

2022 Annual Shareholder Meeting: Group Chief Executive Officer's Address

1. Introduction

E ngā mana, e ngā reo, e ngā rau rangatira, tēnā koutou katoa.

Greetings to all of you, all voices, all authorities and leaders.

E ngā iwi maha o te motu whānui, kei te mihi, kei te mihi.

To the many iwi across the country, I acknowledge you as tangata whenua.

Ki a koutou katoa kua hui mai nei i tēnei rā, tēnā tātou katoa.

To everyone joining us today, thank you.

To say that these are trying times seems glib when faced both with the flow of negative headlines and the complexities at work behind them. The post-pandemic world is fraught with “not for a decade” levels of economic turmoil. Escalating inflation has impacted interest rates and created uncertainty and volatility. Sovereign debt yields have pushed up, raising the discount on future cash flows, reducing asset values.

Despite all this, thus far, conditions are not as bad as post Global Financial Crisis (**GFC**) in 2009-2011. There is very low unemployment and there has been no liquidity or balance sheet crisis.

However, we do not expect our customers to be immune from the economic pressures and as we did in the last two years of the pandemic, we will continue to support them.

But above all, as a growth business, we must keep our eyes on the long-term goals, while ensuring we are able to meet the short-term challenges.

Heartland Group Holdings Limited (**Heartland**) has a strong pedigree in successfully navigating uncertainty. Heartland was forged in the aftermath of the GFC. From difficult times, we have learned lessons.

1. The first is the value of having positions in markets that are either immune to macro-economic stress or are resilient. The best example of this is Reverse Mortgages where growth in the first quarter of the financial year ending 30 June 2023 (**FY2023**) of \$44 million (or 24.4% annualised) was achieved in New Zealand and A\$55 million (18.9% annualised) in Australia, while loan to value ratios remain at conservative levels. We expect resilience in Livestock lending where demand for protein remains constant despite the conditions. And we hope for good growth over the financial year. We anticipate some stress on our Motor loans, recalling however, that during the GFC, Motor loans arrears and losses increased, but were absorbable. And it is pleasing to see Motor growth is returning to levels pre- changes to the New Zealand Credit Contracts and Consumer Finance Act 2003 and the Credit Contracts and Consumer Finance Regulations 2004 (**CCCFA**), introduced on 1 December 2021.
2. Secondly, it is vital to be agile and adapt. Resisting despair with every negative headline, seeking

out opportunities in adversity. The recent announcement of our intention to acquire Challenger Bank Limited (**Challenger Bank**) occurred at an opportune time for values. The cost of purchasing a bank in Australia has moved in our favour.

Despite the economic situation, Heartland is positioned for a transformation. We will continue to challenge operating models, remaining true to our best or only strategy, extracting the benefits of digitalisation: generating efficiencies and delivering market differentiation. But the game-changer is the opportunity to purchase a bank in Australia which drives a quantum shift in growth potential.

I will talk to that in a moment, but first I will update the four pillars of our best or only strategy:

1. Business as Usual Growth
2. Frictionless Service at the Lowest Cost
3. Expansion in Australia
4. Acquisitions.

2. Business as Usual Growth

As the Chair outlined, Heartland achieved earnings of \$95.1 million in the financial year ended 30 June 2022 (**FY2022**), being at the top end of the guidance range, based on 15.3% growth in gross finance receivables (**Receivables**)¹, excluding the impact of the StockCo Holdings 2 Pty Ltd and StockCo Australia Management Pty Limited (together, **StockCo Australia**) acquisition. This level of growth further evidences the resilience of Heartland's market position.

At the same time, Heartland's portfolio mix has moved towards higher quality assets. This is due to four factors:

1. higher aggregate growth in Reverse Mortgages and online Home Loans
2. the introduction of lower impairment livestock loans
3. a shift in the Motor book towards higher quality loans, and
4. the run-off of higher risk personal lending.

Reverse Mortgages have consistently performed well and are expected to continue to do so in this environment where rising costs puts pressure on household budgets. In FY2022, NZ Reverse Mortgages helped their 20,000th customer and saw a 19.9% increase in Receivables compared with the financial year ended 30 June 2021 (**FY2021**). Australian Reverse Mortgages saw a 15.2% increase in Receivables, and grew market share from 29% to 33%². The potential addressable market for reverse mortgages in Australia is estimated to be \$10-15 billion³ – demonstrating clear opportunity for ongoing growth.

