

**IMB Ltd**

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## **2013 Annual General Meeting**

### **Chairman's Address**

Michael Cole

Good morning members

It is a pleasure to be reporting to you again on IMB's recent activities and I look forward to responding to any questions from the floor you may have later in the meeting. However in anticipation of those questions I will deal with a number of the issues raised in questions received from members in the lead up to the meeting in this address.

As I noted earlier I am enthusiastic to be continuing in the role of Chairman of IMB for a final term, particularly given IMB's current strategic focus and growth priorities. I appreciate the confidence my fellow directors and members have shown me in relation to my reappointment.

In Financial Year 2013 (FY13) IMB recorded a net profit after tax of \$28.510 million, which was a decrease of 5.4% over the previous corresponding period.

I have spoken previously about the challenges of the market conditions in which IMB has operated and this year proved no exception. The slowing economic growth outlook generated low housing loan demand which is fundamental to IMB's core business. Further, the resulting monetary policy stimulus to lower official interest rates has caused downward pressure on home lending margins and this provides a demanding context in which IMB continues to strive to achieve sustainable, profitable growth.

Notwithstanding these macro conditions, it is pleasing to report a number of major Key Performance Indicators (KPIs) matched or exceeded expectations. Credit impairment was well below national industry averages and retail deposit growth was strong notwithstanding intense competition.

A number of the KPIs fell short of budget including new residential loan approvals. In a reduced revenue growth environment there continued to be a strong commitment to cost containment. Notwithstanding management's intense focus on the cost to income ratio, it lifted to 63% but if adjusted for abnormal items it was very close to our target level of 60%. The CEO's report will deal with the KPI performance in a more granular manner.

The current operating environment for IMB continues to remain challenging. The primary focus of management remains on the excellent execution of the strategic plan to deliver a sound risk/return outcome for all stakeholders.

At 30 June 2013, IMB's capital adequacy ratio was 16.4%, an increase of 0.6% over the previous year end. The gearing level remains comfortably within current regulatory requirements. The return on equity (ROE) was lower at 10.9%, down from 12.7% in the previous financial year. More than half the recorded decline in the ROE is accounted for by the further deleveraging of the IMB balance sheet in FY13.

Moving from operational to strategic issues, the focus on continued strengthening of the IMB capital base remains a priority. As I foreshadowed at the last AGM, following the strong shareholder member participation in the first buyback, it remains the Board's intention to continue to seek to buyback all ordinary shares on issue through a series of buybacks, subject to the minimum capital requirements previously stated.

To this end the Board has recently announced the second IMB share back which opened yesterday and will close in a month's time. The maximum value of shares to be repurchased is \$14 million. The full buyback details are contained in the Buyback booklet which by now eligible shareholder members will have started to receive in the mail.

A related shareholder member question which continues to be raised is whether the share buyback program rules out demutualisation or an ASX listing at a future point in time. The answer is no, as the two issues are independent over the longer term. However let me restate, the IMB has no current intention to demutualise or list on the ASX and our immediate priority is to continue with the share buyback program in order to simplify IMB's mutual structure and provide IMB with the best possible opportunity to participate in mergers with other mutual entities.

The final issue raised in relation to the buyback was with respect to professional fees incurred. In relation to the ongoing transaction it can be classified into two components. There were establishment fees associated with the first buyback and there will be renewal fees related to each subsequent transaction. Costs associated with the establishment of the buyback were written off against retained earnings in FY2013 as will subsequent costs associated with each buyback.

As expected, and through disciplined cost control, the costs associated with the current year are minor and have been well contained, reflecting fewer requirements for external advice and efficient interactions with the regulators.

Another topic addressed at the last two AGM's but which is still an issue that continues to be raised by shareholder members is the IMB dividend policy that will apply, particularly as the share buyback is implemented over an extended period.

Previously the Board has released its Dividend Guideline which states that while IMB's capital adequacy ratio is above 14% and profits are maintained or increased, it is the Board's intention to pay a full year dividend of 25 cents per share. The Board reaffirms its continued commitment for this Guideline in the current year.

Notwithstanding the decline in net profit by 5.4%, the final dividend for FY13 of 15 cents per share was maintained, with the total dividend for FY13 being 25 cents per share (equivalent to last year).

Having regard to the reduction in share capital following the buyback, the published payout ratio was 32.5%. Following the reduction in share capital as a result of the share buyback and the impact on Contributed Funding, the effective payout ratio to shareholder members has actually increased slightly in the year to approximately 77%.

As was discussed in general business at the 2012 AGM, the dividend guideline does not act as a cap on the level of dividends that may be determined. Consideration will always be given to a range of factors including any significant improvement or deterioration in IMB's financial performance, the current and expected operating environments, capital requirements and prudential controls and the PwC Report on Contributed Funding. The dividend payout ratio will remain a result, rather than a targeted outcome, of those deliberations (subject always to the payout ratio remaining below 50% on account of Mutuality requirements).

