Australian Unity Annual General Meeting

27 October 2014

Glenn Barnes: Chairman's Address

Australian Unity is about to celebrate its 175th year. We date our history back to 1840, when a group of men from varied walks of life established a colonial chapter of the Manchester Unity Independent Order of Oddfellows in Melbourne. Our founders included a chief constable, three builders, a farrier, a brewer and a newspaper proprietor. There are perhaps a handful of Australian companies who can trace their roots back this far, and we are proud to be one of them. We are especially proud that some of the core establishing principles of the new organisation are still a strong part of our identity today. One example is that it would be an organisation run by and for members.

When thinking about our 175th anniversary, we wanted to mark the occasion in some way. We commissioned professional historian Alex McDermott to research our archives and the public records. We asked him to write an historical reflection of the development of Australia during those 175 years, along with the development of friendly societies generally and Australian Unity's antecedent organisations specifically. These antecedent organisations include Manchester Unity and the Australian Natives' Association in Victoria and South Australia. Grand United in NSW is also part of our history. So to are the BHP employees credit union; the South Australian Rechabites and even that state's Free Gardeners, as other examples.

We plan to publish this work as a book early next year, but I thought it would be of interest and relevant to share with you some facts that have been uncovered.

- Friendly societies were founded in Australia along the model of their counterparts in the UK. However, here they were very different. For starters, many of the affiliated orders were technically illegal in Britain until 1850. This was because of fear in post-French Revolution Europe and the UK that any structured organisation of people could facilitate uprising. In Australia, however, the founders of friendly societies placed a high premium on egalitarianism and openly encouraged not just workers but men – and in the early years it was only men – from all classes and all religions – to join.
- A core founding principle of these bodies was freedom. Another was the rejection of any largesse, either from elites or the state.
- As most of you would already know, the roots of the company stem back to the roots of the nation itself, with the Federation movement largely driven by the Australian Natives' Association.
- We have long been aware that Australia's first and second prime ministers, Edmund Barton and Alfred Deakin, along with the first Australian-born governor general, Sir Isaac Isaacs, were members of the Australian Natives' Association. But also among esteemed early members, at least of the associated Australasian Women's Association, were Dame Nellie Melba and the suffragette Vida Goldstein, who was the first woman to nominate for the Federal Senate.
- Over 175 years of history, the organisation has had many challenges. It had to adapt to the gold rush, the great depression, the birth of a new nation, world wars, and the rise of the welfare state. But one of the strongest challenges the organisation had to face was the doctors' dispute of the 1920s. At the time, friendly societies contracted doctors to provide services for their members, and the doctors' union was unhappy with the arrangement. Specifically, it wanted

the access means-tested – something our forebears were strongly opposed to! After decades of disputes, eventually the doctors won a compromise that resulted in the top 10 percent of wage earners, who were lodge members, refused access to the lodge doctors.

- Many of you will ponder that history in the light of recent debate over the means testing of the private health insurance rebate. The very roots of our organisations are based on egalitarianism of access.
- Though formed primarily to offer bonds and insurance products, the organisations that founded this company have long operated in other areas. The first home for the aged and infirm was considered in the 1870s, while building societies and pharmacies are also part of the strength of diversity the organisation built over the years.
- Today, Australian Unity has more than three quarters of a million customers, 300,000 members and runs a number of distinct and varied businesses. At our core, our purpose remains unchanged. Like our forebears we value egalitarianism, enterprise and the desire to be self-reliant.

There are two recurring themes through our history I would like to pick up on. The first is democracy. It is not an overstatement to say that the organisations that were the forebears of Australian Unity made a significant mark upon the country and its government. Within the social laboratory of the friendly societies, ordinary people practiced the basic arts of governance and democracy; electing officials, and debating issues of community importance. It was this, more than anything perhaps, that led to the strong culture of civic engagement in Australia.

Perhaps today this culture is under threat. In recent years – driven by matters such as the greater political influence of independents and minor parties, the 24-hour news cycle and more recently the evolution of social media and the "tweet" – our political system has drifted away from serving the purpose for which it was established. We watch with horror as major policy issues, such as the sustainability of our economic system and environment, are ignored in favour of bickering over trivial matters. Policy decisions, when they are made, are often made without appropriate community debate.