In FY2022, Heartland Bank's Livestock business enjoyed record growth from an increase in customers and facility utilisation rates reaching an historic high. We expect the global demand for protein to drive further growth for Livestock in New Zealand and our recently acquired business, StockCo Australia.

Supply chain disruptions and the unintended effects of the CCCFA changes made in December 2021 caused ebbs and flows in Motor with some normalisation in the last quarter. The portfolio's 7%

¹ Receivables include Reverse Mortgages and StockCo Australia.

² Based on APRA ADI Property Exposure and Heartland Finance data as at 31 March 2021 and 31 March 2022.

³ According to Deloitte at the 2021 Three Pillars Forum.

increase in Receivables for FY2022 was not as strong as we would typically expect. However, the last quarter alone produced almost a doubling in growth on the previous quarter.

Online Home Loans were also affected by the recent CCCFA changes, and more recently by a slowdown in house sales. However, the refinance market is attractive and a book size in excess of \$400 million by the end of FY2023 is targeted.

A more cautious approach will be taken in personal and small business lending given the current environment. This may impact on growth and net interest margin but is prudent risk management.

3. Frictionless Service at the Lowest Cost

Ka whawhai tonu mātou.

The path to delivering frictionless service is a never-ending journey.

Technology moves quickly – faster than people – though behaviours are changing, driven by pandemic necessity. The trend is moving ineluctably towards self-service. This capability via digital platforms and apps has been delivered across both sides of the Tasman, and more is in development.

Telephone wait times are constantly rising. Self-service removes this and other forms of customer friction while creating scale and efficiencies. This flows through to our cost-to-income ratio.

On an underlying basis, the cost to income ratio reduced to 42.5% in FY2022. While this might wobble in the short-term due to investment, we are committed to reducing this further over the long-term. Ultimately, a lower cost-to-income ratio allows us to be more competitive.

4. Expansion in Australia and Acquisitions

Expansion in Australia has been exemplified by Reverse Mortgages growth. The loan book was A\$377 million in April 2014 when acquired by Heartland, and is now just over A\$1 billion.

The acquisition of StockCo Australia in May this year extended Heartland's best or only strategy into the Australian livestock finance market.

In order to realise the full potential of our Australian businesses, we require access to deep and efficient pools of funding. In August, we announced our intention to establish or acquire an authorised deposit-taking institution (**ADI**) licence in Australia. As confirmed recently, we have now entered into an agreement for the acquisition of Challenger Bank from ASX-listed investment management firm, Challenger Limited.

Challenger Bank is an established ADI which offers customers a range of savings and lending products, including government-guaranteed retail term deposits and home loans. It has invested in systems and, in particular, has a very efficient and scalable deposit platform.

Subject to regulatory approvals and transaction completion, Heartland's existing businesses in Australia will be transferred to sit in or under Challenger Bank. This would be Heartland's vehicle for growth in Australia.

The consideration payable by Heartland on completion is expected to be A\$36 million, subject to

adjustments for net assets delivered at completion. We intend to cover this cost through existing resources.

It is important to pause and consider for a moment the opportunity we have of operating as a bank in Australia. There is not just the potential to lift our margin through lower costs of funds, but critically, we also have available to us a much larger market to extend our best or only strategy. Think of the growth we have achieved in New Zealand and then apply that to a market which is several times larger. In New Zealand, Heartland's best or only strategy has driven a tripling of our size in the 10 years since becoming a bank.

5. Conclusion

To conclude, I can confirm that we remain on track to deliver FY2023 net profit after tax within the guidance range of \$109 to \$114 million, excluding any impacts of fair value changes on equity investments held and excluding the impact of the de-designation of derivatives.

Our Heartland employees are crucial to meeting this target and delivering against our strategy. In what has been a challenging year, I would like to thank our employees for their exceptional efforts and commitment to our customers.

He manawa whenua, he manawa tangata, Ko Heartland tēnei.

This is our Heartland.

Thank you also to our shareholders.

Tēnā koutou katoa.

Thank you all.