NZX/ASX and Media Release

HEARTLAND POSTS HALF YEAR PROFIT OF $33.1 MILLION

19 February 2019

Heartland Group Holdings Limited (NZX/ASX:HGH) (**Heartland Group**) achieved a net profit after tax (**NPAT**) of $33.1 million for the six months ended 31 December 2018, an increase of 6.5% from the six months ended 31 December 2017 (previous corresponding reporting period).[1]

Highlights for the six months ended 31 December 2018 include:

- Net profit after tax $33.1 million, up 6.5%
- Gross finance receivables $4.2 billion, up 11.9% (annualised growth excluding the impact of changes in foreign currency exchange rates)
- Return on equity (ROE) 10.3%
- NIM 4.36%
- Cost to income ratio 42.5%, down from 42.9% in the previous corresponding reporting period
- 2019 Interim Dividend 3.5cps
- Corporate restructure successfully completed – removing the funding constraints on growth in Australia previously arising from Reserve Bank of New Zealand regulations, and providing greater flexibility to take advantage of growth opportunities and capital raising options in New Zealand and Australia
- ASX foreign exempt listing successfully completed

---

[1] *This announcement is based on the 31 December 2018 unaudited interim consolidated financial statements of Heartland Group Holdings Limited (HGH). Following a corporate restructure on 31 October 2018, Heartland Bank Limited (HBL) became a 100% controlled subsidiary of HGH and ownership of the Australian group of companies (comprising Heartland Australia Holdings Pty Limited) transferred from HBL to HGH. The interim consolidated financial statements of HGH comprise results for HBL up to 31 October 2018, and HGH from 1 November 2018 to 31 December 2018. As common control has remained the same both before and after the corporate restructure, management believe that the operations of HGH from 1 November 2018 are directly comparable to those of HBL prior to 1 November 2018. All comparative results are based on 31 December 2017 unaudited interim consolidated financial statements of HBL.*

FINANCIAL POSITION

Gross finance receivables increased by $240.7 million (11.9% annualised growth) in the six month period, offset by adverse foreign exchange impact on Australian receivables of $32.0 million resulting in reported 10.3% annualised growth to $4,226.2 million as at 31 December 2018.

- New Zealand Reverse Mortgages gross receivables increased $24.6 million (10.7% annualised growth) to $481.5 million as at 31 December 2018.
- Motor gross receivables increased $79.0 million (16.3% annualised growth) to $1,039.9 million as at 31 December 2018.
- Harmoney and other personal lending gross receivables increased $34.7 million (44.3% annualised growth excluding the impact of changes in foreign currency exchange rates). New Zealand Harmoney and other personal lending increased 37.7% (annualised growth) to $153.6 million while Australia Harmoney increased 77.0% (annualised growth excluding the impact of changes in foreign currency exchange rates) to $35.0 million.
- Business gross receivables increased $32.4 million (6.1% annualised growth) to $1,093.8 million as at 31 December 2018, with Business Intermediated lending up $72.3 million (44.3% annualised growth) and Open for Business (**O4B**) lending up $25.5 million (56.2% annualised growth) to $115.4 million as at 31 December 2018.
- Australian Reverse Mortgages gross receivables increased $85.1 million (24.9% annualised growth excluding the impact of changes in foreign currency exchange rates) to $733.3 million in the six months to 31 December 2018. This was offset by an adverse movement in foreign currency translation of $29.8 million, resulting in reported growth of $55.3 million (16.2% annualised growth) to $733.3 million as at 31 December 2018.

Net finance receivables increased by $214.3 million (10.7% annualised growth) offset by the impact of changes in foreign currency exchange rates of $32.0 million resulting in reported 9.1% annualised growth to $4,167.3 million as at 31 December 2018.

Total assets increased by $205.5 million from 30 June 2018 due to the increase in net finance receivables and cash, cash equivalents and investments.

