HEARTLAND BANK

Disclosure Statement

For the six months ended 31 December 2019

Contents

GENERAL INFORMATION

This Disclosure Statement has been issued by Heartland Bank Limited (the **Bank**) and its subsidiaries (collectively the **Banking Group**) for the six months ended 31 December 2019 in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the **Order**). The interim financial statements of the Banking Group for the six months ended 31 December 2019 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.

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

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 Banking Group were guaranteed.

DIRECTORS

All Directors of the Bank reside in New Zealand with the exception of Ellen Comerford who resides in Australia. Communications to the Directors can be sent to Heartland Bank Limited, 35 Teed Street, Newmarket, Auckland.

There have been no changes in the composition of the Board of Directors of the Bank since 30 June 2019 to the six months ended 31 December 2019.

Vanessa C M Stoddart has resigned from the Board of Directors effective 1 January 2020.

Shelley M Ruha was appointed to the Board of Directors as an independent non-executive director effective 1 January 2020.

AUDITOR

KPMG

KPMG Centre

18 Viaduct Harbour Avenue

Auckland

DIRECTORS' STATEMENTS

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

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.

During the six months ended 31 December 2019:

a. The Bank has complied with the conditions of registration applicable during the period except as noted on page 42.
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 the 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 businesses risks, and that those systems were being properly applied.

This Disclosure Statement is dated 28 February 2020 and has been signed by all the Directors.

B R Irvine (Chair)

K Morrison

J K Greenslade

G T Ricketts

E J Harvey

S M Ruha

E F Comerford

CONSOLIDATED INTERIM STATEMENT OF COMPREHENSIVE INCOME

For the six months ended 31 December 2019

$000's	NOTE	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Interest income	3	148,680	143,367	288,370
Interest expense	3	55,708	57,244	112,678
Net interest income		**92,972**	**86,123**	**175,692**
Operating lease income		2,910	2,871	5,262
Operating lease expenses		1,962	1,801	3,427
Net operating lease income		**948**	**1,070**	**1,835**
Lending and credit fee income		5,079	1,271	2,675
Other income		2,324	1,702	3,518
Net operating income		**101,323**	**90,166**	**183,720**
Operating expenses	4	44,498	41,159	78,210
Profit before impaired asset expense and income tax		**56,825**	**49,007**	**105,510**
Fair value gain on investment property		-	-	1,936
Impaired asset expense	5	8,975	13,164	20,554
Profit before income tax		**47,850**	**35,843**	**86,892**
Profit before income tax from discontinued operations	6	-	6,169	6,169
Income tax expense		12,954	11,616	24,762
Profit for the period/year		**34,896**	**30,396**	**68,299**
Other comprehensive income				
Items that are or may be reclassified subsequently to profit or loss:				
Effective portion of changes in fair value of derivative financial instruments, net of income tax		1,843	781	(4,762)
Movement in fair value reserve, net of income tax		(968)	170	2,968
Movement in foreign currency translation reserve, net of income tax		-	(4,229)	(4,229)
Items that will not be reclassified to profit or loss:				
Movement in defined benefit reserve, net of income tax		-	-	(86)
Other comprehensive expense for the year, net of income tax		**875**	**(3,278)**	**(6,109)**
Total comprehensive income for the period/year		**35,771**	**27,118**	**62,190**

Total comprehensive income for the period is attributable to the owner(s) of the Bank.

The notes on pages 11 to 41 are an integral part of this consolidated interim financial statement.

CONSOLIDATED INTERIM STATEMENT OF CHANGES IN EQUITY

For the six months ended 31 December 2019

$000's	NOTE	Share Capital	Employee Benefits Reserve	Foreign Currency Translation Reserve	Fair Value Reserve	Defined Benefit Reserve	Cash Flow Hedge Reserve	Retained Earnings	Total Equity
Unaudited - December 2019									
Balance at 1 July 2019		**553,239**	**-**	**-**	**4,558**	**171**	**(5,843)**	**51,265**	**603,390**
NZ IFRS 16 adjustment	1	-	-	-	-	-	-	(639)	(639)
Restated balance at beginning of period		**553,239**	**-**	**-**	**4,558**	**171**	**(5,843)**	**50,626**	**602,751**
Total comprehensive income for the period									
Profit for the period		-	-	-	-	-	-	34,896	34,896
Other comprehensive income/(loss) net of income tax		-	-	-	(968)	-	1,843	-	875
Total comprehensive income for the period		**-**	**-**	**-**	**(968)**	**-**	**1,843**	**34,896**	**35,771**
Contributions by and distributions to owners									
Dividends paid	9	-	-	-	-	-	-	(65,000)	(65,000)
Total transactions with owners		**-**	**-**	**-**	**-**	**-**	**-**	**(65,000)**	**(65,000)**
Balance as at 31 December 2019		**553,239**	**-**	**-**	**3,590**	**171**	**(4,000)**	**20,522**	**573,522**

$000's	NOTE	Share Capital	Employee Benefits Reserve	Foreign Currency Translation Reserve	Fair Value Reserve	Defined Benefit Reserve	Cash Flow Hedge Reserve	Retained Earnings	Total Equity
Unaudited - December 2018									
Balance at 1 July 2018		**542,315**	**2,559**	**1,260**	**1,590**	**257**	**(1,081)**	**117,260**	**664,160**
NZ IFRS 9 adjustment (Restated)		-	-	-	-	-	-	(19,283)	(19,283)
Restated balance at beginning of period		**542,315**	**2,559**	**1,260**	**1,590**	**257**	**(1,081)**	**97,977**	**644,877**
Total comprehensive income for the period									
Profit for the period		-	-	-	-	-	-	30,396	30,396
Other comprehensive income/(loss) net of income tax		-	-	(4,229)	170	-	781	-	(3,278)
Total comprehensive income for the period		**-**	**-**	**(4,229)**	**170**	**-**	**781**	**30,396**	**27,118**
Contributions by and distributions to owners									
Dividends paid	9	-	-	-	-	-	-	(30,808)	(30,808)
Dividends to Heartland Group Holdings Limited	9	-	-	-	-	-	-	(61,444)	(61,444)
Sale of business		-	-	2,969	-	-	-	(2,969)	-
Dividend reinvestment plan	9	8,584	-	-	-	-	-	-	8,584
Shares based payments		-	383	-	-	-	-	-	383
Total transactions with owners		**8,584**	**383**	**2,969**	**-**	**-**	**-**	**(95,221)**	**(83,285)**
Balance as at 31 December 2018		**550,899**	**2,942**	**-**	**1,760**	**257**	**(300)**	**33,152**	**588,710**

The notes on pages 11 to 41 are an integral part of this consolidated interim financial statement.

CONSOLIDATED INTERIM STATEMENT OF CHANGES IN EQUITY

For the six months ended 31 December 2019 (continued)

$000's	NOTE	Share Capital	Employee Benefits Reserve	Foreign Currency Translation Reserve	Fair Value Reserve	Defined Benefit Reserve	Cash Flow Hedge Reserve	Retained Earnings	Total Equity
Audited – June 2019									
Balance at 1 July 2018		**542,315**	**2,559**	**1,260**	**1,590**	**257**	**(1,081)**	**117,260**	**664,160**
NZ IFRS 9 adjustment		-	-	-	-	-	-	(19,283)	(19,283)
Restated balance at beginning of year		**542,315**	**2,559**	**1,260**	**1,590**	**257**	**(1,081)**	**97,977**	**644,877**
Total comprehensive income for the year									
Profit for the year		-	-	-	-	-	-	68,299	68,299
Other comprehensive income/(loss) net of income tax		-	-	(4,229)	2,968	(86)	(4,762)	-	(6,109)
Total comprehensive income for the year		**-**	**-**	**(4,229)**	**2,968**	**(86)**	**(4,762)**	**68,299**	**62,190**
Contributions by and distributions to owners									
Dividends paid	9	-	-	-	-	-	-	(30,808)	(30,808)
Dividends to Heartland Group Holdings Limited	9	-	-	-	-	-	-	(81,234)	(81,234)
Transfer of ownership		-	(297)	-	-	-	-	-	(297)
Sale of business		-	-	2,969	-	-	-	(2,969)	-
Dividend reinvestment plan	9	8,584	-	-	-	-	-	-	8,584
Share based payments		-	78	-	-	-	-	-	78
Shares vested		2,340	(2,340)	-	-	-	-	-	-
Total transactions with owners		**10,924**	**(2,559)**	**2,969**	**-**	**-**	**-**	**(115,011)**	**(103,677)**
Balance as at 30 June 2019		**553,239**	**-**	**-**	**4,558**	**171**	**(5,843)**	**51,265**	**603,390**

The notes on pages 11 to 41 are an integral part of this consolidated interim financial statement.

CONSOLIDATED INTERIM STATEMENT OF FINANCIAL POSITION

As at 31 December 2019

$000's	NOTE	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018 (Restated)	Audited 12 months to June 2019
Assets				
Cash and cash equivalents		122,737	75,770	45,228
Investments		307,958	318,961	354,928
Investment properties		11,132	9,196	11,132
Derivative financial instruments		10,806	1,238	12,650
Due from related parties	10(c)	2,063	47,923	21,177
Finance receivables	7(a)	3,101,366	2,984,609	3,029,231
Finance receivables - reverse mortgages	7(b)	586,003	478,037	561,211
Right of use assets		19,225	-	-
Operating lease vehicles		18,549	16,430	15,516
Other assets		14,969	15,265	20,379
Intangible assets		56,781	58,123	57,335
Deferred tax asset		10,019	12,077	9,948
Total assets		**4,261,608**	**4,017,629**	**4,138,735**
Liabilities				
Retail deposits	8	3,244,035	2,988,365	3,153,681
Other borrowings	8	385,163	424,401	345,273
Due to related parties	10(c)	2,138	-	-
Lease liabilities		20,623	-	-
Tax liabilities		6,133	851	5,667
Derivative financial instruments		9,843	148	10,372
Trade and other payables		20,151	15,154	20,352
Total liabilities		**3,688,086**	**3,428,919**	**3,535,345**
Equity				
Share capital	9	553,239	550,899	553,239
Retained earnings and other reserves		20,283	37,811	50,151
Total equity		**573,522**	**588,710**	**603,390**
Total equity and liabilities		**4,261,608**	**4,017,629**	**4,138,735**
Total interest earning and discount bearing assets		4,113,206	3,840,471	4,003,982
Total interest and discount bearing liabilities		3,617,793	3,396,306	3,497,499

The notes on pages 11 to 41 are an integral part of this consolidated interim financial statement.

