with the originally documented risk management strategy, and
- the instruments or counterparty must be a third party external to the Banking Group.

The Banking Group documents, at the inception of the transaction, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Banking Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair value of hedged items.

Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify for fair value hedge accounting are recorded through profit or loss alongside any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

Where the hedged item is carried at amortised cost, the movement in fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to carrying amount of a hedged item carried at amortised cost is amortised to the consolidated statement of comprehensive income on an effective yield basis over the remaining period to maturity of the hedged item. Where a hedged item carried at amortised cost is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the consolidated statement of comprehensive income.

Cash flow hedge accounting
The criteria that must be met for a relationship to qualify for hedge accounting include:

- the hedging relationship must be formally designated and documented at inception of the hedge,
- effectiveness testing must be carried out on an on-going basis to ensure the hedge is effective, consistent with the originally documented risk management strategy, and
- the instruments or counterparty must be a third party external to the Banking Group.

11 Derivative financial instruments (continued)

Cash flow hedge accounting (continued)
The Banking Group documents, at the inception of the transaction, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Banking Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

A fair value gain or loss associated with the effective portion of a derivative designated as a cash flow hedge is recognised initially in the hedging reserve. The ineffective portion of a fair value gain or loss is recognised immediately in the consolidated statement of comprehensive income.

When a hedging derivative expires or is sold, the hedge no longer meets the criteria for hedge accounting, or the Banking Group elects to revoke the hedge designation, the cumulative gain or loss on the hedging derivative remains in the cash flow hedging reserve until the forecast transaction occurs and affects income, at which point it is transferred to the corresponding income or expense line. If a forecast transaction is no longer expected to occur, the cumulative gain or loss on the hedging derivative previously reported in the cash flow hedging reserve is immediately transferred to the consolidated statement of comprehensive income.

The Banking Group actively manages interest rate risk by entering into derivative contracts to hedge against movements in interest rates. As permitted by NZ IFRS 9, the Banking Group has elected to continue to apply the hedge accounting requirements of NZ IAS 39.

The Banking Group's approach to managing market risk, including interest rate risk, is disclosed in Note 24 – Interest rate risk. The Banking Group actively manages residual interest rate risk from the net exposure of its underlying assets and liabilities, associated with the mismatch of the interest rate repricing profiles of its interest earning assets and interest bearing liabilities, by entering into interest rate swaps to hedge against movements in interest rates.

Interest rate swaps are bilateral derivative contracts with commitments to exchange one set of cash flows for another resulting in an economic exchange of interest rates (for example, fixed rate for floating rate) without exchange of principal. Interest rate swap notional values indicate the volume of transactions outstanding at the end of the financial year and provide basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved, therefore don't indicate the Banking Group's exposure to credit or market risks. The fair values of derivative instruments and their notional values are set out in the below table.

	June 2023			June 2022		
$000's	**Notional Principal**	**Fair Value Assets**	**Fair Value Liabilities**	**Notional Principal**	**Fair Value Assets**	**Fair Value Liabilities**
Interest rate related contracts						
Held as economic hedges	260,650	6,539	-	619,005	17,842	1,537
Designated as cash flow hedges	850,068	15,398	941	309,946	7,949	-
Designated as fair value hedges	543,200	15,045	6,683	549,200	18,696	4,798
Interest rate swaps	**1,653,918**	**36,982**	**7,624**	**1,478,151**	**44,487**	**6,335**
Total derivative financial instruments	**1,653,918**	**36,982**	**7,624**	**1,478,151**	**44,487**	**6,335**

11 Derivative financial instruments (continued)

Micro cash flow hedge accounting is applied to interest rate swaps designated as hedges of the Banking Group's floating rate domestic borrowings and deposits by using 'receive floating / pay fixed' interest rate swaps to fix the cost of floating interest rate loans and deposits.

Micro fair value hedge accounting is applied to receive fixed interest rate swaps designated as hedges of interest rate risk arising from fixed-rate subordinated notes and retail bond, and to pay fixed interest rate swaps designated as hedges of interest rate risk arising from fixed-rate investment securities.

The Banking Group determines whether an economic relationship between the hedged item and the hedging instrument exists based on an assessment of the qualitative characteristics of this hedged item and the hedged risk, supported by quantitative analysis. Close alignment of the critical terms of the hedged item and hedging instrument is also considered a strong indication of the presence of an economic relationship by the Banking Group.

The Banking Group establishes a hedge ratio by aligning the par amount of the exposure to be hedged and the notional amount of the interest rate swap designated as a hedging instrument.

Retrospective testing for each reporting period uses a regression model, which compares the change in the fair value of the hedged item and the change in the fair value of the hedging instrument. For a hedge to be deemed effective, the change in fair values should be within 80% and 125% of each other. Should the result fall outside this range the hedge would be deemed ineffective and recognised immediately through the income statement in line with each hedge relationship policy above.

The hedge relationship is reviewed on a monthly basis and the hedging instruments and hedged items are de-designated and re-designated, if necessary, based on the effectiveness test results and changes in the hedged exposure.

Hedge ineffectiveness may arise from timing difference on repricing between the hedged item and the hedging instrument, difference in timing of their cash flows, or due to changes in the counterparties' credit risk affecting the fair value of hedging instruments.

The following table shows the maturity and interest rate risk profiles of the interest rate swaps as hedging instruments in continuing fair value and cash flow hedge relationships.

$000's	**0-6 Months**	**6-12 Months**	**1-2 Years**	**2-5 Years**	**5+ Years**	**Total**
June 2023						
Interest rate risk						
Cash flow hedge relationships						
Pay fixed						
Nominal amounts	-	20,000	295,000	535,068	-	850,068
Average interest rate	-	4.22%	3.78%	4.00%	-	
Fair value hedge relationships						
Pay fixed						
Nominal amounts	54,700	38,000	60,000	160,400	5,100	318,200
Average interest rate	1.17%	0.77%	0.88%	3.06%	1.51%	
Receive fixed						
Nominal amounts	-	125,000	-	100,000	-	225,000
Average interest rate	-	1.78%	-	4.30%	-	
Total interest rate risk nominal amount	**54,700**	**183,000**	**355,000**	**795,468**	**5,100**	**1,393,268**

11 Derivative financial instruments (continued)

$000's	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
June 2022						
Interest rate risk						
Cash flow hedge relationships						
Pay fixed						
Nominal amounts	-	-	-	309,946	-	309,946
Average interest rate	-	-	-	2.49%	-	
Fair value hedge relationships						
Pay fixed						
Nominal amounts	20,000	31,000	92,700	115,400	15,100	274,200
Average interest rate	1.20%	0.81%	1.00%	0.84%	1.45%	
Receive fixed						
Nominal amounts	150,000	-	125,000	-	-	275,000
Average interest rate	4.50%	-	1.78%	-	-	
Total interest rate risk nominal amount	**170,000**	**31,000**	**217,700**	**425,346**	**15,100**	**859,146**

The following table sets out the accumulated fair value adjustments arising from the corresponding fair value hedge relationships and the outcome of the changes in fair value of the hedged item as well as the hedging instruments used as the basis for recognising effectiveness.

	As at 30 June 2023		For the year ended 30 June 2023
$000's	Carrying value	Accumulated amount of fair value hedge adjustment	Hedge ineffectiveness gain/(loss) recognised in income statement
Interest rate risk			
Investments	290,723	(14,893)	2,620
Other borrowings	(219,959)	5,331	473
Total	**70,764**	**(9,562)**	**3,093**
Interest rate swaps	**8,362**	**8,362**	**(3,133)**
Hedge ineffectiveness of financial instruments recognised in other income			**(40)**

11 Derivative financial instruments (continued)

$000's	As at 30 June 2022 Carrying value	Accumulated amount of fair value hedge adjustment	For the year ended 30 June 2022 Hedge ineffectiveness gain/(loss) recognised in income statement
Interest rate risk			
Investments	262,314	(16,914)	(14,793)
Other borrowings	(272,983)	4,858	11,543
Total	**(10,669)**	**(12,056)**	**(3,250)**
Interest rate swaps	**13,898**	**13,898**	**3,295**
Hedge ineffectiveness of financial instruments recognised in other income			**45**

The accumulated amount of fair value hedge adjustments included in the carrying amount of hedged items that have ceased to be adjusted for hedging gains and losses is nil (2022: nil).

The balance of the cash flow hedge reserve, amounts recognised in the reserve, and amounts transferred out of the reserve are shown in the following table.

$000's	June 2023	June 2022
Cash flow hedge reserve		
Balance at beginning of year	7,446	906
Transferred to the income statement	(1,771)	(641)
Net gains from change in fair value	11,453	10,036
Net movement before tax	**9,682**	**9,395**
Tax on net movement in cash flow hedge reserve	(2,418)	(2,855)
Balance at end of year	**14,710**	**7,446**

During the year ended 30 June 2023, a gain of $0.7 million was recognised in fair value gain on derivative financial instruments in the consolidated statement of comprehensive income related to hedge ineffectiveness from cash flow hedge relationships (2022: nil).

There were no transactions for which cash flow hedge accounting had to be ceased as a result of the highly probable cash flows no longer being expected to occur (2022: nil).

There are $10.1 million (2022: $1.6 million) of balances recognised in the cash flow hedge reserve for which hedge accounting is no longer applied on the basis that the associated variable cash flows are still expected to occur over the lifetime of the original hedge relationships. The associated cash flow hedge reserve is being released over the period of the original hedge relationship which has since been de-designated.

12 Finance receivables

Policy
Finance receivables are initially recognised at fair value plus incremental direct transaction costs and are subsequently measured at amortised cost using the effective interest method, less any impairment loss.

Fees and direct costs relating to loan origination, financing and loan commitments are deferred and amortised to interest income over the life of the loan using the effective interest rate method. Lending fees not directly related to the origination of a loan are recognised over the period of service.

$000's	June 2023	June 2022
Gross finance receivables at amortised cost	4,006,945	3,812,658
Less provision for impairment[1]	(52,145)	(50,427)
Net finance receivables at amortised cost	**3,954,800**	**3,762,231**

[1] Refer to Note 22 - Asset quality for further details.

13 Operating lease vehicles

Policy
Operating lease vehicles are stated at cost less accumulated depreciation.

Operating lease vehicles are depreciated on a straight-line basis over their expected useful life after allowing for any residual values. The estimated lives of these vehicles are between one and five years. Vehicles held for sale are not depreciated but are tested for impairment.

$000's	**June 2023**	**June 2022**
Cost		
Opening balance	20,450	16,114
Additions	8,766	10,758
Disposals	(6,303)	(6,422)
Closing balance	**22,913**	**20,450**
Accumulated depreciation		
Opening balance	5,289	5,249
Depreciation charge for the year	3,461	3,103
Disposals	(2,803)	(3,063)
Closing balance	**5,947**	**5,289**
Opening net book value	15,161	10,865
Closing net book value	**16,966**	**15,161**

The future minimum lease payments receivable under operating leases not later than one year is $4.086 million (2022: $3.057 million), within one to five years is $7.598 million (2022: $6.465 million) and over five years is nil (2022: nil).

14 Borrowings

Policy
Borrowings and deposits are initially recognised at fair value including incremental direct transaction costs. They are subsequently measured at amortised cost using the effective interest method.

The Banking Group hedges interest rate risk on certain debt issues. When fair value hedge accounting is applied to fixed rate debt issues, the carrying values are adjusted for changes in fair value related to the hedged risks.

$000's	**June 2023**	**June 2022**
Deposits	4,131,029	3,597,144
Total borrowings related to deposits	**4,131,029**	**3,597,144**
Unsubordinated notes	122,165	272,983
Subordinated notes[1]	97,793	-
Securitised borrowings	227,054	267,779
Certificate of deposit	148,110	198,715
Money market borrowings	20,004	10,001
Total other borrowings	**615,126**	**749,478**
Total deposits and other borrowings	**4,746,155**	**4,346,622**
Due within one year	4,328,399	3,509,295
Due more than one year	417,756	837,327
Total deposits and other borrowings	**4,746,155**	**4,346,622**

[1]Refer to Note 28 - Capital adequacy for further details.

Deposits and unsubordinated notes rank equally and are unsecured.

14 Borrowings (continued)

The Banking Group has the following retail bonds on issue at balance sheet date:

Retail Bonds $000's	Frequency of interest repayments	June 2023	June 2022	Maturity
$150 million	Semi-annually	-	145,142	21 September 2022
$125 million	Semi-annually	122,165	127,841	12 April 2024
Total retail bonds		**122,165**	**272,983**	

The Banking Group had the following securitised borrowings outstanding at balance sheet date:

Securitisation facility	June 2023		June 2022		
$000's	Limit	Drawn	Limit	Drawn	Maturity
Heartland Auto Receivable Warehouse (**HARWT**)	400,000	227,054	400,000	267,779	26 August 2024
Total securitisation borrowings		**227,054**		**267,779**	

HARWT notes issued to investors are secured over motor vehicle loans.

The Banking Group actively engages facility providers in commercial negotiations including tenor extensions, increase in facility limits, refinancing arrangements, and other commercial terms. The Banking Group has a track record of extending or refinancing funding arrangements as they fall due and does not anticipate any difficultly in doing so when the facilities above expire.

15 Share capital and dividends

Policy
Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effect.

000's	June 2023 Number of Shares	June 2022 Number of Shares
Issued shares		
Opening balance	565,430	565,430
Closing balance	**565,430**	**565,430**

There were nil new shares issued during the period (2022:nil).

The issued and fully paid ordinary share capital is included in Tier 1 capital of the Banking Group. Refer to Note 28 - Capital adequacy for further details.

Dividends paid

	June 2023 Date Declared	$000's	June 2022 Date Declared	$000's
Dividend to HGH	22 August 2022	30,000	21 February 2022	35,500
Dividend to HGH	28 February 2023	30,000		
Total dividends paid		**60,000**		**35,500**

16 Other reserves

$000's	Fair Value Reserve	Defined Benefit Reserve	Cash flow Hedge Reserve	Total
June 2023				
Balance as at 30 June 2022	(1,034)	-	7,446	6,412
Movements attributable to fair value hedges	(779)	-	-	(779)
Movements attributable to cash flow hedges	-	-	9,682	9,682
Income tax effect	246	-	(2,418)	(2,172)
Balance as at 30 June 2023	**(1,567)**	**-**	**14,710**	**13,143**
June 2022				
Balance as at 30 June 2021	(322)	171	906	755
Movements attributable to fair value hedges	(1,301)	-	-	(1,301)
Movements attributable to cash flow hedges	-	-	9,395	9,395
Movement in defined benefit reserve	-	(171)	-	(171)
Income tax effect	589	-	(2,855)	(2,266)
Balance as at 30 June 2022	**(1,034)**	**-**	**7,446**	**6,412**

Fair value reserve
Includes changes in the fair value of investment securities measured at fair value through other comprehensive income, net of tax. For debt securities, these changes are reclassified to the profit or loss when the asset is disposed.

Defined benefit reserve
Includes predetermined retirement benefits calculated for employees of a historical amalgamated entity which was wound up during the prior financial year.

Cash flow hedge reserve
This includes fair value gains and losses associated with the effective portion of the designated cash flow hedging instruments, net of tax.

17 Other balance sheet items

Policy
Property, plant and equipment are stated at cost less accumulated depreciation and impairment (if any). Depreciation is calculated on a straight line basis to write off the net cost or revalued amount of each asset over its expected life to its estimated residual value.

$000's	June 2023	June 2022
Other assets		
Trade receivables	381	-
GST receivables	275	1,506
Prepayments	4,280	4,697
Property, plant and equipment[1]	13,993	6,960
Other receivables	668	175
Total other assets	**19,597**	**13,338**

[1]Property, plant and equipment include rural property worth $7.8 million acquired during the year.

17 Other balance sheet items (continued)

Policy

Intangible assets

Intangible assets with finite useful lives

Software acquired or internally developed by the Banking Group is stated at cost less accumulated amortisation and any accumulated impairment losses. Expenditure on software assets is capitalised only when it increases the future economic value of that asset. Certain internal and external costs directly incurred in acquiring and developing software are capitalised when specific criteria are met. Costs incurred on planning or evaluating software proposals during the research phase or on maintaining systems after implementation are not capitalised. Amortisation of software is on a straight line basis, at rates which will write off the cost over the assets' estimated useful lives. The expected useful life of the software varies up to ten years.

Software-as-a-Service (SaaS) arrangements

SaaS arrangements are service agreements that grant the Banking Group the right to access the cloud provider's application software over the contract period. Costs associated with configuring or customising the software, along with ongoing fees for accessing the cloud provider's application, are recognised as operating expenses when the services are received.

Some of these costs pertain to developing software code that enhances or modifies, or creates additional capability to, existing on-premise systems and qualifies as an intangible asset based on its definition and recognition criteria.

The Banking Group capitalises costs incurred in configuring or customising certain suppliers' application software within specific cloud computing arrangements as intangible assets as the Banking Group considers that it would benefit from those costs to implement the cloud-based software over the expected terms of the cloud computing arrangements. However, such capitalisation occurs only if the activities result in creating an intangible asset that the Banking Group has control over and meets the necessary recognition criteria. Costs that do not meet the criteria for capitalisation as intangible assets are expensed as incurred unless they are paid to the suppliers (or subcontractors of the supplier) of the cloud-based software to significantly customise the cloud-based software for the Banking Group (i.e., such services are not distinct from the Banking Group's right to receive access to the supplier's cloud-based software). In the latter case, the upfront costs are recorded as prepayments for services and amortised over the expected terms of the cloud computing arrangements.

Goodwill

Goodwill arising on acquisition represents the excess of the cost of the acquisition over the Banking Group's interest in the fair value of the identifiable net assets acquired. Goodwill that has an indefinite useful life is not subject to amortisation and is tested for impairment annually. Goodwill is carried at cost less accumulated impairment losses.

$000's	June 2023	June 2022
Computer software		
Software - cost	46,714	43,482
Software under development	26,664	11,295
Accumulated amortisation	31,542	26,158
Net carrying value of computer software	**41,836**	**28,619**
Goodwill		
Cost	29,799	29,799
Net carrying value of goodwill	**29,799**	**29,799**
Total intangible assets	**71,635**	**58,418**

For the purposes of impairment testing, goodwill is allocated to cash generating units. A Cash Generating Unit (**CGU**) is the smallest identifiable group of assets that generate independent cash inflows. The Banking Group has assessed that goodwill should be allocated to Heartland Bank Limited as the smallest identifiable CGU.

17 Other balance sheet items (continued)

The recoverable amount of the business was determined on a value in use basis using a discounted cash flow methodology. The model uses a five-year cash flow forecast based on the latest budget approved by the board and extended out based on long term growth rates. The long-term growth rate applied to the future cash flows after year five of the forecast was 2.0% (2022: 2.0%) and a discount rate of 10.0% (2022: 10.0%) was applied which reflect both past experience and external sources of information. The goodwill impairment assessment indicates significant headroom, and that no foreseeable adjustments to key assumptions such as growth rate or discount rate would lead to impairment.

