



Update for IMB Stakeholders

In 2008, IMB's Board sought a report from PricewaterhouseCoopers Securities Ltd (**PwC Securities**) on the relative contribution Shareholder Members have made to the permanent funding of IMB compared to the contribution made by IMB's other Member classes (**Contributed Funding**).

PwC Securities provided its report to IMB's Directors on 4 September 2008 and this report was made available to Members (**the 2008 Report**). The 2008 Report and the covering Explanatory Memorandum issued by IMB in conjunction with the 2008 report are located under the 2008 Market Announcements on IMB's website.

In 2012 IMB undertook the first of a series of off-market buybacks of ordinary shares on issue (the **Buybacks**). As a result, 2.9 million ordinary shares were bought back and cancelled. A second Buyback was undertaken in 2013 with a further 2.1 million ordinary shares bought back and cancelled.

Following the Buybacks, the Board considered it appropriate to understand the effect of the Buybacks on the allocation of Contributed Funding. The Board commissioned PwC Securities to advise on how Buybacks could be incorporated into the Contributed Funding framework developed in 2008. The results of PwC Securities' review are contained in the attached report (**the 2014 Report**).

If you have any questions or comments in relation to these documents, they should be directed to IMB's Company Secretary at (02) 4298 0211 or cosec@imb.com.au.



PRICEWATERHOUSECOOPERS SECURITIES LTD

FINANCIAL SERVICES GUIDE

This Financial Services Guide is dated 24 June 2014

1. About us

PricewaterhouseCoopers Securities Ltd (ABN 54 003 311 617, Australian Financial Services Licence no 244572) ("PwC Securities") has been engaged by IMB Limited ("IMB") to provide a report in the form of a letter of advice in relation to the updating of analysis provided in 2008 on the allocation of Contributed Funding (the "Report") for disclosure on the IMB website.

You have not engaged us directly but have been provided with a copy of the Report as a retail client because of your connection to the matters set out in the Report.

2. This Financial Services Guide

This Financial Services Guide ("FSG") is designed to assist retail clients in their use of any general financial product advice contained in the Report. This FSG contains information about PwC Securities generally, the financial services we are licensed to provide, the remuneration we may receive in connection with the preparation of the Report, and how complaints against us will be dealt with.

3. Financial services we are licensed to provide

Our Australian financial services licence allows us to provide a broad range of services, including providing financial product advice in relation to various financial products such as securities, interests in managed investment schemes, derivatives, superannuation products, foreign exchange contracts, insurance products, life products, managed investment schemes, government debentures, stocks or bonds, and deposit products.

4. General financial product advice

The Report contains only general financial product advice. It was prepared without taking into account your personal objectives, financial situation or needs.

You should consider your own objectives, financial situation and needs when assessing the suitability of the Report to your situation. You may wish to obtain personal financial product advice from the holder of an Australian Financial Services Licence to assist you in this assessment.



5. Fees, commissions and other benefits we may receive

PwC Securities charges fees to produce reports, including this Report. These fees are negotiated and agreed with the entity who engages PwC Securities to provide a report. Fees are charged on an hourly basis or as a fixed amount depending on the terms of the agreement with the person who engages us. In the preparation of this Report our fees are charged on an hourly basis and as at the date of this Report amount to approximately \$80,000.

Directors or employees of PwC Securities, PricewaterhouseCoopers, or other associated entities, may receive partnership distributions, salary or wages from PricewaterhouseCoopers.

6. Associations with issuers of financial products

PwC Securities and its authorised representatives, employees and associates may from time to time have relationships with the issuers of financial products. For example, PricewaterhouseCoopers may be the auditor of, or provide financial services to, the issuer of a financial product and PwC Securities may provide financial services to the issuer of a financial product in the ordinary course of its business. PricewaterhouseCoopers has provided certain consulting services to IMB and PricewaterhouseCoopers Securities previously provided advice in relation to the allocation of Contributed Funding in 2008.

