

HEARTLAND — BANK —

Disclosure Statement

For the six months ended 31 December 2017

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GENERAL INFORMATION

This Disclosure Statement has been issued by Heartland Bank Limited (the bank) and its subsidiaries (the banking group) for the six months ended 31 December 2017 in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the Order). The financial statements of the bank for the six months ended 31 December 2017 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.

GUARANTEE ARRANGEMENTS

As at the date this Disclosure Statement was signed, no material obligations of the bank were guaranteed.

DIRECTORS

There have been no changes to the Board of Directors since the signing of the 30 June 2017 Disclosure Statement.

As at the date this Disclosure Statement was signed, the Directors of the bank are:

Ellen F Comerford

Jeffrey K Greenslade

Edward J Harvey

Bruce R Irvine

Graham R Kennedy

Christopher R Mace

Geoffrey T Ricketts

Vanessa C M Stoddart

Gregory R Tomlinson

CONDITIONS OF REGISTRATION

These conditions apply on and after 1 October 2016.

The registration of Heartland Bank Limited (the bank) as a registered bank is subject to the following conditions:

1. That—

- (a) the Total capital ratio of the banking group is not less than 8%;
- (b) the Tier 1 capital ratio of the banking group is not less than 6%;
- (c) the Common Equity Tier 1 capital ratio of the banking group is not less than 4.5%;
- (d) the Total capital of the banking group is not less than \$30 million;
- (e) the bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued after 1 January 2013 in the calculation of its capital ratios unless it has received a notice of non-objection to the instrument from the Reserve Bank; and
- (f) the bank meets the requirements of Part 3 of the Reserve Bank of New Zealand document "Application requirements for capital recognition or repayment and notification requirements in respect of capital" (BS16) dated November 2015 in respect of regulatory capital instruments.

For the purposes of this condition of registration, -

the Total capital ratio, the Tier 1 capital ratio, the Common Equity Tier 1 capital ratio and Total capital must be calculated in accordance with the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

an Additional Tier 1 capital instrument is an instrument that meets the requirements of subsection 8(2)(a) or (c) of the Reserve Bank of New Zealand document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

a Tier 2 capital instrument is an instrument that meets the requirements of subsection 9(2)(a) or (c) of the Reserve Bank of New Zealand document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

1A. That—

- (a) the bank has an internal capital adequacy assessment process (ICAAP) that accords with the requirements set out in the document "Guidelines on a bank's internal capital adequacy assessment process (ICAAP)" (BS12) dated December 2007;
- (b) under its ICAAP the bank identifies and measures its "other material risks" defined as all material risks of the banking group that are not explicitly captured in the calculation of the Common Equity Tier 1 capital ratio, the Tier 1 capital ratio and the Total capital ratio under the requirements set out in the document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015; and
- (c) the bank determines an internal capital allocation for each identified and measured "other material risk".

1B. That, if the buffer ratio of the banking group is 2.5% or less, the bank must:

- (a) according to the following table, limit the aggregate distributions of the bank's earnings to the percentage limit to distributions that corresponds to the banking groups buffer ratio:

Banking group's buffer ratio	Percentage limit to distributions of the banks' earnings
0% - 0.625%	0%
>0.625% - 1.25%	20%
>1.25% - 1.875%	40%
>1.875% - 2.5%	60%

- (b) prepare a capital plan to restore the banking group's buffer ratio to above 2.5% within any timeframe determined by the Reserve Bank for restoring the buffer ratio; and
- (c) have the capital plan approved by the Reserve Bank.

For the purposes of this condition of registration, -

"buffer ratio", "distributions", and "earnings" have the same meaning as in Part 3 of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

2. That the banking group does not conduct any non-financial activities that in aggregate are material relative to its total activities.

In this condition of registration, the meaning of "material" is based on generally accepted accounting practice.

CONDITIONS OF REGISTRATION (CONTINUED)

3. That the banking group's insurance business is not greater than 1% of its total consolidated assets.

For the purposes of this condition of registration, the banking group's insurance business is the sum of the following amounts for entities in the banking group:

- (a) if the business of an entity predominantly consists of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total consolidated assets of the group headed by the entity; and
- (b) if the entity conducts insurance business and its business does not predominantly consist of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total liabilities relating to the entity's insurance business plus the equity retained by the entity to meet the solvency or financial soundness needs of its insurance business.

In determining the total amount of the banking group's insurance business—

- (a) all amounts must relate to on balance sheet items only, and must comply with generally accepted accounting practice; and
- (b) if products or assets of which an insurance business is comprised also contain a non-insurance component, the whole of such products or assets must be considered part of the insurance business.

For the purposes of this condition of registration,—

"insurance business" means the undertaking or assumption of liability as an insurer under a contract of insurance:

"insurer" and "contract of insurance" have the same meaning as provided in sections 6 and 7 of the Insurance (Prudential Supervision) Act 2010.

4. That aggregate credit exposures (of a non-capital nature and net of any allowances for impairment) of the banking group to all connected persons do not exceed the rating-contingent limit outlined in the following matrix:

Credit rating of the bank ¹	Connected exposure limit (% of the banking group's Tier 1 capital)
AA/Aa2 and above	75
AA-/Aa3	70
A+/A1	60
A/A2	40
A-/A3	30
BBB+/Baa1 and below	15

Within the rating-contingent limit, credit exposures (of a non-capital nature and net of any allowances for impairment) to non-bank connected persons shall not exceed 15% of the banking group's Tier 1 capital.

For the purposes of this condition of registration, compliance with the rating-contingent connected exposure limit is determined in accordance with the Reserve Bank of New Zealand document entitled "Connected exposures policy" (BS8) dated November 2015.

5. That exposures to connected persons are not on more favourable terms (e.g. as relates to such matters as credit assessment, tenor, interest rates, amortisation schedules and requirement for collateral) than corresponding exposures to non-connected persons.
6. That the bank complies with the following corporate governance requirements:
- (a) the board of the bank must have at least five directors;
 - (b) the majority of the board members must be non-executive directors;
 - (c) at least half of the board members must be independent directors;
 - (d) an alternate director,—
 - (i) for a non-executive director must be non-executive; and
 - (ii) for an independent director must be independent;
 - (e) at least half of the independent directors of the bank must be ordinarily resident in New Zealand;
 - (f) the chairperson of the board of the bank must be independent; and
 - (g) the bank's constitution must not include any provision permitting a director, when exercising powers or performing duties as a director, to act other than in what he or she believes is the best interests of the company (i.e. the bank).

¹ This table uses the rating scales of Standard & Poor's, Fitch Ratings and Moody's Investor Service (Fitch Ratings' scale is identical to Standard & Poor's).

CONDITIONS OF REGISTRATION (CONTINUED)

For the purposes of this condition of registration,—

"independent",—

- (a) in relation to a person other than a person to whom paragraph (b) applies, has the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014; and
- (b) in relation to a person who is the chairperson of the board of the bank, means a person who—
 - (i) meets the criteria for independence set out in section 10 except for those in paragraph 10(1)(a) in BS14; and
 - (ii) does not raise any grounds of concern in relation to the person's independence that are communicated in writing to the bank by the Reserve Bank of New Zealand:

"non-executive" has the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014.

- 7. That no appointment of any director, chief executive officer, or executive who reports or is accountable directly to the chief executive officer, is made in respect of the bank unless:
 - (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
 - (b) the Reserve Bank has advised that it has no objection to that appointment.
 - 8. That a person must not be appointed as chairperson of the board of the bank unless:
 - (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
 - (b) the Reserve Bank has advised that it has no objection to that appointment.
 - 9. That the bank has a board audit committee, or other separate board committee covering audit matters, that meets the following requirements:
 - (a) the mandate of the committee must include: ensuring the integrity of the bank's financial controls, reporting systems and internal audit standards;
 - (b) the committee must have at least three members;
 - (c) every member of the committee must be a non-executive director of the bank;
 - (d) the majority of the members of the committee must be independent; and
 - (e) the chairperson of the committee must be independent and must not be the chairperson of the bank.
- For the purposes of this condition of registration, "independent" and "non-executive" have the same meanings as in condition of registration 6.
- 10. That a substantial proportion of the bank's business is conducted in and from New Zealand.
 - 11. That the banking group complies with the following quantitative requirements for liquidity-risk management:
 - (a) the one-week mismatch ratio of the banking group is not less than zero percent at the end of each business day;
 - (b) the one-month mismatch ratio of the banking group is not less than zero percent at the end of each business day; and
 - (c) the one-year core funding ratio of the banking group is not less than 75 percent at the end of each business day.

For the purposes of this condition of registration, the ratios identified must be calculated in accordance with the Reserve Bank of New Zealand documents entitled "Liquidity Policy" (BS13) dated July 2014 and "Liquidity Policy Annex: Liquid Assets" (BS13A) dated December 2011.