CONSOLIDATED INTERIM STATEMENT OF CASH FLOWS

For the six months ended 31 December 2019

$000's	NOTE	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Cash flows from operating activities				
Interest received		159,811	144,412	292,851
Operating lease income received		2,449	2,961	2,930
Lending, credit fees and other income received		4,712	1,871	4,761
Operating inflows		**166,972**	**149,244**	**300,542**
Interest paid		(55,889)	(76,833)	(121,748)
Payments to suppliers and employees		(44,656)	(48,639)	(84,682)
Taxation paid		(9,888)	(15,907)	(21,888)
Operating outflows		**(110,433)**	**(141,379)**	**(228,318)**
Net cash flows from operating activities before changes in operating assets and liabilities		**56,539**	**7,865**	**72,224**
Proceeds from sale of operating lease vehicles		1,101	2,414	4,641
Purchase of operating lease vehicles		(6,613)	(2,996)	(5,495)
Net movement in finance receivables		(103,358)	(224,748)	(368,561)
Net movement in deposits		90,354	105,529	271,876
Net cash flows from / (applied to) operating activities		**38,023**	**(111,936)**	**(25,315)**
Cash flows from investing activities				
Sale of equity investments		12,477	-	-
Net decrease in investments		34,493	21,928	-
Total cash provided from investing activities		**46,970**	**21,928**	**-**
Purchase of office fit-out, equipment and intangible assets		(5,027)	(2,379)	(4,188)
Net increase in investments		-	-	(11,468)
Total cash applied to investing activities		**(5,027)**	**(2,379)**	**(15,656)**
Net cash flows from / (applied to) investing activities		**41,943**	**19,549**	**(15,656)**
Cash flows from financing activities				
Net increase in wholesale funding		41,876	232,404	45,236
Proceeds from issue of Unsubordinated Notes		-	-	125,000
Proceeds from related party repayments		21,252	-	-
Total cash provided from financing activities		**63,128**	**232,404**	**170,236**
Dividends paid	9	(65,000)	(22,224)	(42,014)
Repayments of subordinated Notes		-	(22,846)	(22,846)
Repayments of leasing liabilities		(585)	-	-
Total cash applied to financing activities		**(65,585)**	**(45,070)**	**(64,860)**
Net cash flows from / (applied to) financing activities		**(2,457)**	**187,334**	**105,376**
Net increase in cash held		**77,509**	**94,947**	**64,405**
Opening cash and cash equivalents		45,228	49,588	49,588
Cash transferred on corporate restructure		-	(68,765)	(68,765)
Closing cash and cash equivalents		**122,737**	**75,770**	**45,228**

The notes on pages 11 to 41 are an integral part of this consolidated interim financial statement.

CONSOLIDATED INTERIM STATEMENT OF CASH FLOWS

For the six months ended 31 December 2019 (continued)

$000's	NOTE	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Profit for the period		**34,896**	**30,396**	**68,299**
Add / (less) non-cash items:				
Depreciation and amortisation expense		4,204	2,692	5,754
Depreciation on lease vehicles		1,962	1,681	3,363
Capitalised net interest income		(6,692)	(13,944)	(11,886)
Impaired asset expense		8,975	13,164	21,181
Provision transfer on demerger		-	619	(1,936)
Total non-cash items		**8,449**	**4,212**	**16,476**
Add / (less) movements in operating assets and liabilities:				
Finance receivables		(103,357)	(224,748)	(368,561)
Operating lease vehicles		(4,652)	(582)	(1,354)
Other assets		(6,370)	(3,356)	(6,584)
Right of use asset		19,225	-	-
Current tax		(79)	(8,561)	(3,744)
Derivative financial instruments revaluation		348	(1,948)	(8,676)
Deferred tax		(71)	(7,006)	1,547
Deposits		90,354	105,529	271,876
Other liabilities		(720)	(5,872)	5,406
Total movements in operating assets and liabilities		**(5,322)**	**(146,544)**	**(110,090)**
Net cash flows from / (applied to) operating activities		**38,023**	**(111,936)**	**(25,315)**

The notes on pages 11 to 41 are an integral part of this consolidated interim financial statement.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the 6 months ended 31 December 2019

1 Financial statements preparation

Basis of reporting

The interim financial statements of the Banking Group incorporated in this Disclosure Statement have been prepared in accordance with the Order, Generally Accepted Accounting Practice in New Zealand (NZ GAAP) as defined in the Financial Reporting Act 2013, NZ IAS 34 Interim Financial Reporting as appropriate for publicly accountable for-profit entities and IAS 34 Interim Financial Reporting.

The disclosure statement does not include all notes of the type normally included in an annual financial report. Accordingly, this report is to be read in conjunction with the Disclosure Statement for the year ended 30 June 2019 and any public announcements made by the bank during the interim reporting period.

The interim financial statements presented here are for the following periods:

- 6 month period ended 31 December 2019 – Unaudited
- 6 month period ended 31 December 2018 – Unaudited
- 12 month period ended 30 June 2019 – Audited

The accounting policies adopted are consistent with those of the previous financial year and corresponding interim reporting period with the exception of the adoption of new and amended standards as set out below.

Impact of adopting NZ IFRS 16 Leases

The Banking Group has adopted NZ IFRS 16 retrospectively from 1 July 2019, but has not restated comparatives for the 2019 reporting period, as permitted under the specific transitional provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 July 2019.

Accounting treatment for leasing activities

The Bank 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.

Until 30 June 2019, leases of property, plant and equipment were classified as either finance or operating leases. Payments made under operating leases (net of any incentives received from the lessor) were charged to profit or loss.

From 1 July 2019, leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Banking Group. The right-of-use assets are initially measured at cost, comprising the amount of the initial measurement of lease liability, any lease payments made at or before the commencement date less any lease incentives received, any initial direct costs and restoration costs. The right-of-use asset is depreciated over the shorter of the asset's estimated useful life and the lease term on a straight-line basis. The estimated useful lives of right-of-use assets are determined on the same basis as those of property, plant and equipment.

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

Payments associated with short-term leases and leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less.

On adoption of NZ IFRS 16, the Banking Group recognised lease liabilities in relation to leases which had previously been classified as ‘operating leases’ under the principles of NZ IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee’s incremental borrowing rate as at 1 July 2019. The weighted average lessee’s incremental borrowing rate applied to the lease liabilities on 1 July 2019 was 2.9%.

1 Financial statements preparation (continued)

The Banking Group elected not to reassess whether a contract is, or contains a lease at the date of initial application. Instead, for contracts entered into before the transition date, the Banking Group relied on its assessment made applying NZ IAS 17 and NZ IFRIC 4 Determining whether an Arrangement contains a Lease.

$000's	
Operating lease commitments as at 30 June 2019	**11,573**
Discounted using the Banking Group's incremental borrowing rate on initial application	(1,019)
Adjustments relating to changes in the index or rate effective variable payments	316
Lease liability recognised as at 1 July 2019	**10,870**
Of which are:	
Current lease liabilities	1,762
Non-current lease liabilities	9,108
Total lease liabilities	**10,870**

The associated right-of-use assets of which are substantially in relation to property leases were measured on a retrospective basis as if the new rules had always been applied. There were no onerous lease contracts that would have required an adjustment to the right-of-use assets at the date of initial application.

The change in accounting policy affected the following items in the balance sheet on 1 July 2019.

- Right-of-use assets: increased by $10.0 million
- Deferred tax assets: increased by $0.2 million
- Lease liabilities: increased by $10.8million

The net impact on retained earnings on 1 July 2019 was a decrease of $0.6 million.

The adoption of NZ IFRS 16 has no material impact to the Banking Group's leasing business where the Banking Group acts as the lessor.

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

Accounting standards issued but not yet effective

NZ IFRS 17 Insurance Contracts was issued in July 2017 and is applicable to general and life insurance contracts. NZ IFRS 17 will replace NZ IFRS 4 Insurance Contracts. In mid-2019 an Exposure Draft on amendments to NZ IFRS 17 was issued and proposed that the effective date of NZ IFRS 17 be deferred by one year. As such it is expected that the standard will be effective for the Banking Group for the financial year ending 30 June 2023. The Banking Group is in the process of restructuring its insurance business and will assess the impact arising from NZ IFRS 17 in conjunction with the restructure. Further information on the restructure is included in Note 20 of this Disclosure Statement.

Other amendments to existing standards that are not yet effective are not expected to have a material impact to the Group.

PERFORMANCE

2 Segmental analysis

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

Operating segments

Motor	Motor vehicle finance.
Reverse Mortgages	Reverse mortgage lending.
Other Personal	A comprehensive range of financial services – including term, transactional and savings-based deposit accounts and personal loans to individuals.
Business	Term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium 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 and assets, such as premises, IT and support centre costs are not allocated to operating segments and are included in Other.

The Banking Group's operating segments are different from the industry categories detailed in Note 14- Asset quality. The operating segments are primarily categorised by sales channel, whereas Note 14 - Asset quality is based on credit risk concentrations.