A topic raised by another member is the growth outlook for IMB. This is always an area of focus for the Board and has both an operational and a strategic dimension.

While loans to members since 2010 have increased over that period, the Board is very conscious that aggregate loans to members in fact declined slightly in FY 2013. This can be explained by a very subdued demand for new home loans and our commitment to preserve loan margins and profitability. Maintaining profitability at the expense of balance sheet growth is consistent with our highest priority of building our capital adequacy. For the same reason the branch expansion programme was subject to increased performance hurdles and resulted in new opening deferrals.

In the current financial year we have raised our loan budget consistent with stronger new lending demand and a positive growth outcome is projected for the year. But organic growth still remains challenging.

As a result, the Board has refocussed its attention and engagement on being an active participant in the mutual Approved Deposit Taking Institution (ADI) industry rationalisation. A merger with another mutual ADI is likely to be able to deliver more significant or rapid growth and an uplift in key performance metrics over time as synergies and efficiencies are achieved. We believe this is a scale business and mergers between mutual ADIs based upon a transfer of business methodology avoids the usual premium associated with such transactions, providing a good platform to create a stronger combined entity for the benefit of all IMB stakeholders. Further the strong financial metrics of IMB supports its position to be a merger partner of choice for other smaller ADIs.

The continued operation of the share buyback program has reinforced our commitment to IMB's mutual status in the eyes of our mutual ADI peers. But more may need to be done to reinforce our mutuality and to that end we intend to review the IMB constitution next calendar year and if deemed appropriate, come back to all members in relation to any changes that may further bolster our ability to complete mergers.

A further possible change that I would like to flag at this meeting is a review of IMB's operational trading status. As you may be aware, APRA has given larger ADIs the opportunity to identify as mutual banks and a number of our peers have already elected to make the change from Credit Union or Building Society to mutual bank status. Our review project is being approached with an open mind, and we are seeking the outcome that enables IMB to be most competitively positioned in the market place, particularly in newer markets and in the youth demographic. This project is in its infancy and we will keep all stakeholders updated on our progress.

There were requests from the same members as in prior years for the inclusion of additional information in the annual report, including directors' ages, deposit and loan concentrations, the IMB Community Foundation and share information.

I would point out that as each director is put forward for re-election by members, IMB includes the age of the director within the Notice of Annual General Meeting and we will continue with this practice. There is also information on a state by state basis in relation to loans and deposits. With respect to the other various suggestions received for the inclusion of additional content in the Annual Report, they are noted. However as IMB's Annual Report is already a lengthy document and significantly more detailed than its other mutual peers, IMB is not currently contemplating any changes outside of those necessitated by accounting and regulatory disclosure requirements.

To finish up in relation to questions raised by members, a comment was received in relation to the level of director's remuneration. On this matter, I point out that the remuneration of Directors was approved by members in a general meeting, and in line with the Board's commitment to members, only CPI increases have been passed on for the last four (4) years. I am comfortable that the remuneration of the IMB Board is commensurate with the work effort required, is in line with ADIs of similar size and sophistication and assists to ensure that IMB is able to attract and retain high quality Board members that meet regulatory expectations. I would direct members to page 38 of the Annual Report which provides some perspective on the extensive number of Board and Committee meetings which have been attended by all directors.

I thank all directors for their ongoing commitment and their enthusiasm with respect to ensuring IMB's strategic and operational success.

On behalf of the Directors I would also like to thank our CEO, Robert Ryan, the executive management team and all the staff at IMB for their continued commitment to IMB and all the stakeholders.

Finally I would like to thank all our members for their continuing support of IMB.

## **Chief Executive's Address**

Robert Ryan

Thank you Michael and I would also like to welcome everyone here today.

As mentioned, the 2013 financial year continued to be challenging for financial institutions, with continued volatility in financial markets, the impacts of regulatory changes and strong competition within the sector itself. The continuing uncertainty in European markets and recent events in the United States show that we are some time off returning to 'normal' operating conditions.

Although we have seen overall funding costs reduce slightly since the height of the GFC, upcoming changes to regulatory liquidity requirements and higher wholesale funding costs have seen demand for retail funds increase, which is great for retail investors but places pressure on financial institutions to grow their deposit base.

Over the last 12 months, we have experienced a period of continued low consumer sentiment and a subdued housing market, particularly in the areas IMB operates. There are indications that consumer and business sentiment is starting to improve and we are starting to see signs of increasing demand, however as with the deposit market, competition, particularly from the majors, for retail lending is strong.

Against this backdrop, IMB delivered a solid result for 2012/13.

### **Year in Review**

As discussed last year, IMB significantly increased its capital levels over the last 18 months as we prepared for the implementation of Basel III capital requirements and the first share buyback which was completed last year.