Borrowings increased by $231.7 million from 30 June 2018 (12.1% annualised growth), including an increase in retail deposits of $106.6 million (7.3% annualised growth) funding the 9.0% annualised growth in New Zealand gross finance receivables with additional funding through securitised borrowings.

During the reporting period, Net Assets decreased by $10.0 million to $654.2 million as at 31 December 2018. Net Tangible Assets (NTA) decreased by $13.3 million to $571.1 million as at 31 December 2018. NTA per share was $1.01 at 31 December 2018 compared to $1.04 at 30 June 2018. This reduction in NTA per share is primarily due to opening retained earnings being restated by $18.2 million upon the initial adoption of IFRS9, accounting for $0.03 NTA per share, with a corresponding increase in provisions for impairments.

FINANCIAL PERFORMANCE

Profitability

NPAT was $33.1 million for the six months ended 31 December 2018. This is an increase of $2.0 million (6.5%) from the previous corresponding reporting period.

Return on Equity (ROE) for Heartland Group reduced from 10.8% (annualised) for the six months ended 31 December 2017 to 10.3% (annualised) for the six months ended 31 December 2018. The reduced ROE is a result of higher average equity for the current period.

Earnings per share for Heartland Group for the six months ended 31 December 2018 was 5.9 cents per share, compared to 6.0 cents per share for the six months ended 31 December 2017.

Net Operating Income

Net Operating Income (**NOI**) was $102.1 million, an increase of $8.2 million (8.7%) compared to the previous corresponding reporting period.

Heartland Group's Net Interest Margin (**NIM**) for the six months ended 31 December 2018 was 4.36% compared to 4.44% for the six months ended 31 December 2017. NIM was impacted by $1.1m of break costs incurred due to the early repayment of the Tier 2 Australian dollar subordinated bond, and was 4.41% excluding those break costs. The Tier 2 bond has been replaced by lower cost funding, which is expected to result in lower interest expense in the second half of the financial year.

Costs

Operating costs were $43.4 million, an increase of $3.1 million (7.7%) compared to the previous corresponding reporting period. Higher operating expenses are due to growth, one-off corporate restructure and ASX listing costs of $0.9 million and one-off foreign currency costs of $1.2 million incurred in relation to the corporate restructure.[2]

The cost to income ratio improved to 42.5% compared to 42.9% in the previous corresponding reporting period, although excluding one-off costs related to the corporate restructure, the cost to income ratio improved further to 40.4%.

Impairments

The new accounting standard relating to impairments, IFRS9, came into effect on 1 July 2018. This new standard requires impairments to be provided for on an expected loss basis at the date of loan origination. For the period ending 31 December 2018, whilst receivables have performed largely in line with expectations, there has been an increase in impairment expense due to how changes in product mix and growth are provided for under new IFRS9 methodology.

---

[2] These costs arise from adverse foreign currency movements due to a foreign exchange exposure at the time of the corporate restructure. This exposure has subsequently been hedged, removing the potential for any further negative impact.

Impaired asset expense increased $2.9 million (27.6%) to $13.3 million for the six months ended 31 December 2018. $2.2 million of that increase is a result of the new IFRS9 methodology, which is greater than anticipated due to the timing and mix of our loan portfolio growth.

As a result, impaired asset expense as a percentage of average gross finance receivables increased from 0.58% as at 30 June 2018 to 0.64% as at 31 December 2018.

Despite the increase, underlying receivables performance is stable. Excluding the $2.2 million of impairments due to the new IFRS9 methodology:

- impaired asset expense as a percentage of average gross finance receivables reduced to 0.53%;
- impairment expense in Motor was 0.84% compared to 0.95% in the previous corresponding reporting period; and
- Business lending impairment expense was 0.63% compared to 0.55% in the previous corresponding reporting period (largely due to the growth in O4B).

For Reverse Mortgages, which are valued using fair value methodology, the risk remained stable.

The initial adoption of IFRS9 also resulted in opening adjustments to provisions for impairments of $25.3 million and retained earnings of $18.2 million, after allowance for the deferred tax benefit.