$000's	Motor	Reverse Mortgages	Other Personal	Business	Rural	Other	Total
31 December 2019 (Unaudited)							
Net interest income	28,204	12,176	9,238	28,026	15,380	(52)	92,972
Net other income	1,895	2,824	646	1,317	535	1,134	8,351
Net operating income	**30,099**	**15,000**	**9,884**	**29,343**	**15,915**	**1,082**	**101,323**
Operating expenses	1,615	3,331	1,934	5,980	1,396	30,242	44,498
Profit/(loss) before impaired asset expense and income tax	**28,484**	**11,669**	**7,950**	**23,363**	**14,519**	**(29,160)**	**56,825**
Impaired asset expense	3,611	-	3,345	1,880	139	-	8,975
Profit/(loss) before income tax from continuing operations	**24,873**	**11,669**	**4,605**	**21,483**	**14,380**	**(29,160)**	**47,850**
Income tax expense	-	-	-	-	-	12,954	12,954
Profit/(loss) for the period	**24,873**	**11,669**	**4,605**	**21,483**	**14,380**	**(42,114)**	**34,896**
Total assets	1,127,408	586,003	244,498	1,148,614	615,072	540,013	**4,261,608**
Total liabilities	-	-	-	-	-	3,688,086	**3,688,086**

2 Segmental analysis (continued)

$000's	Motor	Reverse Mortgages	Other Personal	Business	Rural	Other	Total
31 December 2018 (Unaudited)							
Net interest income	27,716	9,937	8,304	26,904	15,426	(2,164)	86,123
Net other income	467	112	1,195	723	404	1,142	4,043
Net operating income	**28,183**	**10,049**	**9,499**	**27,627**	**15,830**	**(1,022)**	**90,166**
Operating expenses	1,203	1,261	2,975	4,539	1,899	29,282	41,159
Profit / (loss) before impaired asset expense and income tax	**26,980**	**8,788**	**6,524**	**23,088**	**13,931**	**(30,304)**	**49,007**
Impaired asset expense / (benefit)	4,654	-	5,036	3,812	(135)	(203)	13,164
Profit / (loss) before income tax	**22,326**	**8,788**	**1,488**	**19,276**	**14,066**	**(30,101)**	**35,843**
Profit before income tax from discontinued operations	-	-	-	-	-	6,169	6,169
Income tax expense	-	-	-	-	-	11,616	11,616
Profit / (loss) for the period	**22,326**	**8,788**	**1,488**	**19,276**	**14,066**	**(35,548)**	**30,396**
Total assets (Restated)	1,021,673	478,037	200,823	1,083,029	634,486	599,581	**4,017,629**
Total liabilities	-	-	-	-	-	3,428,919	**3,428,919**

$000's	Motor	Reverse Mortgages	Other Personal	Business	Rural	Other	Total
30 June 2019 (Audited)							
Net interest income	54,753	20,673	16,345	54,334	30,865	(1,278)	175,692
Net other income	2,313	224	2,563	1,524	816	588	8,028
Net operating income	**57,066**	**20,897**	**18,908**	**55,858**	**31,681**	**(690)**	**183,720**
Operating expenses	2,543	2,279	5,602	9,163	3,263	55,360	78,210
Profit/(loss) before impaired asset expense and income tax	**54,523**	**18,618**	**13,306**	**46,695**	**28,418**	**(56,050)**	**105,510**
Fair value movement on investment property	-	-	-	-	-	1,936	1,936
Impaired asset expense / (benefit)	5,009	268	8,307	7,102	(132)	-	20,554
Profit/(loss) before income tax from continuing operations	**49,514**	**18,350**	**4,999**	**39,593**	**28,550**	**(54,114)**	**86,892**
Profit before income tax from discontinued operations	-	-	-	-	-	6,169	6,169
Income tax expense	-	-	-	-	-	24,762	24,762
Profit/(loss) for the year	**49,514**	**18,350**	**4,999**	**39,593**	**28,550**	**(72,707)**	**68,299**
Total assets	1,074,446	561,211	215,253	1,096,253	643,278	548,294	**4,138,735**
Total liabilities	-	-	-	-	-	3,535,345	**3,535,345**

3 Net interest income

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Interest income			
Cash and cash equivalents	301	312	717
Investments	4,448	4,906	10,864
Finance receivables	124,658	120,521	242,556
Finance receivables - reverse mortgages	19,273	17,628	34,233
Total interest income	**148,680**	**143,367**	**288,370**
Interest expense			
Retail deposits	47,741	48,595	97,119
Other borrowings	6,568	7,239	12,313
Net interest expense on derivative financial instruments	1,399	1,410	3,246
Total interest expense	**55,708**	**57,244**	**112,678**
Net interest income	**92,972**	**86,123**	**175,692**

4 Operating expenses

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Personnel expenses	23,457	21,267	41,730
Directors' fees	310	439	822
Audit and review of financial statements [1]	317	319	472
Other assurance services paid to auditor [2]	31	15	47
Amortisation - intangible assets	2,102	1,803	3,893
Depreciation - property, plant and equipment	1,061	889	1,861
Depreciation - right of use asset	1,041	-	-
Operating lease expense as a lessee	-	831	1,646
Legal and professional fees	1,657	1,226	2,278
Other operating expenses	14,522	14,370	25,461
Total operating expenses	**44,498**	**41,159**	**78,210**

[1] Audit and review of financial statements includes fees paid for both audit of financial statements and review of interim financial statements.
[2] Other assurance services paid to the auditor comprise review of regulatory returns, trust deed reporting, registry audits and other agreed upon procedures engagements.

5 Impaired asset expense

At each reporting date, the Banking Group applies a three stage approach to measuring expected credit loss (ECL) to finance receivables not carried at fair value. The following table details impairment charges of those finance receivables for the six months ended 31 December 2019.

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Non-securitised			
Individually impaired expense / (benefit)	553	(425)	1,311
Collectively impaired expense	8,421	14,245	19,529
Total non-securitised impaired asset expense	**8,974**	**13,820**	**20,840**
Securitised			
Collectively impaired expense	1	(29)	341
Total securitised impaired asset expense	**1**	**(29)**	**341**
Total			
Individually impaired expense	553	(425)	1,311
Collectively impaired expense	8,422	14,216	19,870
Total impaired asset expense	**8,975**	**13,791**	**21,181**
Reconciliation of impaired asset expense:			
Impaired asset expense	8,975	13,164	20,554
Impaired asset expense for discontinued operations	-	627	627
Total impaired asset expense	**8,975**	**13,791**	**21,181**

6 Discontinued operations

Discontinued operations

At the Annual Shareholder Meeting in September 2018, the Bank's shareholders approved a corporate restructure that resulted in the Bank becoming a wholly owned subsidiary of a new company, Heartland Group Holdings Limited (HGH). On 31 October 2018, shares in the Bank were exchanged for shares in HGH, and the Australian group of companies were transferred from the Bank to HGH.

Discontinued operations are shown separately from continuing operations in the comparative consolidated statements.

Results of discontinued operation

The profit before income tax from the discontinued operations of $6.2 million is attributable entirely to the Banking Group. The income tax expense for the discontinued operation was $1.6 million and profit after tax for the period was $4.6 million.

6 Discontinued operations (continued)

Financial position of discontinued operation

$000's	Unaudited October 2018
Financial position of assets of discontinued operation	
Cash and cash equivalents	68,766
Finance receivables	725,146
Other assets	917
Deferred tax asset/liability	1,133
Total discontinued operations assets	**795,962**
Financial position of liabilities of discontinued operation	
Other borrowings	665,950
Tax liabilities	2,047
Due to related parties	81,865
Total discontinued operations liabilities	**749,862**

Cash flow of discontinued operation

$000's	Unaudited October 2018
Cash flows from discontinued operations	
Net cash flows applied to operating activities	(8,060)
Net cash flow from investing activities	-
Net cash flows from financing activities	57,883
Net cash flows for the period	**49,823**

Profit on disposal

$000's	Unaudited October 2018
In specie dividend to Heartland Group Holdings Limited	61,444
Total consideration received	**61,444**
Net assets	46,100
Goodwill	15,344
Gain on disposal	**-**

FINANCIAL POSITION

7 Finance Receivables

(a) Finance receivables held at amortised cost

$000's	Unaudited December 2019	Unaudited December 2018 (Restated)	Audited June 2019
Non-securitised			
Neither 90 days past due nor impaired	3,049,814	2,817,843	3,016,844
At least 90 days past due	46,780	34,854	44,466
Individually impaired	28,433	35,889	26,412
Gross finance receivables	**3,125,027**	**2,888,586**	**3,087,722**
Less provision for impairment	(60,381)	(57,803)	(58,491)
Total non-securitised finance receivables	**3,064,646**	**2,830,783**	**3,029,231**
Securitised			
Neither 90 days past due nor impaired	36,843	154,642	-
At least 90 days past due	-	197	-
Individually impaired	-	-	-
Gross finance receivables	**36,843**	**154,839**	**-**
Less provision for impairment	(123)	(1,013)	-
Total securitised finance receivables	**36,720**	**153,826**	**-**
Total			
Neither 90 days past due nor impaired	3,086,657	2,972,485	3,016,844
At least 90 days past due	46,780	35,051	44,466
Individually impaired	28,433	35,889	26,412
Gross finance receivables	**3,161,870**	**3,043,425**	**3,087,722**
Less provision for impairment	(60,504)	(58,816)	(58,491)
Total finance receivables	**3,101,366**	**2,984,609**	**3,029,231**

Refer to Note 14 – Asset quality for further analysis of finance receivables by credit risk concentration.