Despite the additional cost associated with the capital initiatives, as well as the pressures on interest margins and the subdued credit environment, IMB has delivered a solid operating result for the year, with net profit after tax of \$28.5 million.

The interest margin was slightly lower across the year as a result of further reductions in official interest rates and the previously mentioned strong competition for retail funds and lending. Maintaining our interest margin is an area of focus for management as we look to balance the expectations of both borrowers and depositors. The margin is currently 2.0%, although we expect to see this increase over the coming months. This is of course dependent on the Reserve Bank's decisions regarding official rates.

IMB's bad debt expense decreased by more than 50%, or \$1.1 million, on the previous year, with impairment losses of \$849,000. This is the lowest level of impairment losses since 1998 and reflects IMB's prudent lending practices and the overall quality of lending portfolio. Importantly, IMB has not sought to loosen our lending criteria in order to increase loan writings.

Management continues to maintain a disciplined approach to cost containment, particularly in an environment placing pressures on interest margins. Excluding land development expenses and the write down of IMB's land inventory in the current and prior years, expenses on a like for like basis were \$64.5 million, a very modest 1.4% higher than the previous year. IMB's ratio of non interest expenses to operating income on the same basis was 60.9%, again broadly in line with 2011/12.

IMB's balance sheet grew modestly over the year, with the increase driven by growth in deposit funds, which grew by \$154 million for the period. Reflecting IMB's strategic positioning, much of this growth was in call funds.

On the back of this growth in funding, IMB's liquidity remained strong at 29.6%, with the high quality liquid asset ratio at 16.4%, well above regulatory requirements. The capital ratio also increased during the year to 16.4%.

Loan approvals for the year were \$620 million, slightly lower than the previous year and reflecting the subdued housing market. The quality of IMB's loan book remains very strong, with IMB's level of mortgage arrears well below national averages in all categories. As at the end of September, IMB had only 15 mortgage and 2 commercial loans in arrears by more than 90 days. This is a fantastic result against a portfolio of over 20,000 loans.

In relation to our land development involvement, IMB's strategy is to exit both the One Tree Bay and Kanahooka land development activities. To that end, I am very pleased to report that earlier this month, IMB's wholly owned subsidiary IMB Land Pty Ltd and its joint venture partner, One Tree Bay Pty Ltd, disposed of the large landholding referred to as 'One Tree Bay', located on the south coast of NSW at Sussex Inlet. The sale price achieved is commensurate with the written down value of the asset.

IMB's wholly owned subsidiary IMB Land No.2 Pty Ltd, together with a joint venture partner, has developed an 80 lot residential development known as 'Brooks Terrace' at Kanahooka. Development of this site concluded in late 2012 with land sales to home buyers and builders currently underway.

IMB has no further plans to enter into land development activities.

I would now like to provide an overview of our current and future strategic focus areas:

### **Delivering Strategy**

IMB's Vision is to be the first choice, member owned banking alternative based on service and member satisfaction. The key strategies identified to deliver this Vision include:

- > Member focus
- > Productivity
- > Multi channel distribution
- > Innovation and online
- > Brand and marketing

We have implemented a range of initiatives over the last 12 months that support these strategies, including:

- Online identification and deposit account opening to provide members with an alternative method of engaging with IMB.
- We enhanced our existing mobile banking solutions with the introduction of IMB alerts, delivering up to date account information to members via SMS or email.
- We maintained our commitment to face to face banking, taking care to ensure new facilities matched to the demographics being targeted in that area. This included significant refurbishments in a number of our branches, providing a more modern space for our members to conduct their banking.
- We were awarded a 5 star rating from an independent reviewer for a number of our home loan and deposit products including the IMB Budget Home Loan, IMB Essentials Home Loan, IMB Platinum Package Variable Home Loan, IMB Business Cash Management Account and IMB DIY Super Account.

Each of these initiatives reflects our commitment to providing our members with competitive product and services that meet their everyday banking needs.

Our most recent member satisfaction survey recorded a result of 96%, continuing a three year trend of overall member satisfaction levels above 95%. Roy Morgan customer satisfaction monitor rated IMB members as the most satisfied of all building societies. These results are a testament of the member service provided by our staff and the competitive products offered to our members.

One of the key strategic achievements in the 2012/13 financial year was the successful completion of the first of a series of off market share buybacks. The buying back of IMB's ordinary shares not only aligns with IMB's mutual structure, but over time will also increase IMB's capital levels as earnings are retained by the business. We are currently part way through the second buyback with the closing date for receipt of tender forms being 20 November 2013.

At a corporate level, we have recently introduced some changes to our management structure in order to support the execution of our strategy as we focus on growing the business into the future. Nathan Campbell and Lauren Wise have been affirmed as part of our Executive team in their respective roles of Chief Risk Officer and General Manager Corporate Services. Lauren and Nathan have both been with IMB for more than 10 years.

