# TSB Annual Report 2020

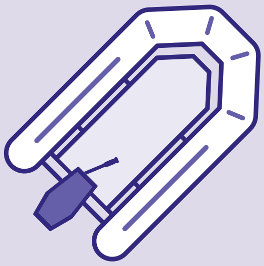
TSB

# Contents

# Highlights

**Launched new TSB purpose**

Created with our people, customers and communities



$165,000

In grants and equipment given to New Zealand Surf Life Saving Clubs to help keep Kiwis safe in the water

**Deposits increased 4.6% to a record high**

$7.4b

**2019 KPMG Customer Experience Excellence Award**

★★★★★

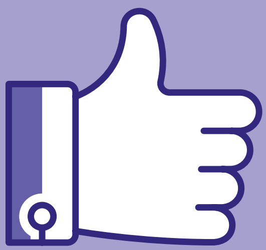
**Lending Growth up 5.7% to**

$6.1b

**Consumer NZ People's Choice Award for Banking winner**

Four years in a row

In just four weeks, TSB had conversations with more than 2,000 customers impacted by COVID-19 about financial support options



The highest customer satisfaction of any bank in New Zealand

81.3%

Roy Morgan (December 2019)

$2.5m

Dividend paid to the TSB Community Trust for its philanthropic work investing millions in the Taranaki community each year

*Final dividend of $7.5m not paid due to RBNZ restricting banks paying out dividends on ordinary shares due to COVID-19.

61

Achieved an Annual Net Promoter Score of 61*

A score which is considered world class, reflecting how likely our customers are to recommend TSB to someone

*According to TSB Voice of Customer Research March 2020

First NZ bank to launch support package information and online application process for COVID-19 Mortgage Payment Deferral

The Bank reported net profit before tax of

$41.5m

Mahi Tahi

New state of the art workspace 'Mahi Tahi' opened in New Plymouth to support team collaboration

"Kia ora koutou. In just a short space of time COVID-19 has had a substantial impact on our economic environment — so I'm pleased to report that TSB remains in a strong and steady position to continue providing support for New Zealand as we recover from this crisis."

John, Chair

**Over the years the Bank has made sensible decisions to ensure a good platform to be able to respond to significant economic events. After a strong first half, TSB's annual result was negatively impacted by an increase in lending provisioning. This was primarily due to COVID-19 and meant net profit before tax was $41.5m — down $21.1m on last year. However, the Bank maintains capital, liquidity and funding well above required thresholds. TSB recognises the importance of its role as a bank during an economic crisis. With a 169 year history, TSB has been there to help New Zealanders through many big events that have affected our community, and it will be no different as we recover from COVID-19.**

**Strategic vision**

The last year has been one of evolution for TSB. The Board has worked closely with the CEO and executive leadership team, along with input from employees, shareholder, customers and supporters, to shape a new and evolving strategy to take the organisation forward.

TSB has a certain x-factor with its unique ownership structure and service accolades, and upholding these strengths continues to be critical to the future growth of the business. But this must be done in line with its ongoing evolution to keep pace with the ever-changing world of banking and remain a close competitor within the sector. Increasing in scale to enable the Bank to give back even more remains a priority and core focus, and for that reason, the Board is pleased with its new vision and supporting purpose. These statements continue to champion what TSB stands for, but allow the Bank to be more focused and forward-looking.

Another key effort in supporting TSB's new strategic vision is a stated commitment to high standards. TSB is operating in a competitive, ever-changing environment along with a range of economic challenges and increased compliance requirements. As a result, it is imperative that the bank builds robust foundations for the future. A core programme of work is underway to mature TSB's risk management policies and procedures and ensure ongoing improvements. This has included moving the director attestation regime to a positive, evidence-based framework.

The Board will continue to drive change like this within TSB as it's rightly what New Zealanders and our regulators expect of this organisation. We have full confidence the Bank is in a sound position to move through a time of crisis, while simultaneously focusing on making deliberate choices to move the business forward.

**The right culture**

The last two years have seen significant change for the banking sector and Donna Cooper and her team are doing an outstanding job in leading TSB through this shift. We've seen a Conduct and Culture review, new capital requirements and many other legislative changes. Overall, there is an increasing industry focus on prioritising customer outcomes, and that is particularly important as we contend with COVID-19. At TSB we're fully onboard with these changes, which have provided a valuable time for reflection and to challenge ourselves to maintain an even-higher standard.

Donna's leadership throughout this time has been excellent and I have full confidence in her ability to lead TSB to a bright future, while still staying true to the Bank's proud history. The organisation has begun to unleash a transformed culture of collaboration and accountability, which will assist it to deliver its purpose.

The way the organisation has responded to COVID-19 is a prime example of this and the Board has felt exceptionally proud of how the team has demonstrated the organisation's values. TSB has a proud history of innovation and this has once again come to the fore with the Bank using its new strategic vision and supporting culture as it reacted and adapted to the developing crisis. While TSB will need to make sensible decisions for its financial future in the current climate, I also look forward to seeing it harness new opportunities arising from this.

**For people and community**

TSB has a legacy of caring and that's what makes this organisation so special. The fact that it is 100% New Zealand-owned by the TSB Community Trust through its group company structure genuinely makes a difference to the way the bank works, and that culture is entrenched at every layer of the business. Delivering good outcomes for TSB's people, customers and wider communities is front of mind in everything it does. I know this because as a Board, we ensure it is at the heart of every decision and we are always challenging the leadership team to seek continuous improvement.

It's been fantastic to see TSB recognised for going the extra mile for its customers this year, taking out three prestigious customer satisfaction awards. I was particularly proud to see the Bank win the 2019 KPMG Customer Experience Excellence Award, ahead of large well-loved organisations such as Air New Zealand.

Over the last few months I've been pondering the importance of TSB's role, both in Taranaki and right across New Zealand, as we face the challenges of recovery from COVID-19. TSB's new strategy plays to its strengths to make the organisation more successful — and I've never been more confident about this approach than in today's climate.

In the COVID-19 space, New Zealanders are doing their bit to support local and give back to those who need a helping hand — so TSB is truly proving its worth as a bank for New Zealand. TSB has an ownership structure which sees it give back millions to its home community, as well as investing to support people right across the country. TSB is locally owned and keeps profits pumping through the New Zealand economy. The Bank has the philosophy of 'doing the right thing for our country' front-and-centre in its decision making; the belief in caring for people like they're part of your family runs right to its very core.

These are the sort of values Kiwis are looking for in an organisation more than ever, and TSB is in a strong position and ready to deliver both. As we respond to this crisis — and well into the future — I look forward to seeing the Bank achieve even more success, with this focus remaining at its core.

Ngā mihi,

John Kelly, Chair

## Donna, CEO

"Tēnā koutou. What a year it's been for TSB. I'm immensely proud of the way our TSB whānau has stepped up and delivered for our people, our customers and our communities — not just in the past few months, but over the whole year.

Our commitment to using our profit for purpose and doing what's right for New Zealanders is now stronger than ever as we respond to the impacts of COVID-19."

**After a strong first half of the financial year, TSB's annual net profit before tax of $41.5m was down from $62.6m the previous year. This result was significantly impacted by an increase in loan impairments expected due to future impacts of COVID-19. However, gross lending was up 5.7% year on year to $6.1b, while deposits were up 4.6% to $7.4b — both all-time highs.**

**While our operating environment has changed rapidly and significantly, TSB's funding and liquidity positions remain strong and our capital levels are well above those required of us by our regulator. We're set to continue playing our role in helping New Zealand through its recovery from COVID-19 and out the other side.**

### Our why

In the last 12 months we've taken a number of significant steps forward as an organisation and our progress has been inspired by our journey to redefine our 'why'. Throughout the year we spoke to hundreds of our people, customers, potential customers and stakeholders about what makes TSB special. This exercise reinforced our strengths and identified our opportunities, and we used this insight to develop a plan to set TSB up for the future.