There was no indication of impairment and no impairment losses have been recognised against the carrying amount of goodwill for the year ended 30 June 2023 (2022: nil).

Policy
Employee benefits
Annual leave entitlements are accrued at amounts expected to be paid. Long service leave is accrued by calculating the probable future value of the entitlements and discounting back to present value. Obligations to defined contribution superannuation schemes are recognised as an expense when the contribution is paid.

$000's	**June 2023**	**June 2022**
Trade and other payables		
Trade payables	12,439	13,329
Insurance liability	915	1,840
Employee benefits	6,158	5,810
Other tax payables	3,829	1,132
Collateral received on derivatives[1]	27,609	32,341
Total trade and other payables	**50,950**	**54,452**

[1]The Banking Group has accepted collateral arising from derivative transactions, included in Cash and cash equivalents.

Policy
Leases
The Banking Group leases office space and car parks. Rental contracts are typically made for fixed periods but may have extension options. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions.

In determining the lease term, all facts and circumstances that create an economic incentive to exercise an extension option are considered. Extension options are only included in the lease term if the lease is reasonably certain to be extended.

Lease liabilities are measured at the present value of the remaining lease payments and discounted using the Banking Group's incremental borrowing rate (**IBR**). Carrying amounts are remeasured only upon reassessments and lease modifications.

Right of use assets are depreciated at the shorter of lease term or the Banking Group’s depreciation policy for that asset class.

$000's	**June 2023**	**June 2022**
Right of use assets		
Balance at beginning of year	13,660	15,654
Depreciation charge for the year, included within depreciation expense in the income statement	(2,150)	(2,122)
Additions to right of use assets	-	128
Total right of use assets	**11,510**	**13,660**
Lease liability		
Current	2,357	3,181
Non-current	11,121	12,545
Total lease liability	**13,478**	**15,726**
Interest expense relating to lease liability	**434**	**470**

18 Related party transactions and balances

Policy
A person or entity is a related party under the following circumstances:

a) A person or a close member of that person's family if that person:
   i) has control or joint control over the Bank;
   ii) has significant influence over the Bank; or
   iii) is a member of the key management personnel of the Bank.

b) An entity is related to the Bank if any of the following conditions applies:
   i) The entity and the Bank are members of the same group;
   ii) One entity is an associate or joint venture of the other entity;
   iii) Both entities are joint ventures of the same third party;
   iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity;
   v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the bank;
   vi) The entity is controlled, or jointly controlled by a person identified in (a); and
   vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(a) Transactions with key management personnel

Key management personnel (**KMP**), are those who, directly or indirectly, have authority and responsibility for planning, directing and controlling the activities of HGH and HBL. This includes all executive staff and Directors.

KMP receive personal banking and financial investment services from the Bank in the ordinary course of business. The terms and conditions, for example interest rates and collateral, and the risks to the Bank are comparable to transactions with other employees and do not involve more than the normal risk of repayment or present other unfavourable features.

All other transactions with KMPs and their related parties are conducted in the ordinary course of business on commercial terms and conditions.

$000's	June 2023	June 2022
Transactions with key management personnel		
Interest income	123	26
Interest expense	(43)	(24)
Key management personnel compensation		
Short-term employee benefits	(1,441)	(2,373)
Short-term employee benefits - HGH parent	(6,642)	(6,417)
Share-based plan benefit/(expense)	14	(1,915)
Total transactions with key management personnel	**(7,989)**	**(10,703)**
Due from/(to) key management personnel		
Lending	4,428	229
Borrowings - deposits	(855)	(508)
Total due from/(to) key management personnel	**3,573**	**(279)**

18 Related party transactions and balances (continued)

(b) Transactions with related parties

The Banking Group's ultimate parent company is HGH.

The Bank has regular transactions with its ultimate parent company, fellow subsidiaries and subsidiaries (collectively known as the Heartland Group) on agreed terms. The transactions include the provision of tax and administrative services and customer operations. Banking facilities are provided by HBL to other Banking Group entities on normal commercial terms as with other customers. There is no lending from the Banking Group to HGH.

Related party transactions between the Banking Group eliminate on consolidation. Related party transactions outside of the Banking Group are as follows:

$000's	June 2023	June 2022
Heartland Group Holdings Limited (HGH)		
Interest expense	122	68
Deposits/(withdrawals)	(4,754)	(31,500)
Dividends paid to HGH	60,000	35,500
Management fees paid to HGH	11,013	8,327
Management fees received from HGH	4,596	2,164

$000's	June 2023	June 2022
Australian Seniors Finance Pty Limited (ASF)		
Management fees paid to ASF	5	-
Management fees received from ASF	4,517	2,752
Heartland Trust (HT)		
Unclaimed monies paid to HT	20	-
Payment to HT for providing goods and services	10	-

(c) Due from/to related parties

$000's	June 2023	June 2022
Due from		
Australian Seniors Finance Pty Limited	-	1,540
Total due from related parties	**-**	**1,540**
Due to		
Heartland Group Holdings Limited	6,956	1,535
Australian Seniors Finance Pty Limited	217	-
Total due to related parties	**7,173**	**1,535**

(d) Other balances with related parties

$000's	June 2023	June 2022
Heartland Group Holdings Limited		
Retail deposits owing to HGH	4	4,636

19 Fair value

Policy
Fair value is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

On initial recognition, the transaction price generally represents the fair value of the financial instrument, unless there is observable information from an active market that provides a more appropriate fair value.

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Banking Group determines fair value using other valuation techniques.

The Banking Group measures fair values using the following fair value hierarchy, which reflects the observability of the inputs used in measuring fair value:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (derived from prices).

Level 3 - Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Banking Group recognises transfers between levels of the fair value hierarchy as at the end of the reporting period during which the change has occurred.

(a) Financial instruments measured at fair value

The following methods and assumptions were used to estimate the fair value of each class of financial asset and liability measured at fair value on a recurring basis in the consolidated statement of financial position.

The Banking Group has an established framework in performing valuations required for financial reporting purposes including Level 3 fair values. The Banking Group regularly reviews and calibrates significant unobservable inputs and valuation adjustments in accordance with market participants' views. If external valuation specialists are engaged to measure fair values, the Banking Group assesses the evidence obtained from these specialists to support the conclusion of these valuations. All significant valuations are reported to the Banking Group's Board Audit Committee for approval prior to its adoption in the financial statements.

Investments in debt securities

Investments in public sector securities and corporate bonds are stated at FVOCI with the fair value being based on quoted market prices (Level 1 under the fair value hierarchy) or modelled using observable market inputs (Level 2 under the fair value hierarchy). Refer to Note - 10 Investments for more details.

Investments valued under Level 2 of the fair value hierarchy are valued either based on quoted market prices or dealer quotes for similar instruments, or discounted cash flows analysis.

Investments in equity securities

Investments in equity securities are classified at FVTPL unless an irrevocable election is made by the Banking Group to measure at FVOCI. Investment in listed securities traded in liquid, active markets where prices are readily observable are measured under Level 1 of the fair value hierarchy with no modelling or assumptions used in the valuation. Investments in unlisted equity securities are measured under Level 3 of the fair value hierarchy with the fair value being based on unobservable inputs using market accepted valuation techniques. Where appropriate, the Banking Group may apply adjustments to the above-mentioned techniques to determine fair value of an equity security to reflect the underlying characteristics. These adjustments are reflective of market participant considerations in valuing the said security.

19 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

Finance receivables - reverse mortgages

The reverse mortgage portfolio is classified and measured at FVTPL under NZ IFRS 9 Financial instruments (**NZ IFRS 9**). NZ IFRS 4 Insurance contracts (**NZ IFRS 4**) requires entities to account for insurance components of lifetime mortgage contracts. The review of the reverse mortgage portfolio valuation determined that the terms and conditions of these loan contracts do not contain a component of significant insurance risk, therefore they continue to be treated under NZ IFRS 9 Financial Instruments classified at FVTPL under NZ IFRS. Application of NZ IFRS 17 going forward will have a policy choice to continue applying NZ IFRS 9 for these instruments.

On initial recognition the Banking Group considers the transaction price to represent the fair value of the loan, on the basis that no reliable fair value can be estimated as there is no relevant active market and fair value cannot be reliably measured using other valuation techniques under NZ IFRS 13 Fair value measurement.

For subsequent measurement, and at balance date, the Banking Group considered whether the fair value can be determined by reference to a relevant active market or using a valuation technique that incorporates observable inputs but has concluded relevant support is not currently available. In the absence of such market evidence the Banking Group has used an actuarial valuation to determine a proxy for the fair value that incorporates changes in the portfolio risk and expectations of the portfolio performance. The actuarial valuation includes inputs such as mortality and potential move into care, voluntary exits, house price changes, interest rate margin and the no equity guarantee. This estimate is highly subjective and a wide range of plausible values are possible. The estimate provides an indication of whether the transaction value is overstated.

The Banking Group does not consider that the actuarial estimate has moved outside of the original expectation range on initial recognition. There has been no fair value movement recognised in profit or loss during the period (2022: nil). Fair value is not sensitive to the above assumptions due to the nature of reverse mortgage loans. In particular, given conservative origination loan-to-value ratio and security criteria, a material deterioration in house prices combined with a material increase in interest rates over a sustained period of time would likely need to occur before any potential impact to fair value.

The Banking Group will continue to reassess the existence of a relevant active market and movements in expectations on an on-going basis.

Derivative financial instruments

Interest rate contracts are recognised in the financial statements at fair value. Fair values are determined from observable market prices as at the reporting date, discounted cash flow models or option pricing models as appropriate (Level 2 under the fair value hierarchy).

The following table analyses financial instruments measured at fair value at the reporting date by the level in the fair value hierarchy into which each fair value measurement is categorised. The amounts are based on the values recognised in the consolidated statement of financial position.

19 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

$000's	Level 1	Level 2	Level 3	Total
June 2023				
Assets				
Investments	315,192	-	1,819	317,011
Derivative financial instruments	-	36,982	-	36,982
Finance receivables - reverse mortgages	-	-	888,600	888,600
Total financial assets measured at fair value	**315,192**	**36,982**	**890,419**	**1,242,593**
Liabilities				
Derivative financial instruments	-	7,624	-	7,624
Total financial liabilities measured at fair value	**-**	**7,624**	**-**	**7,624**
June 2022				
Assets				
Investments	271,790	-	1,503	273,293
Derivative financial instruments	-	44,487	-	44,487
Finance receivables - reverse mortgages	-	-	721,264	721,264
Total financial assets measured at fair value	**271,790**	**44,487**	**722,767**	**1,039,044**
Liabilities				
Derivative financial instruments	-	6,335	-	6,335
Total financial liabilities measured at fair value	**-**	**6,335**	**-**	**6,335**

There were no transfers between levels in the fair value hierarchy in the year ended 30 June 2023 (2022: nil).

The movement in Level 3 assets measured at fair value are below:

$000's	Finance Receivables - Reverse Mortgage	Investments	Total
June 2023			
As at 30 June 2022	721,264	1,503	722,767
New loans	193,845	-	193,845
Repayments	(96,753)	-	(96,753)
Capitalised Interest and fees	70,168	-	70,168
Purchase of investments	-	316	316
Other	76	-	76
As at 30 June 2023	**888,600**	**1,819**	**890,419**
June 2022			
As at 30 June 2021	601,505	1,818	603,323
New loans	162,166	-	162,166
Repayments	(83,629)	-	(83,629)
Capitalised Interest and fees	41,864	-	41,864
Fair value (loss) on investment	-	(315)	(315)
Other	(642)	-	(642)
As at 30 June 2022	**721,264**	**1,503**	**722,767**

19 Fair value (continued)

(b) Financial instruments not measured at fair value

The following assets and liabilities of the Banking Group are not measured at fair value in the consolidated statement of financial position.

Cash and cash equivalents

Cash and cash equivalents are measured at amortised cost and their carrying value is considered equivalent to their fair value due to their short term nature.

Investments

Investments not measured at fair value include bank deposits and are measured using the effective interest rate method. They are held to support the Banking Group's contractual cash flows rather than selling prior to contractual maturity to realise changes in fair value.

Finance receivables

The fair value of the Banking Group's finance receivables is calculated using a valuation technique which assumes the Banking Group's current weighted average lending rates for loans of a similar nature and term.

The current weighted average lending rate used to fair value finance receivables with a fixed interest rate was 10.25% (2022: 7.77%). Finance receivables with a floating interest rate are deemed to be at current market rates. The current amount of credit provisioning has been deducted from the fair value calculation of finance receivables as a proxy for future losses.

Borrowings

The fair value of deposits, bank borrowings and other borrowings is the present value of future cash flows and is based on the current market interest rates payable by the Banking Group for debt of similar maturities. The average current market rate used to fair value other borrowings was 6.66% (2022: 3.57%).

Due to and from related parties

The fair value of amounts due to and from related parties is considered equivalent to their carrying value due to their short term nature.

19 Fair value (continued)

(b) Financial instruments not measured at fair value (continued)

Other financial assets and financial liabilities

The fair value of financial instruments such as short-term trade receivables and payables is considered equivalent to their carrying value due to their short-term nature.

The following table sets out financial instruments not measured at fair value where the carrying value does not approximate fair value, compares their carrying value against their fair value and analyses them by level in the fair value hierarchy.

$000's	June 2023 Fair Value Hierarchy	June 2023 Total Fair Value	June 2023 Total Carrying Value	June 2022 Fair Value Hierarchy	June 2022 Total Fair Value	June 2022 Total Carrying Value
Assets						
Investments	Level 2	-	-	Level 2	2,418	2,421
Finance receivables	Level 3	3,700,196	3,954,800	Level 3	3,701,694	3,762,231
Total financial assets		**3,700,196**	**3,954,800**		**3,704,112**	**3,764,652**
Liabilities						
Deposits	Level 2	4,130,330	4,131,029	Level 2	3,595,554	3,597,144
Other borrowings	Level 2	615,061	615,126	Level 2	749,478	749,478
Total financial liabilities		**4,745,391**	**4,746,155**		**4,345,032**	**4,346,622**

19 Fair value (continued)

(c) Classification of financial instruments

The following tables summarise the categories of financial instruments and the carrying value of all financial instruments of the Banking Group:

$000's	FVOCI Debt Securities	FVTPL	Amortised Cost	Total Carrying Value
June 2023				
Assets				
Cash and cash equivalents	-	-	216,044	216,044
Investments	315,192	1,819	-	317,011
Finance receivables	-	-	3,954,800	3,954,800
Finance receivables - reverse mortgages	-	888,600	-	888,600
Derivative financial instruments	-	36,982	-	36,982
Other financial assets	-	-	1,050	1,050
Total financial assets	**315,192**	**927,401**	**4,171,894**	**5,414,487**
Liabilities				
Deposits	-	-	4,131,029	4,131,029
Other borrowings	-	-	615,126	615,126
Derivative financial instruments	-	7,624	-	7,624
Due to related parties	-	-	7,173	7,173
Other financial liabilities	-	-	40,963	40,963
Total financial liabilities	**-**	**7,624**	**4,794,291**	**4,801,915**
June 2022				
Assets				
Cash and cash equivalents	-	-	221,469	221,469
Investments	271,790	1,503	2,421	275,714
Finance receivables	-	-	3,762,231	3,762,231
Finance receivables - reverse mortgages	-	721,264	-	721,264
Derivative financial instruments	-	44,487	-	44,487
Due from related parties	-	-	1,540	1,540
Other financial assets	-	-	175	175
Total financial assets	**271,790**	**767,254**	**3,987,836**	**5,026,880**
Liabilities				
Deposits	-	-	3,597,144	3,597,144
Other borrowings	-	-	749,478	749,478
Derivative financial instruments	-	6,335	-	6,335
Due to related parties	-	-	1,535	1,535
Other financial liabilities	-	-	47,510	47,510
Total financial liabilities	**-**	**6,335**	**4,395,667**	**4,402,002**

Risk Management

20 Enterprise risk management program

The board of directors (the **Board**) sets and monitors the Banking Group's risk appetite across the primary risk domains of credit, capital, liquidity, market (including interest rate), operational and compliance and general business risk. Management is, in turn, responsible for ensuring appropriate structures, policies, procedures and information systems are in place to actively manage these risk domains, as outlined within the Enterprise Risk Management Framework (**ERMF**). Collectively, these processes are known as the Bank's Enterprise Risk Management Program (**RMP**).

Role of the Board and the Board Risk Committee

The Board, through its Board Risk Committee (**BRC**) is responsible for oversight and governance of the development of the RMP. The role of the BRC is to assist the Board to formulate its risk appetite, and to monitor the effectiveness of the RMP. The BRC has the following specific responsibilities:

- The Board's Risk Appetite Statement.
- Heartland's Internal Capital Adequacy Assessment Program (**ICAAP**) including appropriate stress testing scenarios.
- The effectiveness of the ERMF and internal compliance and risk related policies, including approval or variation of policies, procedures and standards.
- Respond to changes anticipated in the economic, business and regulatory environment.
- Conduct, culture and customer outcomes, including emerging risks and any areas of concern.
- Credit exposures of the Bank, including the Delegated Lending Authority Policy and Framework.
- New products, including the process for approval of new products.

The BRC consists of three non-executive directors. Two members of the BRC sit on the Board Audit Committee (**BAC**). In addition, the HBL CEO, CRO, Head of Internal Audit and the CFO of Heartland Group Holdings Limited (or their nominee, subject to the Chair's prior approval) attend the BRC meetings, and the directors who are not members of the BRC are entitled to attend meetings and to receive copies of the BRC papers.

Board Audit Committee

The BAC focuses on financial reporting and application of accounting policies as part of the internal control and risk assessment framework. The BAC monitors the identification, evaluation and management of all significant risks through the Banking Group. This work is supported by Internal Audit, which provides an independent assessment of the design, adequacy and effectiveness of internal controls. The BAC receives regular reports from Internal Audit.

Charters for both the BRC and the BAC ensure suitable cross representation to allow effective communication pertaining to identified issues with oversight by the Board. The CRO has a direct reporting line to the Chair of the BRC. The Head of Internal Audit has a direct reporting line to the Chair of the BAC.

Internal Audit

The Banking Group has an Internal Audit function, the objective of which is to provide independent, objective assurance over the internal control environment. In certain circumstances, Internal Audit will provide risk and control advice to Management provided the work does not impede the independence of the Internal Audit function. The function assists The Banking Group in accomplishing its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Internal Audit is allowed full, free and unfettered access to any and all of the organisation's records, personnel and physical properties deemed necessary to accomplish its activities.

20 Enterprise risk management program (continued)

Internal Audit (continued)

A regular cycle of review has been implemented to cover all areas of the business, focused on assessment, management and control of risks identified. The audit plan takes into account cyclical review of various business units and operational areas, as well as identified areas of higher identified risk. The audit methodology is designed to meet the International Standards for the Professional Practice of Internal Auditing of The Institute of Internal Auditors.

Each audit has specific audit procedures tailored to the area of business that is being reviewed. The audit procedures are updated during each audit to reflect any process changes. Audit work papers are completed to evidence the testing performed in accordance with the audit procedures.