Net impaired and past due loans over 90 days decreased by $2.0 million from 30 June 2018 to $71.8 million as at 31 December 2018, and as a percentage of gross receivables decreased from 1.84% as at 30 June 2018 to 1.70% as at 31 December 2018.

BUSINESS PERFORMANCE

New Zealand Reverse Mortgages

New Zealand Reverse Mortgages net operating income was $10.0 million, an increase of $1.2 million or 13.5% from the previous corresponding reporting period. New Zealand Reverse Mortgages gross receivables increased $24.6 million (10.7% annualised growth) during the period to $481.5 million as at 31 December 2018.

Motor

Motor vehicle net operating income was $28.2 million, an increase of $2.3 million or 8.9% from the previous corresponding reporting period. Motor vehicle gross receivables increased $79.0 million (16.3% annualised growth) to $1,039.9 million as at 31 December 2018 through Motor Dealer lending (car dealerships, brokers and partnerships such as Holden and Jaguar/Land Rover).

Harmoney and other personal lending

Harmoney and other personal lending net operating income was $9.5 million, an increase of $2.6 million or 38.0% from the previous corresponding reporting period. Harmoney and other personal lending achieved growth in gross receivables of $34.7 million (44.3% annualised growth), offset by a small foreign currency movement of $1.3 million on Australia Harmoney receivables, to $188.6 million as at 31 December 2018.

Heartland has a 13.34% shareholding in Harmoney.

Business

Business lending net operating income was $27.6 million, an increase of $1.5 million or 5.7% from the previous corresponding reporting period.

Business gross receivables increased by $32.4 million (6.1% annualised growth) to $1,093.8 million as at 31 December 2018. Heartland's growth focus continues to be on Intermediated Business and lending through our digital platform, Open for Business. These markets continue to deliver results with Business Intermediated lending up $72.3 million (44.3% annualised growth) and Open for Business lending up $25.5 million (56.2% annualised growth) to $115.4 million as at 31 December 2018. Business Relationship lending continues to be managed down as part of our strategy to reduce concentration risk resulting in Business Relationship gross receivables reducing by $65 million in the period.

Rural

Rural lending net operating income was $15.8 million, a decrease of $0.4 million or 2.7% from the previous corresponding reporting period.

Rural gross receivables decreased in the period by $15.0 million (4.5% annualised decrease). Similarly to Business Relationship lending, we continue to manage down large Rural Relationship lending to reduce concentration risk in this area.

Australia

Net operating income from Australian operations (comprising Australian Reverse Mortgages and business lending to Spotcap) was $11.8 million, an increase of $2.2 million or 23.3% from the previous corresponding reporting period.

Australian Reverse Mortgages gross receivables grew by $85.1 million (24.9% annualised growth) in the six months to 31 December 2018. This growth was offset by an adverse movement in foreign currency translation of $29.8 million, resulting in a reported growth of $55.3 million (16.2% annualised growth) to gross receivables of $733.3 million as at 31 December 2018. Australian business lending to Spotcap increased $4.3 million (45.4% annualised growth), also offset by a small adverse movement in foreign currency translation of $0.8 million to $22.2 million as at 31 December 2018.

Other

New Zealand residential mortgages decreased by $4.4 million to $21.3 million as at 31 December 2018 as Heartland continues to run-down this portfolio.

FUNDING AND LIQUIDITY

The corporate restructure was completed in October 2018 and provides the group greater flexibility for capital and funding options going forward. The Tier 2 Notes (A$20 million) were repaid as part of this corporate restructure.

Retail Deposits grew $106.6 million (7.3% annualised growth) to $3.0 billion as at 31 December 2018. Heartland continues to be a strong market leader in term deposit and call account offerings, providing customers with competitive interest rates and unlimited on call access to their money.

CORPORATE RESTRUCTURE AND ASX LISTING

Under the corporate restructure, all of the shares in Heartland Bank Limited (Heartland Bank) were exchanged for shares in Heartland Group Holdings Limited (Heartland Group), and Heartland Bank became a wholly owned subsidiary of Heartland Group. In addition, the Australian group of companies were transferred from Heartland Bank to Heartland Group.