To guide us with that plan, we worked with our team to reinvigorate our TSB values and develop our new purpose, which is now the guiding statement for everything we do: **Unleashing our unparalleled customer care for community good.** You can read more about our 'why' or as I like to think of it — our reason to get up in the morning — on page 10.

### Unparalleled customer care

Our dedication to 'unparalleled customer care' was proven again this period with TSB topping three customer satisfaction surveys during 2019. We took out the KPMG Customer Experience Excellence Award, the Consumer NZ People's Choice Award for Banking for the fourth year in a row and were number one in the Roy Morgan December 2019 survey — the only bank with a score above 80%.

These results gave me an immense level of pride, which has only been amplified in recent months as I've watched our people go above and beyond to support our customers and community through COVID-19. For example, more than 10% of our workforce took on different roles when we went into lockdown to provide the best level of support for our customers.

Our teams proactively called customers who might need financial assistance and checked in on business customers and people over 70-years-old. In just four weeks we had conversations with more than 2,000 customers impacted by COVID-19 about financial support options and helped hundreds of customers to get up to speed with online and mobile banking, with our amazing team happily spending up to an hour doing this.

Throughout March, it was common for me to open my inbox and find customer feedback like this: "A huge thanks TSB for making the decision to make calls to us to check if we are ok. Never in my life has that happened before and I'm so very grateful. This is what makes TSB a wonderful bank."

What's even more remarkable is that we delivered this level of care when most of our branches were unable to open and 90% of our team were working from home due to COVID-19 restrictions. I encourage you to read the heart-warming stories of our people and their commitment to delivering unparalleled customer care, as well as the responses from our customers who have experienced this first-hand, from page 12.

The adaptability of our workforce through this challenge has been remarkable and we're now focused on taking the initiatives that worked well and using them to our advantage to evolve our customer care philosophy. This includes providing more effective ways for younger New Zealanders to engage with us. For example, the creation of 'TSB Virtual Bank', an online branch where New Zealanders can join TSB, open accounts and discuss their home lending needs via video call.

### Community good

At TSB we're about profit for purpose. We're 100% New Zealand-owned by a philanthropic organisation — the TSB Community Trust, via its group company structure. Each year millions of dollars of profit goes to supporting the Trust's work in the Taranaki community. Our ownership structure means we keep our profits right here in New Zealand to circulate in our local economy and benefit our communities. Not only that, but we're proud to partner with organisations and events across the country doing good for Kiwis.

This 'community good' ethos is something everyone in the TSB team is incredibly proud of, and we use it as a challenge to ensure we're all doing our best for the Bank, our customers and our wider New Zealand communities.

Due to COVID-19, this year the Reserve Bank of New Zealand restricted New Zealand banks paying out dividends on ordinary shares to support our local economy. TSB is still 100% committed to community good, particularly given the work of the Trust is now more important than ever to assist people through the COVID-19 recovery. We have a strong relationship with the Trust and are working closely with them to help support our communities.

TSB has also launched a new kickstarter fund TSB Good Stuff! to support initiatives which will help New Zealand get back on its feet — watch this space!

### Enabling a bright future

In the last year we've done a lot of work on our over-arching business strategy — centred around taking what makes TSB special and turning it into what makes us successful. In order to bring this to life, we've taken a holistic approach to begin shaping our organisational culture and strengthening the foundations of our business.

**Above**
Our TSB People and stakeholders at the Mahi Tahi opening.
—

We've run workshops with all our people to reinvigorate our values by defining the behaviours that support them, and launched a programme of work to ensure good conduct is understood and encouraged at every layer of the organisation.

We're encouraging better collaboration — supported by our purpose-built, modern, open plan workspace 'Mahi Tahi' (work together) at New Plymouth Centre office, which enables our people to achieve better outcomes for each other, our customers and wider New Zealand by working together.

Improvements to our technology have been rolled out regularly to support greater collaboration, as well as assisting frontline teams by giving them a central view of each customer in order to provide a more seamless experience. In March we successfully transitioned our Customer Engagement Centre to a new cloud-based communications platform with better functionality for our people and customers. These technological advancements were critical for enabling the majority of our people to work from home effectively for around six weeks during COVID-19 lockdown, and still achieve great customer outcomes.

Every organisation — small or large — has things they can improve on and our approach is to address these head-on. We are actively looking for gaps and areas of improvement, and identifying and implementing the best solution for the problem. For example, we have an ongoing priority focus on updating and maturing risk management and governance policies and processes. Our continuous improvement journey will never be complete — we will always be looking for ways to do things better, so that we can continue to deliver even better outcomes for our customers and for New Zealand.

These are just some examples of the work we're doing to enable the right culture to achieve our strategic vision for TSB. Our Bank has a challenging time ahead given the current economic environment, and will need — now more than ever — to stay true to our purpose, while also making prudent choices for the future of our business. This means achieving our goals may take longer than before COVID-19, but we will always stay true to our vision and deliver for our people, our customers and our communities.

I'd like to take this opportunity to thank our Board, executive group and the TSB team for the commitment and passion they continue to demonstrate every day, and particularly during the once-in-a-lifetime situation of COVID-19.

I also want to extend my gratitude to our loyal customers — who choose to support local and assist TSB in reinvesting for the betterment of Kiwis.

The future is bright with us working together.

Ngā mihi,

Donna.

Donna Cooper, CEO

"Mahi Tahi enables our people to more easily connect, collaborate and share which will help us create even better outcomes for our customers and communities."

GM People & Strategy, Chris Boggs

# Unleashing our unparalleled customer care for community good

# Our Purpose

## Unleashing our unparalleled customer care for community good

**Introducing our new TSB purpose. In 2019, we asked hundreds of our TSB people, customers, potential customers and stakeholders what makes TSB special. This exercise reinforced our strengths and identified where our opportunities lie.**

**We took this information and worked with our team to develop this overarching aspiration for our business. Our purpose is used as the ruler for which decisions, big and small, are measured.**

### Unleashing

This is our inspiration. We're going to step up, be brave in our decision making and unleash the incredible potential we know TSB has.

### Unparalleled Customer Care

The exceptional care we show our customers and their financial future is in our DNA — it is unparalleled — and that's never going to change.

### Community

Supporting New Zealand communities is at the heart of everything we do — and it always has been. We care about doing what's right; whether for a customer of one, or a community of thousands.

### Good

At TSB we're about profit for purpose. We aim to do good by our customers, communities and each other. This encompasses who we are as a business and the philanthropic work we support our owner, the TSB Community Trust, to do.

# Our Values

**This year all of our people took part in a collaborative workshop to define the behaviours we need to demonstrate every day to truly embody our TSB values. This exercise brought new life to our values, ensuring they're intrinsic to the way we operate.**

**"At TSB, we put people first, by working as one team, with integrity. We keep it simple and continuously look for innovation."**

### People First

I care for others, our customers and communities. We're self-aware, mindful of others and embrace our differences. I enable my own wellbeing and that of others.

### One Team

We collaborate with trust and transparency. We are all responsible for good customer outcomes. We celebrate our successes.

### Integrity

I do what's right over what's nice, fast or comfortable. I take accountability for delivering on commitments. I'm thoughtful, direct and honest.

### Keep it Simple

I communicate in a clear and effective way. I'm focused on creating simplicity. I always have the user front of mind.

### Innovation

I'm open and curious. I'm dedicated to continuous improvement. I take initiative and get things done.

# Our People

## Hector

**Hector Farmer is our Digital Team Manager in TSB's Customer Engagement Centre. He's never felt prouder to be part of the TSB team than while supporting customers through the impact of COVID-19.**

**What has it been like working at TSB through COVID-19?**

The cool thing about being part of an organisation like TSB is that you become a figure of stability and consistency for the public. For us it was all about continuing the same level of service people were accustomed to before. The lenders have done an amazing job supporting customers through conversations like how they can manage their home loan now they don't have a job. TSB has been a shoulder to lean on and a wise voice. It's been awesome to be able to help customers through a once in a lifetime event.