A schedule of all outstanding internal control issues is maintained and presented to the BAC to assist the BAC to track the resolution of previously identified issues. Any issues raised that are categorised as high risk are specifically reviewed by Internal Audit during a follow-up review once the issue is considered closed by management. The follow-up review is performed with a view to formally close out the issue.

Asset and Liability Committee (ALCO)

The ALCO is a group management committee comprising the CEO of HBL, CFO of HGH, CRO of HBL, Head of Retail and Financial Controller of HBL. The ALCO has responsibility for overseeing aspects of risk management of the Banking Group's financial position. The ALCO usually meets monthly, and provides reports to HBL Audit and Risk Committees. ALCO's specific responsibilities include decision making and oversight of risk matters in relation to:

- Market risk covering Foreign exchange risk and Interest rate risk (including non-traded interest rate risk and the investment of capital).
- Liquidity risk (including funding).
- Balance sheet structure.
- Capital management.

Executive Risk Committee (ERC)

The ERC comprises the CEO of HBL, CRO of HBL, CFO of HGH, Financial Controller of HBL and Head of Internal Audit. The ERC has responsibility for overseeing risk aspects including internal control environment to ensure that residual risk is consistent with the Banking Group’s risk appetite. The ERC generally meets monthly and minutes are made available to the BRC. ERC’s specific responsibilities include decision making and oversight of operational risk, compliance risk and credit risk.

Climate-related risks

Climate change risks are managed in accordance with the Banking Group’s RMP and supported by the environmental sustainability framework.

The Banking Group considers the impact of climate-related risks on its financial position and performance (and in this regard, the Board is currently in the process of establishing a new Board Committee to assist it in managing its climate related risks). While the effects of climate change represent a source of uncertainty, the Banking Group has concluded that climate-related risks do not have a material impact on the judgements, assumptions and estimates for the year ended 30 June 2023.

20 Enterprise risk management program (continued)

Operational and compliance risk

Operational and compliance risk is the risk arising from day to day operational activities in the execution of the Banking Group's strategy which may result in direct or indirect loss. Operational and compliance risk losses can occur as a result of fraud, human error, missing or inadequately designed processes, failed systems, damage to physical assets, improper behaviour or from external events. The losses range from direct financial losses, to reputational damage, unfavourable media attention, injury to or loss of staff or clients or as a breach of laws or banking regulations. Where appropriate, risks are mitigated by insurance.

To ensure appropriate responsibility is allocated for the management, reporting and escalation of operational and compliance risk, the Banking Group operates a “three lines of defence” model which outlines principles for the roles, responsibilities and accountabilities for operational and compliance risk management:

- The first line of defence is the business line management of the identification, management and mitigation of the risks associated with the products and processes of the business. This accountability includes regular testing and attestation of the adequacy and effectiveness of controls and compliance with the Banking Group's policies.

- The second line of defence is the Risk and Compliance function, responsible for the design and ownership of the Operational Risk Management Framework. It incorporates key processes including Risk and Control Self-Assessment (**RCSA**), incident management, independent evaluation of the adequacy and effectiveness of the internal control framework and the attestation process.

- The third line of defence is Internal Audit which is responsible for independently assessing how effectively the Banking Group is managing its risk according to its stated risk appetite.

The Banking Group’s exposure to operational and compliance risk is governed by a risk appetite statement approved by the Board and is used to guide management activities. This statement sets out the nature of risk which may be taken and aggregate risk limits, which are monitored by the ERC.

Market risk

Market risk is the possibility of experiencing losses or gains due to factors affecting the overall performance of financial markets in which the Banking Group is exposed. The primary market risk exposures for the Banking Group are interest rate risk and foreign exchange risk. The risk being that market interest rates or foreign exchange rates will change and adversely impact on the Banking Group’s earnings due to either adverse moves in foreign exchange market rates or in the case of interest rate risks mismatches between repricing dates of interest bearing assets and liabilities and/or differences between customer pricing and wholesale rates.

20 Enterprise risk management program (continued)

Interest rate risk

Interest rate risk refers to exposure of an entity's earnings and / or capital because of a mismatch between the interest rate exposures of its assets and liabilities. Interest rate risk for the Banking Group arises from the provision of non-traded retail banking products and services and from traded wholesale transactions entered into to reduce aggregate interest rate risk (known as hedges). This risk arises from four key sources:

- Mismatches between the repricing dates of interest bearing assets and liabilities (yield curve and repricing risk);
- Banking products repricing differently to changes in wholesale market rates (basis risk);
- Loan prepayment or deposit early withdrawal behaviour from customers that deviates from the expected or contractually agreed behaviour (optionality risk); and
- The effect of internal or market forces on a bank's net interest margin where, for example, in a low rate environment any fall in rates will further decrease interest income earned on the assets whereas funding cost cannot be reduced as it is already at the minimum level (margin compression risk).

Refer to Note 24 - Interest rate risk for further details regarding interest rate risk.

Counterparty Credit Risk

The Banking Group has on-going credit exposure associated with:

- Cash and cash equivalents;
- Finance receivables;
- Holding of investment securities; and
- Payments owed to the Banking Group from risk management instruments.

Counterparty credit risk is managed against limits set in the Market Risk Policy including credit exposure on derivative contracts, bilateral set-off arrangements, cash and cash equivalents and investment securities.

21 Credit risk exposure

Credit risk is the risk that a borrower will default on any type of debt by failing to make payments which it is obligated to make. The risk is primarily that of the lender and includes loss of principal and interest, disruption to cash flows and increased collection costs.

Credit risk is managed to achieve sustainable risk-reward performance whilst maintaining exposures within acceptable risk “appetite” parameters. This is achieved through the combination of governance, policies, systems and controls, underpinned by commercial judgement as described below.

To manage this risk the ERC oversees the formal credit risk management strategy. The ERC reviews the Banking Group's credit risk exposures typically on a monthly basis. The credit risk management strategies aim to ensure that:

- Credit origination meets agreed levels of credit quality at point of approval;
- Sector concentrations are monitored;
- Maximum total exposure to any one debtor is actively managed;
- Changes to credit risk are actively monitored with regular credit reviews.

The BRC also oversees the Banking Group's credit risk exposures to monitor overall risk metrics having regard to risk appetite set by the Board.

The BRC has authority from the Board for approval of all credit exposures. Lending authority has been provided by the BRC to the Banking Group's Credit Committee, and to the business units under a detailed Delegated Lending Authority framework. Application of credit discretions in the business operation are monitored through a defined review and hindsight structure as outlined in the Credit Risk Oversight Policy. Delegated Lending Authorities are provided to individual officers with due cognisance of their experience and ability. Larger and higher risk exposures require approval of senior management, the Credit Committee and ultimately through to the BRC.

The Banking Group employs a credit risk oversight process of hindsighting loans to ensure that credit policies and the quality of credit processes are maintained.

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21 Credit risk exposure (continued)

Reverse mortgage loans and negative equity risk

Reverse mortgage loans are a form of mortgage lending designed for the needs of people over 60 years of age. These loans differ to conventional mortgages in that they typically are not repaid until the borrower ceases to reside in the property. Further, interest is not required to be paid, it is capitalised into the loan balance and is repayable on termination of the loan. As such, there are no incoming cash flows and therefore no default risk to manage during the term of the loan. Negative equity risk arises from the promise by the Banking Group that the maximum repayment amount is limited to the net sale proceeds of the borrowers' property.

The Banking Group's exposure to negative equity risk is managed via lending standards specific for this product. In addition to usual criteria regarding the type, and location, of security property that the Banking Group will accept for reverse mortgage lending, a key aspect of the Banking Group's policy is that a borrower's age on origination of the reverse mortgage loan will dictate the loan-to-value ratio of the reverse mortgage on origination.

Business Finance Guarantee Scheme (BFGS)

In April 2020, the Bank along with other registered banks in New Zealand, entered into a Deed of Indemnity with the New Zealand Government to implement the New Zealand Government's Business Finance Guarantee Scheme (the **Scheme**). The purpose of the Scheme was to provide short term credit to eligible small and medium size businesses, who had been impacted by the economic effects of COVID-19. The Scheme allowed banks to lend to a maximum of $5 million for a five-year term. The New Zealand Government guaranteed 80% of any loss incurred (credit risk) with the Bank holding the remaining 20%. The Scheme concluded on 30 June 2021. As at 30 June 2023 the Bank had a total exposure of $54.8 million (2022: $64.8 million) to its customers under this Scheme.

Maximum exposure to credit risk at the relevant reporting dates

The following table represents the maximum credit risk exposure, without taking account of any collateral held. The on balance sheet exposures set out below are based on net carrying amounts as reported in the consolidated statement of financial position.

$000's	June 2023	June 2022
On balance sheet:		
Cash and cash equivalents	216,044	221,469
Investments	315,192	274,211
Finance receivables	3,954,800	3,762,231
Finance receivables - reverse mortgages	888,600	721,264
Derivative financial assets	36,982	44,487
Due from related parties	-	1,540
Other financial assets	1,050	175
Total on balance sheet credit exposures	**5,412,668**	**5,025,377**
Off balance sheet:		
Letters of credit, guarantee commitments and performance bonds	7,378	8,969
Undrawn facilities available to customers	310,423	272,735
Conditional commitments to fund at future dates	24,873	34,791
Total off balance sheet credit exposures	**342,674**	**316,495**
Total credit exposures	**5,755,342**	**5,341,872**

21 Credit risk exposure (continued)

Concentration of credit risk by geographic region

$000's	June 2023	June 2022
New Zealand	5,538,346	5,176,026
Australia	1,137	3,520
Rest of the world [1]	268,004	212,753
	5,807,487	**5,392,299**
Provision for impairment	(52,145)	(50,427)
Total credit exposures	**5,755,342**	**5,341,872**

[1] These overseas assets are primarily NZD-denominated investments in AA+ (Standard & Poor's) and high quality investment grade securities issued by offshore supranational agencies ("Kauri Bonds").

Concentration of credit risk by industry sector

The Australian and New Zealand Standard Industrial Classification (**ANZSIC**) codes have been used as the basis for categorising customer and investee industry sectors.

$000's	June 2023	June 2022
Agriculture	781,065	747,618
Forestry and fishing	130,055	148,797
Mining	8,266	12,524
Manufacturing	80,729	78,432
Finance and insurance	722,404	685,938
Wholesale trade	46,053	41,986
Retail trade and accommodation	402,146	423,975
Households	2,432,860	2,134,097
Other business services	198,377	189,860
Construction	336,333	291,971
Rental, hiring and real estate services	205,079	199,388
Transport and storage	359,865	323,732
Other	104,255	113,981
	5,807,487	**5,392,299**
Provision for impairment	(52,145)	(50,427)
Total credit exposures	**5,755,342**	**5,341,872**

Credit exposures to connected persons

The Banking Group's methodology for calculating credit exposure concentrations is on the basis of actual credit exposures and calculated on a gross basis (net of individual credit impairment allowances and excluding advances of a capital nature) in accordance with the Bank's conditions of registration and the Reserve Bank's Connected Exposures Policy (**BS8**). Peak end-of-day credit exposures to non-bank connected persons are calculated using the Banking Group's Tier 1 capital at the end of the reporting period.

21 Credit risk exposure (continued)

Credit exposures to connected persons (continued)

In accordance with its conditions of registration, the Banking Group's aggregate credit exposures to all connected persons must not exceed its rating contingent limit of 15% of tier one capital. Within the overall rating contingent limit, there is a sub-limit of 15% of tier one capital which applies to the aggregate credit exposures to non-bank connected persons. There have been no rating-contingent limit changes during the accounting period.

	As at June 2023	Peak End-of-Day for Year Ended June 2023
Credit exposures to connected persons ($000's)	-	2,660
As a percentage of Tier 1 capital of the Banking Group at end of the year (%)	0.00%	0.44%
Credit exposures to non-bank connected persons ($000's)	-	2,660
As a percentage of Tier 1 capital of the Banking Group at end of the year (%)	0.00%	0.44%

As at 30 June 2023, the Banking Group had no aggregate contingent exposures to connected persons arising from risk lay-off arrangements in respect of credit exposures to counterparties (excluding counterparties that are connected persons). The aggregate amount of the Banking Group's individual credit provisions provided against credit exposure to connected persons was nil at 30 June 2023.

Credit exposure to individual counterparties

The Banking Group's aggregate concentration of credit exposure to individual counterparties is calculated based on the actual credit exposure. Credit exposures to connected persons, the central government or central bank of any country with a long term credit rating of A- or A3 or above, or its equivalent, and any supranational or quasi-sovereign agency with a long-term credit rating of A- or A3 or above, or its equivalent are excluded.

The peak end-of-day aggregate concentration of credit exposure to individual counterparties has been calculated by determining the maximum end-of-day aggregate amount of credit exposure over the relevant six-month period and then dividing the amount by the Banking Group's common equity tier one capital as 30 June 2023.

	Number of Exposures As at June 2023	Number of Exposures Peak End-of-Day over 6 Months to June 2023
Exposures to banks		
With a long-term credit rating of A- or A3 or above, or its equivalent:		
10% to less than 15% of CET1 capital	-	-
15% to less than 20% of CET1 capital	1	2
20% to less than 25% of CET1 capital	1	1
25% to less than 30% of CET1 capital	-	-
With a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent	-	-
Exposures to non-banks		
Total number of exposures to non-banks that are greater than 10% to less than 15% of CET1 capital that do not have a long-term credit rating.	1	1

21 Credit risk exposure (continued)

Collateral held

The Banking Group employs a range of policies and practices to mitigate credit risk and has internal policies on the acceptability of specific classes of collateral. Collateral is held as security to support credit risk on finance receivables and enforced in satisfying the debt in the event contractual repayment obligations are not met. The collateral held for mitigating credit risk for the Banking Group's lending portfolios is outlined below.

Reverse mortgage and Residential mortgage loans
Reverse mortgage loans are secured by a first mortgage over a residential property which is typically a customer's primary residential dwelling, residential investment property or holiday home. Residential mortgage loans are secured by a residential mortgage over an owner-occupied property located in an approved urban area.

Corporate lending
Business lending including rural lending is typically secured by way of a charge over property and/or specific security agreement over relevant business assets, and, where considered appropriate, a general security agreement to provide the ability to control cash flows.

Other lending
Other lending comprises personal loans, primarily motor loans, which are secured by a motor vehicle or a boat; and other shorter term smaller personal loans which are predominantly unsecured**.**

The Banking Group analyses the coverage of the loan portfolio which is secured by the collateral it holds.

Coverage is measured by the value of security as a proportion of loan balance outstanding and classified as follows:

Fully secured	Greater or equal to 100%
Partially secured	1% - 99.9%
Unsecured	No security held

The Banking Group's loan portfolio have the following coverage from collateral held:

	Corporate	Residential	All Other
June 2023			
Fully Secured	91%	100%	73%
Partially Secured	4%	-	12%
Unsecured	5%	-	15%
Total	**100%**	**100%**	**100%**
June 2022			
Fully Secured	92%	100%	71%
Partially Secured	6%	-	14%
Unsecured	2%	-	15%
Total	**100%**	**100%**	**100%**

22 Asset quality

The disclosures in this note are categorised by the following credit risk concentrations:

Corporate Business lending including rural lending.

Residential Lending secured by a first ranking mortgage over a residential property used primarily for residential purposes either by the mortgagor or a tenant of the mortgagor.

All Other This relates primarily to consumer lending to individuals.

Information is not presented in respect of other financial assets or credit related contingent liabilities as the related allowances for ECL are not material to the Banking Group.

(a) Past due but not individually impaired

$000's	Corporate	Residential	All Other	Total
June 2023				
Less than 30 days past due	4,515	151	4,685	9,351
At least 30 but less than 60 days past due	31,739	-	12,358	44,097
At least 60 but less than 90 days past due	6,514	300	4,543	11,357
At least 90 days past due	35,775	401	36,162	72,338
Total past due but not individually impaired	**78,543**	**852**	**57,748**	**137,143**
June 2022				
Less than 30 days past due	4,147	171	3,249	7,567
At least 30 but less than 60 days past due	15,320	263	10,751	26,334
At least 60 but less than 90 days past due	4,621	85	5,071	9,777
At least 90 days past due	15,276	131	25,872	41,279
Total past due but not individually impaired	**39,364**	**650**	**44,943**	**84,957**

(b) Credit risk grading

The Banking Group's finance receivables are monitored either by account behaviour (**Behavioural portfolio**) or a regular assessment of their credit risk grade based on an objective review of defined risk characteristics (**Judgemental portfolio**).

Finance receivables - reverse mortgages have no arrears characteristics and are assessed on origination against a pre-determined criteria.

The Judgemental portfolio consists mainly of business and rural lending where an on-going and detailed working relationship with the customer has been developed while the Behavioural portfolio consists of consumer, retail and smaller business receivables.

Judgemental loans are individually risk graded based on loan status, financial information, security and debt servicing ability. Exposures in the Judgemental portfolio are credit risk graded by an internal risk grading mechanism where grade 1 is the strongest risk. Grade 8 and grade 9 are the weakest risk grades where a loss is probable. Behavioural loans are managed based on their arrears status.

22 Asset quality (continued)

(b) Credit risk grading (continued)

All loans past due but not impaired have been categorised into three impairments stages (refer to Note 22 – Asset quality (c)) which are in most cases based on arrears status. If a Judgemental loan is risk graded 6 or above it will be classified as stage 2 as a minimum and carry a provision based on lifetime expected credit losses.

	Collectively Assessed			Individually	
$000's	**Stage 1**	**Stage 2**	**Stage 3**	**Assessed**	**Total**
June 2023					
Judgemental portfolio					
Grade 1 - Very Strong	25	-	-	-	25
Grade 2 - Strong	3,658	-	-	-	3,658
Grade 3 - Sound	41,887	477	-	-	42,364
Grade 4 - Adequate	637,993	9,975	3,477	-	651,445
Grade 5 - Acceptable	1,016,113	5,492	602	-	1,022,207
Grade 6 - Monitor	-	64,946	6,763	-	71,709
Grade 7 - Substandard	-	76,955	13,725	-	90,680
Grade 8 - Doubtful	-	-	-	51,284	51,284
Grade 9 - At risk of loss	-	-	-	1,671	1,671
Total Judgemental portfolio	1,699,676	157,845	24,567	52,955	1,935,043
Total Behavioural portfolio	1,990,888	24,335	56,679	-	2,071,902
Gross finance receivables	**3,690,564**	**182,180**	**81,246**	**52,955**	**4,006,945**
Provision for impairment	(12,250)	(2,444)	(21,320)	(16,131)	(52,145)
Total finance receivables	**3,678,314**	**179,736**	**59,926**	**36,824**	**3,954,800**
Undrawn facilities available to customers	57,471	77,150	123,248	-	257,869
June 2022					
Judgemental portfolio					
Grade 1 - Very Strong	26	-	-	-	26
Grade 2 - Strong	10,859	-	-	-	10,859
Grade 3 - Sound	53,756	-	-	-	53,756
Grade 4 - Adequate	697,590	5,382	1,052	-	704,024
Grade 5 - Acceptable	994,079	1,823	53	-	995,955
Grade 6 - Monitor	-	25,106	2,308	-	27,414
Grade 7 - Substandard	-	64,203	4,727	-	68,930
Grade 8 - Doubtful	-	-	-	62,672	62,672
Grade 9 - At risk of loss	-	-	-	3,511	3,511
Total Judgemental portfolio	1,756,310	96,514	8,140	66,183	1,927,147
Total Behavioural portfolio	1,827,025	21,001	37,485	-	1,885,511
Gross finance receivables	**3,583,335**	**117,515**	**45,625**	**66,183**	**3,812,658**
Provision for impairment	(19,201)	(1,863)	(14,362)	(15,001)	(50,427)
Total finance receivables	**3,564,134**	**115,652**	**31,263**	**51,182**	**3,762,231**
Undrawn facilities available to customers	52,949	73,175	110,495	-	236,619

22 Asset quality (continued)

(c) Provision for impairment

Policy

Impairment of finance receivables

At each reporting date, the Banking Group applies a three stage approach to measuring ECL to finance receivables not carried at fair value. The ECL model assesses whether there has been a significant increase in credit risk since initial recognition.