- 12. That the bank has an internal framework for liquidity risk management that is adequate in the bank's view for managing the bank's liquidity risk at a prudent level, and that, in particular:
 - (a) is clearly documented and communicated to all those in the organisation with responsibility for managing liquidity and liquidity risk;
 - (b) identifies responsibility for approval, oversight and implementation of the framework and policies for liquidity risk management;
 - (c) identifies the principal methods that the bank will use for measuring, monitoring and controlling liquidity risk; and
 - (d) considers the material sources of stress that the bank might face, and prepares the bank to manage stress through a contingency funding plan.

CONDITIONS OF REGISTRATION (CONTINUED)

13. That no more than 10% of total assets may be beneficially owned by a SPV.

For the purposes of this condition,—

"total assets" means all assets of the banking group plus any assets held by any SPV that are not included in the banking group's assets:

"SPV" means a person—

- (a) to whom any member of the banking group has sold, assigned, or otherwise transferred any asset;
- (b) who has granted, or may grant, a security interest in its assets for the benefit of any holder of any covered bond; and
- (c) who carries on no other business except for that necessary or incidental to guarantee the obligations of any member of the banking group under a covered bond:

"covered bond" means a debt security issued by any member of the banking group, for which repayment to holders is guaranteed by a SPV, and investors retain an unsecured claim on the issuer.

14. That—

- (a) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the notification threshold, and does not meet the non-objection threshold, unless:
 - (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination and at least 10 working days have passed; and
 - (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011; and
- (b) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the non-objection threshold unless:
 - (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination;
 - (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011; and
 - (iii) the Reserve Bank has given the bank a notice of non-objection to the significant acquisition or business combination.

For the purposes of this condition of registration, "qualifying acquisition or business combination", "notification threshold" and "non-objection threshold" have the same meaning as in the Reserve Bank of New Zealand Banking Supervision Handbook document "Significant Acquisitions Policy" (BS15) dated December 2011.

15. That the bank is pre-positioned for Open Bank Resolution and in accordance with a direction from the Reserve Bank, the bank can—

- (a) close promptly at any time of the day and on any day of the week and that effective upon the appointment of the statutory manager—
 - (i) all liabilities are frozen in full; and
 - (ii) no further access by customers and counterparties to their accounts (deposits, liabilities or other obligations) is possible;
- (b) apply a *de minimis* to relevant customer liability accounts;
- (c) apply a partial freeze to the customer liability account balances;
- (d) reopen by no later than 9am the next business day following the appointment of a statutory manager and provide customers access to their unfrozen funds;
- (e) maintain a full freeze on liabilities not pre-positioned for Open Bank Resolution; and
- (f) reinstate customers' access to some or all of their residual frozen funds.

For the purposes of this condition of registration, "de minimis", "partial freeze", "customer liability account", and "frozen and unfrozen funds" have the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated September 2013.

16. That the bank has an Implementation Plan that—

- (a) is up-to-date; and
- (b) demonstrates that the bank's prepositioning for Open Bank Resolution meets the requirements set out in the Reserve Bank document: "Open Bank Resolution Pre-positioning Requirements Policy" (BS 17).

For the purposes of this condition of registration, "Implementation Plan" has the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated September 2013.

CONDITIONS OF REGISTRATION (CONTINUED)

17. That the bank has a compendium of liabilities that—
- (a) at the product-class level lists all liabilities, indicating which are—
 - (i) pre-positioned for Open Bank Resolution; and
 - (ii) not pre-positioned for Open Bank Resolution;
 - (b) is agreed to by the Reserve Bank; and
 - (c) if the Reserve Bank's agreement is conditional, meets the Reserve Bank's conditions.

For the purposes of this condition of registration, "compendium of liabilities", and "pre-positioned and non pre-positioned liabilities" have the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated September 2013.

18. That on an annual basis the bank tests all the component parts of its Open Bank Resolution solution that demonstrates the bank's prepositioning for Open Bank Resolution as specified in the bank's Implementation Plan.

For the purposes of this condition of registration, "Implementation Plan" has the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated September 2013.

19. That, for a loan-to-valuation measurement period, the total of the bank's qualifying new mortgage lending amount in respect of property-investment residential mortgage loans with a loan-to-valuation ratio of more than 60%, must not exceed 5% of the total of the qualifying new mortgage lending amount in respect of property-investment residential mortgage loans arising in the loan-to-valuation measurement period.
20. That, for a loan-to-valuation measurement period, the total of the bank's qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans with a loan-to-valuation ratio of more than 80%, must not exceed 10% of the total of the qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans arising in the loan-to-valuation measurement period.
21. That the bank must not make a residential mortgage loan unless the terms and conditions of the loan contract or the terms and conditions for an associated mortgage require that a borrower obtain the registered bank's agreement before the borrower can grant to another person a charge over the residential property used as security for the loan.

In these conditions of registration,—

"banking group"—

means Heartland Bank Limited (as reporting entity) and all other entities included in the group as defined in section 6(1) of the Financial Markets Conduct Act 2013 for the purposes of Part 7 of that Act.

"generally accepted accounting practice" has the same meaning as in section 8 of the Financial Reporting Act 2013.

In conditions of registration 19 to 21,—

"loan-to-valuation ratio", "non property-investment residential mortgage loan", "property-investment residential mortgage loan", "qualifying new mortgage lending amount in respect of property-investment residential mortgage loans", "qualifying new mortgage lending amount in respect of non property-investment residential mortgage loans", and "residential mortgage loan" have the same meaning as in the Reserve Bank of New Zealand document entitled "Framework for Restrictions on High-LVR Residential Mortgage Lending" (BS19) dated October 2016:

"loan-to-valuation measurement period" means a period of six calendar months ending on the last day of the sixth calendar month, the first of which ends on the last day of March 2017.

AUDITOR

KPMG
KPMG Centre
18 Viaduct Harbour Avenue
Auckland

PENDING PROCEEDINGS OR ARBITRATION

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.

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 3 October 2017.

OTHER MATERIAL MATTERS

There are no material matters relating to the business or affairs of the bank or the banking group that are not 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.

DIRECTORS' STATEMENTS

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

1. 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.
2. During the six months ended 31 December 2017:
 - (a) the bank complied with all Conditions of Registration;
 - (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 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 business risks, and that those systems were being properly applied.

This Disclosure Statement is dated 20 February 2018 and has been signed by all of the Directors.

G. T. Ricketts (Chair - Board of Directors)

G. R. Kennedy

J. K. Greenslade

C. R. Mace

E. F. Comerford

V. C. M. Stoddart

E. J. Harvey

G. R. Tomlinson

B. R. Irvine

INTERIM STATEMENT OF COMPREHENSIVE INCOME

For the six months ended 31 December 2017

\$000	NOTE	Unaudited 6 mths to Dec 2017	Unaudited 6 mths to Dec 2016	Audited 12 mths to Jun 2017
Interest income	2	152,471	135,789	278,279
Interest expense	2	62,377	56,828	115,169
Net interest income		90,094	78,961	163,110
Operating lease income		3,082	3,688	6,989
Operating lease expenses		2,132	2,728	5,195
Net operating lease income		950	960	1,794
Lending and credit fee income		1,202	1,534	3,005
Other income		1,663	1,567	3,343
Net operating income		93,909	83,022	171,252
Selling and administration expenses	3	40,248	35,966	71,684
Profit before impaired asset expense and income tax		53,661	47,056	99,568
Impaired asset expense	4	10,416	6,892	15,015
Profit before income tax		43,245	40,164	84,553
Income tax expense		12,159	11,072	23,745
Profit for the period		31,086	29,092	60,808
Other comprehensive income				
Items that are or may be reclassified subsequently to profit or loss:				
Effective portion of changes in fair value of cash flow hedges, net of income tax		(492)	1,290	1,108
Movement in available for sale reserve, net of income tax		1,034	(1,736)	(353)
Movement in foreign currency translation reserve, net of income tax		2,510	(279)	761
Items that will not be reclassified to profit or loss:				
Movement in defined benefit reserve, net of income tax		231	(84)	(84)
Other comprehensive income / (loss) for the period, net of income tax		3,283	(809)	1,432
Total comprehensive income for the period		34,369	28,283	62,240
Earnings per share from continuing operations				
Basic earnings per share	5	6c	6c	12c
Diluted earnings per share	5	6c	6c	12c

Total comprehensive income for the period is attributable to owners of the bank.

The notes on pages 15 to 32 are an integral part of these interim financial statements.