**How did the needs of customers change due to COVID-19?**

There was an element of 'I'm not sure what's going on, is TSB safe, is my money safe and am I all good'? In lockdown, all of a sudden people who had built a habit of going into branch to meet their banking needs couldn't. So it wouldn't be uncommon for us to get a call from someone with a simple question, who also just wanted to talk and connect with another human. A strong element of customer queries came through around helping them take control of their own banking. I think one of the cool benefits is how many people we've taught to use online banking.

**How would you describe the overall approach the team has taken during COVID-19?**

The general approach was just to see the human that you're helping, stay consistent, stay focused and take it one phone call at a time. If I could describe it in one phrase, we've really lived our 'one team' value and have certainly aspired to deliver unparalleled customer care.

**What's been a standout moment for you in TSB's response to COVID-19?**

It's all been pretty special how we've adapted and not only survived, but thrived through it. We have amazing customers who have often just thanked us for being there, for picking up the phone, for doing what we were doing to play our part in our New Zealand's five million strong team navigating COVID.

# Courtney

**Courtney Gush, Assistant Manager Botany branch, works hard to build long-lasting, personal relationships with her customers to ensure their financial wellbeing. So when COVID-19 hit, she and the team prioritised getting in touch with customers to see how TSB could support them through the challenge.**

**What sort of proactive measures did you take during lockdown?**

As a team, we sat down and thought about who among our customers might be affected and who we needed to reach out to. We know all our customers, so that was something we were able to do. Everyone we called said it was really nice to feel cared about in that way. We also made 'care calls' to all our elderly customers to make sure they knew we were thinking of them and would be there if they needed us. We got a very positive reaction to that.

**What sort of changes did COVID-19 mean for you?**

One of our strengths at TSB is our personal touch, so making sure we could translate that level of face-to-face care into phone calls was really important. We gave customers the option of waiting to see us when things are back to normal or sorting things out over the phone. It was important to give people that choice so they could decide what they were happiest doing.

**How was it when you were able to see customers face to face again?**

We had some very long appointments! People were keen to come back in, and of course it's been great to talk to all our customers in person again. Typically only the first few minutes would be banking business, and then we'd get updated on all our customers' news.

**How did you deal with people who might have been struggling?**

We had a customer phone in about a small banking matter and it turned out he was pretty lonely and having a tough time of things. Our team member- who normally works as a teller- stayed on that call for an hour because she'd asked how he was doing, and that started a real conversation. Our people feel empowered to do what feels right, and I was really proud of that teller!

**Are there any positives out of this experience for you?**

Some people have been really hard hit, which is awful, but a lot of customers are realising the real value and importance of a 'rainy day fund'. They have been asking us to help them with that, which is really rewarding because we are always encouraging our customers to take control of their financial health.

# Alicia

**Alicia Bristowe is the Lending Support Team Leader. She proudly embraces her Māori heritage to inspire the TSB whānau, including leading the Waiata Group with members from right across the business.**

**Tell us about the TSB Waiata Group.**

It was formed to bring together people from across the business from different backgrounds, to try to reinvigorate Māoritanga at the Bank. Everyone from customer service representatives to heads of departments are part of this team and we all have that one bond in common. I feel like it gets rid of barriers. Everyone is there to learn and there's no judgement.

**Do you find TSB different to other companies you've worked for?**

I like how proactively supportive TSB is of the Waiata Group. It's not just giving us permission; they actively encourage us to do it. We're invited to perform at different meetings and we welcomed Donna when she began as CEO. It's really special being able to represent TSB from a cultural perspective. I've never worked for a company like TSB, I love working for TSB!

**We hear you are inspiring. How do you think you inspire people?**

Who said that? That's very nice. I like to encourage people to push more and do more for themselves and for other people. I don't like being stagnant.

**Who inspires you?**

There are a lot of people that inspire me. My parents definitely inspire me. They're very strong-willed and determined. That's probably where I get my drive from. There are a lot of unseen and unspoken little acts of kindness that go on all over the place at TSB — my team inspire me. Sounds cheesy, but it's true.

# Shaleshni

**Shaleshni Kumar, Customer Service Consultant, Hawera branch, is so popular with her customers that some choose to wait in the branch to get her service.**

**We've heard stories of you going the extra mile for your customers, can you tell us about one?**

A customer came into the branch to get travel insurance for her daughter. In the conversation she said her husband's brother had passed away. In Indian tradition when someone passes away, you are not supposed to cook anything until the funeral takes place. As a family member you are not supposed to even light a fire, because the soul won't rest in peace. They did not have any close relatives here, so I thought it would be a good idea to cook for them for three days. She appreciated that someone cared for them.

**We've heard people wait in the branch until you're free, just to do their banking with you?**

Well I have been here for 11 years and we have built a strong relationship. I think they trust me and I have shown them respect. I care for my customers and I like to feel proud of giving the best service.

**What's the longest people will wait to see you?**

They will take a seat for half an hour, sometimes an hour. I had a situation with a customer who bought a new car and came in when I was busy, so he came in the next day and I was relieving at another branch so still wasn't there. He came in again the next day, and that entire time he didn't insure his car — I told him it was naughty not being insured!

# Executive Leadership Team

**Donna Cooper**
CEO

**Herman Visagie**
Chief of Staff & General Counsel

**Roddy Bennett**
GM Finance

**Justine St John**
GM Marketing & Customer Experience

**Chris Boggs**
GM People & Strategy

**Hamish Archer**
GM Technology

**Tracey Berry**
GM Customer Solutions & Service

**Sean Edwards**
Acting GM Risk

# Board of Directors

**John Kelly**
Chair

**Murray Bain**
Deputy Chair

**Anne Blackburn**
Director

**Natalie Pearce**
Director

**Peter Schuyt**
Director

**Dion Tuuta**
Director

**Harvey Dunlop**
Director

**Peter Dalziel**
Director

# Our Customers

"I'm incredibly proud of the TSB whānau winning three awards for customer satisfaction in 2019. I know our team take real pride in going the extra mile for our customers, not just because they're asked to, but because they genuinely care about supporting New Zealanders. It's very special to see our team's efforts to put people first have been recognised by our customers."

TSB CEO Donna Cooper

### In 2019 TSB took out the top spot in three customer satisfaction surveys:

**2019 KPMG Customer Experience Excellence Award**

Highlighting the top New Zealand brands excelling in customer experience, the KPMG Customer Experience Excellence Awards recognised TSB for its "authentic, customer-first philosophy", with customers scoring TSB highly on the ability to empathise and provide resolution. TSB surpassed other significant brands such as Air New Zealand and Singapore Airlines, as well as beating the other banks by a large margin.

**Number one in Roy Morgan customer satisfaction survey for banking**

TSB was the only bank to receive a rating above 80% in the December 2019 Roy Morgan survey, with a  score of 81.3%.

**Consumer NZ People's Choice Award for banking 2016-2019**

In 2019 TSB won the Consumer NZ People's Choice Award for Banking for the fourth year in a row. The Bank received a customer satisfaction rating of 83%, ranking above-average in four key performance measures — advice on products, fees, timely responses to enquiries and value for money. TSB also rated highly for branch and internet banking. (At the time of printing TSB had made it five-winning the 2020 award).

# Shannon

**Shannon Rogers came to know Peter Bedford during his regular visits to Shannon's cosy retro cafe, 'Holy Shot,' located near TSB Takapuna where he works as a Mobile Mortgage Manager. When Shannon told Peter she and her husband were looking to buy a home, he was there to support them along the way.**

**How have you got to know Peter?**

Peter is one of our regulars at Holy Shot. He started coming in here when we first opened and he comes in three or four times a day. Sometimes not even for a coffee, just for a chat and a laugh.

**How did you get your home?**

Hayden, my husband, and I met with Peter after work one day. He understood what we were after and just went over and above to look after us and value us as people.