Exposures are assessed on a collective basis in each stage unless there is sufficient evidence that one or more events associated with an exposure could have a detrimental impact on estimated future cash flows. Where such evidence exists, the exposure is assessed on an individual basis.

For the purposes of a collective evaluation of impairment, finance receivables are grouped based on shared credit risk characteristics, credit risk ratings, contractual term, date of initial recognition, remaining term to maturity, customer type and other relevant factors.

The ECL model is a forward-looking model where impairment allowances are recognised before losses are actually incurred. On initial recognition, an impairment allowance is required, based on events that are possible in the next 12 months.

Assets may migrate between the following stages based on their change in credit quality:

Stage 1 - 12 months ECL (past due 30 days or less)

Where there has been no evidence of increased credit risk since initial recognition, and finance receivables are not credit impaired upon origination, the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months is recognised.

Stage 2 - Lifetime ECL not credit impaired (greater than 30 but less than 90 days past due)

Where there has been a significant increase in credit risk.

Stage 3 - Lifetime ECL credit impaired (90 days past due or more)

Objective evidence of impairment, are considered to be in default or otherwise credit impaired.

Credit quality of financial assets

The Banking Group internally computes probability of default using historical default data, to assess the potential risk of default of the lending, or other financial services products, provided to counterparties or customers. The Banking Group has defined counterparty probabilities of default across consumer, retail, business and rural portfolios.

The Banking Group considers a receivable to be in default when contractual payments are 90 days or more past due, or when it is considered unlikely that the credit obligation to the Banking Group will be paid in full without recourse to actions, such as realisation of security.

Finance receivables are written off against the related impairment allowance when there is no reasonable expectation of recovery. Any recoveries of amounts previously written off are credited to credit impairment expense in profit or loss.

In determining whether credit risk has increased all available information relevant to the assessment of economic conditions at the reporting date are taken into consideration. To do this the Banking Group considers its historical loss experience and adjusts this for current observable data. In addition to this the Banking Group uses reasonable and supportable forecasts of future economic conditions including experienced judgement to estimate the amount of an expected impairment loss. Future economic conditions consider macroeconomic factors such as unemployment, interest rate, gross domestic product, and inflation, and requires an evaluation of both the current and forecast direction of the economic cycle. The methodology and assumptions including any forecasts of future economic conditions are reviewed regularly as incorporating forward-looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the ECL.

The calculation of expected credit loss is modelled for portfolios of like assets. For portfolios which are either new or too small to model, judgement is used to determine impairment provisions.

22 Asset quality (continued)

Policy (continued)
Credit quality of financial assets (continued)
For assets that are individually assessed for ECL, the allowance for ECL is calculated directly as the difference between the defaulted assets carrying value and the recoverable amount (being the present value of expected future cash flows, including cash flows from the realisation of collateral or guarantees, where applicable).

Modification of contractual cash flows
The Banking Group sometimes modifies the terms of loans provided to customers due to commercial re-negotiations, or for distressed loans, with a view to maximising recovery.

Such restructuring activities include extended payment term arrangements, payment holidays and payment forgiveness. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue.

These policies are kept under continuous review. Restructuring is most commonly applied to term loans.

The Banking Group's models for estimating ECL for each of its portfolios are based on the historic credit experience of those portfolios. The models assume that economic conditions remain static over time. If the Banking Group forecasts that economic conditions may change in the foreseeable future, the Banking Group applies judgement to determine whether the modelled output should be subject to an economic overlay. Judgement is required to establish clear correlation between key economic indicators and the credit performance of the Banking Group's unique portfolios.

The most significant and judgemental provision for impairment is on motor vehicle lending with a collective ECL of $15.1 million at 30 June 2023 (2022: $9.5 million). There are fewer judgements on the other remaining lending portfolios.

The motor vehicle lending impairment allowance is sensitive to changes in the level of unemployment. The modelled provision for motor vehicle lending is a probability weighted estimate based on three scenarios. The forecast of unemployment across all three scenarios uses consensus external data obtained from external economic experts.

The forecast assumes the following for unemployment for all three scenarios:

	2024	2025	2026
Upside	4.00%	4.80%	4.40%
Central	4.60%	5.20%	5.00%
Downside	5.96%	6.13%	5.70%

The probability weights assigned to each scenario are based on management's estimate of their relative likelihood. The following table indicates the weightings applied by the Banking Group as at 30 June 2023:

Upside	15%
Central	50%
Downside	35%

The following sensitivity table shows the provision for impairment based on the probability weighted scenarios and what the impairment allowance for motor vehicle lending would be assuming a 100% weighting is applied to the three scenarios with all other assumptions held constant.

Reported probability weighted impairment allowance	$15.1 million
100% Upside	$9.7 million
100% Central	$12.4 million
100% Downside	$21.2 million

22 Asset quality (continued)

(c) Provision for impairment (continued)

$000's	Collectively Assessed Stage 1	Stage 2	Stage 3	Individually Assessed	Total
June 2023					
Corporate					
Impairment allowance as at 30 June 2022	**19,353**	**901**	**4,941**	**15,001**	**40,196**
Changes in loss allowance					
Transfer between stages[1]	(7,738)	(1,940)	1,346	8,332	-
New and increased provision (net of provision releases)[1]	(526)	2,376	4,653	4,701	11,204
Credit impairment charge	**(8,264)**	**436**	**5,999**	**13,033**	**11,204**
Write-offs	-	-	(2,410)	(11,903)	(14,313)
Impairment allowance as at 30 June 2023	**11,089**	**1,337**	**8,530**	**16,131**	**37,087**
Residential					
Impairment allowance as at 30 June 2022	**115**	**-**	**-**	**-**	**115**
Changes in loss allowance					
Transfer between stages[1]	-	-	-	-	-
New and increased provision (net of provision releases)[1]	12	-	-	-	12
Credit impairment charge	**12**	**-**	**-**	**-**	**12**
Write-offs	-	-	-	-	-
Impairment allowance as at 30 June 2023	**127**	**-**	**-**	**-**	**127**
All Other					
Impairment allowance as at 30 June 2022	**(267)**	**966**	**9,417**	**-**	**10,116**
Changes in loss allowance					
Transfer between stages[1]	(459)	(1,883)	2,342	-	-
New and increased provision (net of provision releases)[1]	1,760	2,028	9,786	-	13,574
Credit impairment charge	**1,301**	**145**	**12,128**	**-**	**13,574**
Write-offs	-	-	(8,759)	-	(8,759)
Impairment allowance as at 30 June 2023	**1,034**	**1,111**	**12,786**	**-**	**14,931**
Total					
Impairment allowance as at 30 June 2022	**19,201**	**1,863**	**14,362**	**15,001**	**50,427**
Changes in loss allowance					
Transfer between stages[1]	(8,197)	(3,823)	3,688	8,332	-
New and increased provision (net of provision releases)[1]	1,246	4,404	14,439	4,701	24,790
Credit impairment charge	**(6,951)**	**581**	**18,127**	**13,033**	**24,790**
Write-offs	-	-	(11,169)	(11,903)	(23,072)
Impairment allowance as at 30 June 2023	**12,250**	**2,444**	**21,320**	**16,131**	**52,145**

[1] The increase in provision when a loan moves to a higher stage is included in New and increased provision (net of provision releases) in the higher stage to which the loan moved. The decrease in provision when a loan moves to a lower stage is included in New and increased provision (net of provision releases) in the higher stage from which the loan moved.

22 Asset quality (continued)

(c) Provision for impairment (continued)

$000's	Collectively Assessed Stage 1	Collectively Assessed Stage 2	Stage 3	Individually Assessed	Total
June 2022					
Corporate					
Impairment allowance as at 30 June 2021	**16,586**	**1,218**	**4,844**	**7,629**	**30,277**
Changes in loss allowance					
Transfer between stages[1]	(3,614)	(1,060)	(601)	5,275	-
New and increased provision (net of provision releases)[1]	6,381	739	4,164	5,507	16,791
Credit impairment charge	**2,767**	**(321)**	**3,563**	**10,782**	**16,791**
Write-offs	-	-	(3,462)	(3,410)	(6,872)
Impairment allowance as at 30 June 2022	**19,353**	**897**	**4,945**	**15,001**	**40,196**
Residential					
Impairment allowance as at 30 June 2021	**88**	**-**	**-**	**-**	**88**
Changes in loss allowance					
Transfer between stages	-	-	-	-	-
New and increased provision (net of provision releases)[1]	27	-	-	-	27
Credit impairment charge	**27**	**-**	**-**	**-**	**27**
Write-offs	-	-	-	-	-
Impairment allowance as at 30 June 2022	**115**	**-**	**-**	**-**	**115**
All Other					
Impairment allowance as at 30 June 2021	**7,758**	**1,138**	**11,787**	**-**	**20,683**
Changes in loss allowance					
Transfer between stages[1]	(192)	(1,440)	1,632	-	-
New and increased provision (net of provision releases)[1]	(7,833)	1,268	7,194	-	629
Credit impairment charge	**(8,025)**	**(172)**	**8,826**	**-**	**629**
Write-offs	-	-	(11,196)	-	(11,196)
Impairment allowance as at 30 June 2022	**(267)**	**966**	**9,417**	**-**	**10,116**
Total					
Impairment allowance as at 30 June 2021	**24,432**	**2,356**	**16,631**	**7,629**	**51,048**
Changes in loss allowance					
Transfer between stages[1]	(3,806)	(2,500)	1,031	5,275	-
New and increased provision (net of provision releases)[1]	(1,425)	2,007	11,358	5,507	17,447
Credit impairment charge	**(5,231)**	**(493)**	**12,389**	**10,782**	**17,447**
Write-offs	-	-	(14,658)	(3,410)	(18,068)
Impairment allowance as at 30 June 2022	**19,201**	**1,863**	**14,362**	**15,001**	**50,427**

[1] The increase in provision when a loan moves to a higher stage is included in New and increased provision (net of provision releases) in the higher stage to which the loan moved. The decrease in provision when a loan moves to a lower stage is included in New and increased provision (net of provision releases) in the higher stage from which the loan moved.

22 Asset quality (continued)

(d) Impact of changes in gross finance receivables held at amortised cost on allowance for ECL

	Collectively Assessed			Individually	
$000's	**Stage 1**	**Stage 2**	**Stage 3**	**Assessed**	**Total**
June 2023					
Corporate					
Gross finance receivables as at 30 June 2022	**2,289,350**	**99,514**	**21,306**	**66,183**	**2,476,353**
Transfer between stages	(180,762)	139,860	29,179	11,723	-
Additions	711,378	-	-	9,326	720,704
Deletions	(509,932)	(80,418)	(2,685)	(15,194)	(608,229)
Write-offs	-	-	(3,091)	(19,083)	(22,174)
Gross finance receivables as at 30 June 2023	**2,310,034**	**158,956**	**44,709**	**52,955**	**2,566,654**
Residential					
Gross finance receivables as at 30 June 2022	**285,844**	-	-	-	**285,844**
Transfer between stages	-	-	-	-	-
Additions	42,721	-	-	-	42,721
Deletions	(6,079)	-	-	-	(6,079)
Write-offs	-	-	-	-	-
Gross finance receivables as at 30 June 2023	**322,486**	**-**	**-**	**-**	**322,486**
All Other					
Gross finance receivables as at 30 June 2022	**1,008,141**	**18,001**	**24,319**	**-**	**1,050,461**
Transfer between stages	(56,358)	21,943	34,415	-	-
Additions	642,266	-	-	-	642,266
Deletions	(536,005)	(16,720)	(14,046)	-	(566,771)
Write-offs	-	-	(8,151)	-	(8,151)
Gross finance receivables as at 30 June 2023	**1,058,044**	**23,224**	**36,537**	**-**	**1,117,805**
Total					
Gross finance receivables as at 30 June 2022	**3,583,335**	**117,515**	**45,625**	**66,183**	**3,812,658**
Transfer between stages	(237,120)	161,803	63,594	11,723	-
Additions	1,396,365	-	-	9,326	1,405,691
Deletions	(1,052,016)	(97,138)	(16,731)	(15,194)	(1,181,079)
Write-offs	-	-	(11,242)	(19,083)	(30,325)
Gross finance receivables as at 30 June 2023	**3,690,564**	**182,180**	**81,246**	**52,955**	**4,006,945**

22 Asset quality (continued)

(d) Impact of changes in gross finance receivables held at amortised cost on allowance for ECL (continued)

	Collectively Assessed			Individually	
$000's	**Stage 1**	**Stage 2**	**Stage 3**	**Assessed**	**Total**
June 2022					
Corporate					
Gross finance receivables as at 30 June 2021	**1,897,900**	**158,218**	**27,565**	**38,143**	**2,121,826**
Transfer between stages	(72,300)	13,380	3,526	55,394	-
Additions	1,326,598	-	-	3,002	1,329,600
Deletions	(862,848)	(72,084)	(7,191)	(26,946)	(969,069)
Write-offs	-	-	(2,594)	(3,410)	(6,004)
Gross finance receivables as at 30 June 2022	**2,289,350**	**99,514**	**21,306**	**66,183**	**2,476,353**
Residential					
Gross finance receivables as at 30 June 2021	**62,534**	**-**	**-**	**-**	**62,534**
Transfer between stages	-	-	-	-	-
Additions	242,672	-	-	-	242,672
Deletions	(19,362)	-	-	-	(19,362)
Write-offs	-	-	-	-	-
Gross finance receivables as at 30 June 2022	**285,844**	**-**	**-**	**-**	**285,844**
All Other					
Gross finance receivables as at 30 June 2021	**1,056,137**	**6,510**	**17,634**	**-**	**1,080,281**
Transfer between stages	(36,751)	11,491	25,260	-	-
Additions	489,911	-	-	-	489,911
Deletions	(501,156)	-	(6,150)	-	(507,306)
Write-offs	-	-	(12,425)	-	(12,425)
Gross finance receivables as at 30 June 2022	**1,008,141**	**18,001**	**24,319**	**-**	**1,050,461**
Total					
Gross finance receivables as at 30 June 2021	**3,016,571**	**164,728**	**45,199**	**38,143**	**3,264,641**
Transfer between stages	(109,051)	24,871	28,786	55,394	-
Additions	2,059,181	-	-	3,002	2,062,183
Deletions	(1,383,366)	(72,084)	(13,341)	(26,946)	(1,495,737)
Write-offs	-	-	(15,019)	(3,410)	(18,429)
Gross finance receivables as at 30 June 2022	**3,583,335**	**117,515**	**45,625**	**66,183**	**3,812,658**

Impact of changes in gross exposures on loss allowances - Corporate exposures
Overall credit impairment provisions for corporate exposures decreased by $3.1 million (7.7%) for the year ended 30 June 2023, mainly due to increase in the corporate exposure portfolio of $90.3 million (3.6%) which was partially offset by the release of provisions previously held against assets written off during the year.

Impact of changes in gross exposures on loss allowances – All other exposures
Overall credit impairment provisions for All other exposures increased by $4.8 million (47.6%) for the year ended 30 June 2023, mainly due to increase in the All other portfolio of $67.4 million (6.4%) and movement of exposures into more advanced stages. This is offset by reduction in loss given default from more effective arrears management.

(e) Other asset quality information

As at 30 June 2023 there were nil undrawn lending commitments available to counterparties for whom drawn balances are classified as individually impaired (2022: $0.003 million). As at 30 June 2023, the Banking Group had $0.349 million assets under administration (2022: $1.015 million).

As at 30 June 2023, the contractual amount outstanding on loans to customers written off during the year and are still subject to enforcement activity was nil (2022:nil).

23 Liquidity risk

Liquidity risk is the risk that the Banking Group is unable to meet its payment obligations as they fall due. The timing mismatch of cash flows and the related liquidity risk in all banking operations is closely monitored by the Banking Group.

Measurement of liquidity risk is designed to ensure that the Banking Group has the ability to generate or obtain sufficient cash in a timely manner and at a reasonable price to meet its financial commitments on a daily basis.

The Banking Group's exposure to liquidity risk is governed by a policy approved by the Board and managed by the ALCO. This policy sets out the nature of the risk which may be taken and aggregate risk limits, and the ALCO must observe. Within this, the objective of the ALCO is to derive the most appropriate strategy for the Banking Group in terms of a mix of assets and liabilities given its expectations of future cash flows, liquidity constraints and capital adequacy. The ALCO employs asset and liability cash flow modelling to determine appropriate liquidity and funding strategies.

Reserve Bank of New Zealand facilities

In March 2020, the Bank was onboarded by the RBNZ as an approved counterparty and executed a 2011 Global Master Repo Agreement providing an additional source for intra-day liquidity for the Banking Group if required.

The Banking Group holds the following liquid assets and committed funding sources for the purpose of managing liquidity risk:

$000's	June 2023	June 2022
Cash and cash equivalents	216,044	221,469
Investments	315,192	274,211
Total liquid assets	**531,236**	**495,680**
Undrawn committed bank facilities	172,946	132,221
Total liquid assets and committed undrawn funding	**704,182**	**627,901**

23 Liquidity risk (continued)

Contractual liquidity profile of financial liabilities

The following tables present the Banking Group's financial liabilities by relevant maturity groupings based upon contractual maturity date. The amounts disclosed in the tables represent undiscounted future principal and interest cash flows. As a result, the amounts in the tables below may differ to the amounts reported on the consolidated statement of financial position.

The contractual cash flows presented below may differ significantly from actual cash flows. This occurs as a result of future actions by the Banking Group and its counterparties, such as early repayments or refinancing of term loans and borrowings. Deposits and other public borrowings include customer savings deposits and transactional accounts, which are at call. These accounts provide a stable source of long term funding for the Banking Group.