INTERIM STATEMENT OF CHANGES IN EQUITY

For the six months ended 31 December 2017

\$000	NOTE	Share Capital	Treasury Shares Reserve	Employee Benefits Reserve	Foreign Currency Translation Reserve	Available for Sale Reserve	Defined Benefit Reserve	Hedging Reserve	Retained Earnings	Total Equity
Unaudited - Dec 2017										
Balance at 1 July 2017		473,128	(2,612)	3,118	(1,055)	609	(83)	(1,152)	97,642	569,595
Total comprehensive income for the period										
Profit for the period		-	-	-	-	-	-	-	31,086	31,086
Other comprehensive income / (loss) , net of income tax		-	-	-	2,510	1,034	231	(492)	-	3,283
Total comprehensive income for the period		-	-	-	2,510	1,034	231	(492)	31,086	34,369
Contributions by and distributions to owners										
Dividends paid	8	-	-	-	-	-	-	-	(28,393)	(28,393)
Dividend reinvestment plan	8	7,495	-	-	-	-	-	-	-	7,495
Issue of share capital	8	59,225	-	-	-	-	-	-	-	59,225
Transaction costs associated with capital raising		(681)	-	-	-	-	-	-	-	(681)
Share based payments		-	-	216	-	-	-	-	-	216
Shares vested		709	-	(1,196)	-	-	-	-	-	(487)
Total transactions with owners		66,748	-	(980)	-	-	-	-	(28,393)	37,375
Balance at 31 December 2017		539,876	(2,612)	2,138	1,455	1,643	148	(1,644)	100,335	641,339
Unaudited - Dec 2016										
Balance at 1 July 2016		421,377	(2,612)	3,878	(1,816)	962	1	(2,260)	78,811	498,341
Total comprehensive income for the period										
Profit for the period		-	-	-	-	-	-	-	29,092	29,092
Other comprehensive (loss) / income, net of income tax		-	-	-	(279)	(1,736)	(84)	1,290	-	(809)
Total comprehensive income for the period		-	-	-	(279)	(1,736)	(84)	1,290	29,092	28,283
Contributions by and distributions to owners										
Dividends paid	8	-	-	-	-	-	-	-	(24,041)	(24,041)
Dividend reinvestment plan	8	5,277	-	-	-	-	-	-	-	5,277
Issue of share capital	8	20,000	-	-	-	-	-	-	-	20,000
Transaction costs associated with capital raising		(411)	-	-	-	-	-	-	-	(411)
Share based payments		-	-	553	-	-	-	-	-	553
Shares vested		1,801	-	(1,801)	-	-	-	-	-	-
Total transactions with owners		26,667	-	(1,248)	-	-	-	-	(24,041)	1,378
Balance at 31 December 2016		448,044	(2,612)	2,630	(2,095)	(774)	(83)	(970)	83,862	528,002

The notes on pages 15 to 32 are an integral part of these interim financial statements.

INTERIM STATEMENT OF CHANGES IN EQUITY (CONTINUED)

For the six months ended 31 December 2017

\$000	NOTE	Share Capital	Treasury Shares Reserve	Employee Benefits Reserve	Foreign Currency Translation Reserve	Available for Sale Reserve	Defined Benefit Reserve	Hedging Reserve	Retained Earnings	Total Equity
Audited - Jun 2017										
Balance at 1 July 2016		421,377	(2,612)	3,878	(1,816)	962	1	(2,260)	78,811	498,341
Total comprehensive income for the year										
Profit for the year		-	-	-	-	-	-	-	60,808	60,808
Other comprehensive income / (loss), net of income tax		-	-	-	761	(353)	(84)	1,108	-	1,432
Total comprehensive income for the year		-	-	-	761	(353)	(84)	1,108	60,808	62,240
Contributions by and distributions to owners										
Dividends paid	8	-	-	-	-	-	-	-	(41,977)	(41,977)
Dividend reinvestment plan	8	10,590	-	-	-	-	-	-	-	10,590
Issue of share capital	8	40,003	-	-	-	-	-	-	-	40,003
Transaction costs associated with capital raising		(655)	-	-	-	-	-	-	-	(655)
Share based payments		-	-	1,053	-	-	-	-	-	1,053
Shares vested		1,813	-	(1,813)	-	-	-	-	-	-
Total transactions with owners		51,751	-	(760)	-	-	-	-	(41,977)	9,014
Balance at 30 June 2017		473,128	(2,612)	3,118	(1,055)	609	(83)	(1,152)	97,642	569,595

The notes on pages 15 to 32 are an integral part of these interim financial statements.

INTERIM STATEMENT OF FINANCIAL POSITION

As at 31 December 2017

\$000	NOTE	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
Assets				
Cash and cash equivalents		117,316	69,655	57,040
Investments		294,197	298,519	318,698
Investment properties		1,724	6,827	4,909
Finance receivables	6	3,783,091	3,321,209	3,545,897
Operating lease vehicles		17,551	21,232	19,038
Other assets		15,522	16,196	10,000
Intangible assets		71,365	65,584	71,237
Deferred tax asset		6,718	7,334	7,852
Total assets		4,307,484	3,806,556	4,034,671
Liabilities				
Borrowings	7	3,633,423	3,247,021	3,429,741
Current tax liabilities		6,722	5,986	9,856
Trade and other payables		26,000	25,547	25,479
Total liabilities		3,666,145	3,278,554	3,465,076
Equity				
Share capital		539,876	448,044	473,128
Treasury shares		(2,612)	(2,612)	(2,612)
Retained earnings and reserves		104,075	82,570	99,079
Total equity		641,339	528,002	569,595
Total equity and liabilities		4,307,484	3,806,556	4,034,671
<hr/>				
Total interest earning and discount bearing assets		4,179,777	3,678,038	3,909,711
Total interest and discount bearing liabilities		3,626,752	3,241,811	3,425,685

The notes on pages 15 to 32 are an integral part of these interim financial statements.

INTERIM STATEMENT OF CASH FLOWS

For the six months ended 31 December 2017

\$000	NOTE	Unaudited 6 mths to Dec 2017	Unaudited 6 mths to Dec 2016	Audited 12 mths to Jun 2017
Cash flows from operating activities				
Interest received		139,100	128,484	261,339
Operating lease income received		2,618	4,394	6,974
Lending, credit fees and other income received		3,335	3,887	6,325
Operating inflows		145,053	136,765	274,638
Payments to suppliers and employees		33,543	37,432	68,017
Interest paid		63,266	64,305	125,022
Taxation paid		14,559	11,884	21,695
Operating outflows		111,368	113,621	214,734
Net cash flows from operating activities before changes in operating assets and liabilities		33,685	23,144	59,904
Proceeds from sale of operating lease vehicles		2,804	4,622	7,678
Purchase of operating lease vehicles		(2,887)	(3,421)	(6,236)
Net movement in finance receivables		(237,056)	(219,505)	(441,400)
Net movement in deposits		131,864	229,878	285,551
Net cash flows (applied to) / from operating activities		(71,590)	34,718	(94,503)
Cash flows from investing activities				
Net proceeds from sale of investment properties		3,185	1,580	3,498
Proceeds from sale of office fit-out, equipment and intangible assets		16	-	-
Net decrease in investments		23,159	-	-
Total cash provided from investing activities		26,360	1,580	3,498
Purchase of office fit-out, equipment and intangible assets		2,437	8,922	15,180
Net increase in investments		-	59,349	82,616
Purchase of equity investment		-	4,000	-
Total cash applied to investing activities		2,437	72,271	97,796
Net cash flows from / (applied to) investing activities		23,923	(70,691)	(94,298)
Cash flows from financing activities				
Net decrease in wholesale funding		(79,703)	20,649	153,726
Proceeds from issue of Unsubordinated Notes	7	150,000	-	-
Increase in share capital	8	59,225	20,000	39,348
Total cash provided from financing activities		129,522	40,649	193,074
Dividends paid	8	20,898	18,764	31,387
Transaction costs associated with capital raising		681	411	-
Total cash applied to financing activities		21,579	19,175	31,387
Net cash flows from financing activities		107,943	21,474	161,687
Net increase / (decrease) in cash held		60,276	(14,499)	(27,114)
Opening cash and cash equivalents		57,040	84,154	84,154
Closing cash and cash equivalents		117,316	69,655	57,040

The notes on pages 15 to 32 are an integral part of these interim financial statements.

INTERIM STATEMENT OF CASH FLOWS (CONTINUED)

For the six months ended 31 December 2017

Reconciliation of profit after tax to net cash flows from operating activities

\$000	Unaudited	Unaudited	Audited
	6 mths to Dec 2017	6 mths to Dec 2016	12 mths to Jun 2017
Profit for the period	31,086	29,092	60,808
Add / (less) non-cash items			
Depreciation and amortisation expense	2,311	1,001	2,376
Depreciation on lease vehicles	1,975	2,435	4,701
Capitalised net interest income	(10,884)	(10,758)	(32,221)
Impaired asset expense	10,416	6,892	15,015
Total non-cash items	3,818	(430)	(10,129)
Add / (less) movements in operating assets and liabilities:			
Finance receivables	(237,056)	(219,505)	(441,400)
Operating lease vehicles	(488)	890	818
Other assets	1,814	(2,994)	5,938
Current tax	(3,134)	(768)	3,102
Derivative financial instruments revaluation	(1,273)	(1,746)	(1,261)
Deferred tax	1,134	(266)	(784)
Deposits	131,864	229,878	285,551
Other liabilities	645	567	2,854
Total movements in operating assets and liabilities	(106,494)	6,056	(145,182)
Net cash flows (applied to) / from operating activities	(71,590)	34,718	(94,503)

The notes on pages 15 to 32 are an integral part of these interim financial statements.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

Basis of Reporting

Reporting entity

The interim financial statements presented are the consolidated financial statements comprising Heartland Bank Limited (the bank) and its subsidiaries (the banking group).