7. Complaints

If you have a complaint, please raise it with us first, using the contact details listed below. We will endeavour to satisfactorily resolve your complaint in a timely manner. In addition, a copy of our internal complaints handling procedure is available upon request.

If we are not able to resolve your complaint to your satisfaction within 45 days of your written notification, you are entitled to have your matter referred to the Financial Ombudsman Service ("FOS"), an external complaints resolution service. FOS can be contacted by calling 1300 780 808. You will not be charged for using the FOS service.

Contact Details

PwC Securities can be contacted by sending a letter to the following address:

Kevin Reeves
Darling Park Tower 2
201 Sussex Street
GPO Box 2650
SYDNEY NSW 1171



24 June 2014

The Directors
IMB Limited
253-259 Crown Street
WOLLONGONG NSW 2500

Dear Directors

Update of advice provided by PwC Securities in 2008 in relation to the allocation of Contributed Funding to reflect the impact of share buybacks

1. Introduction

In accordance with our letter of engagement, PwC Securities has been requested to update the analysis we prepared in our report of 4 September 2008 (the 2008 Report) in relation to the estimated proportions of Contributed Funding provided by Depositor and Borrower Members (D&B Members) and Shareholder Members of IMB as at 30 June 2008.

There is no statutory requirement for IMB to commission this report, or having obtained the report, to provide it to the D&B Members and the Shareholder Members. The report does not constitute an independent expert report within the terms of ASIC Regulatory Guide 111, but instead represents advice provided to the Directors of IMB in response to a specific request.

The report has been prepared exclusively for the use of the Directors. However, the Directors wish to make the report available to D&B Members, Shareholder Members and other parties. We have consented to this disclosure on the basis that the report is disclosed together with the Update for IMB Stakeholders provided by the Directors, the 2008 Explanatory Memorandum and the 2008 Report.

2. Purpose, scope and limitations

This report (Report) has been requested by the Directors to assist them in updating their assessment of the relative contribution of the D&B Members and the Shareholder Members to the permanent funding of IMB and to consider future dividend policy. Our Report does not cover all matters that will be considered by the Directors in relation to dividend policy and the current and future interests of the D&B Members and the Shareholder Members.

The request for the update follows the commencement of the buyback programme by IMB which is a transaction type not incorporated in the original analysis (as no buybacks occurred prior to 2008). Specifically, IMB has requested that we:

- Identify potential mechanisms to incorporate share buybacks into the Contributed Funding framework set out in the 2008 Report.
- Comment on the implication for the Contributed Funding analysis of buybacks being priced at a discount to a Deemed Market Value (which is derived from market trading prices)
- Comment on the implication for the Contributed Funding analysis of the buyback providing significant franking credits attached to the amount of the cash consideration
- Comment on the approximate allocation of Contributed Funding following the second buyback completed in November 2013.

The Report has been provided to the Directors solely for the purposes of their consideration of the relative contributions of D&B Members and Shareholder Members to the Contributed Funding of IMB.



The Report should not be used, and has not been prepared, as advice to any party that might be considering the sale or purchase of ordinary shares in IMB or considering the commencement or termination of a deposit holding or borrowing relationship that gives rise to membership of IMB. The report should not be relied upon by any party considering such a shareholding, deposit holding or borrowing relationship with IMB.

The Report does not constitute advice to the Directors in relation to the value of ordinary shares in IMB, the price at which future buybacks should occur or whether IMB should undertake buybacks. We have not made any assessment of the value of IMB, the value of the ordinary shares in IMB, the price at which future buybacks might occur nor the commercial logic of further buybacks.

As a condition of our engagement, IMB has indemnified PwC Securities and PwC against any claims, cost damages or expenses that may result from any third party claims arising out of or in relation to the provision of services to IMB or the use or circulation of this Report.

This report is to be read in conjunction with the attached Financial Services Guide.

3. Characteristics of the IMB buybacks

IMB has completed two buybacks of ordinary shares in September 2012 and November 2013.