$000's	On Demand	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
June 2023							
Non-derivative financial liabilities							
Deposits	782,775	2,313,983	1,015,525	62,618	42,186	-	4,217,087
Other borrowings	-	184,397	138,217	237,138	22,551	136,274	718,577
Due to related parties	-	7,173	-	-	-	-	7,173
Lease liabilities	-	1,356	1,368	2,643	6,615	2,731	14,713
Other financial liabilities	-	40,963	-	-	-	-	40,963
Total non-derivative financial liabilities	**782,775**	**2,547,872**	**1,155,110**	**302,399**	**71,352**	**139,005**	**4,998,513**
Derivative financial liabilities							
Inflows from derivatives	-	3,583	3,552	4,799	13,469	-	25,403
Outflows from derivatives	-	6,644	6,796	5,773	13,125	-	32,338
Total derivative financial liabilities	**-**	**3,061**	**3,244**	**974**	**(344)**	**-**	**6,935**
Undrawn facilities available to customers	310,423	-	-	-	-	-	310,423
June 2022							
Non-derivative financial liabilities							
Deposits	892,612	2,028,225	561,468	103,192	41,655	-	3,627,152
Other borrowings	-	368,926	7,251	397,859	-	-	774,036
Due to related parties	-	1,535	-	-	-	-	1,535
Lease liabilities	-	1,282	1,292	2,615	6,985	4,911	17,085
Other financial liabilities	-	47,510	-	-	-	-	47,510
Total non-derivative financial liabilities	**892,612**	**2,447,478**	**570,011**	**503,666**	**48,640**	**4,911**	**4,467,318**
Derivative financial liabilities							
Inflows from derivatives	-	5,007	1,759	3,505	813	-	11,084
Outflows from derivatives	-	3,893	3,227	6,621	839	-	14,580
Total derivative financial liabilities	**-**	**(1,114)**	**1,468**	**3,116**	**26**	**-**	**3,496**
Undrawn facilities available to customers	272,735	-	-	-	-	-	272,735

24 Interest rate risk

The Banking Group's market risk is derived primarily of exposure to interest rate risk, predominantly from raising funds through the retail and wholesale deposit market, the debt capital markets and committed and uncommitted bank funding, securitisation of receivables, and offering loan finance products to the commercial and consumer market in New Zealand and Australia.

The Banking Group’s exposure to market risk is governed by a policy approved by the Board and managed by the ALCO. This policy sets out the nature of risk which may be taken and aggregate risk limits, and the ALCO must conform to this. The objective of the ALCO is to derive the most appropriate strategy for the Banking Group in terms of the mix of assets and liabilities given its expectations of the future and the potential consequences of interest rate movements, liquidity constraints and capital adequacy.

The objective of the Banking Group’s interest rate risk policies is to limit underlying net profit after tax (**NPAT**) volatility. The measurement comprises net interest income the Banking Group generates from its interest earning assets and interest bearing liabilities.

The exposure to net interest income comes from a reduction in margins on interest earning assets or interest bearing liabilities and is managed when setting rates by taking into consideration wholesale rates, liquidity premiums, as well as appropriate lending credit margins.

An analysis of the Banking Group’s sensitivity to an increase (+) or decrease (-) in market interest rates by 100 basis points (**BP**) is as follows. An (+)/(-) to market interest rates of 100 BP would result in a $0.2 million (+)/(-) to NPAT (2022: $0.7 million (+)/(-)) with a corresponding impact to equity.

The Banking Group also manages interest rate risk by:

- Monitoring maturity profiles and seeking to match the re-pricing of assets and liabilities;
- Monitoring interest rates daily and regularly (at least monthly) reviewing interest rate exposures; and
- Entering into derivatives to hedge against movements in interest rates.

24 Interest rate risk (continued)

Contractual repricing analysis

The interest rate risk profile of financial assets and liabilities that follows has been prepared on the basis of maturity or next repricing date, whichever is earlier.

$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non-Interest Bearing	Total
June 2023							
Financial assets							
Cash and cash equivalents	216,040	-	-	-	-	4	216,044
Investments	29,828	24,963	37,767	55,460	167,174	1,819	317,011
Derivative financial assets	-	-	-	-	-	36,982	36,982
Finance receivables	1,675,775	302,005	520,923	766,532	689,565	-	3,954,800
Finance receivables - reverse mortgages	888,600	-	-	-	-	-	888,600
Other financial assets	-	-	-	-	-	1,050	1,050
Total financial assets	**2,810,243**	**326,968**	**558,690**	**821,992**	**856,739**	**39,855**	**5,414,487**
Financial liabilities							
Deposits	2,259,258	795,536	962,205	59,026	35,216	19,788	4,131,029
Other borrowings	345,859	49,598	121,195	-	98,474	-	615,126
Derivative financial liabilities	-	-	-	-	-	7,624	7,624
Due to related parties	-	-	-	-	-	7,173	7,173
Lease liabilities	-	-	-	-	-	13,478	13,478
Other financial liabilities	-	-	-	-	-	40,963	40,963
Total financial liabilities	**2,605,117**	**845,134**	**1,083,400**	**59,026**	**133,690**	**89,026**	**4,815,393**
Effect of derivatives held for risk management	1,084,971	(66,798)	(41,181)	(556,676)	(420,316)	-	-
Net financial assets/(liabilities)	**1,290,097**	**(584,964)**	**(565,891)**	**206,290**	**302,733**	**(49,171)**	**599,094**

24 Interest rate risk (continued)

Contractual repricing analysis (continued)

$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non-Interest Bearing	Total
June 2022							
Financial assets							
Cash and cash equivalents	221,460	-	-	-	-	9	221,469
Investments	1,568	854	51,144	91,974	128,672	1,502	275,714
Derivative financial assets	-	-	-	-	-	44,487	44,487
Finance receivables	1,736,646	185,858	334,715	576,037	928,975	-	3,762,231
Finance receivables - reverse mortgages	721,264	-	-	-	-	-	721,264
Due from related parties	-	-	-	-	-	1,540	1,540
Other financial assets	-	-	-	-	-	175	175
Total financial assets	**2,680,938**	**186,712**	**385,859**	**668,011**	**1,057,647**	**47,713**	**5,026,880**
Financial liabilities							
Deposits	2,201,740	684,378	546,718	99,196	38,325	26,787	3,597,144
Other borrowings	548,488	78,911	-	121,191	-	888	749,478
Derivative financial liabilities	-	-	-	-	-	6,335	6,335
Due to related parties	-	-	-	-	-	1,535	1,535
Lease liabilities	-	-	-	-	-	15,726	15,726
Other financial liabilities	-	-	-	-	-	47,510	47,510
Total financial liabilities	**2,750,228**	**763,289**	**546,718**	**220,387**	**38,325**	**98,781**	**4,417,728**
Effect of derivatives held for risk management	986,194	(76,349)	(127,004)	(309,781)	(473,060)	-	-
Net financial assets/(liabilities)	**916,904**	**(652,926)**	**(287,863)**	**137,843**	**546,262**	**(51,068)**	**609,152**

The tables above illustrate the periods in which the cash flows from interest rate swaps are expected to occur and affect profit or loss.

25 Concentrations of funding

(a) Regulatory liquidity ratios (unaudited)

RBNZ requires banks to hold minimum amounts of liquid assets to help ensure that they are effectively managing their liquidity risks. The mismatch ratio is a measure of a bank's liquid assets, adjusted for contractual cash inflows and outflows during a one-month or one-week period of stress. It is expressed as a ratio over the bank's total funding. The Banking Group must maintain its one-month and one-week mismatch ratios above zero on a daily basis. The below one-month and one-week mismatch ratios are averaged over the quarter.

RBNZ requires banks to hold a minimum amount of funding from stable sources called core funding. The minimum amount of core funding is 75% of a bank's total loans. The Banking Group must maintain its core funding ratio above the regulatory minimum on a daily basis. The below measure of the core funding ratio is averaged over the quarter.

	Average for the 3 Months Ended 30 June 2023	Average for the 3 Months Ended 31 March 2023
One-week mismatch ratio	8.29	8.69
One-month mismatch ratio	7.96	8.42
Core funding ratio	90.32	90.17

25 Concentrations of funding (continued)

(b) Concentration of funding by industry

The Australian and New Zealand Standard Industrial Classification codes have been used as the basis for categorising customer and investee industry sectors.

$000's	June 2023	June 2022
Agriculture	113,341	113,848
Forestry and fishing	21,944	14,391
Mining	291	1,524
Manufacturing	19,185	18,643
Finance and insurance	1,009,291	960,175
Wholesale trade	7,634	5,854
Retail trade and accommodation	25,136	19,491
Households	3,215,828	2,754,452
Rental, hiring and real estate services	59,720	43,797
Construction	36,868	28,449
Other business services	66,763	66,731
Transport and storage	7,807	4,598
Other	40,182	41,686
Total	**4,623,990**	**4,073,639**
Unsubordinated notes	122,165	272,983
Total borrowings	**4,746,155**	**4,346,622**

(c) Concentration of funding by geographical area

$000's	June 2023	June 2022
New Zealand	4,634,937	4,241,026
Overseas	111,218	105,596
Total borrowings	**4,746,155**	**4,346,622**

Other Disclosures

26 Significant subsidiaries

Significant Subsidiaries	Country of Incorporation and Place of business	Nature of business	Proportion of ownership and voting power held June 2023	June 2022
VPS Properties Limited	New Zealand	Investment property holding company	100%	100%
Marac Insurance Limited	New Zealand	Insurance services	100%	100%

27 Structured entities

A structured entity is one which has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity. Structured entities are created to accomplish a narrow and well-defined objective such as the securitisation or holding of particular assets, or the execution of a specific borrowing or lending transaction. Structured entities are consolidated where the substance of the relationship is that the Banking Group controls the structured entity.

(a) Heartland Cash and Term PIE Fund (Heartland PIE Fund)

The Banking Group controls the operations of the Heartland PIE Fund which is a portfolio investment entity that invests in the Banking Group's deposits. Investments of Heartland PIE Fund are represented as follows:

$000's	June 2023	June 2022
Deposits	244,258	149,824

(b) Heartland Auto Receivable Warehouse Trust 2018-1 (HARWT)

HARWT securitises motor vehicle loan receivables as a source of funding.

The Banking Group continues to recognise the securitised assets and associated borrowings in the consolidated statement of financial position as the Banking Group remains exposed to and has the ability to affect variable returns from those assets and liabilities. Although the Banking Group recognises those interests in HARWT, the loans sold to HARWT are set aside for the benefit of investors in HARWT. Other depositors and lenders to the Banking Group have no recourse to those assets.

$000's	June 2023	June 2022
Cash and cash equivalents	16,874	20,197
Finance receivables	254,735	312,239
Other borrowings	(258,256)	(315,308)

28 Capital adequacy - unaudited

The Reserve Bank of New Zealand (**RBNZ**) minimum regulatory capital requirements for banks have been established under the RBNZ Capital Adequacy Framework, outlined in the "Banking Prudential Requirements" (**BPRs**) documents. These documents are based on the international framework developed by the Bank for Internal Settlements Committee on Banking Supervision, commonly known as Basel III. These requirements define what is acceptable as capital and provide methods for measuring risks incurred by the banks in New Zealand. Basel III consists of three pillars:

- Pillar One covers the capital requirements for banks for credit, operational, and market risks;
- Pillar Two covers all other material risks not already included in Pillar One; and
- Pillar Three relates to market disclosure.

RBNZ Capital Adequacy Framework

The Banking Group has calculated its Risk Weighted Exposures (**RWEs**) and minimum regulatory capital requirements in accordance with the BPR documents. In doing so, the Banking Group has applied the standardised methodology to Risk Weighted Assets (**RWAs**) as per BPR 131: Standardised credit RWA's, standardised operational risk as per BPR150: Standardised Operational risk, and market risk as per BPR140: Market Risk.

Total regulatory capital is divided into Tier 1 and Tier 2 capital. Tier 1 capital comprises Common Equity Tier 1 (**CET1**) capital and Additional Tier 1 (**AT1**) capital. Tier 1 capital primarily consists of shareholder's equity and other capital instruments acceptable to the RBNZ as per BPR110: Capital Definitions, less intangible assets, cash flow hedge reserves, deferred tax assets, and other prescribed deductions. Tier 2 as per BPR110: Capital Definitions comprises eligible subordinated debt securities.

Regulatory capital adequacy ratios are calculated by expressing capital as a percentage of risk weighted exposures. As a Condition of Registration, the Bank must comply with the following minimum requirements set by the RBNZ:

- Total capital must not be less than 8% of RWE
- Tier 1 capital must not be less than 6% of RWE
- CET1 capital must not be less than 4.5% of RWE
- Capital must not be less than NZ$30m

In addition, if the Prudential Buffer Ratio (**PCR**) is less than 2.5%, the Bank must limit aggregate distributions, other than discretionary payments payable to holders of AT1 capital instruments, to the limits set out within the Banks Conditions of Registration.

Including the PCR, the Banking Group's minimum total capital requirement is 10.5%. On 5 December 2019 the RBNZ finalised their revised Capital Framework for banks which were not domestic systematically important banks (**non D-SIB**). This requires non D-SIB banks in New Zealand to gradually increase their Total Capital ratio to 16% by July 2028. The Banking Group's Total Capital ratio is 14.69% as at 30 June 2023. This means the revised Framework requires the Banking Group to increase its Total Capital ratio by 1.31% over the transitional period.

Capital management

The Board has overall responsibility for ensuring the Banking Group has adequate capital in relation to its risk profile and establishes minimum internal capital levels and limits above the regulatory minimum.

The Banking Group's objectives for the management of capital are to:

- Comply at all times with the regulatory capital requirements set by the RBNZ;
- Maintain a strong capital base to cover the inherent risks of the business in excess of that required by credit ratings agencies to maintain a strong credit rating; and
- Support the future development and growth of the business.

The Bank's Capital Management Framework includes its:

- Internal Capital Adequacy Assessment Process (**ICAAP**);
- Capital Stress Testing Policy; and
- Capital Management Plan (**CMP**)

28 Capital adequacy (continued) - unaudited

Capital management (continued)

The Banking Group has an ICAAP which complies with the requirements set out in BPR100 and is in accordance with its Conditions of Registration. The ICAAP identifies the capital required to be held against other material risks, being strategic business risk, reputational risk, regulatory risk and additional credit risk which is assisted through stress testing conducted in accordance with the Capital Stress Testing policy.

The Banking Group actively monitors its capital adequacy through ALCO and reports this on a regular basis to the Board. This includes forecasting capital requirements to ensure any future capital requirements can be executed in a timely manner. The Banking Group uses a mix of capital instruments to reduce single source reliance and to optimise the Banking Group's mix of capital. ICAAP, CMP and Capital Stress Testing Policy are reviewed annually by the Board.

The capital adequacy tables set out below summarise the composition of regulatory capital and the capital adequacy ratios for the Banking group for the year ended 30 June 2023.

(a) Capital

$000's	**June 2023**
Tier 1 Capital	
CET1 capital	
Paid-up ordinary shares issued by the Banking Group plus related share premium	553,239
Retained earnings (net of appropriations)	162,354
Accumulated other comprehensive income and other disclosed reserves	13,143
Less deductions from CET1 capital	
Intangible assets	(71,650)
Deferred tax assets	(16,760)
Cash flow hedge reserve	(14,710)
Total CET1 capital	**625,616**
AT1 capital	-
Total Tier 1 capital	**625,616**
Tier 2 Capital	
Tier 2 capital instrument[1]	100,000
Total Tier 2 capital	**100,000**
Total capital	**725,616**

[1] Classified as a liability under NZ GAAP and excludes capitalised transaction costs.

(b) Capital structure

The following details summarise each instrument included within Total Capital. None of these instruments are subject to phase-out from eligibility as capital under the RBNZ's Basel III transitional arrangements.

Ordinary shares

In accordance with BPR110, ordinary share capital is classified as CET1 capital. The ordinary shares have no par value. Each ordinary share of the Bank carries the right to vote on a poll at meetings of shareholders, the right to an equal share in dividends authorised by the Board and the right to an equal share in the distribution of the surplus assets of the Bank in the event of liquidation.

28 Capital adequacy (continued) - unaudited

Retained earnings

Retained earnings is the accumulated profit or loss that has been retained in the Banking Group. Retained earnings is classified as CET1 capital.

Reserves classified as CET1 capital

Fair value reserve	The fair value reserve comprises the changes in the fair value of investments, net of tax.
Cash flow hedge reserve	The hedging reserve comprises the fair value gains and losses associated with the effective portion of designated cash flow hedging instruments.

Tier 2 capital

Subordinated notes

A summary of the key terms and features of the subordinated notes is provided below:

Issuer	The Bank
Face value	$100 million
Issue date	28 April 2023
Maturity date	28 April 2033
Optional redemption	28 April 2028 and every quarterly interest payment date thereafter
Interest rate	Fixed at 7.51% for the first five years, thereafter, resets to quarterly floating rate equal to the sum of the applicable 3-month Bank Bill Rate plus 3.2% per annum.

Interest payable
The quarterly payment of interest in respect of the subordinated notes of the Bank are subject to the Bank being solvent at the time of, and immediately following the interest payment.

Early redemption
The Bank may choose to repay all or some of the subordinated notes for their face value together with accrued interest (if any) on 28 April 2028 or any interest payment date thereafter. Early redemption of all the subordinated notes for certain tax or regulatory events is permitted on an interest payment date. Early redemption is subject to certain conditions, including the Bank obtaining the RBNZ prior written approval and the Bank being solvent at the time.

Ranking
In a liquidation of the Bank, the claims of the holders of the subordinated notes will rank:

- Behind the claims of all depositors and other creditors of the Bank;
- equally with the claims of other holders of any other securities and obligations that rank equally with the subordinated notes; and
- ahead of the rights of the Bank's shareholders and holders of any other securities and obligations of the Bank that rank behind the subordinated notes.