As at 31 December 2017, the bank is a listed public company incorporated in New Zealand under the Companies Act 1993, a registered bank under the Reserve Bank of New Zealand Act 1989 and a FMC reporting entity for the purposes of the Financial Markets Conduct Act 2013.

Basis of preparation

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

- 6 month period ended 31 December 2017 - Unaudited
- 6 month period ended 31 December 2016 - Unaudited
- 12 month period ended 30 June 2017 - Audited

The interim financial statements of the banking group incorporated in this Disclosure Statement have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP), NZ IAS 34 Interim Financial Reporting, IAS 34 Interim Financial Reporting and the NZX Main Board Listing Rules. They do not include all of the information required for full annual financial statements and should be read in conjunction with the bank's Annual Report for the year ended 30 June 2017.

The interim financial statements have been prepared on a going concern basis in accordance with historical cost, unless stated otherwise. The accounting policies applied by the banking group in these consolidated interim financial statements are the same as those applied by the banking group in its consolidated financial statements as at and for the year ended 30 June 2017.

Certain comparative information has been restated to comply with the current period presentation.

Performance

1 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.

All income received is from external sources, except those transactions with related parties. Certain selling and administration expenses, such as premises, IT and support centre costs are not allocated to operating segments and are included in Administration and Support (Admin & Support).

Operating segments

The banking group operates predominantly within New Zealand and Australia and comprises the following main operating segments:

Household	Providing both a comprehensive range of financial services to New Zealand families – including term, transactional and savings based deposit accounts together with residential mortgage lending (including reverse mortgages), motor vehicle finance and consumer finance – as well as reverse mortgage lending and other financial services to Australian families.
Business	Providing term debt, plant and equipment finance, commercial mortgage lending and working capital solutions for small-to-medium sized businesses.
Rural	Providing 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.

The banking group's operating segments are different from the industry categories detailed in Note 13 - Asset quality. The operating segments are primarily categorised by sales channel, whereas Note 13 - Asset quality is based on credit risk concentrations.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

1 Segmental analysis (continued)

Operating segments (continued)

\$000	Households	Business	Rural	Admin & Support	Total
Unaudited - 6 months ended 31 December 2017					
Net interest income	47,503	26,115	16,245	231	90,094
Net other income	2,750	176	22	867	3,815
Net operating income	50,253	26,291	16,267	1,098	93,909
Selling and administration expenses	7,357	3,778	2,146	26,967	40,248
Profit / (loss) before impaired asset expense and income tax	42,896	22,513	14,121	(25,869)	53,661
Impaired asset expense	6,695	2,359	1,362	-	10,416
Profit / (loss) before income tax	36,201	20,154	12,759	(25,869)	43,245
Income tax expense	-	-	-	12,159	12,159
Profit / (loss) for the period	36,201	20,154	12,759	(38,028)	31,086
Total assets	2,083,029	1,042,707	676,630	505,118	4,307,484
Total liabilities	-	-	-	3,666,145	3,666,145
Unaudited - 6 months ended 31 December 2016					
Net interest income	42,631	22,394	13,763	173	78,961
Net other income	2,857	664	96	444	4,061
Net operating income	45,488	23,058	13,859	617	83,022
Selling and administration expenses	8,824	4,119	2,120	20,903	35,966
Profit / (loss) before impaired asset expense and income tax	36,664	18,939	11,739	(20,286)	47,056
Impaired asset expense	4,960	1,557	375	-	6,892
Profit / (loss) before income tax	31,704	17,382	11,364	(20,286)	40,164
Income tax expense	-	-	-	11,072	11,072
Profit / (loss) for the period	31,704	17,382	11,364	(31,358)	29,092
Total assets	1,782,053	949,604	617,611	457,288	3,806,556
Total liabilities	-	-	-	3,278,554	3,278,554
Audited - 12 months ended 30 June 2017					
Net interest income	88,346	45,431	29,087	246	163,110
Net other income	4,514	1,629	139	1,860	8,142
Net operating income	92,860	47,060	29,226	2,106	171,252
Selling and administration expenses	13,980	8,195	4,356	45,153	71,684
Profit / (loss) before impaired asset expense and income tax	78,880	38,865	24,870	(43,047)	99,568
Impaired asset expense	10,321	4,377	317	-	15,015
Profit / (loss) before income tax	68,559	34,488	24,553	(43,047)	84,553
Income tax expense	-	-	-	23,745	23,745
Profit / (loss) for the period	68,559	34,488	24,553	(66,792)	60,808
Total assets	1,894,514	999,891	675,439	464,827	4,034,671
Total liabilities	-	-	-	3,465,076	3,465,076

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

2 Net interest income

\$000	NOTE	Unaudited 6 mths to Dec 2017	Unaudited 6 mths to Dec 2016	Audited 12 mths to Jun 2017
Interest income				
Cash and cash equivalents		435	333	825
Investments		4,766	4,242	8,966
Finance receivables		147,270	131,214	268,488
Total interest income		152,471	135,789	278,279
Interest expense				
Retail deposits		44,904	42,442	86,692
Bank and securitised borrowings		13,518	13,310	25,714
Subordinated and Unsubordinated Notes	7	2,568	-	326
Net interest expense on derivative financial instruments		1,387	1,076	2,437
Total interest expense		62,377	56,828	115,169
Net interest income		90,094	78,961	163,110

3 Selling and administration expenses

\$000		Unaudited 6 mths to Dec 2017	Unaudited 6 mths to Dec 2016	Audited 12 mths to Jun 2017
Personnel expenses				
Personnel expenses		22,528	20,167	40,766
Directors' fees		514	313	769
Superannuation		466	310	781
Audit and review of financial statements ¹		223	218	454
Other assurance services paid to auditor ²		26	28	44
Other fees paid to auditor ³		121	102	143
Depreciation - property, plant and equipment		701	697	1,361
Amortisation - intangible assets		1,610	304	1,015
Operating lease expense as a lessee		1,039	1,049	2,102
Legal and professional fees		999	1,065	1,698
Other operating expenses		12,021	11,713	22,551
Total selling and administration expenses		40,248	35,966	71,684

¹ Audit and review of financial statements includes fees paid for both the audit of annual financial statements and the 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 procedure engagements.

³ Other fees paid to the auditor include professional fees in connection with regulatory advisory services, accounting advice and a Health and Safety framework review.

4 Impaired asset expense

\$000	NOTE	Unaudited 6 mths to Dec 2017	Unaudited 6 mths to Dec 2016	Audited 12 mths to Jun 2017
Non-securitised				
Individually impaired expense		1,876	1,197	4,505
Collectively impaired expense		8,383	4,818	9,199
Total non-securitised impaired asset expense		10,259	6,015	13,704
Securitised				
Collectively impaired expense		157	877	1,311
Total securitised impaired asset expense		157	877	1,311
Total				
Individually impaired expense	13(d)	1,876	1,197	4,505
Collectively impaired expense	13(d)	8,540	5,695	10,510
Total impaired asset expense		10,416	6,892	15,015

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

5 Earnings per share

	Dec 2017			Dec 2016			Jun 2017		
	Earnings per share	Net profit after tax	Weighted average no. of shares	Earnings per share	Net profit after tax	Weighted average no. of shares	Earnings per share	Net profit after tax	Weighted average no. of shares
	cents	\$000	000	cents	\$000	000	cents	\$000	000
Basic earnings	6	31,086	520,741	6	29,092	482,334	12	60,808	493,177
Diluted earnings	6	31,086	520,795	6	29,092	485,368	12	60,808	496,725

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of fully paid shares less treasury shares.

Financial Position

6 Finance receivables

	NOTE	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
\$000				
Non-securitised				
Neither at least 90 days past due nor impaired		3,617,858	2,979,768	3,285,911
At least 90 days past due		36,634	32,405	33,047
Individually impaired		35,944	15,921	28,578
Gross finance receivables		3,690,436	3,028,094	3,347,536
Less provision for impairment		28,256	21,535	24,762
Less fair value adjustment for present value of future losses ¹		3,325	4,404	3,851
Total non-securitised finance receivables		3,658,855	3,002,155	3,318,923
Securitized				
Neither at least 90 days past due nor impaired		124,103	316,449	225,495
At least 90 days past due		440	3,786	2,582
Individually impaired		-	14	-
Gross finance receivables		124,543	320,249	228,077
Less provision for impairment		307	1,195	1,103
Total securitized finance receivables		124,236	319,054	226,974
Total				
Neither at least 90 days past due nor impaired		3,741,961	3,296,217	3,511,406
At least 90 days past due		37,074	36,191	35,629
Individually impaired		35,944	15,935	28,578
Gross finance receivables		3,814,979	3,348,343	3,575,613
Less provision for impairment	13(d)	28,563	22,730	25,865
Less fair value adjustment for present value of future losses ¹		3,325	4,404	3,851
Total finance receivables		3,783,091	3,321,209	3,545,897

¹ A fair value adjustment of \$8m for the present value of future losses was recognised on acquisition of New Sentinel Limited and Australian Seniors Finance Pty Limited. This fair value adjustment is being amortised over the estimated lifetime of the finance receivables acquired.