7 Finance Receivables (continued)

(a) Finance receivables held at amortised cost (continued)

Movement in provision

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

$000's	12- month ECL	Lifetime ECL Not credit impaired	Lifetime ECL Credit impaired	Specific provision	Total
Unaudited - December 2019					
Non-securitised					
Impairment allowance as at 1 July 2019	30,421	1,780	18,427	7,863	58,491
Changes in loss allowance					
Transfer between stages	(925)	(127)	1,046	-	(6)
New and increased provision (net of collective provision releases)	168	665	8,196	1,638	10,667
Recovery of amounts written off	-	-	(1,767)	-	(1,767)
Credit impairment charge	**(757)**	**538**	**7,475**	**1,638**	**8,894**
Recovery of amounts previously written off	-	-	1,767	-	1,767
Write offs	-	-	(8,671)	(100)	(8,771)
Impairment allowance as at 31 December 2019	**29,664**	**2,318**	**18,998**	**9,401**	**60,381**
Securitised					
Impairment allowance as at 1 July 2019	-	-	-	-	-
Changes in loss allowance					
Transfer between stages	122	-	-	-	122
New and increased provision (net of collective provision releases)	-	1	-	-	1
Recovery of amounts written off	-	-	-	-	-
Credit impairment charge	**122**	**1**	**-**	**-**	**123**
Recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	-	-	-
Impairment allowance as at 31 December 2019	**122**	**1**	**-**	**-**	**123**
Total					
Impairment allowance as at 1 July 2019	30,421	1,780	18,427	7,863	58,491
Changes in loss allowance					
Transfer between stages	(803)	(127)	1,046	-	116
New and increased provision (net of collective provision releases)	168	666	8,196	1,638	10,668
Recovery of amounts written off	-	-	(1,767)	-	(1,767)
Credit impairment charge	**(635)**	**539**	**7,475**	**1,638**	**9,017**
Recovery of amounts previously written off	-	-	1,767	-	1,767
Write offs	-	-	(8,671)	(100)	(8,771)
Impairment allowance as at 31 December 2019	**29,786**	**2,319**	**18,998**	**9,401**	**60,504**

7 Finance Receivables (continued)

(a) Finance receivables held at amortised cost (continued)

$000's	12-month ECL (Restated)	Lifetime ECL Not credit impaired (Restated)	Lifetime ECL Credit impaired (Restated)	Collective provision June 2018	Specific provision (Restated)	Total (Restated)
Unaudited - December 2018						
Non-securitised						
Impairment allowance as at 30 June 2018	-	-	-	20,301	9,066	29,367
Restated for adoption of NZ IFRS 9	31,784	1,365	14,945	(20,301)	(169)	27,624
Restated impairment allowance as at 1 July 2018	31,784	1,365	14,945	-	8,897	56,991
Changes in loss allowance						
Transfer between stages	(607)	(108)	637	-	-	(78)
New and increased provision (net of collective provision releases)	106	354	11,095	-	1,791	13,346
Recovery of amounts written off	-	-	(293)	-	(13)	(306)
Credit impairment charge	**(501)**	**246**	**11,439**	**-**	**1,778**	**12,962**
Recovery of amounts previously written off	-	-	293	-	13	306
Write offs	-	-	(7,953)	-	(4,503)	(12,456)
Impairment allowance as at 31 December 2018	**31,283**	**1,611**	**18,724**	**-**	**6,185**	**57,803**
Securitised						
Impairment allowance as at 30 June 2018	-	-	-	304	-	304
Restated for adoption of NZ IFRS 9	400	20	345	(304)	-	461
Restated impairment allowance as at 1 July 2018	400	20	345	-	-	765
Changes in loss allowance						
Transfer between stages	616	-	(369)	-	-	247
New and increased provision (net of collective provision releases)	-	1	-	-	-	1
Recovery of amounts written off	-	-	-	-	-	-
Credit impairment charge	**616**	**1**	**(369)**	**-**	**-**	**248**
Recovery of amounts previously written off	-	-	-	-	-	-
Write offs	-	-	-	-	-	-
Impairment allowance as at 31 December 2018	**1,016**	**21**	**(24)**	**-**	**-**	**1,013**
Total						
Impairment allowance as at 30 June 2018	-	-	-	20,605	9,066	29,671
Restated for adoption of NZ IFRS 9	32,184	1,385	15,290	(20,605)	(169)	28,085
Restated impairment allowance as at 1 July 2018	32,184	1,385	15,290	-	8,897	57,756
Changes in loss allowance						
Transfer between stages	9	(108)	268	-	-	169
New and increased provision (net of collective provision releases)	106	355	11,095	-	1,791	13,347
Recovery of amounts written off	-	-	(293)	-	(13)	(306)
Credit impairment charge	**115**	**247**	**11,070**	**-**	**1,778**	**13,210**
Recovery of amounts previously written off	-	-	293	-	13	306
Write offs	-	-	(7,953)	-	(4,503)	(12,456)
Impairment allowance as at 31 December 2018	**32,299**	**1,632**	**18,700**	**-**	**6,185**	**58,816**

7 Finance Receivables (continued)

(a) Finance receivables held at amortised cost (continued)

$000's	12-month ECL	Lifetime ECL Not credit impaired	Lifetime ECL Credit impaired	Collective provision June 2018	Specific provision	Total
Audited - June 2019						
Non-securitised						
Impairment allowance as at 30 June 2018	-	-	-	20,301	9,066	29,367
Restated for adoption of NZ IFRS 9	31,784	1,365	14,945	(20,301)	(169)	27,624
Restated impairment allowance as at 1 July 2018	31,784	1,365	14,945	-	8,897	56,991
Changes in loss allowance						
Transfer between stages	(1,071)	(205)	11,671	-	(43)	10,352
New and increased provision (net of collective provision releases)	(292)	620	7,531	-	4,002	11,861
Recovery of amounts written off	-	-	(829)	-	-	(829)
Credit impairment charge	**(1,363)**	**415**	**18,373**	**-**	**3,959**	**21,384**
Recovery of amounts written off	-	-	829	-	-	829
Write offs	-	-	(15,720)	-	(4,993)	(20,713)
Impairment allowance as at 30 June 2019	**30,421**	**1,780**	**18,427**	**-**	**7,863**	**58,491**
Securitised						
Impairment allowance as at 30 June 2018	-	-	-	304	-	304
Restated for adoption of NZ IFRS 9	400	20	345	(304)	-	461
Restated impairment allowance as at 1 July 2018	400	20	345	-	-	765
Changes in loss allowance						
Transfer between stages	(400)	(21)	(345)	-	-	(766)
New and increased provision (net of collective provision releases)	-	1	-	-	-	1
Recovery of amounts written off	-	-	-	-	-	-
Credit impairment charge	**(400)**	**(20)**	**(345)**	**-**	**-**	**(765)**
Recovery of amounts written off	-	-	-	-	-	-
Write offs	-	-	-	-	-	-
Impairment allowance as at 30 June 2019	**-**	**-**	**-**	**-**	**-**	**-**
Total						
Impairment allowance as at 30 June 2018	-	-	-	20,605	9,066	29,671
Restated for adoption of NZ IFRS 9	32,184	1,385	15,290	(20,605)	(169)	28,085
Restated impairment allowance as at 1 July 2018	32,184	1,385	15,290	-	8,897	57,756
Changes in loss allowance						
Transfer between stages	(1,471)	(226)	11,326	-	(43)	9,586
New and increased provision (net of collective provision releases)	(292)	621	7,531	-	4,002	11,862
Recovery of amounts written off	-	-	(829)	-	-	(829)
Credit impairment charge	**(1,763)**	**395**	**18,028**	**-**	**3,959**	**20,619**
Recovery of amounts written off	-	-	829	-	-	829
Write offs	-	-	(15,720)	-	(4,993)	(20,713)
Impairment allowance as at 30 June 2019	**30,421**	**1,780**	**18,427**	**-**	**7,863**	**58,491**

7 Finance Receivables (continued)

(a) Finance receivables held at amortised cost (continued)

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

$000's	12-month ECL	Lifetime ECL Not credit impaired	Lifetime ECL Credit impaired	Specific provision	Total
Unaudited - December 2019					
Gross finance receivables as at 1 July 2019	2,794,414	197,630	69,266	26,412	3,087,722
Transfer between stages	(40,590)	9,697	27,069	3,824	-
Additions	922,101	62,329	6,788	-	991,218
Net Repayments	(224,169)	(15,773)	(6,567)	(1,803)	(248,312)
Deletions	(579,628)	(58,431)	(20,818)	-	(658,877)
Write offs	(1,590)	(1,960)	(6,331)	-	(9,881)
Gross finance receivables as at 31 December 2019	**2,870,538**	**193,492**	**69,407**	**28,433**	**3,161,870**

(b) Finance receivables held at fair value

When the Bank enters into a reverse mortgage loan the Bank has set expectations regarding the loan's current and future risk profile and expectation of performance. This expectation references a wide range of assumptions including:

- mortality and move to care;
- voluntary exits;
- house price changes;
- no negative equity guarantee; and
- interest rate margin.

At balance date the Bank does not consider any of the above expectations to have moved outside of the original expectation range. Therefore the Bank has continued to estimate the fair value of the portfolio at transaction price. There has been no fair value movement recognised in profit or loss during the period, given the loan terms and the current market conditions the fair value as recorded is not considered to be sensitive to changes in house prices or interest rates.

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Gross finance receivables - reverse mortgages	586,003	478,037	561,211
Finance receivables - reverse mortgages	**586,003**	**478,037**	**561,211**

8 Borrowings

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Deposits	3,244,035	2,988,365	3,153,681
Total borrowings relating to deposits	**3,244,035**	**2,988,365**	**3,153,681**
Unsubordinated notes	285,337	151,902	285,435
Bank borrowings	-	-	25,002
Certificate of deposits	69,811	144,555	34,836
Borrowings - securitised	30,015	127,944	-
Total other borrowings	**385,163**	**424,401**	**345,273**
Total borrowings	**3,629,198**	**3,412,766**	**3,498,954**

Deposits and unsubordinated notes rank equally and are unsecured.

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

Principal	Valuation	NOTE	Issue date	Maturity Date	Frequency
$125 million	Fair value	11(a)	12 April 2019	12 April 2024	Half yearly
$150 million	Fair value	11(a)	21 September 2017	21 September 2022	Half yearly

9 Share capital and dividends

000's	Unaudited December 2019 Number of shares	Unaudited December 2018 Number of shares	Audited June 2019 Number of shares
Issued shares			
Opening balance	565,430	560,588	560,588
Dividend reinvestment plan	-	5,283	5,283
Shares issued during the period	-	-	-
Cancelled shares	-	(441)	(441)
Closing balance	**565,430**	**565,430**	**565,430**

There were no new shares issued during the period. The Bank had previously issued 5,282,619 new shares at $1.6250 per share on 21 September 2018 under the Dividend Reinvestment Plans for the financial year ended 30 June 2019.

Dividends paid

	December 2019			June 2019		
	Date declared	**Cents per share**	**$000's**	**Date declared**	**Cents per share**	**$000's**
Final dividend				15 August 2018	5.5	30,808
In specie dividend to HGH				31 October 2018	-	61,444
Interim dividends to HGH	01 August 2019	-	35,000	19 February 2019	-	19,790
	29 November 2019	-	20,000			
	16 December 2019	-	10,000			
Total dividends paid			**65,000**			**112,042**

10 Related party transactions and balances

A person or entity that 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).
   - 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).

10 Related party transactions and balances (continued)

(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 Executives and Non-Executive Directors and their immediate family members are included below.