The buyback mechanism involves Shareholder Members tendering shares by reference to a nominated discount to a Deemed Market Value. Deemed Market Value is determined by reference to volume weighted trading prices for IMB shares prior to the buyback announcement indexed in the period up to the closing date of the buyback offer in line with movements in the S&P/ASX Small Ordinaries index. Shares are bought back at the discount equal to the minimum discount required to purchase the number of shares determined by the directors of IMB to be acquired under the buyback.

The following table summarises the buybacks completed in 2012 and 2013:

Buyback date	Shares bought back Million	Shares bought back %	Buyback Price \$	Buyback consideration (\$ Mil)
September 2012	2.9	7.3	3.28	9.5
November 2013	2.1	5.8	4.07	8.7

To the extent that buybacks are funded from the balance sheet of IMB, they do not reflect direct transfers of value from D&B Members to Shareholder Members (as would be the case if D&B Members were buying out Shareholder Members using external funds). The buybacks reduce the relative interest of Shareholder Members, but also reduce the value of the overall IMB entity by the amount of the consideration. Therefore, so long as there are continuing Shareholder Members, the pricing of share buybacks will affect the continuing interests in IMB of both D&B Members and Shareholder Members.

4. The 2008 Report on Contributed Funding

In updating the advice set out in the 2008 Report, we note the following points in relation to the methodology set out in that report:

- The allocation of Contributed Funding set out in the 2008 Report was approximate reflecting the fact that it was not based on a legally defined concept and the need to make significant estimates in our analysis to reflect transactions that had occurred over an extended period. During that period, there was no explicit guidance on the assessed interests of D&B Members and Shareholder members in the Contributed Funding of IMB as a continuing entity.

- The methodology identified the value reasonably allocable to Shareholder Members based on the initial subscription for shares in 1989 and subsequent further issues of shares (primarily by way of dividend reinvestment) and retention of profits.
- In the absence of any commercial guidance to D&B Members and Shareholder Members prior to 2008 on their assessed interests in the Contributed Funding of IMB, the assumption was made that retained profits in any year were shared pro rata to their estimated interest in Contributed Funding at the beginning of each year.
- Analysis of Contributed Funding in the 2008 Report was aligned with the shareholder funds of IMB up to 30 June 2008. For the purposes of the allocation, the 2008 Report considered two scenarios where:
 - The economic value of an interest in IMB was considered to be equal to the underlying share of the shareholder funds of IMB (Appendix 2 of the 2008 Report);
 - The economic value of IMB at relevant times was different to the underlying shareholder funds. For the purpose of this it was assumed that the original subscription would have been made at a discount to net asset value per share, but subscriptions in subsequent years would have been made based on the economic value of interests in IMB being up to twice the net asset value (Appendix 3 of the 2008 Report).
- The assumptions made in the analysis in the 2008 Report on the relationship of the economic value of IMB to net asset value was based on very broad estimates of financial sector valuation parameters across an extended period from 1989 to 2005 (when the dividend reinvestment plan ceased).

The analysis in the 2008 Report applying the two scenarios estimated that the interest of the Shareholder Members as at June 2008 was between 40.8% and 46.4% (or 43.6% expressed as an average).

Since there were no further equity subscriptions between June 2008 and June 2012 (the balance sheet date immediately prior to the first share buyback), the above estimated range of 40.8% to 46.4% for the Shareholder Member interest would remain unchanged up to June 2012 based on the exact methodology applied in the 2008 Report for the period 1989 to 2008.

5. Allocation of retained profits in the period since the 2008 Report

During the period 1989 to 2008, there was no clear guidance on the exact interests of D&B Members and Shareholder Members in IMB as a continuing entity. For the purposes of the analysis in the 2008 Report, it was assumed that retained profits were shared between D&B Members and Shareholder Members pro rata to their interests at the beginning of each financial year. We consider that this assumption was commercially appropriate given the absence of any explicit guidance and was not inconsistent with the dividend policy over the period 1989 to 2008.