Refer to Note 13 - Asset quality for further analysis of finance receivables by credit risk concentration.

7 Borrowings

	NOTE	Unaudited 6 mths to Dec 2017	Unaudited 6 mths to Dec 2016	Audited 12 mths to Jun 2017
\$000				
Deposits		2,703,234	2,512,629	2,573,980
Subordinated Bonds		3,379	3,379	3,378
Subordinated Notes		22,277	-	21,180
Unsubordinated Notes		151,902	-	-
Bank borrowings		637,572	454,317	616,838
Borrowings - securitised	17(b)	115,059	276,696	214,365
Total borrowings		3,633,423	3,247,021	3,429,741

On 21 September 2017, the bank issued unsubordinated fixed rate notes (Unsubordinated Notes). These notes are paid a fixed rate of interest every 6 months and will mature on 21 September 2022.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

7 Borrowings (continued)

Deposits and Unsubordinated notes rank equally and are unsecured. The Subordinated bonds and Subordinated Notes rank below all other general liabilities of the banking group.

Securitised borrowings held by investors in Heartland ABCP Trust 1 (ABCP Trust) rank equally with each other and are secured over the securitised assets of that trust. Securitised borrowings comprise notes issued by ABCP Trust and drawings under the ABCP Trust's bank facilities. The ABCP Trust has bank facilities of \$175 million (December 2016: \$350 million; June 2017: \$300 million) which mature on 28 February 2018.

The banking group has an Australian bank facility provided by Commonwealth Bank of Australia (CBA bank facility) totalling AUD \$600 million, with AUD \$495 million drawn (December 2016: AUD \$363 million; June 2017: AUD \$440 million). The CBA bank facility is secured over the shares in Australian Seniors Finance Pty Limited (ASF) and the assets of the ASF group (comprising ASF, the ASF Settlement Trust and the Seniors Warehouse Trust). The CBA bank facility has a maturity date of 30 September 2019.

The banking agreements include covenants for the provision of information, attainment of minimum financial ratios and equity, compliance with specified procedures and certification of due performance by ASF Group.

8 Share capital and dividends

	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
000s	Number of shares	Number of shares	Number of shares
Issued shares			
Opening balance	516,236	476,469	476,469
Shares issued during the period	37,161	19,123	32,860
Dividend reinvestment plan	4,163	3,573	6,907
Closing balance	557,560	499,165	516,236
Less treasury shares	(2,299)	(2,299)	(2,299)
Net closing balance	555,261	496,866	513,937

On 14 December 2017, the bank issued 34,838,414 new shares at \$1.70 per share under a Pro Rata Rights Offer. Other shares issued during the period relate to staff share schemes.

Under dividend reinvestment plans, the banking group issued 4,163,008 new shares at \$1.8004 per share on 21 September 2017 (December 2016: 3,573,104 new shares at \$1.4766 per share on 7 October 2016; June 2017: 3,573,104 new shares at \$1.4766 per share on 7 October 2016 and 3,334,049 new shares at \$1.5939 per share on 7 April 2017).

The shares have equal voting rights, rights to dividends and distributions and do not have a par value.

(a) Dividends paid

	Dec 2017			Dec 2016			Jun 2017		
	Date declared	Cents per share	\$000	Date declared	Cents per share	\$000	Date declared	Cents per share	\$000
Final dividend	14 Aug 17	5.5	28,393	16 Aug 16	5.0	24,041	16 Aug 16	5.0	24,041
Interim dividend							21 Feb 17	3.5	17,936
Total dividends paid		5.5	28,393		5.0	24,041		8.5	41,977

9 Related party transactions and balances

Transactions with key management personnel

Key management personnel, being directors of the bank, the Chief Executive Officer (CEO) and those executive staff reporting directly to the CEO and their immediate relatives, have transacted with the banking group during the period as follows:

	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
\$000			
Transactions with key management personnel			
Interest income	3	3	8
Interest expense	(69)	(382)	(691)
Total transactions with key management personnel	(66)	(379)	(683)
Due from / (to) key management personnel			
Finance receivables	63	79	71
Borrowings - deposits	(8,464)	(22,928)	(9,153)
Total due (to) key management personnel	(8,401)	(22,849)	(9,082)

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

10 Fair value

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the banking group determines fair value using valuation techniques.

The banking group measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements.

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (derived from prices).
- Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The banking group recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

(a) Financial instruments measured at fair value

The following methods and assumptions were used to estimate the fair value of each class of financial asset and liability measured at fair value on a recurring basis in the Interim Statement of Financial Position.

Investments

Investments in public sector securities and corporate bonds are classified as being available for sale and are stated at fair value, with the fair value being based on quoted market prices (Level 1 under the fair value hierarchy) or modelled using observable market inputs (Level 2 under the fair value hierarchy).

Investments valued under Level 2 of the fair value hierarchy are valued either based on quoted market prices or dealer quotes for similar instruments, or discounted cash flows analysis.

Investments in unlisted equity securities are classified as being fair valued through profit or loss and are valued under Level 3 of the fair value hierarchy, with the fair value being based on unobservable inputs.

Finance receivables

Fixed rate reverse mortgage loans classified as finance receivables are stated at fair value with the fair value being based on present value of future cash flows discounted using observable market interest rates (Level 2 under the fair value hierarchy).

Derivative items

Interest rate swaps are classified as held for trading and are recognised in the interim financial statements at fair value. Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are determined on the basis of discounted cash flow analysis using observable market prices and adjustments for counterparty credit spreads (Level 2 under the fair value hierarchy).

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 Interim Statement of Financial Position.

\$000	Level 1	Level 2	Level 3	Total
Unaudited - Dec 2017				
Assets				
Investments	284,856	-	9,341	294,197
Finance receivables	-	3,717	-	3,717
Total assets measured at fair value	284,856	3,717	9,341	297,914
Liabilities				
Derivative liabilities held for risk management	-	2,568	-	2,568
Total liabilities measured at fair value	-	2,568	-	2,568
Unaudited - Dec 2016				
Assets				
Investments	287,228	-	11,291	298,519
Finance receivables	-	17,733	-	17,733
Derivative assets held for risk management	-	178	-	178
Total assets measured at fair value	287,228	17,911	11,291	316,430
Liabilities				
Derivative liabilities held for risk management	-	2,860	-	2,860
Total liabilities measured at fair value	-	2,860	-	2,860

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

10 Fair value (continued)

(a) Financial instruments measured at fair value (continued)

\$000	Level 1	Level 2	Level 3	Total
Audited - Jun 2017				
Assets				
Investments	306,907	-	11,791	318,698
Finance receivables	-	11,211	-	11,211
Total assets measured at fair value	306,907	11,211	11,791	329,909
Liabilities				
Derivative liabilities held for risk management	-	3,349	-	3,349
Total liabilities measured at fair value	-	3,349	-	3,349

(b) Financial instruments not measured at fair value

The following table sets out the fair values of financial instruments not measured at fair value and analyses these by the level in the fair value hierarchy into which each fair value measurement is categorised.

		Unaudited	Unaudited	Unaudited	Unaudited	Audited	Audited
		Total Fair Value	Total Carrying Value	Total Fair Value	Total Carrying Value	Total Fair Value	Total Carrying Value
\$000		Dec 2017	Dec 2017	Dec 2016	Dec 2016	Jun 2017	Jun 2017
Assets							
Cash and cash equivalents	Level 1	117,316	117,316	69,655	69,655	57,040	57,040
Finance receivables	Level 3	3,645,531	3,655,138	2,975,084	2,984,422	3,300,325	3,307,712
Finance receivables - securitised	Level 3	124,344	124,236	319,474	319,054	227,166	226,974
Other financial assets	Level 3	5,189	5,189	5,030	5,030	101	101
Total financial assets		3,892,380	3,901,879	3,369,243	3,378,161	3,584,632	3,591,827
Liabilities							
Borrowings	Level 2	3,521,873	3,518,364	2,974,043	2,970,325	3,220,344	3,215,376
Borrowings - securitised	Level 2	115,059	115,059	276,696	276,696	214,365	214,365
Other financial liabilities	Level 3	23,352	23,352	22,604	22,604	22,130	22,130
Total financial liabilities		3,660,284	3,656,775	3,273,343	3,269,625	3,456,839	3,451,871

Further information on valuation techniques and assumptions used for determining fair value is included in Note 16 of the bank's Annual Report for the year ended 30 June 2017.

Risk Management

11 Risk management policies

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 Annual Report for the year ended 30 June 2017.

12 Credit risk exposure

Credit risk is the risk that a borrower will default on any type of debt by failing to make payments when it is obligated to do so. The risk is primarily that of the lender and includes loss of principal and interest, disruption to cash flows and increased collection costs.

Credit risk is managed to achieve sustainable and superior risk-reward performance whilst maintaining exposures within acceptable risk "appetite" parameters. This is achieved through the combination of governance, policies, systems and controls, underpinned by sound commercial judgement as described below.