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 Bank are comparable to transactions with other employees and did not involve more than the normal risk of repayment or present other unfavourable features.

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Transactions with key management personnel			
Interest income	-	-	-
Interest expense	(55)	(31)	(76)
Total transactions with key management personnel	**(55)**	**(31)**	**(76)**
Due from / (to) key personnel			
Borrowings - deposits	(2,322)	(2,960)	(3,019)
Total due (to) key management personnel	**(2,322)**	**(2,960)**	**(3,019)**

(b) Transaction 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 administrative services, tax transactions, and customer operations and call centre. Banking facilities are provided by the Bank to other Heartland 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.

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Heartland Group Holdings Limited			
Deposits	10,010	-	-
Interest expense	10	-	-
Dividends	65,000	92,252	112,042
Disposal of investment in Harmoney Corp Limited	11,900	-	-
Heartland Australia Group Pty Limited			
Interest income	678	639	1,846
Funding repaid to the Bank	27,225	-	-

(c) Due from/to related parties

$000's	Unaudited 6 months to December 2019	Unaudited 6 months to December 2018	Audited 12 months to June 2019
Due from			
Heartland Group Holdings Limited	2,063	-	-
Heartland Australia Group Pty Limited (Restated)	-	47,923	24,179
Total due from related parties	**2,063**	**47,923**	**24,179**
Due to			
Heartland Group Holdings Limited	-	-	3,002
Heartland Australia Group Pty Limited (Restated)	2,138	-	-
Total due to related parties	**2,138**	**-**	**3,002**

11 Fair value

(a) Financial instruments measured at fair value

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 Statement of Financial Position.

$000's	Level 1	Level 2	Level 3	Total
Unaudited - December 2019				
Assets				
Investments	282,428	16,572	1,988	300,988
Derivative financial assets	-	10,806	-	10,806
Finance receivables - reverse mortgages	-	-	586,003	586,003
Total financial assets measured at fair value	**282,428**	**27,378**	**587,991**	**897,797**
Liabilities				
Derivative financial liabilities	-	9,843	-	9,843
Unsubordinated notes	-	285,337	-	285,337
Total financial liabilities measured at fair value	**-**	**295,180**	**-**	**295,180**
Unaudited - December 2018				
Assets				
Investments	209,048	100,219	9,694	318,961
Derivative financial assets	-	1,238	-	1,238
Finance receivables - reverse mortgages	-	-	478,037	478,037
Total financial assets measured at fair value	**209,048**	**101,457**	**487,731**	**798,236**
Liabilities				
Derivative financial liabilities	-	148	-	148
Unsubordinated notes (restated)	-	151,902	-	151,902
Total financial liabilities measured at fair value	**-**	**152,050**	**-**	**152,050**
Audited - June 2019				
Assets				
Investments	255,875	86,618	12,435	354,928
Derivative financial assets	-	12,650	-	12,650
Finance receivables - reverse mortgage	-	-	561,211	561,211
Total financial assets measured at fair value	**255,875**	**99,268**	**573,646**	**928,789**
Liabilities				
Derivative financial liabilities	-	10,372	-	10,372
Unsubordinated notes (restated)	-	285,435	-	285,435
Total financial liabilities measured at fair value	**-**	**295,807**	**-**	**295,807**

11 Fair value (continued)

(b) Financial instruments measured not 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.

	Unaudited			Unaudited			Audited		
	Fair value Hierarchy	Total Fair Value	Total Carrying Value	Fair value Hierarchy	Total Fair Value (Restated)	Total Carrying Value (Restated)	Fair value Hierarchy	Total Fair Value (Restated)	Total Carrying Value (Restated)
$000's		**Dec-19**	**Dec-19**		**Dec-18**	**Dec-18**		**Jun-19**	**Jun-19**
Assets									
Cash and cash equivalents	Level 1	122,737	122,737	Level 1	75,770	75,770	Level 1	45,228	45,228
Investments [1]	Level 2	6,961	6,970	Level 2	-	-	Level 2	-	-
Due from related parties	Level 3	2,063	2,063	Level 2	47,923	47,923	Level 2	27,248	21,177
Finance receivables	Level 2	3,082,052	3,101,366	Level 2	2,971,370	2,984,609	Level 2	3,017,327	3,029,231
Other financial assets	Level 3	1,784	1,784	Level 3	1,337	1,337	Level 3	3,215	3,215
Total financial assets		**3,215,597**	**3,234,920**		**3,096,400**	**3,109,639**		**3,093,018**	**3,098,851**
Liabilities									
Retail deposits	Level 2	3,255,204	3,244,035	Level 2	2,993,208	2,988,365	Level 2	3,160,426	3,153,681
Borrowings - securitised	Level 2	30,015	30,015	Level 2	127,944	127,944	Level 2	-	-
Other borrowings	Level 2	69,811	69,811	Level 2	144,555	144,555	Level 2	59,838	59,838
Due to related parties	Level 3	2,138	2,138	Level 3	-	-	Level 3	-	-
Other financial liabilities	Level 3	10,897	10,897	Level 3	5,981	5,981	Level 3	10,769	10,769
Total financial liabilities		**3,368,065**	**3,356,896**		**3,271,688**	**3,266,845**		**3,231,033**	**3,224,288**

[1] Included within investments are bank deposits which are held to support its contractual cash flows. Such investments are measured at amortised cost.

Further information on valuation techniques and assumptions used for determining fair value is included in Note 21 of the Bank's Disclosure Statement for the year ended 30 June 2019.

RISK MANAGEMENT

12 Enterprise risk management program

There have been no material changes in the Banking group's policies for managing risk, or material exposures to any new types of risk since the reporting date of the previous disclosure statement, refer to the Bank's disclosure statement for the year ended 30 June 2019.

13 Credit risk exposure

(a) Maximum exposure to credit risk at the equivalent reporting dates

The following table represents the maximum credit risk exposure, without taking account of any collateral held. The exposures set out below are based on net carrying amounts as reported in the Statement of Financial Position.

$000's	**Unaudited December 2019**
Cash and cash equivalents	122,737
Investments	307,958
Finance receivables	3,101,366
Finance receivables - reverse mortgages	586,003
Derivative financial assets	10,806
Due from related parties	2,063
Other financial assets	1,784
Total on balance sheet credit exposures	**4,132,717**

(b) Concentration of credit by geographical region

$000's	**Unaudited December 2019**
New Zealand:	
Auckland	1,187,425
Wellington	253,439
Rest of North Island	1,186,936
Canterbury	521,223
Rest of South Island	605,396
Australia:	
Queensland	10,707
New South Wales	66,489
Victoria	22,970
Western Australia	9,495
South Australia	3,993
Rest of Australia	2,870
Rest of the world [1]	322,278
	4,193,221
Provision for impairment	(60,504)
Total on balance sheet credit exposures	**4,132,717**

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

13 Credit risk exposure (continued)

(c) Concentration of credit by industry sector

$000's	Unaudited Dec-19
Agriculture	709,731
Forestry and Fishing	90,469
Mining	14,185
Manufacturing	86,612
Finance & Insurance	28,675
Wholesale Trade	40,768
Retail Trade	138,997
Households	1,468,802
Property and Business Services	249,981
Transport and Storage	256,182
Other [1]	1,108,819
	4,193,221
Collective provision	(60,504)
Total on balance sheet credit exposures	**4,132,717**

[1] Industry sectors classified within Other include religious services, parking services, laundry and dry cleaning, other machinery and equipment repair and maintenance.

As at 31 December 2019 there was nil of undrawn lending commitments available to counterparties for whom drawn balances were classified as individually impaired.

(d) Credit exposures to individual counterparties

As at 31 December 2019 the Banking Group had 1 period end or peak end-of-day over the relevant six month period credit exposures over 10% of equity to individual counterparties (not being members of groups of closely related counterparties) or groups of closely related counterparties (excluding central government of any country with a long-term credit rating of A- or A3 or above, or its equivalent, or any bank with a long-term credit rating of A- or A3 or above, or its equivalent, and connected persons).

The exposure information in the table below excludes 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.

$000's	As at 31 December 2019	Peak end-of-day over 6 months to 31 December 2019
Exposures to banks		
Total number of exposures to banks that are greater than 10% of CET1 capital	1	1
with a long-term credit rating of A- or A3 or above, or its equivalent	1	1
with a credit rating of at least BBB- or Baa3, or its equivalent, and at the most BBB+	-	-
or Baa1 or its equivalent	-	-
Exposures to non-banks		
Total number of exposures to banks that are greater than 10% of CET1 capital	-	-
with a long-term credit rating of A- or A3 or above, or its equivalent	-	-
with a credit rating of at least BBB- or Baa3, or its equivalent, and at the most BBB+	-	-
or Baa1 or its equivalent		

14 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

(a) Finance receivables by credit risk concentration

$000's	Corporate	Residential	All Other	Total
Unaudited - December 2019				
Neither 90 days past due nor impaired	1,894,580	610,775	1,167,305	3,672,660
At least 90 days past due	34,281	512	11,987	46,780
Individually impaired	28,433	-	-	28,433
Gross Finance Receivables	1,957,294	611,287	1,179,292	3,747,873
Provision for impairment	(35,593)	(146)	(24,765)	(60,504)
Total net finance receivables	**1,921,701**	**611,141**	**1,154,527**	**3,687,369**

(b) Past due but not impaired

Unaudited - December 2019				
Less than 30 days past due	32,847	996	39,835	73,678
At least 30 days but less than 60 days past due	9,796	141	14,125	24,062
At least 60 days but less than 90 days past due	3,335	461	21,552	25,348
At least 90 days past due	34,281	512	11,987	46,780
Total past due but not impaired	**80,259**	**2,110**	**87,499**	**169,868**

(c) Individually impaired assets

Unaudited - December 2019				
Opening	26,412	-	-	26,412
Additions	3,638	-	-	3,638
Deletions	(1,517)	-	-	(1,517)
Write offs	(100)	-	-	(100)
Closing gross individually impaired assets	**28,433**	**-**	**-**	**28,433**
Less: provision for individually impaired assets	(9,401)			(9,401)
Total net impaired assets	**19,032**	**-**	**-**	**19,032**