For the allocation of retained profits after 2008, there are two potential approaches:

- The methodology applied in the 2008 Report for the period 1989 to 2008 could be replicated. This would mean that Shareholder Members continue to share in retained profits (i.e. after dividends are paid to Shareholder Members) pro rata to their assessed interest in the Contributed Funding of IMB. Given that there have been no share issues subsequent to the 2008 Report; this approach would mean that the interest of the Shareholder Members prior to the first buy back would have been the same as at the date of the 2008 Report. **(Approach 1)**

- Alternatively, it could be considered that, once the respective interests of the D&B Members and Shareholder Members were defined in 2008, annual post tax profit should be allocated between the D&B Members and Shareholder Members pro rata to their assessed interests in Contributed Funding. To the extent that dividends were paid to Shareholder Members, the dividend would be charged against their share of post-tax profits. This approach would effectively consider D&B Members as being equivalent to Shareholder Members in sharing in the returns generated by IMB, but with none of their share of profit being paid out by way of dividends. To the extent that no dividends were charged against share of profits allocated to D&B Members, this would mean that the proportional interest of the Shareholder Members in Contributed Funding would dilute over time due to the higher implicit reinvestment by D&B Members. **(Approach 2)**

We set out below an analysis of the impact of buybacks on the allocation of Contributed Funding. We have not assessed whether Approach 1 or Approach 2 is more appropriate. However, we note that Approach 2 would reflect a position where the interests of the D&B Members and Shareholder Members in IMB were considered to be restricted to ownership interests. By way of contrast, the allocation under Approach 1 would arguably reflect more a situation where D&B Members were considered to be receiving significant other benefits as a result of their membership of IMB.

6. Using Approach 1, buybacks cannot be directly incorporated into the Contributed Funding calculations in the 2008 Report

Buybacks were not addressed in the methodology set out in the 2008 Report as the analysis addressed a period when no buybacks occurred.

The 2008 Report allocated value between D&B Members and Shareholder Members in financial and economic terms using a fixed range of relativities (in the case of dividends reinvested, it was assumed that the economic value of IMB was between 100% and 200% of the balance sheet shareholders funds of IMB during the period 1989 to 2005). The models did not seek to compare the actual share prices at the date of dividend reinvestments over this period to the economic values implied by the assumed relativities.

The models in Appendix 2 and Appendix 3 of the 2008 Report cannot therefore be simply updated for buybacks (by including the buyback cash consideration paid as a negative subscription) as the buyback price will not align with the different assumptions in the two models (where economic value is assumed to be either 100% or 200% of balance sheet shareholder funds of IMB).

Further the 2008 models did not incorporate analysis of the number of actual shares on issue at any time. This could lead to anomalous results. By way of demonstration, using a hypothetical example:

- If all the 39.9 million shares on issue at June 2012 had been bought back at a price of \$1 per share (e.g. a negative cash subscription of \$39.9 million), both of the 2008 models would continue to disclose significant Contributed Funding attributable to Shareholder Members despite the fact that no shares remained on issue.
- If a substantial portion of the 39.9 million shares had been bought back at very high prices, the 2008 models would potentially show all Shareholder Member Contributed Funding being eliminated before all Shareholder Members had their shares bought back.

As such, the models in the 2008 Report cannot be adapted to reflect the buybacks without the relationship between buyback price and the assumed economic value of IMB, at the time of each buyback, being specifically incorporated into the analysis.

Instead, in the following section, we set out a relatively simple method of calculation to adjust the estimated Shareholder Member interest in Contributed Funding for a buyback that is consistent with the principles in the 2008 Report and Approach 1.



7. Updating the estimated interest of Shareholder Members following buybacks where the interest prior to the first buy back is assessed in line with Approach 1

The pricing of future buybacks and the number of shares bought back will affect the aggregate financial resources available to IMB. If buybacks are made at a higher price, they will reduce the aggregate economic value of IMB by a greater amount than if the same buyback is made at a lower price. However, once the final price for a buyback has been set by the Directors, the economic value attributed to, and cash paid to, selling Shareholder Members is effectively being provided pro rata by the D&B Members and continuing Shareholder Members.