To manage this risk the Board Risk Committee (BRC) has been delegated the task of overseeing a formal credit risk management strategy. The BRC reviews the banking group's credit risk exposures to ensure consistency with the banking group's credit policies to manage all aspects of credit risk.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

12 Credit risk exposure (continued)

The credit risk management strategies ensure that:

- Credit origination meets agreed levels of credit quality at point of approval.
- Sector and geographical risks are actively managed.
- Industry concentrations are actively monitored.
- Maximum total exposure to any one debtor is actively managed.
- Changes to credit risk are actively monitored with regular credit reviews.

(a) Maximum exposure to credit risk

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 Interim Statement of Financial Position.

\$000	Unaudited Dec 2017
Cash and cash equivalents	117,316
Investments	284,856
Finance receivables	3,783,091
Other financial assets	5,189
Total on balance sheet credit exposures	4,190,452

(b) Concentration of credit risk by geographic region

New Zealand:	
Auckland	1,074,776
Wellington	232,265
Rest of North Island	1,065,767
Canterbury	496,277
Rest of South Island	594,543
Australia:	
Queensland	150,127
New South Wales	270,347
Victoria	132,597
Western Australia	29,830
South Australia	22,731
Rest of Australia	12,359
Rest of the world ¹	131,978
	4,213,597
Collective provision	(19,820)
Less acquisition fair value adjustment for present value of future losses	(3,325)
Total on balance sheet credit exposures	4,190,452

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

(c) Concentration of credit risk by industry sector

Agriculture	754,754
Forestry and Fishing	81,412
Mining	17,030
Manufacturing	77,895
Finance & Insurance	384,639
Wholesale Trade	37,185
Retail Trade	188,770
Households	1,923,556
Property and Business Services	396,171
Transport and Storage	202,831
Other	149,354
	4,213,597
Collective provision	(19,820)
Less acquisition fair value adjustment for present value of future losses	(3,325)
Total on balance sheet credit exposures	4,190,452

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

12 Credit risk exposure (continued)

(d) Credit exposure to individual counterparties

At 31 December 2017 the banking group did not have any period end or peak end-of-day 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) (December 2016: nil; June 2017: nil).

The peak aggregate end-of-day credit exposure is determined by taking the maximum end-of-day aggregate amount of credit exposure over the period divided by the banking group's equity as at the end of the period. Credit exposures disclosed are based on actual exposures. The credit rating is applicable to an entity's long term senior unsecured obligations payable in New Zealand, in New Zealand dollars.

13 Asset quality

The disclosures below are categorised by the following credit risk concentrations:

Rural	Lending to the farming sector primarily livestock, rural mortgage lending, seasonal and working capital financing, as well as leasing solutions to farmers. Includes lending to individuals and small to medium enterprises.
Other Corporate	Business lending other than 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	NOTE	Rural	Other Corporate	Residential	All Other	Total
Unaudited - Dec 2017						
Neither at least 90 days past due nor impaired		813,339	996,793	1,096,605	835,224	3,741,961
At least 90 days past due		10,692	9,461	802	16,119	37,074
Individually impaired		6,179	26,963	2,489	313	35,944
Fair value adjustment for present value of future losses		-	-	(3,325)	-	(3,325)
Provision for impairment	13(d)	(5,172)	(13,191)	(2,959)	(7,241)	(28,563)
Total net finance receivables		825,038	1,020,026	1,093,612	844,415	3,783,091

(b) Past due but not impaired

Unaudited - Dec 2017						
Less than 30 days past due		19,384	22,046	2,757	33,662	77,849
At least 30 days but less than 60 days past due		5,648	11,611	2,085	10,026	29,370
At least 60 days but less than 90 days past due		1,860	5,755	713	5,801	14,129
At least 90 days past due		10,692	9,461	802	16,119	37,074
Total past due but not impaired		37,584	48,873	6,357	65,608	158,422

(c) Individually impaired assets

Unaudited - Dec 2017						
Opening		2,313	25,550	714	-	28,577
Additions		9,381	10,268	1,988	313	21,950
Deletions		(4,567)	(8,253)	(206)	-	(13,026)
Write offs		(948)	(602)	(7)	-	(1,557)
Closing gross individually impaired assets		6,179	26,963	2,489	313	35,944
Less: provision for individually impaired assets	13(d)	685	7,701	232	125	8,743
Total net impaired assets		5,494	19,262	2,257	188	27,201

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

13 Asset quality (continued)

(d) Provision for impairment

\$000	Rural	Other Corporate	Residential	All Other	Total
Unaudited - Dec 2017					
Provision for individually impaired assets					
Opening provision for individually impaired assets	1,005	7,288	129	-	8,422
Impairment loss for the period					
- charge for the period	628	1,015	110	123	1,876
- recoveries	-	-	-	2	2
- write offs	(948)	(602)	(7)	-	(1,557)
Closing provision for individually impaired assets	685	7,701	232	125	8,743
Provision for collectively impaired assets					
Opening provision for collectively impaired assets	3,144	5,699	2,340	6,260	17,443
Impairment loss for the period					
- charge for the period	1,398	629	345	6,168	8,540
- effect of changes in foreign exchange rates	-	-	86	-	86
- recoveries	-	4	-	272	276
- write offs	(55)	(842)	(44)	(5,584)	(6,525)
Closing provision for collectively impaired assets	4,487	5,490	2,727	7,116	19,820
Total provision for impairment	5,172	13,191	2,959	7,241	28,563

(e) Undrawn balances for individually impaired assets

As at 31 December 2017 there \$0.20 million undrawn lending commitments to counterparties for whom drawn balances are classified as individually impaired (December 2016: nil; June 2017: \$0.22 million).

(f) 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 2017, the banking group had \$1.60 million assets under administration (December 2016: \$1.31 million; June 2017: \$1.20 million).

14 Liquidity risk

The banking group holds the following financial assets for the purpose of managing liquidity risk:

\$000	Unaudited Dec 2017
Cash and cash equivalents	117,316
Investments	284,856
Undrawn committed bank facilities	60,000
Total liquidity	462,172

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 table represents undiscounted future principal and interest cash flows. As a result, the amounts in the table below may differ to the amounts reported in the Interim Statement of Financial Position.

The contractual cash flows presented below may differ significantly from actual cash flows. This occurs as a result of future actions by the banking group and its counterparties, such as early repayments 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.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

14 Liquidity risk (continued)

\$000	On Demand	0-6 Months	6-12 Months	1-2 Years	2-5 Years	5+ Years	Total
Unaudited - Dec 2017							
Financial assets							
Cash and cash equivalents	117,316	-	-	-	-	-	117,316
Investments	-	21,956	42,468	101,044	135,489	9,341	310,298
Finance receivables	-	785,632	422,022	695,951	1,163,327	4,482,122	7,549,054
Finance receivables - securitised	-	44,018	32,806	39,925	20,377	-	137,126
Other financial assets	-	5,189	-	-	-	-	5,189
Total financial assets	117,316	856,795	497,296	836,920	1,319,193	4,491,463	8,118,983
Financial liabilities							
Borrowings	852,165	1,131,703	614,591	675,191	364,747	785	3,639,182
Borrowings - securitised	-	115,266	-	-	-	-	115,266
Derivative financial liabilities	-	2,568	-	-	-	-	2,568
Other financial liabilities	-	23,352	-	-	-	-	23,352
Total financial liabilities	852,165	1,272,889	614,591	675,191	364,747	785	3,780,368
Net financial (liabilities) / assets	(734,849)	(416,094)	(117,295)	161,729	954,446	4,490,678	4,338,615
Unrecognised loan commitments	164,153	-	-	-	-	-	164,153
Undrawn committed bank facilities	60,000	-	-	-	-	-	60,000

Undrawn committed bank facilities of \$60.0 million are available to be drawn down on demand. To the extent drawn, \$60.0 million is contractually repayable in 0-6 months' time upon facility expiry.

15 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.