**How is TSB different from other banks?**

We really wanted to support a Kiwi-owned bank. Hayden and I really liked that there's money going back into local communities rather than just offshore. TSB makes me feel relaxed and not so uptight about banking. When you go in, it's not a stuffy atmosphere. You kind of feel like you're going to be offered some tea and scones!

**Would you say you, Hayden and Peter have become friends?**

Yeah totally. As soon as we move into our house, we're inviting Peter and his wife Donna around for dinner. He's got the best pizza base recipe apparently so I'm trying to get that off him!

# Caroline

**For TSB Nelson customer Caroline Larnach, COVID-19 caused an unexpected disruption to her family's work and income, but Caroline says TSB helped her feel confident about staying in control of her finances.**

**How would you describe TSB's response to the COVID-19 restrictions?**

They never made me feel like I was a problem. Dealing with other institutions, I was on the phone for ages and it was all quite difficult, but TSB has such a sense of positivity. They seemed to see everything in terms of how they could help us get through.

**Was your family affected financially by COVID-19?**

Yes, like a lot of people, COVID-19 put us in a bit of turmoil and has affected our plans for the future, but just as I was starting to think about calling the Bank to make a plan, Alicia from TSB called us. She actually didn't know what was going on with us, she was just reaching out to check we were doing ok and see if there was anything TSB could do to help.

**What sort of difference did that make for you?**

It made all the difference. It meant I didn't need to make a difficult phone call myself — she was right there offering to help and get things sorted for us. We talked through the various options and put a plan in place and then she talked me through the next steps, so I understood exactly what was happening. I felt like TSB really cared and it gave me back my sense of control when things had been feeling so uncertain.

**How does your experience with TSB compare with other organisations?**

Other places had sent us emails, but that was all. Nobody made personal contact like TSB did. A friendly voice at the end of the phone was so welcome at that stressful time and it helped me feel confident about the financial decisions we needed to make. It's so nice to know TSB really does care.

# Lloyd

**Lloyd Evans is an electrician who never believed buying his own home was a possibility, until at age 45 an opportunity presented itself. Supported by Julie Wadsworth from our Hawera branch, Lloyd was able to make his home ownership dreams a reality, and he's been proudly mowing his own lawns ever since.**

**How did TSB help you to become a homeowner?**

TSB set me up with a really good mortgage, one which I could cope with. Actually, the simplicity of it is probably the biggest selling point because I'm not very good at keeping track of accounts and insurances. I dealt with Julie Wadsworth, who did an absolutely fantastic job, she said they could take care of absolutely everything. All I needed to do was go over the paperwork. I think it was maybe three or four visits to the Bank at most. TSB made it so easy for me.

**How did it feel to own your first home?**

Owning my own home was a feeling that was a complete shock to me. That Sunday I mowed my lawns for the first time and was grinning uncontrollably. People were driving past and the neighbours were looking at me, I must have looked like a muppet, but I couldn't help it. Mowing my lawns was so enjoyable because they were my lawns — my own lawns for the very first time in my whole life.

**How do you feel about it now?**

I couldn't be more happy or proud. It impacts on other areas of your life; it helps you to feel like your life is coming together. They're definitely not the prettiest lawns in town, but they're probably the most loved!

# Coralie

**Coralie Pringle from Waitara is a longtime TSB customer. During COVID-19 she needed some personal banking help, but was worried about visiting the branch, so Coralie turned to her TSB neighbour.**

**What did the period of lockdown mean for you?**

My husband is over 70 and he also has compromised immunity as a cancer survivor, so we needed to stay home even before the lockdown began. We were fine health wise, but it turned out we did need a hand with a few banking things.

**How was your normal banking affected by the COVID-19 restrictions?**

We had never got around to setting up internet banking and mainly used Eftpos, some automatic payments and a few cheques to pay our bills. But the post was affected by lockdown as well, and we got a late payment notice for a bill that we had already mailed a cheque for. We needed to issue a new cheque and cancel the old one.

**How was TSB able to help?**

My neighbour Gaye works for TSB. We've been neighbours for at least 20 years and whenever I want anything from the Bank, I go to Gaye and she sorts it for me. When I visit the branch, we always say 'hi neighbour!' to each other, so I think all the staff know who I am! I saw Gaye out walking during Alert Level Three, and I asked 'are you working from home or what?'. She said to give her a call and she would help me out. I didn't know her number, so I just went over and called out what I needed from her front porch.

**Were you able to get your banking sorted out?**

Absolutely, Gaye said 'I can do anything you need'. She had full access and she sorted out the bill and helped with some account transfers and other business, all from her work-from-home set-up. We had a chat and we've decided that when this is all over, she is going to come over to my place and help me set up internet banking, so I won't have to worry about any more cheques getting lost in the mail.

# Our Communities

## As a profit for purpose organisation, we strive to make a positive impact in our communities

**This ethos is intrinsic in everything we do at TSB. As a New Zealand owned bank, we keep our profits here, where they help boost the local economy.**

We are proud to partner with national and regional organisations and events, which generate positive outcomes for our communities. As well as this, 100% of TSB is owned by a philanthropic organisation, the TSB Community Trust. In the last 30 years the Trust has invested over $137 million into Taranaki communities from its assets.

TSB's success plays an important role in the work the Trust does to support Taranaki to build a thriving, inclusive and equitable community. The Bank is proud to contribute millions each year towards this work benefiting our communities.

## Committed to supporting Taranaki through COVID-19

**In March 2020, due to COVID-19 the Reserve Bank of New Zealand restricted New Zealand's banks paying out dividends on ordinary shares.**

The Bank had already paid a half year dividend of $2.5 million to the TSB Community Trust, but the restriction meant TSB was not allowed to pay the remaining $7.5 million full year dividend.

The Trust remains in a strong position to continue significantly supporting the Taranaki community and is focused on helping the region through the challenge of COVID-19. TSB is 100% committed to continuing its support of the Trust, whose work is now more important than ever.

"TSB remains in a strong financial position, with capital and cash reserves well above the levels required by our regulator. We are financially able to pay this dividend, but the Reserve Bank has rightly put in place additional measures to support the New Zealand economy at this time. We are working closely with the TSB Community Trust and exploring other ways we can provide support."
— Donna Cooper, TSB CEO.

**Left**
Donna Cooper and Taranaki community leaders in panel discussion on COVID-19
—
Photo by Strategy Collective

**Right**
Tanya Anaha,
WhyOra Manager
—

# WhyOra — assisting Taranaki Māori into careers in health

**WhyOra is one of the many community groups supported by the TSB Community Trust. The organisation helps Māori develop their health career pathways by assisting with training and education, through to securing internships and jobs. We spoke to Manager Tanya Anaha to learn more about WhyOra and what the long-term support from the Trust and TSB has enabled.**

**Tell us about how and why you started WhyOra?**

We were set up in 2010 to increase the Māori health and disability workforce. We want our people in good positions, we want our people thriving and to be able to contribute to our community. When it comes to health, Māori tip all the scales — we're at the top end of most health issues. So we asked for support and this was set up with the help of the TSB Community Trust. If you think back ten years ago, to say 'would you support something that specifically supports Māori, only Māori students in secondary school, or Māori that are wanting to get into the workforce'; saying 'we're going to back you' was really brave at the time. When we look at our community, we're proud of the difference that it's making.

**What difference is WhyOra making that you are most proud of?**

We're accessing careers for our rangatahi in health, a sector they might not have had a clear pathway to work in before. They may have left school and just gone into a job, but we're really supporting them to get into a career. We've had 107 people going into the health workforce as employees, 32 of those are nurses. When you look at the income of a nurse, and then potentially someone on minimum wage, that's a big difference to their whānau and it's a big difference to their contribution to their community. So that's what I'm most proud of. Proud that they can make a difference for their families as well.