14 Asset quality (continued)

(d) Movements in credit loss allowance

$'000s	12 month ECL	Lifetime ECL Not credit impaired	Lifetime ECL Credit impaired	Specific provision	Total
Corporate					
Impairment allowance as at 1 July 2019	21,404	670	4,533	7,863	34,470
Changes in loss allowance					
Transfer between stages	18	41	58	-	117
New and increased provision (net of collective provision releases)	(400)	540	460	1,638	2,238
Recovery of amounts written off	-	-	-	-	-
Credit Impairment Charge	**(382)**	**581**	**518**	**1,638**	**2,355**
Add back recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	-	(100)	(100)
Impairment allowance as at 31 December 2019	**21,022**	**1,251**	**5,051**	**9,401**	**36,725**
Residential					
Impairment allowance as at 1 July 2019	21	3	80	-	104
Changes in loss allowance					
Transfer between stages	-	(2)	2	-	0
New and increased provision (net of collective provision releases)	(4)	0	50	-	46
Recovery of amounts written off	-	-	-	-	-
Credit Impairment Charge	**(4)**	**(2)**	**52**	-	**46**
Add back recovery of amounts previously written off	-	-	-	-	-
Write offs	-	-	-	-	-
Impairment allowance as at 31 December 2019	**17**	**1**	**132**	-	**150**
All Other					
Impairment allowance as at 1 July 2019	8,996	1,107	13,814	-	23,917
Changes in loss allowance					
Transfer between stages	(821)	(166)	986	-	(1)
New and increased provision (net of collective provision releases)	572	126	7,686	-	8,384
Recovery of amounts written off	-	-	(1,767)	-	(1,767)
Credit Impairment Charge	**(249)**	**(40)**	**6,905**	-	**6,616**
Add back recovery of amounts previously written off	-	-	1,767	-	1,767
Write offs	-	-	(8,671)	-	(8,671)
Impairment allowance as at 31 December 2019	**8,747**	**1,067**	**13,815**	-	**23,629**
Total					
Impairment allowance as at 1 July 2019	30,421	1,780	18,427	7,863	58,491
Changes in loss allowance					
Transfer between stages	(803)	(127)	1,046	-	116
New and increased provision (net of collective provision releases)	168	666	8,196	1,638	10,668
Recovery of amounts written off	-	-	(1,767)	-	(1,767)
Credit Impairment Charge	**(635)**	**539**	**7,475**	**1,638**	**9,017**
Add back recovery of amounts previously written off	-	-	1,767	-	1,767
Write offs	-	-	(8,671)	(100)	(8,771)
Impairment allowance as at 31 December 2019	**29,786**	**2,319**	**18,998**	**9,401**	**60,504**

(e) Other assets under administration

Other assets under administration are any loans, not being individually impaired or 90 days or more past due, where the customer is in any form of voluntary or involuntary administration, including receivership, liquidation, bankruptcy or statutory management. As at 31 December 2019, the Banking Group had $3.5 million assets under administration (December 2018: $2.29 million; June 2019: $5.8 million).

15 Liquidity risk

The Banking Group holds the following financial assets for the purpose of managing liquidity risk:

$000's	Unaudited December 2019
Cash and cash equivalents	122,737
Investments	305,970
Undrawn committed bank facilities	119,985
Total liquidity	**548,692**

Contractual liquidity profile of financial assets and liabilities

The following tables present the Banking Group's financial assets and 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 the actual cash flows. This occurs as a result of future actions by the Banking Group and its counterparties, such as early repayment or refinancing of term loans and borrowings. Deposits and other public borrowings include customer savings deposits and transactional accounts, which are at call. History demonstrates that such accounts provide a stable source of long term funding for the Banking Group.

The Banking Group does not manage its liquidity risk on a contractual liquidity basis.

$000's	On Demand	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
Unaudited - 31 December 2019							
Financial assets							
Cash and cash equivalents	122,737	-	-	-	-	-	122,737
Investments	-	98,350	18,643	62,779	130,199	5,145	315,116
Finance receivables	-	1,059,953	487,984	891,643	1,163,939	219,428	3,822,947
Finance receivables - reverse mortgages	-	7,207	7,207	13,476	47,692	1,704,128	1,779,710
Due from related parties	-	2,063	-	-	-	-	2,063
Derivative financial instruments	10,806	-	-	-	-	-	10,806
Other financial assets	-	1,784	-	-	-	-	1,784
Total financial assets	**133,543**	**1,169,357**	**513,834**	**967,898**	**1,341,830**	**1,928,701**	**6,055,163**
Financial liabilities							
Borrowings	1,001,355	1,545,821	473,418	257,706	393,160	-	3,671,460
Borrowings – securitised	-	30,048	-	-	-	-	30,048
Due to related parties	-	2,138	-	-	-	-	2,138
Lease liabilities	-	1,056	1,284	2,622	10,597	8,139	23,698
Derivative financial instruments	9,843	-	-	-	-	-	9,843
Other financial liabilities	-	10,897	-	-	-	-	10,897
Total financial liabilities	**1,011,198**	**1,589,960**	**474,702**	**260,328**	**403,757**	**8,139**	**3,748,084**
Net financial (liabilities) / assets	**(877,655)**	**(420,603)**	**39,132**	**707,570**	**938,073**	**1,920,562**	**2,307,079**
Undrawn facilities available to customers	134,743	-	-	-	-	-	134,743
Undrawn committed bank facilities	119,985	-	-	-	-	-	119,985

16 Interest rate risk

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.

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

$000's	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non-interest bearing	Total
Unaudited - 31 December 2019							
Financial assets							
Cash and cash equivalents	122,734	-	-	-	-	3	122,737
Investments	34,690	60,279	15,534	59,787	135,680	1,988	307,958
Finance receivables	1,543,914	215,723	355,919	563,825	417,055	4,930	3,101,366
Finance receivables - reverse mortgages	586,003	-	-	-	-	-	586,003
Due from related parties	2,063	-	-	-	-	-	2,063
Derivative financial assets	-	-	-	-	-	10,806	10,806
Other financial assets	-	-	-	-	-	1,784	1,784
Total financial assets	**2,289,404**	**276,002**	**371,453**	**623,612**	**552,735**	**19,511**	**4,132,717**
Financial liabilities							
Borrowings - Retail deposits	1,698,288	602,765	597,217	235,773	96,449	13,543	3,244,035
Other borrowings	71,665	968	-	-	282,515	-	355,148
Borrowings - securitised	30,015	-	-	-	-	-	30,015
Derivative financial liabilities	-	-	-	-	-	9,843	9,843
Due from related parties	2,138	-	-	-	-	-	2,138
Lease liabilities	-	-	-	-	-	20,623	20,623
Other financial liabilities	-	-	-	-	-	10,897	10,897
Total financial liabilities	1,802,106	603,733	597,217	235,773	378,964	54,906	3,672,699
Effect of derivatives held for risk management	380,373	(437)	(94,721)	(291,712)	6,497	-	-
Net financial assets / (liabilities)	**867,671**	**(328,168)**	**(320,485)**	**96,127**	**180,268**	**(35,395)**	**460,018**

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Banking Groups' financial assets and liabilities to various standard and nonstandard interest rate scenarios. Standard scenarios which are considered on a monthly basis include a 100 basis point parallel fall or rise in the yield curve. There is no material impact on profit or loss in terms of a fair value change from movement in market interest rates. Furthermore there is no material cash flow impact on the Consolidated Statement of Cash flows from a 100 basis point change in interest rates.

17 Concentrations of funding

(a) Regulatory liquidity ratios

The table below shows the arithmetic 3 month average of the respective daily ratio values in accordance with RBNZ's Liquidity Policy (BS13/BS13A) ("BS13") and the Banks conditions of registration relating to liquidity-risk management.

The one week mismatch ratio is a measure of the Banking Group's one week mismatch amount over its total funding, where the one-week mismatch amount represents the Banking Group's portfolio of primary liquid assets plus expected cash inflows minus expected cash outflows during a one-week period of stress. The Bank is required to maintain this ratio at not less than the minimum level of zero percent on a daily basis. The one-week mismatch ratio = 100 x (one-week mismatch dollar/total funding).

The one-month mismatch ratio is a measure of the Banking Group's one-month mismatch over its total funding, where the one-month mismatch amount represents the Banking Group's portfolio of primary and secondary liquid assets plus expected cash inflows, minus expected cash outflows during a one-month period of stress. The Bank is required to maintain this ratio at not less than the minimum level of zero percent on a daily basis. The one-month mismatch ratio = 100 x (one-month mismatch dollar value/total funding).

The one year core funding ratio measures the extent to which loans and advances are funded by the funding that is considered stable. The one-year core funding ratio = 100 x (one-year core funding dollar amount/BS13 total loans and advances) and must currently remain at not less than 75% on a daily basis.

	Average for the 3 months ended	
	31 December 2019	**30 September 2019**
One-week mismatch ratio	8.72%	8.91%
One-month mismatch ratio	10.58%	10.84%
Core funding ratio	**93.94%**	**94.42%**

Concentrations of funding by industry

	Unaudited
$000's	**31 December 2019**
Agriculture	76,107
Forestry and Fishing	28,798
Mining	165
Manufacturing	9,033
Finance & Insurance	631,118
Wholesale Trade	13,333
Retail Trade	21,214
Households	2,351,276
Property and Business Services	91,678
Transport and Storage	4,567
Other	116,572
	3,343,861
Unsubordinated notes	285,337
Total borrowings	**3,629,198**

Concentrations of funding by geographical area

	Unaudited
$000's	**31 December 2019**
Auckland	1,116,071
Wellington	335,935
Rest of North Island	805,225
Canterbury	965,854
Rest of South Island	274,089
Overseas	132,024
Total borrowings	**3,629,198**

Other Disclosures

18 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 hold 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 (Heartland PIE Fund)

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

	Unaudited	Unaudited	Audited
$000's	**31 December 2019**	**31 December 2018**	**30 June 2019**
Deposits	165,602	140,012	146,094

(b) Heartland Auto Receivables Warehouse Trust 2018-1 (Auto Warehouse)

The Banking Group had securitised a pool of receivables comprising commercial and motor vehicle loans sold to Auto Warehouse.