The corporate restructure provides Heartland greater flexibility to explore and take advantage of future growth opportunities and funding options in New Zealand and Australia outside of the banking group. This helps to enable Heartland to achieve the strategic priorities set out below.

REGULATORY UPDATE

There has been considerable recent scrutiny of the financial services sector, with the Financial Markets Authority (**FMA**) and Reserve Bank of New Zealand (**Reserve Bank**) reporting on their findings following a review of conduct and culture in New Zealand retail banks, the Australian Securities and Investments Commission (**ASIC**) releasing a report following its review of reverse mortgages in Australia, and the Australian Royal Commission publishing its final report on its findings on misconduct in the Australian banking, superannuation and financial services industry.

The FMA and Reserve Bank report found no evidence of widespread conduct and culture issues; however, the findings did reveal opportunities to strengthen the governance and management of conduct risks industry-wide. Heartland is required to develop a plan to address the findings, to be completed by end of March 2019, and will continue to focus on iterative improvement of conduct and culture bank-wide.

ASIC's review of reverse mortgage lending in Australia highlighted the increasing need for equity release products and that "reverse mortgage products can help many Australians achieve a better quality of life in retirement".[3] The report also identified several areas for improvement from lenders, and Heartland has already acted on these and is very much aligned with ASIC in being committed to ensuring customers make informed decisions. Heartland is a member of a working group which was formed to ensure that ASIC's expectations for improved lending practices for reverse mortgages are satisfied.

---

[3] ASIC Deputy Chair Peter Kell, ASIC Review of reverse mortgage lending in Australia (report 586)

The final Royal Commission report makes a number of recommendations, including changes in the way that brokers are remunerated for introducing clients to financial service providers.

Heartland does not expect any of the reports, or any expected legislative response to any of them, to have any material impact on Heartland's business.

Finally, as noted in the capital requirements section below, the Reserve Bank also released a consultation paper seeking public views on a proposal to increase the minimum level of regulatory capital in the banking system. At this stage, there is some detail to be clarified and the Reserve Bank is yet to make any final decisions.

STRATEGIC PRIORITIES

Following the corporate restructure, the Group's activity comprises three areas of strategic focus: Australia Reverse Mortgages, New Zealand Banking and Digital Platform Services.

Australia Reverse Mortgages

Australia Reverse Mortgages continues to experience strong growth in a market with compelling fundamentals. Population demographics are accelerating favourably with the number of Australians over 65 being projected to grow from 15% of the population in 2018 to 23% by 2050.[4]

This provides Heartland with a unique opportunity as the primary originator of reverse mortgages in Australia. Heartland plans to accelerate growth through raising product awareness under dedicated marketing initiatives, including a television campaign (TVC), to reach the total estimated market of approximately A$6billion[5]**.** Heartland intends to leverage off the key experiences and success achieved in the New Zealand market.

The combination of favourable demographics, limited active originators and raising product awareness through increased marketing activity presents the opportunity for significant growth and to cement Heartland's position as the market leader in reverse mortgage origination in Australia.

To support this growth opportunity, Heartland continues to diversify its sources of funding and to fund growth with improved capital efficiency. Heartland Australia has established an A$ medium-term note programme, has engaged with a number of Australian fixed income investors and is in the process of launching an inaugural A$ bond offering. A number of other options are currently being explored, including additional warehouse facilities and long-term funding sourced offshore.

Digital Platform Services

The Digital strategy aims to deliver three main benefits:

- simple and fast customer service

---

[4] Australian Bureau of Statistics

[5] Based on peak penetration from the Deloitte annual reverse mortgage report 2015, combined with current Australian Bureau of Statistics population and housing statistics and APRA and HSF reverse mortgage data.