**What type of support did the TSB Community Trust provide WhyOra?**

The support from the Trust wasn't just 'here's some funding go forth and go get on with what you need to do in your community'. We worked together for a long time and we still do now. The support is not just funding, I could go in and say: 'hey I need some media support, what can we do?', or 'I need to look at some reports, or actually my website's really not that great how can we improve it?'. They're experts and are able to help us and improve us as a non-profit organisation. When you work as non-profit you don't have access to HR and all the rest of it, so we're really lucky to have started that relationship with the Trust ten years ago.

**How has TSB contributed to this success?**

We're lucky to have our bank, to obviously have the support of staff who generate the income to be able to support the TSB Community Trust and this (WhyOra) is the result of it. This is what's come out of it. We get to support things that there's a need for in our community. It's pretty outstanding that we've got that.


**Above**
New Plymouth Old Boys Surf Life Saving Club members with Donna Cooper and their new IRB bought with a TSB grant
—

# Helping keep Kiwis safe at the beach

**TSB is proud to be in its fourth year as a major partner of Surf Life Saving New Zealand (SLSNZ)**

CEO Donna Cooper says as a New Zealand bank which cares about people, helping Kiwis stay safe at the beach is a cause everyone in the organisation is proud to get behind.

"SLSNZ lifeguards saved over 550 lives last year, that's more than 550 families who have a loved one with them because of the work they do. It's a remarkable statistic which demonstrates how much this organisation does for New Zealand, but it's even more incredible when you consider that this is a charity, and the vast majority of the 4,900 lifesavers are volunteers."

SLSNZ Chief Executive Officer Paul Dalton says as a not-for-loss charity, funding from major partners like TSB is the lifeblood that allows them to operate and create security to invest for the future.

"We're incredibly grateful for TSB's backing. Like us, TSB looks after New Zealanders, they understand how important the work we do is, and one of their goals is supporting local communities, so it's a fitting partnership."

**Getting behind community clubs**

In addition to this ongoing partnership, in the 2019/20 financial year TSB once again supported the essential work done by Surf Life Saving Clubs around the country by giving out $165,000 in grants and equipment.

The money has been used to fund volunteer support and education, as well as essential equipment ranging from a new ATV for a club in Canterbury, to junior training initiatives in Palmerston North and Tairua, and new boards, skis and tubes for many others.

Surf Life Saving Clubs in New Zealand are heavily dependent on donations and SLSNZ CEO Paul Dalton says the money from TSB helps save Kiwi lives.

"Our clubs provide a vital service, but it's not cheap to fund new equipment, education and services so TSB's grant support each year makes a huge difference."

## Hanging out with TSB at WOMAD

**This year marked the 11th year of TSB being a major support partner for WOMAD — the rich and vibrant music festival held in the beautiful TSB Bowl of Brooklands in Taranaki each year.**

WOMAD takes music and uses it as an opportunity to bring people together to experience different cultures, ideas and means of expression, all while still celebrating individuals and their distinctiveness.

With more than 41,400 attendees over three days, WOMAD 2020 provided plenty of opportunity for festivalgoers to 'hang out with TSB'. This year TSB hosted a fun, modern space called the 'Hammock Hangout' for people to relax and recharge over the music-filled weekend.

TSB CEO Donna Cooper says the Bank is thrilled to be a long-term partner of this special and iconic event.

"We're pleased to get behind an event which brings communities together, and in doing so, generates significant social and economic benefits for Taranaki and wider New Zealand."

## Glowing reviews for TSB Festival of Lights

**Nothing says summer in Taranaki quite like the TSB Festival of Lights — a highly successful community event the Bank has backed for 17 years running.**

This year the Festival hosted a stunning range of light displays, with installations coming from as far away as Russia, Peru and Canada, as well as a wide range of activities and entertainment on offer across the 50 days of the Festival.

The 2019–20 Festival season proved to be more popular than ever before, with a record number of people visiting the event from all over New Zealand during December and January. Of the 150,000 people who attended, around 69,000 were from outside the Taranaki region.

"We're proud to partner with a festival which mirrors what TSB is all about — putting people first, celebrating community and giving back to Taranaki and New Zealand," says Donna Cooper.

**Above**
Children enthralled by the 'Trilogy' light installation at the TSB Festival of Lights
—

**Left**
Happy hammock hanger. Photo by Federico Pagola
—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# Financial Statements

## GENERAL INFORMATION

This Disclosure Statement contains information as required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) ('the Order').

### Name and Registered Office of Registered Bank

TSB Bank Limited is a registered bank (elsewhere in this statement referred to as the "Bank").

Registered Office: Level Five, TSB Centre, 120 Devon Street East, New Plymouth.

### Principal Activity

The Bank continues to offer a full range of Retail Banking Services to its customers along with support areas of operation in Real Estate and Foreign Exchange. The Bank has no direct exposure to the funds management industry, though it promotes the sale of Fisher Funds products, a related party.

### Details of Incorporation

The Bank was established in 1850, incorporated under the provisions of the Trustee Bank Restructuring Act 1988 and the Companies Act 1955 on 30 August 1988 and reregistered under the Companies Act 1993 in May 1997.

### Ownership

The Bank is wholly owned by the TSB Community Trust (an independent body), through the Trust's fully owned subsidiary, TSB Group Limited, and is domiciled in New Zealand. TSB Community Trust appoints the Board of Directors. Address for Service is 21 Dawson Street, PO Box 667, New Plymouth, 4340.

| Results and Distributions | $000 |
|---|---|
| Net profit after tax | 30,817 |
| Dividends | |
| Interim dividend paid | 2,500 |
| Final dividend | - |
| Retained profit for the Year | 28,317 |

### Financial and Supplementary Disclosures

This Disclosure Statement is inclusive of the Bank's audited financial statements for the year ended 31 March 2020. All necessary additional financial and supplementary disclosures are included in the notes attached to the financial statements.

### Guarantee Arrangements

No material obligations of the Bank are guaranteed.

### Pending Proceedings or Arbitration

The Bank has no proceedings or arbitration pending in New Zealand or elsewhere which may have a material adverse effect on the Bank. See Other Material Matters in General Information for further reference.

### Other Material Matters

As indicated in the Bank's 'September 2019 Disclosure Statement', a review of the Bank's Anti-Money Laundering and Countering Financing of Terrorism Programme had identified areas for improvement. The Bank is continuing to actively remediate the issues identified by the Reserve Bank and is providing regular updates to the Reserve Bank on its progress.

Further to this, the Bank is now in constructive discussions with the Reserve Bank regarding the alleged breaches and the civil proceedings that may result from them.

The Bank is fully co-operating with the Reserve Bank. A provision in respect of a prospective liability has been made. Given the ongoing nature of the discussions with the Reserve Bank, further detail on this will be disclosed upon completion.

The alleged breaches relate to the Bank's obligations under its Risk Assessment and Compliance Programme. It is not alleged that any money laundering has occurred through the Bank.

The Bank's Directors are of the opinion that there are no other matters relating to the business or affairs of the Bank 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.

### Items Excluded by Shareholder Agreement

The report has been prepared so as to include all information required to be disclosed under the Companies Act 1993 except where the Shareholder has resolved to take advantage of the reporting concessions available to them under section 211 (3) of the Companies Act 1993.

The Shareholder has resolved to exclude remuneration received by the most highly paid employees during the accounting period.

### AUDITOR

It is proposed that our Auditor, KPMG, continue in accordance with Section 196 of the Companies Act 1993.

KPMG
10 Customhouse Quay
Wellington 6011

### CREDIT RATING

The Bank has a credit rating applicable to its long term senior unsecured obligations payable in New Zealand, in New Zealand dollars. The rating in effect on the date on which the disclosure statement is signed, is A-/Stable/a-, a Long Term Issuer Default Rating, which was reaffirmed by Fitch Ratings on 7 August 2019.

Rating scale for long term senior unsecured obligations:

**AAA** Extremely strong capacity to pay interest and repay principal in a timely manner.

**AA** Very strong capacity to pay interest and repay principal in a timely manner.

**A** Strong capacity to pay interest and repay principal in a timely manner but may be more susceptible to adverse effects of changes in circumstances and economic conditions than higher rated entities.