28 Capital adequacy (continued) - unaudited

(c) Credit risk

On balance sheet exposures

	Total Exposure After Credit Risk Mitigation $000's	Average Risk Weight %	Risk Weighted Exposure $000's	Minimum Pillar 1 Capital Requirement $000's
June 2023				
Cash	-	0%	-	-
Sovereigns and central banks	275	0%	-	-
Multilateral development banks	174,274	0%	-	-
Multilateral development banks	89,834	20%	17,967	1,437
Banks - Short term - Tier 1	-	20%	-	-
Banks - Short term - Tier 2	216,044	20%	43,209	3,457
Banks - Short term - Tier 3	-	20%	-	-
Banks - Long term - Tier 1	-	20%	-	-
Banks - Long term - Tier 2	41,203	50%	20,601	1,648
Banks - Long term - Tier 3	-	50%	-	-
Public sector entity (AA- and above)	9,882	20%	1,976	158
Public sector entity (A- and above)	-	50%	-	-
Public sector entity (BBB+, BBB, BBB-)	-	100%	-	-
Corporates (AA- and above)	-	20%	-	-
Corporates (A- and above)	-	50%	-	-
Corporates (BBB- and above)	-	100%	-	-
Corporate Exposures - BFGS	41,022	20%	8,204	656
Corporate Exposures- unrated	2,082,338	100%	2,082,338	166,587
Welcome Home Loans - loan to value ratio (LVR) <= 80%[1]	1,265	35%	443	35
Welcome Home Loans - loan to value ratio (LVR) <= 90%[1]	-	35%	-	-
Welcome Home Loans - LVR 90% <= 100%[1]	-	50%	-	-
Welcome Home Loans - LVR > 100%[1]	-	100%	-	-
Reverse Residential mortgages <= 60% LVR	879,382	50%	439,691	35,175
Reverse Residential mortgages 60 <= 80% LVR	9,218	80%	7,374	590
Reverse Residential mortgages > 80% LVR	-	100%	-	-
Reverse Residential mortgages > 100% LVR	-	100%	-	-
Non Property Investment Mortgage Loan <=80% LVR	318,450	35%	111,458	8,917
Non Property Investment Mortgage Loan 80 <= 90% LVR	-	50%	-	-
Non Property Investment Mortgage Loan 90 <= 100% LVR	727	75%	545	44
Non Property Investment Mortgage Loan > 100% LVR	-	100%	-	-
Property Investment Mortgage Loan <= 80% LVR	1,639	40%	655	52
Property Investment Mortgage Loan 80 <= 90% LVR	-	70%	-	-
Property Investment Mortgage Loan 90 <= 100% LVR	-	90%	-	-
Property Investment Mortgage Loan > 100% LVR	-	100%	-	-
Past due residential mortgages	278	100%	278	22
Other past due assets - provision >= 20%	42,398	100%	42,398	3,392
Other past due assets - provision < 20%	37,562	150%	56,344	4,508
Equity holdings	-	300%	-	-
All other equity holdings	1,804	400%	7,215	577
Fixed Assets	13,027	100%	13,027	1,042
Leased Assets	11,510	100%	11,510	921
Other assets	1,464,284	100%	1,464,284	117,143
Not risk weighted assets	88,410	0%	-	-
Total on balance sheet exposures	**5,524,826**		**4,329,517**	**346,361**

[1] The LVR classification above is calculated in line with the Bank's Pillar 1 Capital requirement which includes relief for Welcome Home loans that are guaranteed by the Crown.

28 Capital adequacy (continued) - unaudited

(c) Credit risk (continued)

Off balance sheet exposures

	Total Exposure $000's	Credit Conversion Factor %	Credit Equivalent Amount $000's	Risk Weight %	Risk Weighted Exposure $000's	Minimum Pillar 1 Capital Requirement $000's
June 2023						
Direct credit substitute	3,897	100%	3,897	100%	3,897	312
Performance-related contingency	3,480	50%	1,740	100%	1,740	139
Other commitments where original maturity is more than one year	165,874	50%	82,937	100%	82,937	6,635
Other commitments where original maturity is more than one year	42,393	50%	21,197	35%	7,419	594
Other commitments where original maturity is less than or equal to one year	73,237	20%	14,647	100%	14,647	1,172
Other commitments where original maturity is less than or equal to one year	52,554	20%	10,511	50%	5,256	420
Other commitments where original maturity is less than or equal to one year	1,238	20%	248	35%	87	7
Counterparty credit risk[1]						
Interest rate contracts	1,653,918	N/A	35,198	34%	11,965	957
FX forward contracts	-	N/A	-	0%	-	-
Total off balance sheet exposures	**1,996,591**		**170,375**		**127,948**	**10,236**
Credit valuation adjustment	-		-		13,969	1,118
Total off balance sheet exposures	**1,996,591**		**170,375**		**141,917**	**11,354**

[1] The credit equivalent amount was calculated using the current exposure method.

(d) Additional mortgage information – LVR range

$000's	**On Balance Sheet Exposures**	**Off Balance Sheet Exposures[2]**	**Total Exposures**
June 2023			
Does not exceed 80%	1,209,954	94,848	1,304,802
Exceeds 80% and not 90%	-	-	-
Exceeds 90%	1,005	-	1,005
Total exposures	**1,210,959**	**94,848**	**1,305,807**

[2] Off balance sheet exposures means unutilised limits.

At 30 June 2023, there were no Welcome Home loans whose credit risk is mitigated by the Crown included in “Exceeds 90% residential mortgages”. Other loans in the exceeds 90% LVR range is primarily business and rural lending where residential mortgage security is only a part of the total security. For capital adequacy calculations only the value of the first mortgages over residential property is included in the LVR calculation, in accordance with BPR131. All new residential mortgages in respect of non-property investments lending have a loan-to-valuation ratio of less than or equal to 80%.

28 Capital adequacy (continued) - unaudited

(e) Reconciliation of mortgage related amounts

$000's	Note	June 2023
Gross finance receivables - reverse mortgages	19	888,600
Loans and advances - loans with residential mortgages	22d	322,486
On balance sheet residential mortgage exposures subject to the standardised approach		**1,211,086**
Less: collective provision for impairment	22c	(127)
On balance sheet residential mortgage exposures after collective provision	28d	**1,210,959**
Off balance sheet mortgage exposures subject to the standardised approach	28d	94,848
Total residential exposures subject to the standardised approach		**1,305,807**

(f) Credit risk mitigation

As at 30 June 2023 the Banking Group had $1.3 million of Welcome Home Loans (2022: $1.6 million), whose credit risk was mitigated by the Crown. Other than this the Banking Group does not have any exposures covered by eligible collateral, guarantees and credit derivatives.

(g) Operational risk

$000's	Implied Risk Weighted Exposure	Total Operational Risk Capital Requirement
June 2023		
Operational risk	300,483	24,039

Operational risk is calculated based on the previous 12 quarters of the Banking Group.

(h) Market risk

Market risk is the risk that market interest rates or foreign exchange rates will change and impact on the Banking Group's earnings due to either mismatches between repricing dates of interest bearing assets and liabilities and/or differences between customer pricing and wholesale rates.

$000's	Implied Risk Weighted Exposure	Aggregate Capital Charge
June 2023		
Market risk end-of-period capital charge		
Equity risk	1,804	144
Interest rate risk	159,466	12,757
Foreign currency risk	48	4
Market risk peak end-of-period capital charge		
Equity risk	1,804	144
Interest rate risk	159,466	12,757
Foreign currency risk	223	18

The Banking Group's aggregate market exposure is derived in accordance with BPR140. Peak end-of-day capital charge disclosure is derived by taking the highest month end market exposure over the six months ended 30 June 2023. Interest rate risk, foreign exchange risk and equity risk are calculated monthly using the month end position. The Banking Group has investigated the impact of daily aggregate market risk exposure. Certain identified system limitations that cause anomalous results are being addressed so that a satisfactory future daily peak period exposure can be obtained.

28 Capital adequacy (continued) - unaudited

(i) Total capital requirement

$000's	Total Exposure After Credit Risk Mitigation	Risk Weighted Exposure or Implied Risk Weighted Exposure	Total Capital Requirement
June 2023			
Total credit risk			
On balance sheet	5,524,826	4,329,517	346,361
Off balance sheet	1,996,591	141,917	11,354
Operational risk	n/a	300,483	24,039
Market risk	n/a	161,318	12,901
Total	**7,521,417**	**4,933,235**	**394,655**

(j) Capital ratios

%	June 2023	June 2022
Capital ratios compared to minimum ratio requirements		
Common Equity Tier 1 capital ratio	12.68%	13.49%
Minimum Common Equity Tier 1 Capital as per Conditions of Registration	4.50%	4.50%
Tier 1 capital ratio	12.68%	13.49%
Minimum Tier 1 Capital as per Conditions of Registration	6.00%	6.00%
Total capital ratio	14.71%	13.49%
Minimum Total Capital as per Conditions of Registration	8.00%	8.00%
Buffer ratio	6.68%	5.49%
Buffer trigger ratio	2.50%	2.50%

(k) Solo capital adequacy

%	June 2023	June 2022
Capital ratios		
Common Equity Tier 1 capital ratio	12.77%	14.37%
Tier 1 capital ratio	12.77%	14.37%
Total capital ratio	14.93%	14.37%

For the purposes of calculating capital adequacy on a solo basis, subsidiaries which are both wholly owned and wholly funded by the Bank are to be consolidated with the Bank.

(l) Capital for other material risks

In addition to the material risks included in the calculation of the capital ratios, the Banking Group has identified other material risks to be included in the capital allocation (being strategic risk, business risk, regulatory and additional credit risk). As at 30 June 2023, the Banking Group has made an internal capital allocation of $20.01 million to cover these risks (2022: $8.4 million).

29 Securitisation, funds management and other fiduciary activities

Securitisation

As at 30 June 2023, the Banking Group had $254.74 million securitised assets (2022: $312.24 million).

There have been no material changes to the Banking Group's involvement in the securitisation activities.

Funds management and other fiduciary activities

The Banking Group, through Heartland PIE Fund Limited, controls, manages and administers the Heartland Cash and Term PIE Fund and its products (Heartland Call PIE and Heartland Term Deposit PIE). Note 27 - Structured entities has further details. The Heartland Cash and Term PIE Fund deals with the Bank in the normal course of business, in the Bank's capacity as Registrar of the Fund and also invests in the Bank's deposits. The Banking Group is considered to control the Heartland Cash and Term PIE Fund, and as such the Heartland Cash and Term PIE Fund is consolidated within the financial statements of the Banking Group.

Risk management

The Banking Group has in place policies and procedures to ensure that the fiduciary activities identified above are conducted in an appropriate manner. It is considered that these policies and procedures will ensure that any difficulties arising from these activities will not impact adversely on the Banking Group. The policies and procedures include comprehensive and prominent disclosure of information regarding products, and formal and regular review of operations and policies by management and internal auditors. Further information on the Banking Group's risk management policies and practices is included in Note 20 - Enterprise risk management.

Provision of financial services and asset purchases

Over the accounting period, financial services provided by the Banking Group to entities which were involved in the activities above (including trust, custodial, funds management and other fiduciary activities) were provided on arm's length terms and conditions and at fair value.

Any assets purchased from such entities have been purchased on arm's length terms and conditions and at fair value.

29 Securitisation, funds management and other fiduciary activities (continued)

Peak aggregate funding to entities

The Banking Group did not provide any funding to entities conducting funds management and other fiduciary activities, or insurance product or marketing and distribution activities described in this note, during the year (2022: nil).

The Bank provided the following funding in relation to securitisation entities.

	Total Trusts	
	June 2023	**June 2022**
Peak end-of-day aggregate amount of funding provided ($000's)	308,755	305,038
Peak end-of-day aggregate amount of funding provided as a percentage of the Banking Group's Tier 1 Capital as at the end of the year (%)	49.4%	49.0%

For this purpose, peak ratio information was derived by determining the maximum end-of-day aggregate amount of funding over the financial year and then dividing that amount by the amount of the entity's assets or the Banking Group's Tier 1 Capital (as the case required) as at the end of the year.

	HARWT	
	June 2023	**June 2022**
Peak end-of-day aggregate amount of funding provided ($000's)	308,755	305,038
Peak end-of-day aggregate amount of funding provided as a percentage of the total assets of the individual entity as at the end of the year [1]	114.8%	93.5%

[1] Total assets as at the end of the year in June 2023 are lower compared to the timing of the peak end-of-day aggregate amount of funding provided due to a repurchase.

For this purpose, peak ratio information was derived by determining the maximum end-of-day aggregate amount of funding and then dividing that amount by the amount of the entity's assets or the Banking Group's Tier 1 Capital (as the case required) as at the end of the year.

30 Offsetting financial instruments

The Banking Group offsets financial assets and financial liabilities and reports the net balance in the balance sheet where there is currently a legally enforceable right to set off and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Banking Group enters into contractual arrangements with counterparties to manage the credit risks associated primarily with over-the-counter derivatives. The Banking Group has entered into credit support annexes (**CSAs**) which form a part of International Swaps and Derivatives Association (**ISDA**) Master Agreement, in respect of certain exposures relating to derivative transactions. As per these CSAs, the Banking Group or the counterparty needs to collateralise the market value of outstanding derivative transactions. As at 30 June 2023, the Banking Group has received $27.61 million of cash collateral (2022: $32.34 million) against derivative assets. Cash collateral includes amounts of cash obtained to cover the net exposure between the counterparty in the event of default or insolvency. The cash collateral received is not netted off against the balance of derivative assets disclosed in the consolidated statement of financial position and is disclosed within trade and other payables.

The following table sets out financial assets and financial liabilities which have not been offset but are subject to enforceable master netting agreements (or similar arrangements) and the related amounts not offset in the balance sheet. Financial instruments refer to amounts that are subject to relevant close out netting arrangements under a relevant ISDA agreement. ISDA and similar master netting arrangements do not meet the criteria for offsetting in the statement of financial position because under such agreements the counterparties typically have the right to offset only following an event of default, insolvency or bankruptcy or following other predetermined events.

	Effects of offsetting on the balance sheet			**Related amounts not offset**		
$000's	**Gross Amount**	**Gross amounts set off in the balance sheet**	**Net amounts reported in the balance sheet**	**Financial Instruments**	**Cash collateral received**	**Net amount**
June 2023						
Derivative financial assets	36,982	-	36,982	(7,624)	(27,609)	1,749
Total financial assets	**36,982**	**-**	**36,982**	**(7,624)**	**(27,609)**	**1,749**
Derivative financial liabilities	7,624	-	7,624	(7,624)	-	-
Total financial liabilities	**7,624**	**-**	**7,624**	**(7,624)**	**-**	**-**
June 2022						
Derivative financial assets	44,487	-	44,487	(6,335)	(32,341)	5,811
Total financial assets	**44,487**	**-**	**44,487**	**(6,335)**	**(32,341)**	**5,811**
Derivative financial liabilities	6,335	-	6,335	(6,335)	-	-
Total financial liabilities	**6,335**	**-**	**6,335**	**(6,335)**	**-**	**-**

31 Contingent liabilities and commitments

The Banking Group in the ordinary course of business will be subject to claims and proceedings against it whereby the validity of the claim will only be confirmed by uncertain future events. In such circumstances the contingent liabilities are possible obligations, or present obligations if known, where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised, but are disclosed, unless they are remote. Where some loss is probable, provisions have been made on a case by case basis.

Contingent liabilities and credit related commitments arising in respect of the Banking Group's operations were:

$000's	**June 2023**	**June 2022**
Letters of credit, guarantee commitments and performance bonds	7,378	8,969
Total contingent liabilities	**7,378**	**8,969**
Undrawn facilities available to customers	310,423	272,735
Conditional commitments to fund at future dates	24,873	34,791
Total commitments	**335,296**	**307,526**

32 Events after reporting date

In July 2023, Heartland Bank Limited purchased AU$30 million reverse mortgage loans from Senior Warehouse Trust.

The Bank resolved to pay a cash dividend to its parent company HGH of $43 million on its ordinary shares on 28 August 2023.

There were no other events subsequent to the reporting period which would materially affect the consolidated financial statements.

Independent auditor's report

To the shareholder of Heartland Bank Limited

Our opinion

In our opinion, the accompanying:

- financial statements, excluding the information disclosed in accordance with Schedules 4, 7, 9, 13, 14, 15 and 17 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order"), of Heartland Bank Limited (the "Bank"), including the entities it controlled as at 30 June 2023 or from time to time during the financial year (the "Banking Group"), present fairly, in all material respects, the financial position of the Banking Group as at 30 June 2023, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards ("NZ IFRS") and International Financial Reporting Standards ("IFRS"); and
- information disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order (the "Supplementary Information"), in all material respects:
  - presents fairly the matters to which it relates; and
  - is disclosed in accordance with those schedules; and
  - has been prepared in accordance with any conditions of registration relating to disclosure requirements imposed under section 74(4)(c) of the Banking (Prudential Supervision) Act 1989.

What we have audited

- The Banking Group's financial statements (the "Financial Statements") required by clause 24 of the Order, comprising:
  - the consolidated statement of financial position as at 30 June 2023;
  - the consolidated statement of comprehensive income for the year then ended;
  - the consolidated statement of changes in equity for the year then ended;
  - the consolidated statement of cash flows for the year then ended; and
  - the notes to the Financial Statements, excluding the information disclosed in accordance with Schedules 4, 7, 9, 13, 14, 15 and 17 of the Order within notes 20, 21, 22, 23, 24, 25, 28 and 29, which includes significant accounting policies and other explanatory information.
- The Supplementary Information within the consolidated statement of financial position and notes 20, 21, 22, 23, 24, 25, 28 and 29 of the Financial Statements for the year ended 30 June 2023 of the Banking Group.

  We have not audited the information relating to capital adequacy and regulatory liquidity requirements disclosed in accordance with Schedule 9 of the Order within notes 25 and 28 of the Financial Statements and our opinion does not extend to this information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Statements and the Supplementary Information* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Banking Group in accordance with Professional and Ethical Standard 1 *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the *International Code of Ethics for Professional Accountants (including International Independence Standards)* issued by the International Ethics Standards Board for Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our firm carries out other services for the Banking Group. These services are audit and assurance related services comprising: insurance solvency, trust deed reporting, supervisor reporting and registry audits and other services. Other services are actuarial services in respect of reverse mortgages for the Banking Group prior to our appointment as auditor and the provision of an executive reward survey report. In addition, certain partners and employees of our firm may deal with the Banking Group on normal terms within the ordinary course of trading activities. The provision of these other services and these relationships have not impaired our independence as auditor of the Banking Group.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Statements and the Supplementary Information of the current year. These matters were addressed in the context of our audit of the Financial Statements and the Supplementary Information as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Description of the key audit matter	How our audit addressed the key audit matter
Provision for impairment of finance receivables As disclosed in note 22 of the Financial Statements, the impairment allowance totalled $52.1 million at 30 June 2023. For the determination of the collectively assessed impairment allowance, this requires the use of credit risk methodologies that are applied in models using the Banking Group's historical experience of the correlations between defaults and losses, borrower creditworthiness, segmentation of customers or portfolios and economic	We obtained an understanding of control activities over the Banking Group's impairment allowance, and for relevant control activities assessed whether they are appropriately designed. For controls relevant to our planned audit approach we tested, on a sample basis, whether they operated effectively, throughout the financial year. In addition, we, along with our credit risk modelling expert, performed the following procedures, amongst others, on a targeted or sample basis, to assess the reasonableness of the Banking Group's collective allowance for impairment:

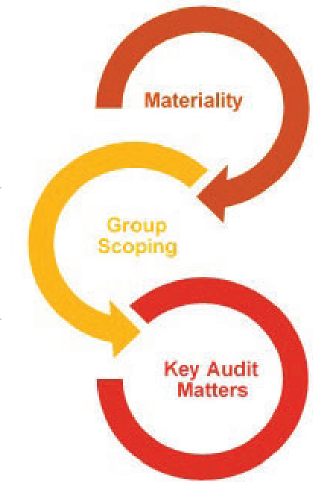
Description of the key audit matter	How our audit addressed the key audit matter
conditions. The assumptions we focused our audit on included those with greater levels of management judgement and for which variations have the most significant impact on the impairment allowance. For finance receivables that meet specific risk based criteria, the impairment allowance is individually assessed by the Banking Group. These allowances are measured using probability weighted scenarios which are intended to reflect a range of reasonably possible outcomes, and incorporate assumptions such as estimated future cash proceeds expected to be recovered from the realisation of security held as collateral by the Banking Group. We considered this a key audit matter due to the significant audit effort required and the inherent estimation uncertainty present in its determination, which is due to the subjectivity and extent of judgement used by the Banking Group in the impairment allowance recognition and measurement.	• Assessed the appropriateness of the methodology inherent in the models used against the requirements of NZ IFRS 9 *Financial Instruments*; • Challenged and assessed the appropriateness of the collective allowance for impairment inclusive of the impacts of any post model adjustments; • We challenged management's modelling outcomes using a range of what we consider reasonably possible assumptions to assess the collective impairment allowance; and • Tested the completeness and accuracy of critical data elements used in the calculations. With respect to individually assessed allowances we: • For a sample of business and rural loans not identified as impaired, considered the borrowers latest financial information provided to the Banking Group to assess the credit risk grade rating allocated to the borrower to assess whether the borrower has had a significant increase in credit risk, a critical data element which involves significant management judgement; • For loans where an impairment was individually assessed, we considered the borrower's latest financial information, value of security held as collateral and probability weighted scenario outcomes (where applicable) to test the basis of measuring the impairment allowance. We also considered the impacts of events occurring subsequent to balance date on the impairment allowances. Where applicable, we considered the competency, capabilities, objectivity and nature of the work of certain experts used by the Banking Group to assist in determining the individual impairment allowance. We also assessed the reasonableness of the disclosures against the requirements of the accounting standards.