To the extent that a high price or a low price is paid under the buyback, it will not affect the post buyback allocation of value between D&B Members and continuing Shareholder members as they will effectively “fund” any premium, or receive the “benefit” of any discount, pro rata to their post buyback interests.

Reflecting this logic, the Shareholder Member interest following a buyback (allowing for the fact that the buyback is funded by both D&B Members and Shareholder Members) can be generalised by the following equation:

$$SMI_{post} = \frac{(SMI_{pre} \times PROP_{post})}{(1 - (SMI_{pre} \times PROP_{bb}))}$$

Where:

SMI_{post} is the percentage Shareholder Member Interest post buyback

SMI_{pre} is the Shareholder Member interest pre buyback (estimated to be 43.6% immediately prior to the 2012 buyback based on application of the methodology in the 2008 Report)

PROP_{post} is the proportion of shares pre buyback that remain on issue post the buyback (92.7% in the case of the 2012 buyback)

PROP_{bb} is the proportion of shares bought back (7.3% in the case of the 2012 buyback)

The denominator in the above equation addresses the characteristic of a buyback that it reduces the overall economic value of IMB as well as the relative interest of the Shareholder Members.

Applying this formula to the 2012 buyback, the following estimates for Shareholder Member post buyback interest are derived based on the assumed starting mid point interest for Shareholder Members of 43.6%:

$$SMI_{post} = \frac{43.6 \% \times 92.7 \%}{(1 - (43.6 \% \times 7.3 \%))} = \frac{40.42 \%}{(1 - 0.032)} = 41.8 \%$$

Applying the formula to the 2013 buyback, the estimated interest of Shareholder Members would be further reduced in line with the following calculation:

$$\frac{41.8 \% \times 94.2 \%}{(1 - (41.8 \times 5.8 \%))} = \frac{39.38}{(1 - 0.024)} = 40.3 \%$$



In appendix A to this Report we set out an indicative analysis of the way that future Shareholder Member interest would decrease from the levels implied by Approach 1 in a scenario where future buybacks were made at a rate of 4 million shares per annum (with all outstanding shares being repurchased in the tenth year of the buyback programme).

8. Movements in the interest of Shareholder Members since 2008 and the impact of buybacks where Approach 2 is applied

Approach 2 is based on the premise that post tax profit is allocated to D&B Members and Shareholder Members in line with their assessed interests in Contributed Funding post 2008. Applying that approach, dividends paid to Shareholder Members would be charged against their notional share of profit after tax (with the remaining amount of undistributed profit effectively being the contribution to retained profits).

To the extent that no dividends are payable to D&B Members, Approach 2 would imply that the interest of Shareholder Members declined in the period after 2008 as their notional contribution to retained earnings was considerably less than that notionally provided by D&B Members.

There is no definitive way of modelling how the relative interest of Shareholder Members would decline over time in line with applying Approach 2. However, in appendix B, we have developed a relatively simple analysis of the period 2009 to 30 June 2013 which we consider provides a commercial estimate of how the Shareholder Member interest has changed over time based on Approach 2.

The simplified analysis is based on the following assumptions and approximations:

- The interest of the Shareholder Members at 30 June 2008 was 43.6% in line with the 2008 Report.
- The relative interests of D&B Members and Shareholder Members at 30 June 2008 is recorded by assuming each group held a notional number of shares in IMB in line with the assessed interests in Contributed Funding at that date. Based on the fact that the Shareholder Members actually held 39.9 million shares representing an assessed 43.6% interest, this would imply that the total number of notional shares was around 91.5 million (39.9 million/0.436). The balance of notional shares attributable to D&B Members would be around 51.6 million.
- Subsequent to 30 June 2008, annual profit after tax is allocated to the D&B Members and Shareholder Members pro rata to their assessed interest in Contributed Funding at the beginning of the financial year (i.e. the Shareholder members would be allocated 43.6% of profit after tax in the year to 30 June 2009).
- The dividend paid to Shareholder Members in respect of each year subsequent to 2008 would be charged against their share of the profit after tax in that year. Any amount of profit after tax attributable to Shareholder Members that was not distributed would be used to acquire notional shares in IMB.
- The retained profits arising from the allocation of post-tax profit to D&B Members (to whom no dividends are paid) would be assumed to be used to acquire notional shares on behalf of the D&B Member interest.
- The number of notional shares allocated to the retained profits provided by the Shareholder Members and D&B Members would be based on the market value of the shares issued. As a broad proxy for that value, we have used the average IMB share price during the financial year in which the retained profits were generated. This assumption is approximate (and for example does not allow for the fact that the notional shares assumed to be held by Shareholder Members will gradually increase above the number of shares on issue), however, it provides an indicative objective measure of the relationship between the cash profits retained relative to a market measure of the value of IMB shares.



- At the end of each year, the relative interest of the D&B Members and Shareholder Members is recalculated based on the estimated number of notional shares held by each grouping following the assumed issues of notional shares.
- Using Approach 2, the impact of the buybacks would be reflected by reducing the number of notional shares allocable to Shareholder Members pro rata to the proportion of actual shares bought back. For example, if 5% of the actual shares were bought back, it would be assumed that 5% of the notional shares held by the Shareholder Members immediately prior to the buyback were bought back. This method of adjustment gives a consistent result to the calculation applied under Approach 1.

An analysis of the movement in the Shareholder Member interest over the period from 2008 to the completion of the 2013 buyback under Approach 2 applying the above assumptions is set out in appendix B. The principal implications of applying Approach 2 are:

- In the period from 30 June 2008 to 30 June 2012 (immediately prior to the first buyback), under Approach 2 the interest of Shareholder Members would have reduced from 43.6% to 36.6%
- Following the 2013 buyback, applying Approach 2 would indicate that the interest of Shareholder Members was reduced to 32.1%

The extent to which Shareholder Member interest will decline in future applying Approach 2 would depend on the level of future buybacks, the future post tax profits generated by IMB, the prevailing share price (to the extent it would affect the level of notional reinvestment by D&B Members and Shareholder Members) and dividends paid to Shareholder Members.

In appendix C, we have set out a simulation of possible future movements in Shareholder Member interest over the next five years applying Approach 2 on the following assumptions:

- No further buybacks occur
- IMB profit after tax increases at a rate of 2.5% in line with long term inflation targets
- Annual dividend remains constant at 25 cents per share
- Notional dividend reinvestment occurs at a future share price of \$4.50

While the analysis in appendix C is indicative (and based on broad assumptions), it demonstrates how Approach 2 would imply further progressive declines in Shareholder Member interest even where buybacks do not occur.

To the extent that further buybacks occur in future, the decline in Shareholder Member interest would be greater than that shown in appendix C.

The simulation in appendix C is indicative to demonstrate principles only. Parameters in future years for profit after tax, dividends and future share price are for demonstration purposes only. These parameters will vary according to future events and decisions made by the Directors. The use of the parameters shown above does not mean that they represent estimates of future values by PwC Securities or the Directors.

9. Implication of share buybacks being made at a discount to Deemed Market Value and treatment of franking credits

It is likely that in future buybacks, “bidding” will result in buybacks being made at discounts to Deemed Market Values derived from the prices at which IMB shares trade. This reflects – inter alia - the fact that franking credits attach to part of the buyback consideration.



As discussed in the previous sections, the allocation of relative interests between D&B Members and Shareholder Members following a buyback is not sensitive to the actual pricing of the buyback. Accordingly, no adjustment is required to the formula set out in section 6 or the approach in Section 8 to reflect the fact that buybacks may be made at a discount to prevailing share prices.