**BBB** Adequate capacity to pay interest and repay principal in a timely manner but are more likely to be weakened by adverse changes in circumstances and economic conditions than higher rated entities.

**BB** A degree of speculation exists with respect to the ability of an entity with this credit rating to pay interest and repay principal in a timely manner. Adverse business, financial or economic conditions could impair the borrower's capacity or willingness to meet debt service commitments in a timely manner.

**B** Entities rated B are more vulnerable to adverse business, financial or economic conditions than entities in higher rated categories. Adverse business, financial or economic conditions will likely impair the borrower's capacity or willingness to meet debt service commitments in a timely manner.

**CCC** Entities rated CCC are currently vulnerable to default and are dependent on favourable business, financial or economic conditions to meet debt service commitments in a timely manner. In the event of adverse business, financial or economic conditions the entity is likely to default.

**CC** Entities rated CC are currently vulnerable to non-payment of interest and principal.

**C** Entities rated C have filed a bankruptcy petition or taken similar action, but payment of obligations are being continued.

**D** 'D' rated entities are in default. This is assigned when interest or principal payments are not made on the date due or when an insolvency petition or a request to appoint a receiver is filed.

Plus (+) or Minus (-): The ratings from 'AA' to 'CCC' may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

**DIRECTORATE**

All Directors of the Bank reside in New Zealand.

| | |
|---|---|
| **J. J. (John) Kelly**<br>Independent and non-executive Director<br>(Chair — Board of Directors)<br>Company Director | External Directorship: John Kelly Livestock Limited, Te Tapu Lands Limited, Taranaki Veterinary Centre Limited, J & M Kelly Trustees Limited, JJ Kelly Family Trust, Taranaki Rugby Football Union, Neurological Foundation of New Zealand. |
| **M. I. (Murray) Bain,** MCom (Hons), BSc, C.F.Inst.D<br>Independent and non-executive Director<br>(Deputy Chair — Board of Directors)<br>Company Director | External Directorship: Oryx Technologies Limited, M.I. Bain & Associates Limited, Central Region's Technical Advisory Services Limited, ESA Publications (NZ) Limited, Optimum Services Limited, Open Polytechnic of NZ, NorthTec Limited. |
| **M. A. (Anne) Blackburn,** MA, BA<br>Independent and non-executive Director<br>Company Director | External Directorship: Warren and Mahoney Limited, Ten Gracie Square Limited, Committee for Auckland Limited, Fisher Funds Management Limited, Resolution Life New Zealand Limited, Government Superannuation Fund Authority. |
| **N. (Natalie) Pearce,** BCom<br>Independent and non-executive Director<br>Consultant | External Directorship: Home of the Brave. |
| **P. M. (Peter) Schuyt,** BCom, C.F.Inst.D<br>Independent and non-executive Director<br>Company Director | External Directorship: Tax Management New Zealand Limited, Dairy NZ Inc. (DairyNZ Limited), The Tatua Co-operative Dairy Company Limited, Foodstuffs North Island Limited, Ahikouka Holdings Limited, Alliance Group Limited, Dairy Investment Fund Limited. |
| **D. J. (Dion) Tuuta**<br>Independent and non-executive Director<br>CEO | External Directorship: Port Nicholson Fisheries General Partner Limited, Koura Inc General Partner Limited, Te Ohu Kaimoana Custodian Limited, Tuuta Waetford Tapui Limited, Seafood New Zealand Limited, Charisma Developments Limited, Southern Seabirds Trust, Parininihi ki Waitotara Incorporation, Parininihi ki Waitotara Trust, Te Ohu Kaimoana Trust. |
| **H. F. (Harvey) Dunlop,** BCom (Ag)<br>Non-executive Director<br>Company Director | External Directorship: Taradise Holdings Limited, Taradise Holdings 2004 Limited, Taradise Holdings 2006 Limited, Taradise Property Management Limited, Renaissance Holdings Limited, TSB Group Limited, TSB Community Trust, H & K Dunlop Family Trust. |
| **P.S. (Peter) Dalziel,** MBA, C.M.Inst.D'<br>Non-executive Director<br>Farmer | External Directorship: Dolly's Milk Limited, Barberry Hill Farm Limited, PS & ME Dalziel Partnership, Stratford Business Association, Stratford District Council, TSB Community Trust, Tutaki Youth Trust, Raw Drinking Milk Association NZ, The Scyber Trust. |

There have been no changes to the composition of the Board of Directors since the publication of the Bank's disclosure statement and of the Board of Directors since the publication of the Bank's disclosure statement and annual report for the year ended 31 March 2019.

There have been no transactions between the Bank and any Director or immediate relative or close business associate of any Director which either, has been entered into on terms other than those which would in the ordinary course of business of the Bank be given to any other person of the like circumstances or means or, which could be reasonably likely to influence materially the exercise of the Director's duties.

The Address to which any communication to the Directors may be sent is: TSB Bank Limited, PO Box 240, New Plymouth 4310.

## DIRECTORATE (CONTINUED)

### Policy on Directors' Conflicts of Interest

As per Clause 22 of the Constitution of the Bank a Director who is in any way, whether directly or indirectly interested in a contract or proposed contract with the company shall declare the nature of his or her interest at a meeting of the Directors in accordance with section 140 of the Companies Act 1993 as amended, but failure to do so shall not disqualify the Director or invalidate the contract or proposed contract or render him or her liable to account. A general notice by a Director that he or she is a member of a specific firm or company and is to be regarded as interested in all transactions with that firm or company shall be sufficient disclosure under this Clause as regards such Director and any such transaction and after such general notice it shall not be necessary for such Director to give a special notice relating to any particular transaction with that firm or company. All declarations and notices given by Directors pursuant to this Clause shall be recorded in the minutes.

### Directors Fees

Directors Fees received by the Directors for the year ended 31 March 2020.

| | Board Fee | Audit Committee | Risk Committee | People, Culture and Capability Committee | Total |
|---|---|---|---|---|---|
| | NZD | NZD | NZD | NZD | NZD |
| **Name of Director** | | | | | |
| J. J. Kelly | (Chair) 151,748 | - | - | - | 151,748 |
| M. I. Bain | (Deputy Chair) 100,952 | 7,082 | (Chair) 7,082 | 5,832 | 120,948 |
| P. M. Schuyt | 76,887 | (Chair) 7,082 | 7,082 | - | 91,051 |
| M. A. Blackburn | 76,887 | 7,082 | 7,082 | - | 91,051 |
| D. J. Tuuta | 76,887 | - | - | 5,832 | 82,719 |
| N. Pearce | 76,887 | 7,082 | 7,082 | (Chair) 5,832 | 96,883 |
| P. S. Dalziel | 76,887 | 7,082 | - | 5,832 | 89,801 |
| H. F. Dunlop | 76,887 | - | 7,082 | - | 83,969 |
| **Total** | **714,022** | **35,410** | **35,410** | **23,328** | **808,170** |

Fees paid to Directors of the Bank for the year totalled $808,170 (31 March 2019: $724,465).

### Directors' and Officers' Liability Insurance

The Bank has effected insurance for Directors and Officers in respect of liability and costs that may arise from their positions in accordance with Section 162 of the Companies Act 1993. The insurance does not cover liabilities arising from criminal actions.

### Directors' Interests

Directors maintain personal banking relationships with the Bank and these are undertaken fulfilling normal bank criteria. Directors are required to table all possible conflicts of interest at the Board of Directors' meetings and are required to abstain from any vote on those proceedings. The Bank complies with all the requirements of the Companies Act 1993 in terms of registers and notices for Directors' conflict of interest.

## DIRECTORS' STATEMENT

The Directors believe, after due enquiry, that as at the date of this Disclosure Statement:

**(a)** The Disclosure Statement contains all the information required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order");
**(b)** The Disclosure Statement is not false or misleading.