Description of the key audit matter	How our audit addressed the key audit matter
Fair value of reverse mortgages The Banking Group's fair value of finance receivables – reverse mortgages ("Reverse mortgages") totalled $888.6 million at 30 June 2023 as disclosed in note 19 of the Financial Statements. Reverse mortgages are held at fair value through profit or loss. The fair value of reverse mortgages is subject to significant judgement and is highly complex. In addition, the current impacts of rising interest rates and declining house prices, combined with the economic outlook, increases the possibility of increasing outflows under the no negative equity guarantee provided by the Banking Group to the borrower. Accordingly, we consider this to be a key audit matter. The Banking Group records the estimated fair value of the reverse mortgages at transaction price on the basis no reliable fair value can be estimated as there is no relevant active market and fair value cannot be reliably estimated using other valuation techniques under NZ IFRS 13 *Fair Value Measurement (NZ IFRS 13)*. To assess whether the transaction price remains an appropriate proxy for fair value, the Banking Group considers the impact on future discounted cash flows of changes in the risk profile and expectations of performance since loan origination. Specifically considering changes in mortality and potential move into care, voluntary exits, house prices, likelihood of cash outflows under the no negative equity guarantee and interest rate margins.	Our audit procedures included assessing the design and implementation of controls relating to the Banking Group's assessment of the fair value of reverse mortgages. In addition, our audit procedures included: • Assessing the reasonableness of the Banking Group's approach to estimating the fair value based on the transaction cost against the requirements of NZ IFRS 13; • Assessing whether there was evidence of a relevant active market or observable inputs in which to establish fair value using a market approach; • Engaging our internal actuarial experts to independently estimate the value of discounted future cash flows from the reverse mortgages, including any expected outflows under the no negative equity guarantee and comparing this to the transaction cost of reverse mortgages (carrying value) to assess any potential shortfall (a shortfall would indicate the transaction value was overstated); • Tested the completeness and accuracy of a sample of critical data elements used as inputs to our internal actuarial expert assessment of the value of discounted future cash flows; • Assessed the reasonableness of key assumptions (such as future house prices, voluntary exits, interest rate margins, future interest rates) used by our internal actuarial expert in their assessment of the value of discounted future cash flows; and • Considered the appropriateness of the disclosures in note 19 of the Financial Statements against the requirements of the accounting standards.

Description of the key audit matter	How our audit addressed the key audit matter
Operation of financial reporting information technology (IT) systems and controls The Banking Group's operations and financial reporting processes are heavily dependent on IT systems for the capture, processing, storage and extraction of significant volumes of transactions which is critical to the recording of financial information and the preparation of the Banking Group's Financial Statements. Accordingly, we consider this to be a key audit matter. In common with other banking entities, access management controls are important to ensure both access and changes made to applications and data are appropriate. Ensuring that only appropriate staff have access to IT systems, that the level of access itself is appropriate, and that access is periodically monitored, are key controls in mitigating the potential for fraud or error as a result of a change to an application or underlying data. The Banking Group's controls over IT systems are intended to ensure that: ● changes to existing systems operate as intended and are authorised; ● access to process transactions or change data is appropriate and maintains an intended segregation of duties; ● the use of privileged access to systems and data is restricted and monitored; and ● IT processing is approved and where issues arise they are resolved	For material financial statement transactions and balances, our procedures included obtaining an understanding of the business processes, IT systems used to generate and support those transactions and balances, associated IT application controls, and IT dependencies in manual controls. This involved assessing, where relevant to the audit: ● change management: the processes and controls used to develop, test and authorise changes to the functionality and configurations within systems; ● security: the access controls designed to enforce segregation of duties, govern the use of generic and privileged accounts, or ensure that data is only changed through authorised means; and ● IT operations: the controls over certain IT batch processes used to ensure that any issues that arise are managed appropriately. Where relevant to our planned audit approach, we, along with our IT specialists, evaluated and tested the design and operating effectiveness of certain controls over the continued integrity of IT systems that are relevant to financial reporting. We also carried out tests, on a sample basis, of IT application controls that were key to our audit testing strategy in order to assess the accuracy of relevant system calculations, automated controls and the operation of certain system enforced access controls. Where we identified design or operating effectiveness matters relating to IT systems and application controls relevant to our audit, we performed alternative or additional audit procedures.

Our audit approach

Overview



Overall Banking Group materiality: $5.0 million, which represents approximately 5% of profit before tax.

We chose profit before tax because, in our view, it is the benchmark against which the performance of the Banking Group is most commonly measured by users, and is a generally accepted benchmark.

Following our assessment of the risk of material misstatement, we performed a full scope audit over the consolidated financial information of the Banking Group.

As reported above, we have three key audit matters, being:

- Provision for impairment of finance receivables
- Fair value of reverse mortgages
- Operation of financial reporting information technology (IT) systems and controls

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the Financial Statements and the Supplementary Information. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality
The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance about whether the Financial Statements and the Supplementary Information are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Statements and the Supplementary Information.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Banking Group materiality for the Financial Statements and the Supplementary Information, as a whole, as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate, on the Financial Statements and the Supplementary Information, as a whole.

How we tailored our group audit scope
We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the Financial Statements and the Supplementary Information, as a whole, taking into account the structure of the Banking Group, the financial reporting processes and controls, and the industry in which the Banking Group operates.

The scope of our audit and the nature, timing and extent of audit procedures performed were determined by our risk assessment, the financial significance of components and other qualitative factors (including history of misstatement through fraud or error).

Other information

The Directors are responsible for the other information. The other information comprises the information included in the Disclosure Statement presented in accordance with Schedule 2 of the Order on pages 1 to 4 and 90 to 99, and the information relating to capital adequacy and regulatory liquidity requirements disclosed in accordance with Schedule 9 of the Order within notes 25 and 28, but does not include the Financial Statements, the Supplementary Information and our auditor's report thereon.

Our opinion on the Financial Statements and the Supplementary Information does not cover the other information and we do not express any form of audit opinion or assurance conclusion thereon. We issue a separate limited assurance report on the information relating to capital adequacy and regulatory liquidity requirements disclosed in accordance with Schedule 9 of the Order.

In connection with our audit of the Financial Statements and the Supplementary Information, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Financial Statements and the Supplementary Information or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Disclosure Statement

The Directors are responsible, on behalf of the Bank, for the preparation and fair presentation of the Financial Statements in accordance with clause 24 of the Order, NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of Financial Statements and Supplementary Information that are free from material misstatement, whether due to fraud or error.

In addition, the Directors are responsible, on behalf of the Bank, for the preparation and fair presentation of the Disclosure Statement which includes:

- all of the information prescribed in Schedule 2 of the Order; and
- the information prescribed in Schedules 4, 7, 9, 13, 14, 15 and 17 of the Order.

In preparing the Financial Statements, the Directors are responsible for assessing the Banking Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Banking Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Statements and the Supplementary Information

Our objectives are to obtain reasonable assurance about whether the Financial Statements, as a whole, and the Supplementary Information, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (NZ) and ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Statements and the Supplementary Information.

A further description of our responsibilities for the audit of the Financial Statements and the Supplementary Information is located at the External Reporting Board's website at:

https://www.xrb.govt.nz/assurance-standards/auditors-responsibilities/audit-report-1/

This description forms part of our auditor's report.

Who we report to

This report is made solely to the Bank's shareholder. Our work has been undertaken so that we might state those matters which we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's shareholder, for our work, for this report, or for the opinions we have formed.

The engagement partner on the engagement resulting in this independent auditor's report is Karen Shires.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
28 August 2023

Auckland

Independent Assurance Report

To the shareholder of Heartland Bank Limited

Limited assurance report on compliance with the information required on capital adequacy and regulatory liquidity requirements

Our conclusion

We have undertaken a limited assurance engagement on Heartland Bank Limited's (the "Bank") compliance, in all material respects, with clause 21 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order") which requires information prescribed in Schedule 9 of the Order relating to capital adequacy and regulatory liquidity requirements to be disclosed in its full year Disclosure Statement for the year ended 30 June 2023 (the "Disclosure Statement").

Based on the procedures we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that the Bank's information relating to capital adequacy and regulatory liquidity requirements, included in the Disclosure Statement in compliance with clause 21 of the Order and disclosed in notes 25 and 28, is not, in all material respects, disclosed in accordance with Schedule 9 of the Order.

Basis for conclusion

We have conducted our engagement in accordance with Standard on Assurance Engagements 3100 (Revised) *Compliance Engagements* ("SAE 3100 (Revised)") issued by the New Zealand Auditing and Assurance Standards Board.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.

Directors' responsibilities

The Directors are responsible on behalf of the Bank for compliance with the Order, including clause 21 of the Order which requires information relating to capital adequacy and regulatory liquidity requirements prescribed in Schedule 9 of the Order to be included in the Disclosure Statement, for the identification of risks that may threaten compliance with that clause, controls that would mitigate those risks and monitoring ongoing compliance.

Our independence and quality management

We have complied with the independence and other ethical requirements of Professional and Ethical Standard 1 *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* issued by the New Zealand Auditing and Assurance Standards Board, which is founded on the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

We apply Professional and Ethical Standard 3 *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, which requires our firm to design, implement and operate a system of quality management including policies or procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

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We are independent of the Bank and the entities it controlled at 30 June 2023 or from time to time during the period (together, the “Banking Group”). In our role as auditor, we provided other audit and assurance related services comprising: insurance solvency, trust deed reporting, supervisor reporting and registry audits and other services. Other services are actuarial services in respect of reverse mortgages for the Banking Group (prior to our appointment as assurance practitioner) and the provision of an executive reward survey report. In addition, certain partners and employees of our firm may deal with the Banking Group on normal terms within the ordinary course of trading activities of the Banking Group. The provision of these other services and these relationships have not impaired our independence.

Assurance practitioner’s responsibilities

Our responsibility is to express a limited assurance conclusion on whether the Bank’s information relating to capital adequacy and regulatory liquidity requirements, included in the Disclosure Statement in compliance with clause 21 of the Order is not, in all material respects, disclosed in accordance with Schedule 9 of the Order. SAE 3100 (Revised) requires that we plan and perform our procedures to obtain limited assurance about whether anything has come to our attention that causes us to believe that the Bank’s information relating to capital adequacy and regulatory liquidity requirements, included in the Disclosure Statement in compliance with clause 21 of the Order, is not, in all material respects, disclosed in accordance with Schedule 9 of the Order.

In a limited assurance engagement, the assurance practitioner performs procedures, primarily consisting of discussion and enquiries of management and others within the entity, as appropriate, and observation and walk-throughs, and evaluates the evidence obtained. The procedures selected depend on our judgement, including identifying areas where the risk of material non-compliance with clause 21 of the Order in respect of the information relating to capital adequacy and regulatory liquidity requirements is likely to arise.

Given the circumstances of the engagement we:

- obtained an understanding of the process, models, data and internal controls implemented over the preparation of the information relating to capital adequacy and regulatory liquidity requirements;
- obtained an understanding of the Bank’s compliance framework and internal control environment to ensure the information relating to capital adequacy and regulatory liquidity requirements is in compliance with the Reserve Bank of New Zealand’s (the “RBNZ”) prudential requirements for banks;
- obtained an understanding and assessed the impact of any matters of non-compliance with the RBNZ’s prudential requirements for banks that relate to capital adequacy and regulatory liquidity requirements and inspected relevant correspondence with the RBNZ;
- performed analytical and other procedures on the information relating to capital adequacy and regulatory liquidity requirements disclosed in accordance with Schedule 9 of the Order, and considered its consistency with the annual financial statements; and
- agreed the information relating to capital adequacy and regulatory liquidity requirements disclosed in accordance with Schedule 9 of the Order to information extracted from the Bank’s models, accounting records or other supporting documentation.

The procedures performed in a limited assurance engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement and consequently the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed. Accordingly, we do not express a reasonable assurance opinion on compliance with the compliance requirements.

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Inherent limitations
Because of the inherent limitations of an assurance engagement, together with the internal control structure, it is possible that fraud, error or non-compliance with the compliance requirements may occur and not be detected.

A limited assurance engagement on the Bank's information relating to capital adequacy and regulatory liquidity requirements prescribed in Schedule 9 of the Order to be included in the Disclosure Statement in compliance with clause 21 of the Order does not provide assurance on whether compliance will continue in the future.

Use of report
This report has been prepared for use by the Bank’s shareholder for the purpose of establishing that these compliance requirements have been met.

Our report should not be used for any other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility for any reliance on this report to anyone other than the Bank and the Bank’s shareholder, or for any purpose other than that for which it was prepared.

The engagement partner on the engagement resulting in this independent assurance report is Karen Shires.

PricewaterhouseCoopers

Chartered Accountants
28 August 2023

Auckland

Historical Summary of Financial Statements

For the year ended 30 June 2023

$000's	June 2023	June 2022	June 2021	June 2020	June 2019
Interest income	372,688	275,770	272,562	297,512	284,064
Interest expense	158,027	66,205	73,753	108,476	111,665
Net interest income	**214,661**	**209,565**	**198,809**	**189,036**	**172,399**
Other net income	12,458	33,704	15,006	15,742	9,409
Net operating income	**227,119**	**243,269**	**213,815**	**204,778**	**181,808**
Operating expenses	101,337	96,203	100,852	90,782	76,298
Profit before impaired asset expense and income tax	**125,782**	**147,066**	**112,963**	**113,996**	**105,510**
Fair value (loss)/gain on investments	-	(315)	215	-	1,936
Impaired asset expense	22,891	14,692	14,579	29,372	20,554
Profit before income tax	**102,891**	**132,059**	**98,599**	**84,624**	**86,892**
Profit before income tax from discontinued operations	-	-	-	-	6,169
Income tax expense	28,389	36,068	27,090	23,924	24,762
Profit for the year	**74,502**	**95,991**	**71,509**	**60,700**	**68,299**
Dividends paid to equity holders	60,000	35,500	30,000	65,000	112,042

As at 30 June 2023

$000's	June 2023	June 2022	June 2021	June 2020	June 2019
Total assets	5,561,808	5,154,652	4,419,488	4,314,559	4,143,828
Individually impaired assets	52,955	66,183	38,143	24,667	26,412
Total liabilities	4,833,072	4,447,149	3,777,660	3,717,522	3,540,438
Total equity	728,736	707,503	641,828	597,037	603,390

The amounts above have been extracted from the audited financial statements of the Banking Group.

Amendments to Conditions of Registration

Changes in Conditions of Registration

With effect from 1 June 2023 LVR restrictions were eased from:

- 10% limit for loans with LVR above 80% for owner occupiers, and
- 5% limit for loans with LVR above 60% for investors

To:

- 15% limit for loans with LVR above 80% for owner occupiers, and
- 5% limit for loans with LVR above 65% for investors

The previous LVR settings were put in place November 2021 when risks were elevated. The restrictions built resilience in the financial system, which has been evident in the past year as house prices have fallen without widespread impacts to financial stability.

With effect on or after 1 July 2022:

The Bank's implicit risk capital requirement (formerly referenced in conditions 1C) has been removed.

As at 30 June 2023, there have been no other changes to the Conditions of Registration.

Conditions of Registration

These conditions apply on and after 1 June 2023.

The registration of Heartland Bank Limited ("the bank") as a registered bank is subject to the following conditions:

1.That—

(a) the Total capital ratio of the banking group is not less than 8%;
(b) the Tier 1 capital ratio of the banking group is not less than 6%;
(c) the Common Equity Tier 1 capital ratio of the banking group is not less than 4.5%;
(d) the Total capital of the banking group is not less than $30 million.

For the purposes of this condition of registration,—

"Total capital ratio", "Tier 1 capital ratio", and "Common Equity Tier 1 capital ratio" have the same meaning as in Subpart B2 of BPR100: Capital Adequacy;

"Total capital" has the same meaning as in BPR110: Capital Definitions.

1A. That—
(a) the bank has an internal capital adequacy assessment process ("ICAAP") that accords with the requirements set out in Part D of BPR100: Capital Adequacy;
(b) under its ICAAP the bank identifies and measures its "other material risks" defined in Part D of BPR100: Capital Adequacy; and
(c) the bank determines an internal capital allocation for each identified and measured "other material risk".

1B. That, if the Prudential Capital Buffer (PCB) ratio of the banking group is 2.5% or less, the bank must—

(a) according to the following table, limit the aggregate distributions of the bank's earnings, other than discretionary payments payable to holders of Additional Tier 1 capital instruments, to the percentage limit on distributions that corresponds to the banking group's PCB ratio; and

Banking group's PCB ratio	**Percentage limit on distributions of the bank's earnings**	**Capital Buffer Response Framework stage**
0% – 0.5%	0%	Stage 3
>0.5 – 1%	30%	Stage 2
>1 – 2%	60%	Stage 1
>2 – 2.5%	100%	None

(b) comply with the Capital Buffer Response Framework requirements as set out in Part D of BPR120: Capital Adequacy Process Requirements.

For the purposes of this condition of registration,—

"prudential capital buffer ratio", "distributions", and "earnings" have the same meaning as in Subpart B2 of BPR100: Capital Adequacy;

an Additional Tier 1 capital instrument is an instrument that meets the requirements of B2.2(2)(a), (c) or (d) of BPR110: Capital Definitions.

1BA. That the bank must not make any distribution on a transitional AT1 capital instrument on or after the date on which on any conversion or write-off provision in the terms and conditions of the instrument is triggered due to either a loss absorption trigger event or a non-viability trigger event.