As a company this trend worries us, partly because we experience the consequences of poor policy, but mainly because we worry for the community that major problems are not being confronted. We would like to see a situation where the community becomes, once more, engaged in a debate about what kind of government we want. We need conversations about what we expect in terms of the major policy issues and the trade-offs, quality and cost of implementation. This is a conversation that Australian Unity, because of our history as well as our contemporary operations, seeks to stimulate and to be actively involved in.

The second theme is self-reliance. Self-reliance has many forms. At the time of the birth of our organisation, it was forged very much from a reaction to the then-historical context. Our earliest members were reacting to both the convict era and laws that governed the poor in Britain. At heart was a rejection of charity or largesse – and the desire to build community and personal wellbeing.

Today, we believe our customers and members still put a large store in personal independence. As a company we believe we offer the kinds of products and services customers need in order to retain as much control and independence over their lives as possible.

Of course, this is all relative. For older Australians, independence is often a diminishing luxury. The consequences of loss of independence affect a person's wellbeing, and add strain to their families. It is with this in mind that we continually seek to find inventive ways to foster quality of life, particularly for our older members. One initiative we have invested much time and effort in over recent years is the Remedy Healthcare programs. These programs provide free coaching and support to members dealing with debilitating chronic diseases. Remedy also offers rehabilitation in the home programs that allow members to get out of hospital sooner without compromising clinical care.

Another area is our "Better Together" model of aged care. We have been developing this over recent years in preparation for the opening of the Rathdowne Place aged care centre in Carlton. The model firmly puts the resident at the centre of decisions that affect their daily life. We want to free them from bureaucratically-convenient timetables and activities. We want them to flourish and have choice in how to live each day. This means being in control of as much of their daily lives as possible, from mealtimes to external activities. This sounds like an obvious thing, but be assured that it has required extensive work on rethinking the model of care. Almost everything has been reviewed, from rostering to training to resident empowerment. And we have created this new way of operating within the constraints of government funding and staffing models that skew toward institutionalisation.

Rohan Mead, in his address, will provide you with specific details about the operations of the company. In summary, this year we had a 21 percent increase in operating earnings, and reported a profit after tax of $29.6 million. This is a very pleasing result in a tough operating environment and one that speaks to the strength of our business operations and the sound efforts of our management and staff.

Later in this meeting you will get an opportunity to consider a number of important resolutions. Two of them relate to our formal presentation to you of the financial report and the remuneration report. These are regular items of business at the AGM.

The third is the election of two directors in accordance with the company's constitution – Ms Eve Crestani and Ms Melinda Cilento. These directors will be deemed to be elected without a vote from members because the number of nominations did not exceed the number of vacancies. This is because of the way the constitution is currently written.

At this AGM, we are asking members to vote on changing the constitution. If that vote is passed, in future members will be required to vote on the election and re-election of all directors standing for office. This is the fourth resolution set out in the notice of meeting, and we will discuss this more formally later. The Board believes that this proposal will improve our governance settings. It will give members improved capacity to be better connected to the governance of the organisation.

The final resolution concerns a modest proposed increase to the directors' remuneration aggregate limit. The aggregate limit has not been increased since 2007. This is a maximum amount that the company can use for directors' fees and the proposal for a modest increase is a reflection of the increasing complexity of the company and its business operations. There are a few points I'd like to make here.

- Australian Unity is among Australia's largest companies by revenue generated, with revenue today almost twice as much it was in 2007.

- It operates in extremely complex regulatory and technical environments.
- Directors need strong business acumen and must meet "fit and proper" tests.
- There are increasing demands on them to get involved in more detail with regulator interaction and governance requirements.
- To remain competitive Australian Unity must have highly skilled and experienced directors, executives and staff members.
- Finally, an increased aggregate cap is a mechanism by which we can continue our program of board renewal, bringing on new directors for a time with a hand-over period with more experienced directors.

Directors of Australian Unity must also have a strong commitment to the core purpose of the company; that is to enable millions of Australians to enjoy wellbeing. We are not purely driven by profits or commercial success, though of course we operate under strong commercial principles. At a wider level, we seek to influence members to make decisions that improve their own wellbeing. We hope to also influence opinion leaders and policymakers to make decisions that will improve community wellbeing. This latter objective is more challenging in the light of the current general environment. But both these objectives are felt at all levels of the organisation in the way we do business as much as the business we do.

I would like to take this opportunity to thank my fellow directors, the management team and all Australian Unity employees for their dedicated hard work and their commitment to these ideals. We need to continue to ensure that Australian Unity, which has been an important Australian institution for the best part of 175 years, continues to play its part in building a better Australia.