\$000	0-3 Months	3-6 Months	6-12 Months	1-2 Years	2+ Years	Non-interest bearing	Total
Unaudited - Dec 2017							
Financial assets							
Cash and cash equivalents	117,308	-	-	-	-	8	117,316
Investments	34,655	1,530	37,282	91,796	119,593	9,341	294,197
Finance receivables	2,561,007	143,753	241,529	355,580	351,508	5,478	3,658,855
Finance receivables - securitised	20,341	18,333	29,434	36,701	19,427	-	124,236
Other financial assets	-	-	-	-	-	5,189	5,189
Total financial assets	2,733,311	163,616	308,245	484,077	490,528	20,016	4,199,793
Financial liabilities							
Borrowings	2,075,396	504,536	588,801	108,875	231,517	9,239	3,518,364
Borrowings - securitised	115,059	-	-	-	-	-	115,059
Derivative financial liabilities	2,568	-	-	-	-	-	2,568
Other financial liabilities	-	-	-	-	-	23,352	23,352
Total financial liabilities	2,193,023	504,536	588,801	108,875	231,517	32,591	3,659,343
Effect of derivatives held for risk management	253,570	(40,955)	(86,630)	(172,165)	46,180	-	-
Net financial assets / (liabilities)	793,858	(381,875)	(367,186)	203,037	305,191	(12,575)	540,450

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

16 Concentrations of funding

(a) Concentration of funding by industry

\$000	Unaudited Dec 2017
Agriculture	52,550
Forestry and Fishing	22,783
Mining	490
Manufacturing	11,094
Finance & Insurance	932,965
Wholesale Trade	10,502
Retail Trade	15,839
Households	2,174,775
Property and Business Services	104,890
Transport and Storage	7,917
Other	125,439
	3,459,244
Subordinated notes	22,277
Unsubordinated notes	151,902
Total borrowings	3,633,423

(b) Concentration of funding by geographical area

Auckland	986,476
Wellington	233,195
Rest of North Island	628,842
Canterbury	864,846
Rest of South Island	233,995
Overseas	686,069
Total borrowings	3,633,423

Other Disclosures

17 Structured entities

(a) Heartland Cash and Term PIE Fund (Heartland PIE Fund)

The banking group controls the operations of 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:

\$000	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
Deposits	97,546	90,078	93,998

(b) Heartland ABCP Trust 1 (ABCP Trust)

The banking group has securitised a pool of receivables comprising commercial and motor vehicle loans to the ABCP Trust.

The banking group continues to recognise the securitised assets and associated borrowings in the Interim Statement of Financial Position through the holding of subordinated debt of the ABCP Trust and the receipt of deferred purchase consideration from that trust. Whilst the bank has those interests in the ABCP Trust, the loans sold to the trust are set aside for the benefit of investors in the ABCP Trust and bank depositors have no recourse to these assets. The ABCP Trust's material assets and liabilities are represented as follows:

\$000	NOTE	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
Cash and cash equivalents - securitised		11,360	9,699	9,272
Finance receivables - securitised	6	124,236	319,054	226,974
Borrowings - securitised	7	(115,059)	(276,696)	(214,365)
Derivative financial liabilities - securitised		(822)	(1,043)	(1,042)

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

17 Structured entities (continued)

(c) Seniors Warehouse Trust (SW Trust) and ASF Settlement Trust (ASF Trust)

SW Trust and ASF Trust form part of ASF's reverse mortgage business and were set up by ASF as asset holding entities. The Trustee for both Trusts is ASF Custodians Pty Limited and the Trust Manager is ASF. The balances of SW Trust and ASF Trust are represented as follows:

	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
\$000			
Cash and cash equivalents	8,940	3,315	9,126
Finance receivables	616,485	472,161	520,572
Borrowings	(537,969)	(414,527)	(462,298)
Derivative financial liabilities	(195)	(1,309)	(547)

18 Capital adequacy

The banking group is subject to regulation by the Reserve Bank of New Zealand (RBNZ). The RBNZ has set minimum regulatory capital requirements for banks that are consistent with the internationally agreed framework developed by the Basel Committee on Banking Supervision. The resulting Basel II and III requirements define what is acceptable as capital and provide for methods of measuring the risks incurred by the banking group.

The bank's Conditions of Registration prescribe minimum capital adequacy ratios calculated in accordance with the Capital Adequacy Framework (Standardised Approach) BS2A.

The banking group has adopted the Basel II standardised approach per the RBNZ BS2A to calculate its regulatory requirements. Basel II is made up of the following three Pillars:

- Pillar 1 sets out the minimum capital requirements for credit, market and operational and compliance risks.
- Pillar 2 is designed to ensure that banks have adequate capital to support all risks (not just those set out under Pillar 1 above) and is enforced through the requirement for supervisory review.
- Pillar 3 outlines the requirements for adequate and transparent disclosure.

Basel III was developed in order to strengthen the regulation, supervision and risk management of the banking sector. The measures aim to improve the banking sector's ability to absorb shocks arising from financial and economic stress; improve risk management and governance; and strengthen banks' transparency and disclosures. The requirements that impact capital are as follows:

- The level of capital required to be held by banks increased through the introduction of new minimum capital requirements for Common Equity Tier 1 (CET1) capital, Additional Tier 1 (AT1) capital and Total capital as a percentage of risk-weighted-assets (RWAs).
- A capital conservation buffer held over and above the minimum capital ratio requirements used to absorb losses during periods of financial and economic stress.
- A counter-cyclical capital buffer be held and to be used at the RBNZ's discretion, to assist in attaining the macro-prudential goal of protecting the banking sector from periods of extraordinary excess aggregate credit growth.
- Strengthen the calculation of RWAs, particularly in respect of counterparty credit risk.

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 2017.

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 additional capital required to be held against other material risks, being concentration risk, strategic / business risk, reputational risk, regulatory risk and model risk. See Note 18(l) for further details.

Compliance with minimum capital levels is monitored by the Asset and Liability Committee and reported to the Board monthly. The ICAAP and CMP is reviewed annually by the Board.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

18 Capital adequacy (continued)

(a) Capital ratios

\$000	Unaudited Dec 2017
Tier 1 capital	
CET1 capital	
Paid-up ordinary shares issued by the bank	539,876
Retained earnings (net of appropriations)	100,335
Accumulated other comprehensive income and other disclosed reserves	(327)
<i>Less deductions from CET1 capital</i>	
Intangible assets	(71,365)
Deferred tax assets	(6,718)
Hedging reserve	1,644
Defined benefit superannuation fund asset	(659)
Total CET1 capital	562,786
AT1 capital	
Nil	-
Total Tier 1 capital	562,786
Tier 2 capital	
Subordinated Bonds	485
Subordinated Notes	15,829
Foreign currency translation reserve	1,455
Total Tier 2 capital	17,769
Total capital	580,555

(b) 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 in 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.

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

<i>Treasury shares reserve</i>	The treasury shares reserve comprises shares in Heartland Bank Limited held by the bank.
<i>Employee benefits reserve</i>	The employee benefits reserve comprises employee share options which have been recognised as an expense but not yet been exercised and converted into ordinary shares.
<i>Available for sale reserve</i>	The available for sale reserve comprises the changes in the fair value of available for sale securities, net of tax. These changes are recognised in profit or loss as other income when the asset is either derecognised or impaired.
<i>Defined benefit reserve</i>	The defined benefit plan 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.
<i>Hedging reserve</i>	The hedging reserve comprises the fair value gains and losses associated with the effective portion of designated cash flow hedging instruments.

Foreign currency translation reserve

The foreign currency translation reserve represents the differences in translation which arise when converting the financial statements of the Australian controlled entities from their functional currency into the presentational currency. It constitutes Tier 2 capital of the banking group.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

18 Capital adequacy (continued)

Subordinated bonds and notes

Heartland's 2018 Subordinated Bonds (the Subordinated Bonds) constitute Tier 2 Capital of the banking group. The Subordinated Bonds had an issue period from 12 July 2013 to 15 December 2013 and have a maturity date of 15 December 2018. The Subordinated Bonds pay quarterly interest in arrears at a rate of 6.5% per annum, provided the bank will be solvent immediately after the payment is made. The bank may elect to repay the Subordinated Bonds prior to 15 December 2018 if a regulatory event or tax event occurs and provided it will be solvent immediately after the repayment and the Reserve Bank has consented to the repayment. The Subordinated Bonds are subordinated to all other general liabilities of the banking group and are denominated in New Zealand dollars.

Heartland's 2027 Subordinated Unsecured Convertible Notes (the Subordinated Notes) constitute Tier 2 Capital of the banking group. The Subordinated Notes had an issue date of 7 April 2017 and have a maturity date of 7 April 2027. The Subordinated Notes pay quarterly interest in arrears at a rate of BBSW+4.15% per annum, provided the bank will be solvent immediately after the payment is made. The bank may elect to repay some or all of the Subordinated Notes on the First Optional Redemption Date (7 April 2022) or on any scheduled Interest Payment Date thereafter, as well as if a regulatory event or tax event occurs. Early repayment may only be made provided the bank will be solvent immediately after the repayment and the Reserve Bank has consented to the repayment. The Subordinated Notes are subordinated to all other general liabilities of the banking group and are denominated in Australian dollars.

If the Reserve Bank or a Statutory Manager requires the bank to convert all or part of the Subordinated Bonds, or to convert or write off (if conversion is not able to be effected) all or part of the Subordinated Notes, the Subordinated Bonds or Subordinated Notes will be converted or written off (as applicable) and could in each case be reduced to zero to comply with the Reserve Bank's loss absorbency requirements. The bank has not had any defaults of principal, interest or other breaches with respect to the Subordinated Bonds or Subordinated Notes.