The Directors believe, after due enquiry, that over the financial year to 31 March 2020:

**(a)** The Bank has complied with the Conditions of Registration;
**(b)** Credit Exposures to Connected Persons were not contrary to the interests of the Bank; and
**(c)** Subject to the items outlined in Other Material Matters, note 15. Risk Governance and note 19. Capital Adequacy, the Bank has systems in place to monitor and control adequately the Bank's material risks 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.

**J.J. Kelly**
(Chair — Board of Directors)
3 July 2020

**M.I. Bain**
(Deputy — Board of Directors)
3 July 2020

**M.A. Blackburn**
3 July 2020

**N. Pearce**
3 July 2020

**P.M. Schuyt**
3 July 2020

**D.J. Tuuta**
3 July 2020

**P.S. Dalziel**
3 July 2020

**H.F. Dunlop**
3 July 2020

All in $000's

# Historical Summary of Financial Statements

| | 2020 | 2019 | 2018 | 2017 | 2016 |
|---|---|---|---|---|---|
| **Financial performance** | | | | | |
| Total interest income | 307,137 | 312,614 | 296,270 | 290,385 | 317,809 |
| Interest expense | 164,549 | 174,591 | 169,465 | 158,850 | 187,810 |
| **Net interest income** | **142,588** | **138,023** | **126,805** | **131,535** | **129,999** |
| Other income | 21,909 | 23,746 | 36,518 | 17,224 | 13,829 |
| **Net operating income** | **164,497** | **161,769** | **163,323** | **148,759** | **143,828** |
| Operating expenses | 102,678 | 94,955 | 87,340 | 80,241 | 67,003 |
| Credit impairment losses / (reversal of credit impairment losses) | 20,362 | 4,236 | 3,918 | 4,010 | (8,723) |
| **Profit before tax** | **41,457** | **62,578** | **72,065** | **64,508** | **85,548** |
| Tax expense | 10,640 | 17,539 | 20,192 | 18,168 | 23,985 |
| **Net profit attributable to shareholder** | **30,817** | **45,039** | **51,873** | **46,340** | **61,563** |
| Dividend | 2,500 | 10,000 | 20,000 | 10,000 | 19,850 |
| **Retained profit for the year** | **28,317** | **35,039** | **31,873** | **36,340** | **41,713** |
| | | | | | |
| **Financial Position** | | | | | |
| Total assets | 8,179,275 | 7,819,045 | 7,416,277 | 6,802,680 | 6,427,143 |
| Total impaired assets - loans and advances | 17,637 | 3,814 | 4,400 | 8,919 | 10,434 |
| Deposits | 7,420,524 | 7,093,017 | 6,740,890 | 6,156,809 | 5,813,192 |
| Total liabilities | 7,499,323 | 7,165,920 | 6,803,262 | 6,214,556 | 5,872,735 |
| | | | | | |
| **Shareholder's Equity** | | | | | |
| Retained profit for the year | 28,317 | 35,039 | 31,873 | 36,340 | 41,713 |
| Total shareholder's equity | 679,952 | 653,125 | 613,015 | 588,124 | 554,408 |
| | | | | | |
| **Performance** | | | | | |
| Return on shareholder's equity | 4.53% | 6.90% | 8.46% | 7.88% | 11.10% |
| Return on average total assets | 0.39% | 0.59% | 0.73% | 0.70% | 1.00% |
| Growth in total assets | 4.61% | 5.43% | 9.02% | 5.84% | 8.71% |
| Growth in depositors' funds | 4.62% | 5.22% | 9.49% | 5.91% | 8.33% |
| Residential lending | 5,222,565 | 4,844,453 | 4,389,811 | 3,851,176 | 3,125,154 |
| Total lending | 6,126,597 | 5,792,049 | 5,309,357 | 4,657,668 | 3,829,983 |
| | | | | | |
| Net profit after tax | | | | | |
| — as a % of average shareholder's equity | 4.62% | 7.11% | 8.64% | 8.11% | 11.70% |
| — per employee | 63.94 | 93.83 | 111.73 | 105.26 | 158.67 |
| Operating expenses to net operating income | 62.42% | 58.70% | 53.48% | 53.94% | 46.59% |
| | | | | | |
| **Prudential** | | | | | |
| Shareholder's equity as a % of total assets | 8.31% | 8.35% | 8.27% | 8.65% | 8.63% |
| Common equity Tier 1 capital ratio | 14.32% | 14.57% | 14.28% | 14.60% | 14.52% |
| Total capital | 14.32% | 14.57% | 14.28% | 14.60% | 14.52% |

The amounts set out in the Financial Summary have been prepared from audited financial statements of the Bank. The Bank has no extraordinary items or minority interests.

# Statement of Comprehensive Income

For the year ended 31 March 2020
All in $000's

| | Note | 2020 | 2019 |
|---|---|---|---|
| Interest income calculated using the effective interest method | | 266,041 | 260,550 |
| Other interest income | | 41,096 | 52,064 |
| Interest expense | | 163,871 | 174,487 |
| Finance cost on lease liabilities | | 678 | 104 |
| **Net interest income** | 2 | **142,588** | **138,023** |
| Other operating income | 3 | 21,909 | 23,746 |
| **Net operating income** | | **164,497** | **161,769** |
| Operating expenses | 4 | 102,678 | 94,955 |
| **Profit before impairment and tax** | | **61,819** | **66,814** |
| Credit impairment losses / (reversal of credit impairment losses) | 16.(f) | 20,362 | 4,236 |
| **Profit before tax** | | **41,457** | **62,578** |
| Tax expense | 5 | 10,640 | 17,539 |
| **Net profit after tax** | | **30,817** | **45,039** |
| **Other comprehensive income:** | | | |
| Items that may be reclassified subsequently to profit or loss: | | | |
| Movement in fair value reserve (debt instruments) | | (3,254) | 6,487 |
| Movement in effective portion of changes in fair value of cash flow hedges | | 1,184 | 1,549 |
| Income tax on items that may be reclassified to profit or loss | 5 | 580 | (2,250) |
| **Other comprehensive income for the year (net of tax)** | | **(1,490)** | **5,786** |
| **Total comprehensive income for the year** | | **29,327** | **50,825** |

Total comprehensive income for the year is attributable to the shareholder of the Bank.

From 1 April 2019, the Bank has adopted and applied NZ IFRS 16 in the preparation of the Statement of Comprehensive Income. Refer to note 1.(i) Changes in accounting policy for further information.

These financial statements are to be read in conjunction with the notes on pages 43-90.

# Statement of Changes in Equity

For the year ended 31 March 2020
All in $000's

| For the year ended March 2020 | Note | Share capital | Fair value reserve | Cash flow hedge reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|---|
| **Balance at 1 April 2019** | | **10,000** | **13,217** | **(2,172)** | **632,080** | **653,125** |
| **Total comprehensive income for the period:** | | | | | | |
| Net profit after tax | | - | - | - | 30,817 | 30,817 |
| Other comprehensive income: | | | | | | |
| Movement in cash flow hedge reserve | | - | - | 1,184 | - | 1,184 |
| Movement in fair value reserve | | - | (3,254) | - | - | (3,254) |
| Related tax | | | 911 | (331) | - | 580 |
| Total other comprehensive income | 14 | - | (2,343) | 853 | - | 5,786 |
| **Total comprehensive income for the period** | | **-** | **(2,343)** | **853** | **30,817** | **29,327** |
| Transactions with owner, recorded directly in equity: Dividends to equity holder | 13 | - | - | - | (2,500) | (2,500) |
| **Total transactions with owner** | | **-** | **-** | **-** | **(2,500)** | **(2,500)** |
| **Balance at 31 March 2020** | | **10,000** | **10,874** | **(1,319)** | **660,397** | **679,952** |

| For the year ended March 2019 | Note | Share capital | Fair value reserve | Cash flow hedge reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|---|
| **Balance at 1 April 2018** | | **10,000** | **8,546** | **(3,287)** | **597,041** | **612,300** |
| **Total comprehensive income for the period:** | | | | | | |
| Net profit after tax | | - | - | - | 45,039 | 45,039 |
| Other comprehensive income: | | | | | | |
| Movement in cash flow hedge reserve | | - | - | 1,549 | - | 1,549 |
| Movement in available-for-sale revaluation reserve | | - | 6,487 | - | - | 6,487 |
| Related tax | | | (1,816) | (434) | | (2,250) |
| Total other comprehensive income | 14 | - | 4,671 | 1,115 | - | (6,982) |
| **Total comprehensive income for the period** | | **-** | **4,671** | **1,115** | **45,039** | **50,825** |
| Transactions with owner, recorded directly in equity: Dividends to equity holder | 13 | - | - | - | (10,000) | (10,000) |
| **Total transactions with owner** | | **-** | **-** | **-** | **(10,000)** | **(10,000)** |
| **Balance at 31 March 2019** | | **10,000** | **13,217** | **(2,172)** | **632,080** | **653,125** |