I will now ask our Group Managing Director, Rohan Mead, to present his report.

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Rohan Mead: Group Managing Director's Address

Thank you Chairman. I would like to also extend a special welcome to you all. I am pleased to be able to report on the company's performance this year. Before I do, I'd like to mention a small piece of interesting news.

This year Australian Unity was ranked in the top 20 of IBIS Worlds's Top 500 private companies in Australia – the definition of private including being not listed for equity on the sharemarket. Interestingly, six of the top 20 companies are mutual companies or cooperative enterprises. I mention this only because there has been much debate in recent years over the relevance of the mutual model, and there seems to be a perception that, with events such as the upcoming float of Medibank Private, that participation in the share market is the optimal form of business structure. I beg to differ on this. I think we can confidently say that the model we have adopted has served us extremely well over the past 175 years, and has served the community well across a broad range of sectors.

One of the points often made in relation to mutuals is that it is difficult for them to access capital for growth. I can confidently say that this has not been our experience to date and we don't anticipate it being an issue as we continue with our plans to significantly grow the company.

Turning to the financial results we have had an increase in revenues of 7 percent, to $1.3

billion.

Operating earnings, which is profit before tax less investment income and borrowing costs, has also increased, by 21 percent, to $38.2 million. This is an important figure as it shows our performance driven by our own trading position, unaffected by the earnings we make on investible funds. This result was achieved despite lower earnings in our healthcare business, which I will talk about more shortly.

This year, our investment income, of $17.8 million was significantly lower than last year's $27.5 million. This was largely due to significant one-off amounts in the prior year, and also the patchiness of the investment markets in the year under review. Investment income performance varies from year to year and depends upon many external factors such as market sentiment and the performance of the economy as well as the abilities of our funds management team.

Both profit before tax and profit after tax held relatively steady at $35.1 million and $29.6 million respectively. I believe these results can be characterised as sound, given the context of some of the challenges in the health insurance business and the performance of our Investment income.

As you know, we operate a portfolio of businesses. Traditionally, health insurance has been the largest business and it remains so today. But the non health insurance businesses are now contributing just over 50 percent of the company's adjusted Earnings Before Interest, Tax, Depreciation and Amortisation, excluding corporate functions and eliminations. This demonstrates they are building momentum in their respective sectors.

This organisation has always sought to observe wider needs in the community, but then to proffer practical solutions and test them in the commercial world. There are many recent examples of this as well as historical ones. You will be aware that we identified some years ago that Australia would be subject to the weight of chronic disease, and we sought to play our part in the solution.

The establishment of Remedy Healthcare was at the time a significant shift in the role of health insurance, and required a substantial amount of effort on our part, not least being lobbying to change the legislation governing private health insurance funds.

Another example of our approach to build commercial solutions for community problems is the development of aged care and retirement living. The first time our antecendent organsiations did this was in the 1870s, when they set aside some land in Melbourne for the aged and infirm. It wasn't until the middle of the 20th century that this part of the organisation's business became firmly established, with homes and villages built by both Grand United in NSW and Manchester Unity in Victoria. The contemporary aspect of this business is a number of significant investments in both the built form and in the operating model behind it, responding to the marketly changing demography of these times.

The chairman has mentioned Rathdowne Place, and we are pleased with the initial response of the community to this facility. We are also energised by our development of the "better together" model, which seeks to allow residents to direct and control their own daily choices and activities.

We hope to replicate this model in the Peninsula Grange aged care facility due to open in Mornington next year.

We are making further bricks and mortar investments in the expansion of The Governor's Retirement Resort and the development of Sienna Grange, both in Port Macquarie, NSW.

In Glen Waverley in Melbourne, we are about to embark on plans to redevelop Wahroonga Aged Care into a 102-bed residential aged care facility together with 55 low rise independent living apartments. This redevelopment, to be known as "Campbell Place" will offer an enhanced choice of services and living opportunities including day respite, palliative care and community care. In each instance we seek to continuously shape the quality of services offered, and the structure of the environment, to shift the focus of attention to the resident. In so doing, we hope to lead community and industry to change the way aged care and retirement living is experienced.