The Banking Group continues to recognise the securitised assets and associated borrowings in the Consolidated Statement of Financial Position as the bank remains exposed to and has the ability to affect variable returns from those assets and liabilities. Although the Banking Group recognises those interests in Auto Warehouse, the loans sold to the Trust are set aside for the benefit of investors in Auto Warehouse and other depositors and lenders to the Banking Group have no recourse to those assets.

	Unaudited	Unaudited	Audited
$000's	**31 December 2019**	**31 December 2018**	**30 June 2019**
Finance receivables - securitised	36,720	153,826	-
Borrowings - securitised	(30,015)	(127,944)	-

19 Capital adequacy

The capital adequacy tables set out on the following pages summarise the composition of regulatory capital and the capital adequacy ratios for the Banking Group as at 31 December 2019.

*Internal Capital Adequacy Assessment Process (**ICAAP**)*

The Banking Group has an ICAAP which complies with the requirements set out in the "Guidelines on a Bank's Internal Capital Adequacy Assessment Process (**ICAAP**)" BS12 and is in accordance with its Conditions of Registration.

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 has established a Capital Management Policy (**CMP**) to determine minimum capital levels for Tier 1 and Total capital under Basel III and in accordance with its Conditions of Registration. The documented process ensures that the Banking Group has sufficient available capital to meet minimum capital requirements, even in stressed events. It describes the risk profile of the Banking Group and the risk appetite and tolerances under which it operates, and assesses the level of capital held against the material risks of the Banking Group (both Pillar 1 and Pillar 2).

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.

Compliance with minimum capital levels is monitored by the ALCO and reported to the Board. The ICAAP and CMP is reviewed regularly by the Board.

$000's	**Unaudited December 2019**
Tier 1 capital	
CET1 capital	
Paid-up ordinary shares issued by the Bank	553,239
Retained earnings (net of appropriations)	20,522
Accumulated other comprehensive income and other disclosed reserves	(239)
Less deductions from CET1 capital	
Intangible assets	(56,781)
Deferred tax assets	(10,019)
Hedging reserve	4,000
Defined benefit superannuation fund asset	(715)
Reverse residential mortgage loan greater than value of security	(58)
Adjustment under the corresponding deduction approach	(500)
Total CET1 capital	**509,449**
AT1 capital	-
Total Tier 1 capital	**509,449**
Tier 2 capital	-
Total Tier 2 capital	**-**
Total capital	**509,449**

(a) 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 BS2A, 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 of 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.

19 Capital adequacy (continued)

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 debt instrument fair value reserve comprises the changes in the fair value of investments, net of tax.
Defined benefit reserve	The defined benefit reserve represents the excess of the fair value of the assets of the defined benefit superannuation plan over the net present value of the defined benefit obligations.
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.

(b) Credit risk

(i) 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
Unaudited - December 2019				
Cash	3	0%	-	-
Multilateral development banks	125,080	0%	-	-
Multilateral development banks	126,710	20%	25,342	2,027
Banks - Tier 1	134,886	20%	26,977	2,158
Banks - Tier 2	11,422	50%	5,711	457
Banks - Tier 3	18,102	100%	18,102	1,448
Public sector entity (AA- and above)	9,361	20%	1,872	150
Public sector entity (A- and above)	-	50%	-	-
Corporates (AA- and above)	-	20%	-	-
Corporates (A- and above)	1,024	50%	512	41
Corporates (BBB- and above)	4,126	100%	4,126	330
Corporates other	1,624,582	100%	1,624,582	129,967
Welcome Home Loans - loan to value ratio (LVR) <= 90%[1]	2,928	35%	1,025	82
Welcome Home Loans - LVR 90% >= 100%[1]	-	50%	-	-
Welcome Home Loans - LVR > 100%[1]	-	100%	-	-
Reverse Residential mortgages <= 60% LVR	572,566	50%	286,283	22,903
Reverse Residential mortgages 60 <= 80% LVR	10,558	80%	8,446	676
Reverse Residential mortgages > 80% LVR	2,322	100%	2,322	186
Reverse Residential mortgages > 100% LVR	499	100%	499	40
Non Property Investment Mortgage Loan <=80% LVR	13,389	35%	4,686	375
Non Property Investment Mortgage Loan 80 <= 90% LVR	-	50%	-	-
Non Property Investment Mortgage Loan 90 <= 100% LVR	433	75%	325	26
Non Property Investment Mortgage Loan > 100% LVR	590	100%	590	47
Property Investment Mortgage Loan <= 80% LVR	6,331	40%	2,532	203
Property Investment Mortgage Loan 80 <= 90% LVR	1,005	70%	703	56
Property Investment Mortgage Loan 90 <= 100% LVR	-	90%	-	-
Property Investment Mortgage Loan < 100% LVR	-	100%	-	-
Past due residential mortgages	464	100%	464	37
Other past due assets - provision >= 20%	14,398	100%	14,398	1,152
Other past due assets - provision < 20%	18,250	150%	27,374	2,190
All other equity holdings	1,488	400%	5,950	476
Other assets	1,495,025	100%	1,495,025	119,602
Not risk weighted assets	68,074	0%	-	-
Total on balance sheet exposures	**4,263,616**		**3,557,846**	**284,629**

[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.

19 Capital adequacy (continued)

(ii) Off balance sheet exposures

	Total exposure	Credit conversion factor	Credit equivalent amount	Average risk weight	Risk weighted exposure	Minimum Pillar 1 capital requirement
	$000's	%	$000's	%	$000's	$000's
Unaudited - December 2019						
Off balance sheet exposures						
Direct credit substitute	408	100%	408	100%	408	33
Performance-related contingency	2,558	50%	1,279	100%	1,279	102
Other commitments where original maturity is more than one year	145,336	50%	72,668	100%	72,668	5,813
Other commitments where original maturity is more than one year	7,565	50%	3,783	50%	1,892	151
Other commitments where original maturity is less than or equal to one year	2,569	20%	514	100%	514	41
Market related contracts: [1]						
Interest rate contracts (< 1 year)	781,178	n/a	-	20%	-	-
Interest rate contracts (> 1 year)	2,721,317	0.5%	13,607	20%	2,721	218
FX forward contracts (< 1 year)	158,422	1.0%	1,584	20%	317	25
Total off balance sheet exposures	**3,819,353**		**93,843**		**79,799**	**6,383**

The credit equivalent amount for market related contracts was calculated using the current exposure method.

(c) Additional mortgage information – LVR range

$000's	On balance sheet exposures	Off balance sheet exposures	Total exposures
Unaudited - December 2019			
Does not exceed 80%	602,842	1,879	604,721
Exceeds 80% but not 90%	6,255	-	6,255
Exceeds 90%	2,044	-	2,044
Total exposures	**611,141**	**1,879**	**613,020**

[1] Off balance sheet exposures means unutilised limits

At 31 December 2019 Nil Welcome Home loans whose credit risk is mitigated by the Crown is 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 BS2A. All new residential mortgages in respect of non-property investments lending have a loan-to-valuation ratio of less than or equal to 80%.

(d) Reconciliations of mortgage related amounts

$000's	NOTE	Unaudited December 2019
Gross finance receivables - reverse mortgages	7(b)	586,003
Loans and advances - loans with residential mortgages		25,284
On balance sheet residential mortgage exposures subject to the standardised approach	14(a)	**611,287**
Less: collective provision for impairment		(146)
Off balance sheet mortgage exposures subject to the standardised approach		1,879
Total residential exposures subject to the standardised approach		**613,020**

19 Capital adequacy (continued)

(e) Credit risk mitigation

As at 31 December 2019 the Banking Group had $2.928 million of Welcome Home Loans, 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.

(f) Operational risk

$000's	Implied risk weighted exposure	Total operational risk capital requirement
Unaudited - December 2019		
Operational risk	269,662	21,573

Operational risk is calculated based on the previous 12 quarters of the Banking Group.

(g) 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
Unaudited - December 2019			
Market risk end-of-period capital charge	Equity rate risk only	1,488	119
Market risk peak end-of-day capital charge	Equity rate risk only	1,488	119
Market risk end-of-period capital charge	Interest rate risk only	141,539	11,323
Market risk peak end-of-day capital charge	Interest rate risk only	141,539	11,323
Market risk end-of-period capital charge	Foreign currency risk only	7,324	586
Market risk peak end-of-day capital charge	Foreign currency risk only	10,056	804

Peak end of day aggregate capital charge at the end of the period is derived by following the risk methodology for measuring capital requirements within Part 10 of the standardised approach. Peak-end-of-day aggregate capital charge is derived by determining the maximum end of month capital charge over the reporting period. Based on the portfolio of the Banking Group's risk exposures, it is considered by management that the difference between end of month aggregate capital charge and end-of-day aggregate capital charge is insignificant.

(h) Total capital requirements

$000's	Total exposure after credit risk mitigation	Risk weighted exposure or implied risk weighted exposure	Total capital requirement
Unaudited - December 2019			
Total credit risk			
On balance sheet	4,263,616	3,557,846	284,629
Off balance sheet	3,819,353	79,799	6,383
Operational risk	n/a	269,662	21,573
Market risk	n/a	150,351	12,028
Total	**n/a**	**4,057,658**	**324,613**

19 Capital adequacy (continued)

(i) Capital ratios

	Unaudited December 2019	Unaudited December 2018
Capital ratios compared to minimum ratio requirements		
Common Equity Tier 1 capital expressed as a percentage of total risk weighted exposures	12.56%	13.25%
Minimum Common Equity Tier 1 capital as per Conditions of Registration	4.50%	4.50%
Tier 1 capital expressed as a percentage of total risk weighted exposures	12.56%	13.25%
Minimum Tier 1 capital as per Conditions of Registration	6.00%	6.00%
Total capital expressed as a percentage of total risk weighted exposures	12.56%	13.25%
Minimum Total capital as per Conditions of Registration	8.00%	8.00%
Buffer ratio	4.56%	5.25%
Buffer ratio requirement	2.50%	2.50%

(j) Solo capital adequacy

	Unaudited December 2019	Unaudited December 2018
Common Equity Tier 1 capital expressed as a percentage of total risk weighted exposures	12.62%	13.74%
Tier 1 capital expressed as a percentage of total risk weighted exposures	12.62%	13.74%
Total capital expressed as a percentage of total risk weighted exposures	12.62%	13.74%

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. Therefore, capital adequacy on a solo basis is calculated based on the Bank and its subsidiaries excluding Auto Warehouse.