To the extent that the franking credits attaching to a portion of the buyback consideration may result in future buybacks occurring at a discount, value for franking credits will be generated for all members:

- Selling Shareholder Members electing to participate in the buyback will actually receive and utilise franking credits.
- Shareholder Members not participating in the buyback will benefit from the fact that the cash cost of buying back shares is potentially reduced and hence the value of their continuing interest increased.
- D&B Members will also benefit from any reduced cash cost of buying back ordinary shares and the consequent higher economic value of IMB going forward.

To the extent that the availability of franking credits in a buyback can be used to reduce the price of future buybacks, economic value will be realised by both D&B Members and Shareholder Members.

We do not consider the amount of franking credits attaching to buyback consideration requires specific adjustment to the methods set out in section 7 to 8 for measuring the interests of Shareholder Members in Contributed Funding following buybacks. However, it should be a commercial objective for the Directors of IMB to generate value for franking credits on behalf of all continuing D&B Members and Shareholder Members and seeking to minimise the cash cost of future buybacks.

10. Conclusion

In this advice, we have addressed the potential movement in the notional interest of Shareholder Members in the Contributed Funding of IMB subsequent to our 2008 Report.

Clearly, the buyback of shares in 2012 and 2013 have reduced the relative interest of Shareholder Members below that assessed at the time of the 2008 Report of 43.6%.

If the methodology applied in the 2008 Report to allocate retained profits in the period 1989 to 2008 is rolled forward (Approach 1), the assessed Shareholder Member interest of 43.6% prior to the 2012 buyback would be reduced to around 40% immediately following the 2013 buyback,

However, in considering capital management and dividend policy going forward, there is scope for the Directors to consider whether other factors may have affected the relative interest of Shareholder Members in IMB since the 2008 Report. Specifically, it could be considered whether – once the interests of the different classes of member in IMB had been more clearly addressed in 2008 – it remains appropriate to assume that retained profits are shared pro rata by D&B Members and Shareholder Members.

As set out as Approach 2, a view might be that the D&B Members and Shareholder Members have similar interests in the profits of IMB with the fundamental difference that D&B Members fully reinvest their share of profits whereas Shareholder Members take a substantial part of their share of profits through dividends. As set out in section 8 and the indicative calculations in appendix 2, this approach would result in a lower assessment of the Shareholder Member interest of around 32% immediately following the 2013 buyback.



As demonstrated in appendix 3, Approach 2 would result in further declines in the relative interest of Shareholder Members even where no further buybacks occur. The extent of this decline would depend on the future profitability of IMB, future dividend payments and the prevailing IMB share price. Based on applying the assumptions detailed in appendix 3, a further decline in the relative Shareholder Member interest to around 27% would be projected in the period to June 2018 under Approach 2. We note that different outcomes would result from alternative assumptions, but - as a principle - the relative interest of Shareholder Members would decline under Approach 2 in any year in which dividends are paid.

Yours faithfully,

A handwritten signature in black ink that reads 'K. D. Reeves'. The signature is written in a cursive style and is positioned above a solid horizontal line.

Kevin Reeves
Authorised Representative



pwc

Appendix A

Approach 1: Simulation of mechanism to update allocation of Contributed Funding (CF) for buybacks

Year	Opening Shares million	Buyback Shares million	Closing Shares million	Opening SM interest in CF %	Closing SM interest in CF %
Year 1	39.9	2.9	37.0	43.6%	41.8%
Year 2	37.0	2.1	34.9	41.8%	40.3%
Year 3	34.9	4.0	30.9	40.3%	37.4%
Year 4	30.9	4.0	26.9	37.4%	34.3%
Year 5	26.9	4.0	22.9	34.3%	30.7%
Year 6	22.9	4.0	18.9	30.7%	26.8%
Year 7	18.9	4.0	14.9	26.8%	22.4%
Year 8	14.9	4.0	10.9	22.4%	17.4%
Year 9	10.9	4.0	6.9	17.4%	11.8%
Year 10	6.9	6.9	0.0	11.8%	0.0%

Notes

Opening year 1 Shareholder Member (SM) position reflects mid-point of estimated range at 30 June 2012 based on continuing to apply the methodology in 2008 report.