Along similar lines, we established a peronal financial advice business on a fee-for-service basis. This was long before community disquiet about the role of commissions-based structures reached the peak it has over the last several years. Reform in this industry sector is not done, in our opinion. But attention should now turn to the development of policies that encourage and facilitate Australians to, where possible, take charge of their own financial security. It is a troubling fact that today 77 percent of Australians over the age of 65 rely, at least in part, on government welfare support; and even more troubling that this figure is unlikely to decline. Continuous tinkering with superannuation may not be the answer, as it erodes trust in the system. But nor is the answer to allow a system to continue unsustainably.

It is important to remember that by 2047, the proportion of Australians over 65 will rise to a quarter of the population. Surely if we expect that almost 80 percent of these people will need to rely on the aged pension, noting that today the average length of pension support is 13 years, we are destined for one of two outcomes. Forced impoverishment for those on welfare or an increasing taxation burden for the shrinking population of working age.

Australian Unity will continue to urge solutions to these important and complex contemporary problems.

Before I turn my attention to the details of our operational results, I would like to introduce members of the Australian Unity executive team.

The Chairman has already introduced you to Kevin McCoy, our Chief Financial Officer and Verran Fehlberg, our Company Secretary and General Counsel. Both of these executives are fresh faces to these roles this year, but not entirely fresh faces to members. Kevin has taken on the position of Chief Financial Officer after a period in a strategic role on the executive team, and I welcome him to this role and congratulate him on his first year being responsible for the preparation of the company's accounts.

Some of you will think Verran is also familiar. That's because Verran is a former Company Secretary and General Counsel, who has returned to the role after five years living and working off-shore looking after family. I am sure you will join me in welcoming Verran back to the company.

They are joined today by colleagues, and I'll introduce them starting with Amanda Hagan, the chief executive of our Healthcare business. David Bryant is our Chief Investment Officer and the chief executive responsible for our Investments business.

Derek McMillan is the chief executive who heads up our Retirement Living business. Steve Davis is the CEO of our Personal Financial Services area.

Sharon Beaumont is the group executive responsible for Human Resources and Kimina Lyall is group executive of Corporate Development.

Tahir Tanveer is the group executive in charge of Business Technology. Finally, Tony Connon is strategic adviser to the group managing director. You may also recognise Tony for his long service as the company's Chief Financial Officer prior to this year.

I now turn to each of our businesses and their performance over the 2013-2014 financial year.

Our healthcare business includes the traditional operations of health insurance, along with our increasing focus on preventative healthcare.

In health insurance, we, like the rest of the industry, continue to adjust to the legislative changes to the federal government's private health insurance rebate.

Some time ago, we warned that the consequences of these changes were likely to be that the healthier members of a particular fund cohort might downgrade or drop their cover, leaving a generally more vulnerable group to share the risk that remains.

Unfortunately, this year, we began to see this pattern emerge, particularly in our corporate health insurance business, GU Health. After years of out-performance, the results of the GU Health business were adversely affected by higher than anticipated claims. This situation accounted for most of the drop in performance of the healthcare business as a whole. GU Health was also affected by the downturn in the resources sector, a sector which is a large part of its client base.

Overall, our healthcare operations recorded a 7 percent increase in revenues to $789 million and adjusted earnings before interest, tax, depreciation and amortisation – or EBITDA – of $43.6 million for the year, down from $47.8 million.

This year we also experienced another year of growth in policyholders, however this was not as significant as in past years. For the first time in four years, both our retail health fund and the corporate fund increased numbers of policyholders below the industry growth rate of less than 3 percent.

It is worth pointing out that the industry growth rates have dropped 30 percent since before the global financial crisis, and before government means testing and other detrimental policies were introduced.

The healthcare business has been spending a significant amount of effort this year in rethinking its product sets. We introduced a new range of products that are designed to support people with refunds for activities designed for self-improvement, such as active lifestyles and some cosmetic services. This is a totally new product set that has no connection with traditional health insurance but allows us to expand our offerings for members and attract new customers. We are currently in the process of further refining our product designs before stepping up our marketing and distribution efforts for these products.

Our preventative health business, Remedy Healthcare, continued to experience strong demand, with the number of patients enrolled in or completing one of its programs passing the 46,000 mark.

We also had more than 56,000 patients visit an Australian Unity dental clinic. Since the end of the financial year we have welcomed a new dental clinic at Hughesdale in Melbourne, into the Australian Unity fold.