(k) 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/business risk, regulatory and additional credit risk). As at 31 December 2019, the Banking Group has made an internal capital allocation of $7.0 million to cover these risks (2018: $48.2 million)

20 Insurance business, securitisation, funds management, other fiduciary activities

Insurance business

The Banking Group conducts insurance business through its subsidiary MARAC Insurance Limited (**MIL**).

The Banking Group's aggregate amount of insurance business comprises the total consolidated assets of MIL of $11.6 million, which is 0.27% of the total consolidated assets of the Banking Group.

Since the reporting date of the previous disclosure statement the Banking Group has undertaken a strategic review of its insurance business in line with its core banking business. The Bank has entered into a distribution agreement with DPL Insurance Limited (DPL) to distribute DPL's insurance products through the Banking Group's network and has stopped writing insurance policies in December 2019. The Banking Group will gradually exit from the insurance business as the existing written policies expire over time.

Securitisation, funds management and other fiduciary activities

Changes to the Banking Group's involvement in securitisation activities are set out in Note 18(b). There have been no material changes to the Banking Group's involvement in funds management and other fiduciary activities, in either case since the reporting date of the previous disclosure statement.

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. There has been no material changes to those policies and procedures since the reporting date of the previous disclosure statement.

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.

21 Contingent liabilities and commitments

Contingent liabilities are possible obligations, whose existence will be confirmed only by uncertain future events, or present obligations 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.

There are no pending legal proceedings or arbitrations concerning any member of the Banking Group at the date of this Disclosure Statement that may have a material adverse effect on the Bank or the Banking Group.

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

$000's	Unaudited December 2019	Unaudited December 2018	Audited June 2019
Letters of credit, guarantee commitments and performance bonds	5,990	6,417	6,757
Total contingent liabilities	**5,990**	**6,417**	**6,757**
Undrawn facilities available to customers	134,743	78,535	102,285
Conditional commitments to fund at a future date	20,726	18,797	22,921
Total commitments	**155,469**	**97,332**	**125,206**

22 Events after the reporting date

There are no material events after the reporting date that are not already included in this Disclosure Statement.

CONDITIONS OF REGISTRATION

NON-COMPLIANCE WITH CONDITIONS OF REGISTRATION

As reported in the 30 June 2019 Disclosure Statement, the Bank had not been calculating its regulatory liquidity and capital ratios in compliance with the Conditions of Registration. The Bank engaged an external consultant to undertake reviews of its calculations which has identified some discrepancies with the calculation of the Banks regulatory liquidity and capital ratios. The reviews are largely complete and further updates will be provided if necessary. The Bank has remained above all RBNZ ratio requirements at all times.

Condition of Registration 1

In December 2019, the Bank disclosed to the RBNZ that the independent review of regulatory capital ratios identified that the Bank has incorrectly calculated market risk and operational risk across a number of areas. Further the review identified that in respect of credit risk there were a number of incorrect calculations. Together this resulted in the regulatory capital ratios being up to 24 basis points lower than originally reported. As a result of the errors the Bank was not compliant with BS2A in prior periods before 31 December 2018. The calculation errors have now been corrected and are reflected in the regulatory capital reported for the six months ended 31 December 2019. At all times the Bank remained above all RBNZ ratio requirements.

Condition of Registration 11

In November 2019, the Bank disclosed to the RBNZ that the independent review of regulatory liquidity ratios identified that the Bank has incorrectly calculated its One-week mismatch ratio, One-month mismatch ratio and One-year core funding ratio across a number of areas with the ratios being up to 15, 42 and 140 basis points respectively lower than previously reported. As a result of the errors the Bank was non-compliant with condition of registration 11 in prior periods. To the extent the Bank is able to correct the calculation errors this has been reflected in the regulatory liquidity ratios from 30 November 2019. There remains some areas of non-compliance which the Bank is consulting with the RBNZ in respect of.

CHANGES TO CONDITIONS OF REGISTRATION

There are no changes to the conditions of registration since the reporting date for the previous disclosure statement.

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 24 October 2019.

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

Changes to the Capital Adequacy Framework for Registered Banks in New Zealand

The Reserve Bank of New Zealand (RBNZ) released a consultation paper in December 2018 in relation to proposed changes to the Capital Adequacy Framework for Registered Banks in New Zealand (the Framework). On 5 December 2019, the RBNZ released its final decision on the revised Framework.

The revised Framework requires Heartland Bank Limited (Heartland Bank), as a standardised registered bank, to increase its Total Capital ratio to 16% over a seven year transitional period. Heartland Bank's Total Capital ratio was 12.56% as at 31 December 2019. This means the revised Framework requires Heartland to increase its Total Capital ratio by 3.44% over the transitional period. This equates to an increase of 0.49% per year, based on Heartland Bank's financial position as at 31 December 2019.

The Bank does not expect the revised Framework to result in any changes to the underlying business model or its approach to raising equity, given:

- the quantum of the capital requirement;
- that some of the capital requirement may be satisfied through hybrid capital instruments rather than common equity;
- the length of the transitional period;
- The Bank's existing capital position.

The corporate structure of Heartland Group Holdings Limited (HGH), the ultimate parent company provides the Banking Group with flexibility to mitigate the impact of the revised Framework. Various capital raising options available include using HGH's dividend reinvestment plan, or raise debt and use the proceeds to subscribe for new capital in the Bank.
The Bank will continue to assess the options available to it to meet the requirements of the revised Framework over the transitional period.

There are no other 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.

Independent Review Report

To the shareholder of Heartland Bank Limited

Report on the consolidated half year disclosure statement of Heartland Bank Limited (the "Bank") and its controlled entities (the "Banking Group")

Conclusion

Based on our review of the consolidated interim financial statements and supplementary information of the Bank and the Banking Group on pages 5 to 41, nothing has come to our attention that causes us to believe that:

i. the consolidated interim financial statements do not present fairly in all material respects the Banking Group's financial position as at 31 December 2019 and its financial performance and cash flows for the 6 month period ended on that date;

ii. the consolidated interim financial statements (excluding the supplementary information disclosed in accordance with Schedules 5, 7, 9, 13, 16 and 18 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order")), have not been prepared, in all material respects, in accordance with NZ IAS 34 Interim Financial Reporting ("NZ IAS 34");

iii. the supplementary information, does not fairly state, in all material respects, the matters to which it relates in accordance with Schedules 5, 7, 9, 13, 16 and 18 of the Order; and

iv. the supplementary information relating to capital adequacy and regulatory liquidity requirements, has not been prepared, in all material respects, in accordance with the Registered Banks conditions of registration, Capital Adequacy Framework (Standardised Approach) (BS2A) and disclosed in accordance with Schedule 9 of the Order.

We have completed a review of the accompanying consolidated half year disclosure statement which comprises:

— the consolidated interim financial statements formed of:
  - the consolidated interim statement of financial position as at 31 December 2019;
  - the consolidated interim statements of comprehensive income, changes in equity and cash flows for the 6 month period then ended; and
  - notes to the interim financial statements, including a summary of significant accounting policies and other explanatory information.

— the supplementary information prescribed in Schedules 5, 7, 9, 13, 16 and 18 of the Order.

Emphasis of matter

We draw attention to the conditions of registration on page 42 of the consolidated interim financial statements which reference the Banking Group's identification of adjustments to the capital and liquidity ratios, as required under conditions of registration 1 and 11. Our opinion is not modified in respect of this matter.

Basis for conclusion

A review of the consolidated half year disclosure statement in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity* ("NZ SRE 2410") is a limited assurance engagement. The auditor performs procedures, consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

As the auditor of Heartland Bank Limited, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

Our firm has also provided other services to the Banking Group in relation to an assessment of the Banking Group's compliance with the quantitative requirements of BS13. Subject to certain restrictions, partners and employees of our firm may also deal with the Banking Group on normal terms within the ordinary course of trading activities of the business of the Banking Group. These matters have not impaired our independence as reviewer of the Banking Group. The firm has no other relationship with, or interest in, the Banking Group.

Use of this independent review report

This independent review report is made solely to the shareholder as a body. Our review work has been undertaken so that we might state to the shareholder those matters we are required to state to them in the independent review 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 shareholder as a body for our review work, this independent review report, or any of the opinions we have formed.

Responsibilities of the Directors for the consolidated half year disclosure statement

The Directors, on behalf of the Banking Group, are responsible for:

— the preparation and fair presentation of the consolidated half year disclosure statement in accordance with NZ IAS 34 and Schedules 3, 5, 7, 13, 16 and 18 of the Order;

— the preparation and fair presentation of the supplementary information in regards to capital adequacy and regulatory liquidity requirements in accordance with the Registered Banks conditions of registration, Capital Adequacy Framework (Standardised Approach) (BS2A) and Schedule 9 of the Order;

— implementing necessary internal control to enable the preparation of a consolidated half year disclosure statement that is fairly presented and free from material misstatement, whether due to fraud or error; and

— assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.

Auditor’s responsibilities for the review of the consolidated half year disclosure statement

Our responsibility is to express a conclusion on the consolidated half year disclosure statement based on our review. We conducted our review in accordance with NZ SRE 2410. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that:

— the consolidated interim financial statements do not present fairly in all material respects the Banking Group’s financial position as at 31 December 2019 and its financial performance and cash flows for the 6 month period ended on that date;

— the consolidated interim financial statements do not, in all material respects, comply with NZ IAS 34;

— the supplementary information does not fairly state, in all material respects, the matters to which it relates in accordance with Schedules 5, 7, 13, 16 and 18 of the Order; and

— the supplementary information relating to capital adequacy and regulatory liquidity requirements is not prepared, in all material respects, in accordance with the Registered Banks Conditions of Registration, Capital Adequacy Framework (Standardised Approach) (BS2A) and disclosed in accordance with Schedule 9 of the Order.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on the consolidated half year disclosure statement.

KPMG

KPMG
Auckland

28 February 2020