Year 1 buyback is the actual buyback undertaken in 2012

Year 2 buyback is actual buyback undertaken in 2013

Highlighted data for buyback shares in subsequent years are for demonstration purposes only.



Appendix B

Approach 2: Implied movement in Shareholder Member (SM) interest in Contributed Funding (CF) 2009 to 2013

Year	Profit after Tax (PAT) \$,000	SM share of PAT \$,000	Dividend Declared \$,000	SM retained Profit \$,000	D&B share of PAT retained \$,000	Average share price re notional reinvestment \$	Notional shares allocated to SM ,000	Notional shares allocated to D&B ,000	SM notional shares c/f ,000	SM notional shares bought back ,000	SM notional shares post BB ,000	D&B notional shares ,000	Total notional shares ,000	SM interest post buyback
2008									39,912		39,912	51,629	91,541	43.6%
2009	22,850	9,963	9,379	584	12,887	2.83	206	4,554	40,118		40,118	56,183	96,301	41.7%
2010	29,071	12,111	11,573	538	16,960	3.10	173	5,471	40,292		40,292	61,654	101,946	39.5%
2011	31,018	12,259	9,977	2,282	18,759	3.98	573	4,713	40,865		40,865	66,367	107,233	38.1%
2012	30,148	11,489	9,978	1,511	18,659	3.74	404	4,989	41,269	(3,007)	38,262	71,357	109,619	34.9%
2013	28,510	9,951	9,250	701	18,559	3.58	196	5,184	38,458	(2,226)	36,232	76,540	112,772	32.1%

Notes

The 2012 buyback represented 7.3% of outstanding ordinary shares. Notional shares attributed to Shareholder Members reduced in line with that proportion.

The 2013 buyback represented 5.8% of outstanding ordinary shares. Notional shares attributed to Shareholder Members reduced in line with that proportion.



pwc

Appendix C

Approach 2: Simulation of possible future movements in the shareholder member (SM) interest in Contributed Funding (CF) 2014 to 2018 using basic assumptions

Year	Profit after Tax (PAT) \$,000	SM share of PAT \$,000	Dividend Declared \$,000	SM retained Profit \$,000	D&B share of PAT retained \$,000	Average share price re notional reinvestment \$	Notional shares allocated to SM ,000	Notional shares allocated to D&B ,000	SM notional shares c/f ,000	SM notional shares bought back ,000	SM notional shares post BB ,000	D&B notional shares ,000	Total notional shares ,000	SM interest post buyback
2013									38,458	(2,226)	36,232	76,540	112,772	32.1%
2014	29,223	9,389	8,716	673	19,834	4.50	150	4,408	36,382	-	36,382	80,948	117,330	31.0%
2015	29,953	9,288	8,716	572	20,665	4.50	127	4,592	36,509	-	36,509	85,540	122,049	29.9%
2016	30,702	9,184	8,716	468	21,518	4.50	104	4,782	36,613	-	36,613	90,322	126,935	28.8%
2017	31,470	9,077	8,716	362	22,393	4.50	80	4,976	36,693	-	36,693	95,298	131,992	27.8%
2018	32,256	8,967	8,716	252	23,289	4.50	56	5,175	36,749	-	36,749	100,474	137,223	26.8%

Assumptions applied in Simulation:

- No further buybacks occur
- IMB profit after tax increases at a rate of 2.5% in line with long term inflation targets
- Annual dividend remains constant at 25 cents per share
- Notional dividend reinvestment occurs at a future share price of \$4.50

The simulation is indicative to demonstrate principles only. Parameters in future years for profit after tax, dividends and future share price are for the demonstration purposes only. The parameters will vary according to the future events and decisions made by the Directors. The use of the parameters shown above does not mean that they represent estimates of future values by PwC Securities or the Directors.