CHAIRMAN'S SPEECH
Annual General Meeting, 23 October 2013

Good afternoon and welcome to our 2013 Annual General Meeting. Thank you for your attendance today.

Heritage's performance in the 2012/13 financial year maintained our strong track record for strength and security. We achieved our 14th consecutive year of record pre-tax profit and reached more than $8.5 billion in total consolidated assets. Heritage has retained its Moody's rating of A3/P-2 with a stable outlook, and our Fitch rating of BBB+/F2 with a stable outlook - both very strong assessments of our security and our prospects.

In 2012/13, we added an extra 40 staff members to our payroll and opened our 61st branch in Oakey. That came at a time when other financial institutions were cutting staff, moving jobs offshore, and closing branches. We plan to add a further 12 employees this year. This investment in our business is both to take advantage of new opportunities but also to ensure that we deliver on our *People first* philosophy for our customers. After all, our customers are the main reason we exist.

As Chairman of Heritage, I can proudly say that we deliver great value for customers. For confirmation, you only need look at analysis carried out by independent research company Canstar for the 2012/13 financial year. That review found that Heritage customers were $40.7 million better off by banking with us rather than one of the big four banks. That was made up of a $9.6 million benefit on rates and fees on our lending products, and a $31.1 million benefit on better rates and fees on our deposit products.

Our excellent results in the last 14 years have come during a period in which the Global Financial Crisis and its flow-on impacts have created turmoil in the financial sector. While other financial institutions around the world have imploded, Heritage has remained rock solid. That's no accident. Heritage has a solid business model, a very respected brand, and a top leadership team and skilled staff.

We can look back with satisfaction on our financial results and on the way Heritage has evolved into a sophisticated modern banking institution. But we obviously can't afford to keep looking backwards. We will need to draw on all our strengths both in the short term and in the long term to continue delivering great value to our customers into the future.

In the short term, the year ahead does hold challenges. Interest rates are currently at record low levels, which is great news for borrowers but not so good news for investors. We have to carefully manage our interest income to make sure we maintain profitability while also looking to meet the needs of all our customers.

The GFC fallout has also left us in an era where the appetite for credit is considerably subdued. People are not borrowing as much these days and are paying off loans at a faster rate. That has created fierce competition from other financial institutions, both for borrowers and for depositors. As a mutual, we are absolutely committed to being the best custodians we can of our customers' funds, which means we do take a relatively conservative approach in our lending criteria. What that means is a challenging year ahead. But we are confident that we can rise to that challenge and maintain our position of strength.

While Heritage has navigated the GFC well, we are not immune from its fall-out. The financial sector worldwide has responded to the GFC by introducing stricter prudential standards that we must meet – the Basel III reforms that APRA in Australia has been particularly active in promulgating. These reforms are aimed at preventing the catastrophic failures of financial institutions that have occurred overseas. Everyone in the industry agrees that prudent supervision is a good thing. But in reality, the increased vigilance translates into much more red tape and compliance costs for Heritage, which impact smaller institutions like us disproportionately higher than the big banks.

The total cost to Heritage to allocate staff and resources to meet all compliance and regulatory matters is now over $3 million – money that does not belong to Heritage but to our members, and the indications are that this will continue to grow as a consequence. This is placing an enormous burden on our staff and causing a considerable diversion from the main activities of the Bank. However, at the same time, I would like to acknowledge the assistance given to us by the Queensland representatives of APRA who have helped us with a number of these issues.

As well as those short term pressures, we must look further ahead to ensure that Heritage keeps building and evolving into an institution that remains relevant to our customers.

Earlier this year the Board endorsed a three-year strategic plan for Heritage that sets out the roadmap for our continued success. This plan is based on three strategic pillars – growth, service and profit.

We need to grow our customer numbers and also build the depth of our relationship with existing customers. We will grow by diversifying into new business streams, such as in our pre-paid cards area that is already generating results. Qantas earlier this year released a new Frequent Flyers card that doubles as a reloadable debit card, for which we are the issuer. We already partner with Australia Post in issuing pre-paid cards and continue to work with Optus on a project to embed pre-paid card technology in mobile phones.

We need to sharpen our focus on customer service in all areas. We are currently rolling out projects to examine all our processes and look for ways to be more efficient and customer-focussed. This means taking advantage of new technologies that can automate processes. But it also means thinking outside the traditional ways we have done things to find more customer-friendly approaches. Customer service is a key point of differentiation for Heritage and we must stay ahead of our competitors in this area.

We also need to grow our profits. This desire may seem at odds with our mutual philosophy, but it is actually crucial to our continued strength and success. That's because we are required by our regulators to hold a certain level of capital for every loan that we write, as a safeguard measure. As a result of the GFC, we now have to hold higher and higher levels of capital. So, where do we get that capital from? The simple answer is that it comes from the profits that we make. That's why, as a mutual, it's still extremely important for us to continue being profitable. If we don't make a profit, we don't get extra capital. If we don't get extra capital, we can't do more lending to customers.

The success we have enjoyed in previous years has set us up well to meet the challenges ahead. I would also like to acknowledge the contributions that my fellow board members, our CEO John and his management team, and all our dedicated staff, have made toward ensuring continued success.

We look forward to another great year for Heritage and our members.