- greater customer reach
- low cost on-boarding and transaction processing

The three major areas of activity have been: Deposits, where 10 percent of deposit customers use the Heartland mobile app (an increase of 20 percent over the past three months); Australian Reverse Mortgages, where 30 percent of customers are direct, and 93 percent of those are generated online; and O4B.

O4B targets Small to Medium Enterprises (SMEs) with loans of less than $250,000. Automated approvals are possible within minutes for loans up to $75,000.

Since 2015 O4B has grown to $115.4 million (gross receivables), including an annualised growth of 56.2 percent in the six months to December 2018. During this period the offering has been continuously improved to ensure a frictionless end to end process.

The platform has reached a stage where increased marketing is required to develop awareness and extend reach into a target market estimated to be $5.6 billion.[6] Consideration is being given to attracting external investment from specialist investors who can help Heartland to take O4B to the next stage of growth. An update will be provided to the market in due course should any transaction eventuate.

Heartland Bank Limited

Heartland Bank's focus will remain on delivering best or only products to depositors and borrowers, through continued growth in core lending activities:

- New Zealand Reverse Mortgages (gross receivables annualised growth of 10.7 percent),
- Business lending (gross receivables annualised growth of 6.1 percent),
- Motor Finance (gross finance receivables annualised growth of 16.3 percent), and
- Harmoney and other consumer lending (gross receivables annualised growth of 44.3 percent)

Like Australian Reverse Mortgages, there are significant growth opportunities for New Zealand Reverse Mortgages, and Heartland intends to continue to leverage off its success achieved to date in the New Zealand market.

Larger Business and Rural relationship lending is being managed down as part of our strategy to reduce concentration risk in these areas. Options are also being considered with regard to the acceleration of the run down which would free up capital to be dedicated to core lending activities.

[6] Based on the number of SMEs in New Zealand (Ministry of Business, Innovation and Employment Small Business Fact Sheet 2017) with a turnover, risk profile and needs consistent with O4B.

INTERIM DIVIDEND

Heartland is pleased to declare a 2019 interim dividend of 3.5 cents per share. The interim dividend will be paid on Friday 29 March 2019 (**Payment Date**) to shareholders on the company's register as at 5.00pm on Friday 15 March 2019 (**Record Date**) and will be fully imputed.

In December 2018, Heartland Group established a DRP, giving eligible shareholders opportunity to reinvest some or all of their dividend payments into new ordinary shares. The DRP will apply to the interim dividend with a 2.5 percent discount[7]. Shareholders are encouraged to participate in order to support Heartland's capital needs given its strong asset growth.

It is important to note that shareholders' previous election under the Heartland Bank Limited DRP has not automatically been carried across to the Heartland Group DRP. Shareholders who previously participated in the Heartland Bank Limited DRP, and wish to continue to receive shares instead of dividend payments, must make a new election to participate in the Heartland Group DRP in one of the ways specified in the DRP offer document by 5.00pm on 18 March 2019 (being the first trading day after the Record Date). The DRP offer document and participation form is available on our shareholder website at: https://shareholders.heartland.co.nz/shareholder-resources/dividends.

OUTLOOK

Underlying balance sheet growth supports a result in line with the original forecast in the range of $75 million to $77 million. However, the one-off costs incurred in relation to the corporate restructure and ASX listing, and the higher than anticipated impact of IFRS9 as a result of receivables growth, have caused some pressure on earnings. Whilst Heartland considers that it could still achieve a result at the bottom end of guidance, it would come at a cost to further investment in growth. Accordingly, an updated guidance range of $73 million to $75 million is now considered prudent. The midpoint of that range would see the delivery of approximately 10% NPAT growth for FY19 compared to FY18.

- Ends -

For further information, please contact:

Jeff Greenslade
Chief Executive Officer
MOB 021 563 5493
jeff.greenslade@heartland.co.nz

Julia Belk
Investor Relations Manager
DDI 09 926 3837
julia.belk@heartland.co.nz

---

[7] That is, the strike price under the DRP will be 97.5 percent 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 Heartland Group Holdings Limited DRP offer document dated 10 December 2018.