We are also currently in the process of recruiting for a newly created position of General Manager Sales and look forward to welcoming a new addition to the Executive team in the not too distant future.

We are confident that these changes will enable greater focus on key strategies and achievement of business targets.

### **Looking ahead**

Looking ahead, we will continue with our focus on improving productivity, maintaining the strong balance sheet, increasing our brand awareness and ensuring that we are meeting the banking needs of our Members.

A critical component of our strategy is continuing to invest in technology. We will be enhancing our online and mobile banking capabilities including the introduction of a mobile banking application for Android smartphones, in addition to upgrading our mobile site to better reflect IMB's website product information and functionality.

With the payments area currently being a very dynamic space, we will be introducing a contactless Visa debit card, allowing members to pay for purchases with Visa's payWave technology. We have also agreed to partner with Visa to offer a new digital wallet service providing members with a secure way to make payments online.

As part of future online banking upgrades we are reviewing options to introduce mobile payments through mobile devices, email and social media.

We have undertaken a review of our personal lending processes with the aim of providing members with a straight-through application process and member response times matching the best in market. This review will also provide improvements to supporting processes for other products available through online channels, streamlining and enhancing the experience for members on a wider product offering.

We consider that the small to medium business segment presents a key growth opportunity for IMB. To support this growth and ensure we're positioned as a full service, competitive alternative to the major banks we will develop segment based product bundling, deliver enhanced payment facilities for small businesses, increase the size and geographic reach of our business banking teams and improve customer processes to ensure our service levels continue to set us apart from our competitors.

The concept of Mutual Bank was also discussed at last year's AGM. There are now 10 of our mutual peers that call themselves a mutual bank – particularly credit unions with an industry related membership base.

Earlier this year IMB conducted a survey of members and non members to gauge reaction to the concept of IMB calling itself a bank rather than a building society. On the whole, the feedback was positive, however prior to considering such a change, both Board and management want to ensure that such a change will be in the best interests of IMB and particularly our members. We expect to undertake further research on this matter and are maintaining a watching brief over those institutions that have changed their name to 'mutual bank'.

As seems to be the case each year, there are a number of regulatory changes and requirements that we are working to implement. A cross section of the regulatory requirements we, and our peers, are currently working on include:

- APRA's Financial Claim Scheme and reporting of a Single Client View
- Implementing the US's Foreign Account Tax Compliance Act which is focused on strengthening information reporting and withholding tax compliance with respect to US persons
- Responding to further Basel III changes, particularly with regard to liquidity and capital
- implementing enhanced compliance policies and procedures to address the new Australian Privacy Principles and the expanded regime relating to the use and disclosure of an individual's credit reporting information
- maintaining a watching brief for a range of new risk management requirements have been foreshadowed by APRA over the coming months

As you would appreciate, there is considerable effort across many business channels in implementing these changes.

This is a brief summary of what we are doing from a business perspective. I'd like to now take a moment to discuss the activities of the IMB Community Foundation.

### **Supporting Local Communities**

The IMB Community Foundation was established in 1999 to provide financial support to community groups with positive ideas and concepts to help them convert their ideas into working projects.

Since its inception, the IMB Community Foundation has granted \$6.6 million to support over 400 projects with a diverse range of project themes, throughout our local communities.

This year, the Foundation has donated a further \$500,000 to 52 local projects including disadvantaged youth, senior community involvement, mental health groups, health programs and educational opportunities.

In addition to the support provided by the Community Foundation, IMB also supports a range of charity, sporting and community organisations, as well as numerous other grassroots local projects and events that directly benefits the communities where IMB members live and work.

We are very proud of the difference the IMB Community Foundation is making within the community. In many instances, the funding provided by the Foundation not only allows the realisation of identified outcomes for these groups but also broader outcomes for the community.

### **Conclusion**

Looking ahead, we expect the current low rate environment to continue, with strong competition between financial institutions as they look to increase their share of both consumer lending and retail deposits. This competition will continue to place pressure on interest margins and overall financial performance.

We remain confident about our future financial performance however this will be dependent on broader economic conditions.

I would like to acknowledge the ongoing dedication and commitment of our staff. During a year that presented many challenges, IMB's staff continue to provide excellent service to our members. Through the efforts of our staff, IMB continues to deliver Better Value Banking to members which distinguishes us from our competitors.

I would also like to thank the Board for their continued support and guidance over the past year. The additional time and effort that our Board members contribute to IMB's business in addition to their other duties is greatly appreciated. IMB's strength is a testament to their prudent oversight.

And finally, I would also like to thank our loyal members for their continued support of IMB.

In our 134th year, IMB remains a strong and secure mutual financial institution providing our members with a competitive alternative to the banks and I look forward to building on this year's success in the year ahead.

Thank you.