(c) Credit risk

(i) On-balance-sheet exposures

	Total exposure after credit risk mitigation	Average Risk weight	Risk weighted exposure	Minimum Pillar 1 capital requirement
	\$000	%	\$000	\$000
Unaudited - Dec 2017				
Cash	9	0%	-	-
Multilateral development banks	68,235	0%	-	-
Multilateral development banks	51,603	20%	10,321	826
Banks - Tier 1	194,487	20%	38,897	3,112
Banks - Tier 2	868	50%	434	35
Banks - Tier 3	19,957	100%	19,957	1,597
Public sector entity (AA- and above)	49,666	20%	9,933	795
Public sector entity (A- and above)	6,991	50%	3,496	280
Corporates (AA- and above)	1,855	20%	371	30
Corporates (A- and above)	3,026	50%	1,513	121
Corporates (BBB- and above)	5,475	100%	5,475	438
Welcome Home Loans - loan to value ratio (LVR) <= 90% ¹	3,714	35%	1,300	104
Welcome Home Loans - LVR 90% >= 100% ¹	1,118	50%	559	45
Reverse Residential mortgages <= 60% LVR	998,563	50%	499,282	39,943
Reverse Residential mortgages 60 <= 80% LVR	26,527	80%	21,222	1,698
Reverse Residential mortgages > 80% LVR	2,499	100%	2,499	200
Non Property Investment Mortgage Loan <=80% LVR	28,219	35%	9,877	790
Non Property Investment Mortgage Loan 80 <= 90% LVR	4,355	50%	2,178	174
Non Property Investment Mortgage Loan 90 <= 100% LVR	462	75%	347	28
Non Property Investment Mortgage Loan > 100% LVR	2,562	100%	2,562	205
Property Investment Mortgage Loan <= 80% LVR	16,099	40%	6,440	515
Property Investment Mortgage Loan 80 <= 90% LVR	1,582	70%	1,107	89
Property Investment Mortgage Loan < 100% LVR	5,262	100%	5,262	421
Past due residential mortgages	2,650	100%	2,650	212
Other past due assets - provision >= 20%	14,025	100%	14,025	1,122
Other past due assets - provision < 20%	55,177	150%	82,766	6,621
All other equity holdings	9,341	400%	37,364	2,989
Other assets	2,654,415	100%	2,654,415	212,353
Not risk weighted assets	78,742	0%	-	-
Total on balance sheet exposures	4,307,484		3,434,252	274,743

¹ The LVR classification above is calculated in line with the banking group's Pillar 1 Capital requirement which includes capital relief for Welcome Home loans that are guaranteed by the Crown.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

18 Capital adequacy (continued)

(c) Credit risk (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	%	\$000	%	\$000	\$000
Unaudited - Dec 2017						
Off balance sheet exposures						
Direct credit substitute	1,913	100%	1,913	100%	1,913	153
Performance-related contingency	4,977	50%	2,489	100%	2,489	199
Other commitments where original maturity is more than one year	69,603	50%	34,802	100%	34,802	2,784
Other commitments where original maturity is less than or equal to one year	171,960	20%	34,392	100%	34,392	2,751
Market related contracts: ¹						
Interest rate contracts	337,633	n/a	-	20%	-	-
Interest rate contracts	275,985	0.5%	1,380	20%	276	22
Total off balance sheet exposures	862,071		74,976		73,872	5,909

¹ The credit equivalent amount for market related contracts was calculated using the current exposure method.

(d) Additional mortgage information - LVR range

\$000	On balance sheet exposures	Off balance sheet exposures ²	Total exposures
Unaudited - Dec 2017			
Does not exceed 80%	1,069,408	10,044	1,079,452
Exceeds 80% but not 90%	12,150	-	12,150
Exceeds 90%	12,054	-	12,054
Total exposures	1,093,612	10,044	1,103,656

² Off balance sheet exposures represent unutilised limits.

At 31 December 2017 \$1.12 million relating to 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 are 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 first mortgages over residential property is included in the LVR calculation, in accordance with BS2A. All new residential mortgage loans are in respect of non property investments lending and have a loan-to-valuation ratio of less than or equal to 80%.

(e) Reconciliation of mortgage related amounts

\$000	Unaudited Dec 2017
Loans and advances - loans with residential mortgages	1,093,612
On balance sheet residential mortgage exposures subject to the standardised approach	1,093,612
Off balance sheet mortgage exposures subject to the standardised approach	10,044
Total residential exposures subject to the standardised approach	1,103,656

(f) Credit risk mitigation

As at 31 December 2017 the banking group has \$4.83 million of Welcome Home Loans, whose credit risk is mitigated by the Crown. Other than this the banking group does not have any exposures covered by eligible collateral, guarantees and credit derivatives.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

18 Capital adequacy (continued)

(g) Operational risk

\$000	Implied risk weighted exposure	Total operational risk capital requirement
Unaudited - Dec 2017		
Operational risk	224,626	17,970

(h) Market risk

\$000		Implied risk weighted exposure	Aggregate capital charge
Unaudited - Dec 2017			
Market risk end-of-period capital charge	Interest rate risk only	117,377	9,390
Market risk peak end-of-day capital charge	Interest rate risk only	131,464	10,517
Market risk end-of-period capital charge	Foreign currency risk only	83,354	6,668
Market risk peak end-of-day capital charge	Foreign currency risk only	83,354	6,668

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.

(i) Total capital requirements

\$000	Total exposure after credit risk mitigation	Risk weighted exposure or implied risk weighted exposure	Total capital requirement
Unaudited - Dec 2017			
Total credit risk			
On balance sheet	4,307,484	3,434,252	274,743
Off balance sheet	862,071	73,872	5,909
Operational risk	n/a	224,626	17,970
Market risk	n/a	200,731	16,058
Total	n/a	3,933,481	314,680

(j) Capital ratios

	Unaudited Dec 2017	Unaudited Dec 2016
Capital ratios compared to minimum ratio requirements		
Common Equity Tier 1 capital expressed as a percentage of total risk weighted exposures	14.31%	12.99%
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	14.31%	12.99%
Minimum Tier 1 capital as per Conditions of Registration	6.00%	6.00%
Total capital expressed as a percentage of total risk weighted exposures	14.76%	12.96%
Minimum Total capital as per Conditions of Registration	8.00%	8.00%
Buffer ratio	6.76%	4.96%
Buffer ratio requirement	2.50%	2.50%

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the six months ended 31 December 2017

18 Capital adequacy (continued)

(k) Solo capital adequacy

	Unaudited Dec 2017	Unaudited Dec 2016
Common Equity Tier 1 capital expressed as a percentage of total risk weighted exposures	15.70%	14.34%
Tier 1 capital expressed as a percentage of total risk weighted exposures	15.70%	14.34%
Total capital expressed as a percentage of total risk weighted exposures	16.19%	14.34%

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 ABCP Trust, SW Trust and ASF Trust.

(l) 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 concentration risk, strategic/ business risk, reputational risk, regulatory and model risk). As at 31 December 2017, the banking group has made an internal capital allocation of \$104.89 million (December 2016: \$55.2 million) to cover these risks.

19 Insurance business, securitisation, funds management and 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 \$13.3 million, which is 0.31% of the total consolidated assets of the banking group.

The banking group's objective is to minimise the insurance risk to within acceptable levels through the policies and procedures implemented by management. Should adverse conditions arise, these policies and procedures are expected to mitigate the impact of the conditions on the banking group.

Marketing and distribution of insurance products

The banking group markets and distributes term life insurance and general insurance covering risks such as redundancy, bankruptcy or suspension of employment. The insurance products are either underwritten by MIL, a subsidiary of the bank, or sold by MIL on behalf of other parties who underwrite those products themselves. There have been no material changes in the banking group's marketing and distribution of insurance products since the reporting date of the previous disclosure statement.

Securitisation, funds management and other fiduciary activities

There have been no material changes to the bank's involvement in securitisation activities, and no material changes to the bank's involvement in funds management and other fiduciary activities, in either case since the reporting date of the previous disclosure statement.

20 Contingent liabilities and commitments

\$000	Unaudited Dec 2017	Unaudited Dec 2016	Audited Jun 2017
Letters of credit, guarantee commitments and performance bonds	6,890	10,567	10,903
Total contingent liabilities	6,890	10,567	10,903
Undrawn facilities available to customers	164,153	99,061	120,948
Conditional commitments to fund at future dates	77,410	120,820	153,166
Total commitments	241,563	219,881	274,114

21 Events after reporting date

There have been no material events after the reporting date that would affect the interpretation of the interim financial statements or the performance of the banking group.



Independent auditor's review report

To the shareholders of Heartland Bank Limited

Report on the half year disclosure statement of Heartland Bank Limited (the "bank") and its controlled entities (the "banking group")

Review conclusion

Based on our review of the consolidated interim financial statements and supplementary information of the bank and the banking group on pages 9 to 32, 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 2017 and its financial performance and cash flows for the six month period ended on that date;
- ii. the 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, 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, 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 interim financial statements formed of:
 - the interim statement of financial position as at 31 December 2017;
 - the 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.



Basis for conclusion

A review of the 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 the bank, 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 regulatory and accounting advisory services, and a health and safety framework review. 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 shareholders as a body. Our review work has been undertaken so that we might state to the shareholders 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 shareholders 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 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 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.



**x  Auditor's responsibilities for the review of the bank and banking group
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:

- the consolidated interim financial statements do not present fairly in all material respects the banking group's financial position as at 31 December 2017 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 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.

This description forms part of our independent review report.

KPMG
Auckland
20 February 2018