I would like to move on now to our retirement living business. This business has had a very positive year. As the Chairman has already mentioned, we recently opened our flagship new aged care facility, Rathdowne Place, not far from here in Carlton and you can see the building growing on the screen behind me. We had planned to fill it slowly to allow for staffing numbers to grow in line with resident demand, but found that the response from the community was so high that we had to speed up our plans. The 162-bed facility opened in April and is now two-thirds full.

Australian Unity's retirement living business model is to create service-rich communities that provide a continuum of care to allow older Australians to both age-in-place and age in a community of their choosing. In line with this strategy, we plan to build independent living units within the same complex and to further expand our footprint into the nearby community with the provision of home care packages.

The business was challenged during the year by the introduction of the Living Longer

Living Better reforms of the previous government. We believe these reforms add significant complexity to consumers when they are making decisions about their care and accommodation needs. To illustrate this, we created a decision-making map of the kinds of decisions that people now need to make to protect their financial wellbeing when they are moving into aged care. I don't propose to go through this, but you can see the level of complexity involved. It is essentially a financial exam government is inflicting on 80-year old homeowners in Australia. We are actively working with Government to encourage it to review and reconsider some of these setttings.

Business highlights include strong occupancy rates across the portfolio of villages we operate in Victoria and NSW.

We almost doubled the revenue of the home care business, and increased staff by more than 50 percent.

We continue to develop our properties in Mornington, Victoria, and Sienna Grange in Port Macquarie. We plan to open the Peninsula Grange aged care facility in Mornington over the coming year.

Overall, our retirement living operations recorded a 22 percent increase in revenue to $89.2 million and a 69 percent increase in adjusted EBITDA of $21.3 million for the year, up from $12.6 million.

I will now turn to our Investments business. This business area is connected to external risk. This year the patchiness of the financial markets, along with the strong Australian dollar and low interest rates during the financial year under review affected the division’s performance in both asset management and in the banking area.

As members may be aware, the Investments business operates in the direct, retail and institutional markets with in-house asset management skills in property and specialised products. We have also built a boutique asset management structure to provide customers with access to experts in Australian and international equities and fixed interest.

The business reported an 8 percent decrease in revenue to $103.2 million and a 10 percent decrease in adjusted EBITDA to $13.8 million.

This business did perform well on the measure of funds under management, growing 4 percent to $7.4 billion.

At the end of the financial year, Big Sky Building Society had total on-balance sheet assets of more than $700 million compared to $618 million the previous year. The business was also awarded “best cash management account” in the Smart Investor Blue Ribbon Awards in both 2013 and 2014.

Another significant highlight was the completion of Phase 1 of the $90 million expansion of Waurn Ponds shopping centre in Geelong. This is a property that is managed by us on behalf of investors. The subsequent sale of a 50 percent stake in the property resulted in a capital gain for those investors and will allow us to explore other opportunities in the retail property sector.

Once again, the Personal Financial Services business had a very positive year, building on its inaugural positive contribution in last year's results.

Revenue was $39.8 million, up 18 percent; and adjusted EBITDA increased to $2.3 million, up from $2.1 million in the prior year.

This positive result is also reflected in an increase in Funds Under Advice of 12 percent, to almost $3.5 billion.

As in prior years, these financial results reflect a continuing confidence of advisers wishing to join our dealership group, with 14 new adviser practices over the year. Australian Unity is now in the top 20 financial planning businesses outside of those owned by the large banks and life insurers. We believe advisers are attracted to join us because of our focus on improving the financial wellbeing of our clients, the open architecture advice environment and the effectiveness of the team and systems we have in place.

Our relationships with small accounting practices across Australia also contributes to our overall success. This approach enables accountants to better meet the broader financial wellbeing needs of their clients.

We hope to continue to grow this business, but will always balance the growth plans with our commitment to providing strong levels of support for advisers and their clients.

I would finally like to note the contribution of the company's employees. This has been an exciting year, but also one that has not been without its challenges.

Our regular survey of employees this year indicated that the people who work at Australia Unity are by and large strongly engaged with the company and its activities.

I am privileged to lead a dedicated group of executives, senior managers and staff who are engaged with the company's vision and determined to work hard on behalf of members and customers in delivering services that they value and I thank them for their efforts.

Ladies and Gentlemen, it is my submission that the company remains a strong part of the business and general community and continues to operate soundly in a dynamic environment. Our results reflect our ambition to grow in a sustainable and valuable way for our members and customers. I thank you for your continued support.

END GROUP MANAGING DIRECTOR'S ADDRESS