Conditions of Registration (continued)

For the purposes of this condition of registration, “transitional AT1 capital instrument” has the meaning given in section A2.3 of BPR110: Capital Definitions and “loss absorption trigger event” and “non-viability trigger event” have the meanings given in sub-section C2.2(3) of BPR120: Capital Adequacy Requirements.

1C. That:

(a) the bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued on or after 1 July 2021 in the calculation of its capital ratios unless it has completed the notification requirements in Part B of BPR120: Capital Adequacy Process Requirements in respect of the instrument; and
(b) the bank meets the requirements of Part C of BPR120: Capital Adequacy Process Requirements in respect of regulatory capital instruments.

For the purposes of this condition of registration, —

an Additional Tier 1 capital instrument is an instrument that meets the requirements of subsection B2.2(2)(a) or (c) of BPR110: Capital Definitions;
a Tier 2 capital instrument is an instrument that meets the requirements of subsection B3.2(2)(a) or (c) of BPR110: Capital Definitions.

2. That the banking group does not conduct any non-financial activities that in aggregate are material relative to its total activities.

In this condition of registration, the meaning of “material” is based on generally accepted accounting practice.

3. That the banking group’s insurance business is not greater than 1% of its total consolidated assets.

For the purposes of this condition of registration, the banking group’s insurance business is the sum of the following amounts for entities in the banking group:

(a) if the business of an entity predominantly consists of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total consolidated assets of the group headed by the entity; and
(b) if the entity conducts insurance business and its business does not predominantly consist of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total liabilities relating to the entity’s insurance business plus the equity retained by the entity to meet the solvency or financial soundness needs of its insurance business.

In determining the total amount of the banking group’s insurance business—

(a) all amounts must relate to on balance sheet items only, and must comply with generally accepted accounting practice; and
(b) if products or assets of which an insurance business is comprised also contain a non-insurance component, the whole of such products or assets must be considered part of the insurance business.

Conditions of Registration (continued)

For the purposes of this condition of registration,—

"insurance business" means the undertaking or assumption of liability as an insurer under a contract of insurance:

"insurer" and "contract of insurance" have the same meaning as provided in sections 6 and 7 of the Insurance (Prudential Supervision) Act 2010.

4. That aggregate credit exposures (of a non-capital nature and net of any allowances for impairment) of the banking group to all connected persons do not exceed the rating-contingent limit outlined in the following matrix

Credit rating of the Bank[1]	**Connected exposure limit (% of the Banking Group's Tier 1 capital)**
AA/Aa2 and above	75
AA-/Aa3	70
A+/A1	60
A/A2	40
A-/A3	30
BBB+/Baa1 and below	15

Within the rating-contingent limit, credit exposures (of a non-capital nature and net of any allowances for impairment) to non-bank connected persons shall not exceed 15% of the banking group's Tier 1 capital.

For the purposes of this condition of registration, compliance with the rating-contingent connected exposure limit is determined in accordance with the Reserve Bank of New Zealand document entitled "Connected exposure policy" (BS8) dated October 2021.

5. That exposures to connected persons are not on more favourable terms (e.g. as relates to such matters as credit assessment, tenor, interest rates, amortisation schedules and requirement for collateral) than corresponding exposures to non-connected persons.

6. That the Bank complies with the following corporate governance requirements:
   (a) the board of the Bank must have at least five directors;
   (b) the majority of the board members must be non-executive directors;
   (c) at least half of the board members must be independent directors;
   (d) an alternate director,—
      (i) for a non-executive director must be non-executive; and
      (ii) for an independent director must be independent;
   (e) at least half of the independent directors of the Bank must be ordinarily resident in New Zealand;
   (f) the chairperson of the board of the Bank must be independent; and
   (g) the Bank's constitution must not include any provision permitting a director, when exercising powers or performing duties as a director, to act other than in what he or she believes is the best interests of the company (i.e. the Bank).

   For the purposes of this condition of registration,—

   "independent,"—

   (a) in relation to a person other than a person to whom paragraph (b) applies, has the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014; and
   (b) in relation to a person who is the chairperson of the board of the Bank, means a person who—
      (i) meets the criteria for independence set out in section 10 except for those in paragraph 10(1)(a) in BS14; and
      (ii) does not raise any grounds of concern in relation to the person's independence that are communicated in writing to the Bank by the Reserve Bank of New Zealand:

[1] This table uses the rating scales of Standard & Poor's, Fitch Ratings and Moody's Investors Service. (Fitch Ratings' scale is identical to Standard & Poor's.)

Conditions of Registration (continued)

"non-executive" has the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014.

7. That no appointment of any director, chief executive officer, or executive who reports or is accountable directly to the chief executive officer, is made in respect of the Bank unless:
   (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
   (b) the Reserve Bank has advised that it has no objection to that appointment.

8. That a person must not be appointed as chairperson of the board of the Bank unless:
   (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
   (b) the Reserve Bank has advised that it has no objection to that appointment.

9. That the bank has a board audit committee, or other separate board committee covering audit matters, that meets the following requirements:
   (a) the mandate of the committee must include: ensuring the integrity of the bank's financial controls, reporting systems and internal audit standards;
   (b) the committee must have at least three members;
   (c) every member of the committee must be a non-executive director of the Bank;
   (d) the majority of the members of the committee must be independent; and
   (e) the chairperson of the committee must be independent and must not be the chairperson of the Bank.

   For the purposes of this condition of registration, "independent" and "non-executive" have the same meanings as in condition of registration 6.

10. That a substantial proportion of the Bank's business is conducted in and from New Zealand.

11. That the Banking Group complies with the following quantitative requirements for liquidity-risk management:
    (a) the one-week mismatch ratio of the Banking Group is not less than zero percent at the end of each business day;
    (b) the one-month mismatch ratio of the Banking Group is not less than zero percent at the end of each business day; and
    (c) the one-year core funding ratio of the Banking Group is not less than 75 percent at the end of each business day.

    For the purposes of this condition of registration, the ratios identified must be calculated in accordance with the Reserve Bank of New Zealand documents entitled "Liquidity Policy" (BS13) dated July 2022 and "Liquidity Policy Annex: Liquid Assets" (BS13A) dated July 2022.

12. That the Bank has an internal framework for liquidity risk management that is adequate in the Bank's view for managing the Bank's liquidity risk at a prudent level, and that, in particular:
    (a) is clearly documented and communicated to all those in the organisation with responsibility for managing liquidity and liquidity risk;
    (b) identifies responsibility for approval, oversight and implementation of the framework and policies for liquidity risk management;
    (c) identifies the principal methods that the Bank will use for measuring, monitoring and controlling liquidity risk; and
    (d) considers the material sources of stress that the Bank might face, and prepares the Bank to manage stress through a contingency funding plan.

13. That no more than 10% of total assets may be beneficially owned by a SPV.
    For the purposes of this condition,—
    "total assets" means all assets of the banking group plus any assets held by any SPV that are not included in the banking group's assets:
    "SPV" means a person—
    (a) to whom any member of the Banking Group has sold, assigned, or otherwise transferred any asset;
    (b) who has granted, or may grant, a security interest in its assets for the benefit of any holder of any covered bond; and
    (c) who carries on no other business except for that necessary or incidental to guarantee the obligations of any member of the Banking Group under a covered bond:

    "covered bond" means a debt security issued by any member of the Banking Group, for which repayment to holders is guaranteed by a SPV, and investors retain an unsecured claim on the issuer.

Conditions of Registration (continued)

14. That—
   (a) no member of the Banking Group may give effect to a qualifying acquisition or business combination that meets the notification threshold, and does not meet the non-objection threshold, unless:
      (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination and at least 10 working days have passed; and
      (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011; and
   (b) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the non-objection threshold unless:
      (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination;
      (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011; and
      (iii) the Reserve Bank has given the Bank a notice of non-objection to the significant acquisition or business combination.

   For the purposes of this condition of registration, "qualifying acquisition or business combination", "notification threshold" and "non-objection threshold" have the same meaning as in the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011.

15. That the Bank is pre-positioned for Open Bank Resolution and in accordance with a direction from the Reserve Bank, the Bank can—
   (a) close promptly at any time of the day and on any day of the week and that effective upon the appointment of the statutory manager—
      (i) all liabilities are frozen in full; and
      (ii) no further access by customers and counterparties to their accounts (deposits, liabilities or other obligations) is possible;
   (b) apply a de minimis to relevant customer liability accounts;
   (c) apply a partial freeze to the customer liability account balances;
   (d) reopen by no later than 9am the next business day following the appointment of a statutory manager and provide customers access to their unfrozen funds;
   (e) maintain a full freeze on liabilities not pre-positioned for open bank resolution; and
   (f) reinstate customers' access to some or all of their residual frozen funds.

   For the purposes of this condition of registration, "de minimis", "partial freeze", "customer liability account", and "frozen and unfrozen funds" have the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated June 2022.

16. That the Bank has an Implementation Plan that—
   (a) is up-to-date; and
   (b) demonstrates that the Bank's prepositioning for Open Bank Resolution meets the requirements set out in the Reserve Bank document: "Open Bank Resolution Pre-positioning Requirements Policy" (BS 17) dated June 2022.

   For the purposes of this condition of registration, "Implementation Plan" has the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated June 2022.

17. That the Bank has a compendium of liabilities that—
   (a) at the product-class level lists all liabilities, indicating which are—
      (i) pre-positioned for Open Bank Resolution; and
      (ii) not pre-positioned for Open Bank Resolution;
   (b) is agreed to by the Reserve Bank; and
   (c) if the Reserve Bank's agreement is conditional, meets the Reserve Bank's conditions.

   For the purposes of this condition of registration, "compendium of liabilities", and "pre-positioned and non pre-positioned liabilities" have the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated June 2022.

Conditions of Registration (continued)

18. That on an annual basis the bank tests all the component parts of its Open Bank Resolution solution that demonstrates the bank's prepositioning for Open Bank Resolution as specified in the bank's Implementation Plan.

    For the purposes of this condition of registration, "Implementation Plan" has the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated June 2022.

19. That, for a loan-to-valuation measurement period ending on or after 30 November 2023, the total of the bank's qualifying new mortgage lending amount in respect of property-investment residential mortgage loans with a loan-to-valuation ratio of more than 65%, must not exceed 5% of the total of the qualifying new mortgage lending amount in respect of property-investment residential mortgage loans arising in the loan-to-valuation measurement period.

20. That, for a loan-to-valuation measurement period ending on or after 30 November 2023, the total of the bank's qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans with a loan-to-valuation ratio of more than 80%, must not exceed 15% of the total of the qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans arising in the loan-to-valuation measurement period.

21. That the bank must not make a residential mortgage loan unless the terms and conditions of the loan contract or the terms and conditions for an associated mortgage require that a borrower obtain the registered bank's agreement before the borrower can grant to another person a charge over the residential property used as security for the loan.

In these conditions of registration,—
"Banking Group" means Heartland Bank Limited (as reporting entity) and all other entities included in the Group as defined in section 6(1) of the Financial Markets Conduct Act 2013 for the purposes of Part 7 of that Act.

"generally accepted accounting practice" has the same meaning as in section 8 of the Financial Reporting Act 2013.

In these conditions of registration, the version dates of the Reserve Bank of New Zealand Banking Prudential Requirement (BPR) documents that are referred to in the capital adequacy conditions 1 to 1C, or are referred to in turn by those documents or by Banking Supervision Handbook (BS) documents, are—

BPR document	Version date
BPR100: Capital adequacy	1 October 2021
BPR110: Capital definitions	1 October 2021
BPR120: Capital adequacy process requirements	1 July 2021
BPR130: Credit risk RWAs overview	1 July 2021
BPR131: Standardised credit risk RWAs	1 October 2021
BPR132: Credit risk mitigation	1 October 2021
BPR133: IRB credit risk RWAs	1 October 2021
BPR134: IRB minimum system requirements	1 July 2021
BPR140: Market risk exposure	1 October 2021
BPR150: Standardised operational risk	1 July 2021
BPR151: AMA operational risk	1 July 2021
BPR160: Insurance, securitisation, and loan transfers	1 July 2021
BPR001: Glossary	1 July 2021

Conditions of Registration (continued)

In conditions of registration 19 to 21,—

> “loan-to-valuation ratio”, “non property-investment residential mortgage loan”, “property-investment residential mortgage loan”, “qualifying new mortgage lending amount in respect of property-investment residential mortgage loans”, “qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans”, and “residential mortgage loan” have the same meaning as in the Reserve Bank of New Zealand document entitled “Framework for Restrictions on High-LVR Residential Mortgage Lending” (BS19) dated October 2021:
>
> “loan-to-valuation measurement period” means a period of six calendar months ending on the last day of the sixth calendar month.

Conditions of Registration – Non Compliance

Conditions of Registration Non-Compliance

The Bank has complied with the conditions of registrations since its last disclosure statement.

Pending Proceedings or Arbitration

There are no pending legal proceedings or arbitrations concerning any member of the Banking Group at the date of Disclosure Statement that may have a material adverse effect on the Bank or the Banking Group.

Credit Ratings

As at the date of signing this Disclosure Statement, the Bank's credit rating issued by Fitch Australia Pty Ltd (**Fitch Ratings**) was BBB stable. This BBB credit rating was issued on 14 October 2015 and is applicable to long term unsecured obligations payable in New Zealand, in New Zealand dollars. This BBB stable credit rating was affirmed by Fitch Ratings on 7 April 2022.

The following is a summary of the descriptions of the ratings categories for rating agencies for the rating of long-term senior unsecured obligations:

Fitch Ratings	Standard & Poor's	Moody's Investors Service	Description of Grade
AAA	AAA	Aaa	Ability to repay principal and interest is extremely strong. This is the highest investment category.
AA	AA	Aa	Very strong ability to repay principal and interest in a timely manner.
A	A	A	Strong ability to repay principal and interest although somewhat susceptible to adverse changes in economic, business, or financial conditions.
BBB	BBB	Baa	Adequate ability to repay principal and interest. More vulnerable to adverse changes.
BB	BB	Ba	Significant uncertainties exist which could affect the payment of principal and interest on a timely basis.
B	B	B	Greater vulnerability and therefore greater likelihood of default.
CCC	CCC	Caa	Likelihood of default considered high. Timely repayment of principal and interest is dependent on favourable financial conditions.
CC-C	CC-C	Ca-C	Highest risk of default.
RD to D	D	-	Obligations currently in default.

Credit ratings from Fitch Ratings and Standard & Poor's may be modified by the addition of a plus or minus sign to show relative status within the major rating categories. Moody's Investors Service apply numerical modifiers 1, 2, and 3 to show relative standing within the major rating categories, with 1 indicating the higher end and 3 the lower end of the rating category.

Other Material Matters

There are no material matters relating to the business or affairs of the Bank or the Banking Group that are not already contained elsewhere in this Disclosure Statement which would, if disclosed in this Disclosure Statement, materially affect the decision of a person to subscribe for debt securities of which the Bank or any member of the Banking Group is the issuer.

HEARTLAND GROUP

[*Name*]
[*Address*]

29 August 2023

Dear shareholder,

Proposed Buyback of Shares from Long Term Incentive Scheme Participants

Heartland Group Holdings Limited (**Heartland** or the **Company**) gives notice to its shareholders that it intends to make an offer to acquire certain shares to be issued or transferred by the Company as part of its executive long term incentive scheme from the participants in that scheme in order to fund the tax liability that will arise for those participants upon receipt of shares under that scheme (**Buyback Offer**). This disclosure document is for your information only and is given pursuant to section 61(5) of the Companies Act 1993.

The Company operates a long term incentive scheme under which selected executives of Heartland, Heartland Bank Limited and Australian Seniors Finance Pty Limited (**Participants**) were issued performance share rights (**Performance Rights**), which are eligible to be converted to ordinary shares in the Company (**Shares**) for nil consideration, subject to certain vesting conditions being met (**Scheme**). Vesting conditions for a number of Performance Rights issued under the Scheme in FY21 will be assessed on 30 August 2023, being the business day after Heartland releases its full year results for the year ended 30 June 2023.

The Company has determined that it will assist Participants meet the tax obligations that will arise if the Performance Rights vest and Shares are issued or transferred to them by offering to apply the PAYE rules on the Participants' behalf in respect of the Shares issued or transferred to them and to make the Buyback Offer in order for Participants to fund the corresponding liability to the Company. The terms of the Buyback Offer are as follows:

- The Company will pay PAYE on each Participant's behalf in relation to the Shares issued or transferred to that Participant and the Participant shall be required to make a payment to the Company that is equal to the PAYE paid on their behalf in respect of their Shares.

- The Company shall offer to buyback such number of Shares as is equal in value to the Participant's PAYE liability which the Company has agreed to meet on their behalf (rounded to the nearest whole share), with the purchase price for those Shares to be retained by Heartland in satisfaction of the payment the Participant is required to make to the Company in respect of their PAYE liability. At a marginal tax rate of 39%, this means that 39% of a Participant's Shares would be bought back by the Company.

- The price at which Shares will be bought back from Participants will be the market value of the Shares on issue, calculated as the volume weighted average price of Heartland's ordinary shares traded on market on the NZX for the five days prior to the issue of Shares.

- The Buyback Offer will be made on 13 September 2023 and must be accepted by Participants by no later than 5pm on 18 September 2023. It is intended that the Shares will be issued or transferred and acquired by the Company under the Buyback Offer by 19 September 2023.

The Participants to whom the Buyback Offer will be made are as follows:

Participant Name	***Participant Title***
Andrew Dixson	Group Chief Financial Officer, Heartland Group Holdings Limited
Michael Drumm	Group Chief Operating Officer, Heartland Group Holdings Limited
Peter Griffin	General Manager, Business, Heartland Bank Limited
Darryl Harnett	General Manager, Consumer, Heartland Bank Limited
Keira Billot	General Manager, Retail & Reverse Mortgages New Zealand, Heartland Bank Limited
Chris Fletcher	Head of Customer Care, Heartland Bank Limited
Sharon Yardley	General Manager, Reverse Mortgages, Australian Seniors Finance Pty Limited

To give effect to the Buyback Offer, the Board resolved on 28 August 2023:

1. To make the Buyback Offer;

2. That the acquisition of the Shares under the Buyback Offer is in the best interests of the Company and of benefit to the remaining shareholders;

3. That the terms of the Buyback Offer and the consideration offered for the Shares are fair and reasonable to both the Company and the remaining shareholders;

4. That it is not aware of any information that will not be disclosed to shareholders:

   4.1 which is material to an assessment of the value of the Shares; and

   4.2 as a result of which the terms of the Buyback Offer and consideration offered for the Shares are unfair to shareholders accepting the Buyback Offer;

5. That the Board is satisfied that the Company will, immediately after acquiring the Shares, satisfy the solvency test applied under section 52 of the Companies Act 1993;

6. That, for the purposes of section 67A of the Companies Act 1993, the Shares shall not be cancelled on acquisition; and

7. To authorise Greg Tomlinson to sign such documents and do such other things as may be necessary or appropriate to complete the Buyback Offer.

Yours faithfully

Greg Tomlinson
For the Board of Directors