From 1 April 2019, the Bank has adopted and applied NZ IFRS 16 in the preparation of the Statement of Changes in Equity. Refer to note 1.(i) Changes in accounting policy for further information.

These financial statements are to be read in conjunction with the notes on pages 43-90.

# Statement of Financial Position

For the year ended 31 March 2020
All in $000's

| | Note | 2020 | 2019 |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents | | 232,588 | 149,065 |
| Derivative financial instruments | 9 | 13,942 | 6,519 |
| Investment securities | 8 | 1,741,504 | 1,827,810 |
| Loans and advances to customers | 7 | 6,126,597 | 5,792,049 |
| Property, plant and equipment | | 34,150 | 28,072 |
| Intangible assets | | 15,404 | 9,010 |
| Deferred tax asset | 5 | 12,650 | 4,319 |
| Other assets | | 2,440 | 2,201 |
| **Total assets** | | **8,179,275** | **7,819,045** |
| | | | |
| **Liabilities** | | | |
| Deposits | 10 | 7,420,524 | 7,093,017 |
| Derivative financial instruments | 9 | 17,799 | 12,117 |
| Current tax liability | | 5,600 | 6,423 |
| Other liabilities | 11 | 55,400 | 54,363 |
| **Total liabilities** | | **7,499,323** | **7,165,920** |
| | | | |
| **Shareholder's Equity** | | | |
| Share capital | 13 | 10,000 | 10,000 |
| Fair value reserve | 14 | 10,874 | 13,217 |
| Cash flow hedge reserve | 14 | (1,319) | (2,172) |
| Retained earnings | | 660,397 | 632,080 |
| **Total shareholder's equity** | | **679,952** | **653,125** |
| **Total liabilities and shareholder's equity** | | **8,179,275** | **7,819,045** |
| | | | |
| Total interest earning and discount bearing assets | | 8,081,795 | 7,725,277 |
| Total interest and discount bearing liabilities | | 6,968,817 | 6,711,111 |

From 1 April 2019, the Bank has adopted and applied NZ IFRS 16 in the preparation of the Statement of Financial Position. Refer to note 1.(i) Changes in accounting policy for further information.

For and on behalf of the Board of Directors:

**J.J. Kelly**
(Chair — Board of Directors)
3 July 2020

**M.I. Bain**
(Deputy — Board of Directors)
3 July 2020

These financial statements are to be read in conjunction with the notes on pages 43-90.

# Statement of Cash Flows

For the year ended 31 March 2020
All in $000's

| | Note | 2020 | 2019 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Cash provided from (applied to): | | | |
| Interest income received | | 308,564 | 314,338 |
| Other income received | | 21,672 | 22,951 |
| Interest paid | | (168,191) | (174,970) |
| Operating expenditure | | (81,688) | (82,424) |
| Taxes and subvention payments | | (19,214) | (19,189) |
| **Cash flows from operating profits before changes in operating assets and liabilities** | | **61,142** | **60,706** |
| Net changes in operating assets and liabilities: | | | |
| Increase in loans and advances to customers | | (357,754) | (488,173) |
| Derivative financial instruments | | (558) | (211) |
| Increase in deposits | | 331,826 | 352,609 |
| **Cash flows from operating assets and liabilities** | | **(26,485)** | **(135,775)** |
| **Net cash flows from operating activities** | 6 | **34,657** | **(75,069)** |
| | | | |
| **Cash flows from investing activities** | | | |
| Cash provided from (applied to): | | | |
| Net (purchase) / maturity of investment securities | | 84,469 | 110,671 |
| Property, plant and equipment purchased | | (13,764) | (11,657) |
| Intangible assets purchased | | (9,620) | (3,097) |
| **Net cash flows from investing activities** | | **61,085** | **95,917** |
| | | | |
| **Cash flows from financing activities** | | | |
| Cash provided from (applied to): | | | |
| Dividends paid | | (10,000) | (9,844) |
| Lease payments | | (2,219) | (62) |
| **Net cash flows from financing activities** | | **(12,219)** | **(9,906)** |
| | | | |
| **Net increase in cash and cash equivalents** | | **83,523** | **10,942** |
| Add cash and cash equivalents at beginning of the year | | 149,065 | 138,123 |
| **Cash and cash equivalents at end of year** | | **232,588** | **149,065** |
| | | | |
| **Reconciliation of cash and cash equivalents to the Statement of Financial Position** | | | |
| Cash and cash at bank | | 21,966 | 22,666 |
| Balances with Reserve Bank | | 210,622 | 126,399 |
| **Total cash and cash equivalents at end of Year** | | **232,588** | **149,065** |

Application of NZ IFRS 16 has had an impact on the presentation in the Statement of Cash Flows. The reduction of the lease liability is categorised as a financing activity. The interest expense paid on leases is categorised as an operating activity. Refer to note 1.(i) Changes in accounting policy for further information.

These financial statements are to be read in conjunction with the notes on pages 43-90.

# Notes to the Financial Statements

## Basis of Preparation



## Financial Performance



## Financial Position



## Risk Management



## Other Disclosures

# Basis of Preparation

## 1. Statement of Compliance and General Accounting Policies

### (a) Statement of compliance

TSB Bank Limited (the Bank) is a profit-oriented company registered under the Companies Act 1993 and incorporated in New Zealand. The Bank's principal business activity is retail banking in New Zealand. These financial statements have been prepared in accordance with the requirements of the Companies Act 1993, the Financial Reporting Act 2013, and the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order"). The financial statements also comply with the requirements of the Financial Markets Conduct Act 2013 and the Order.

The Bank's financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards, as appropriate for profit-oriented entities. The financial statements comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). This is the first set of the Bank's annual financial statements in which NZ IFRS 16 Leases has been applied and the changes in accounting policies are described in note 1.(i).

The financial statements were approved by the Board of Directors on 3 July 2020.

### (b) Basis of measurement

The financial statements have been prepared on a historical cost basis, except for certain financial instruments measured at fair value as required by relevant accounting standards.

### (c) Presentation currency and rounding

The amounts contained in this disclosure statement and the financial statements are presented in New Zealand dollars and are rounded to the nearest thousand dollars. New Zealand dollars is the functional currency of the Bank.

### (d) Comparative data

To ensure consistency with the current period, comparative figures have been restated where appropriate.

### (e) Segment reporting

The Bank operates as one segment, in the business of retail banking in New Zealand. The Bank has no debt or equity instruments trading in the public market. The Bank therefore falls outside the scope of NZ IFRS 8 Operating Segments. On this basis no detailed segment information is presented as it is not required.

### (f) Foreign currency translation

The Bank trades foreign currency throughout its branch network. All foreign currency monetary assets and liabilities are converted at the rates of exchange ruling as at balance date. Unrealised gains and losses arising from these revaluations and gains and losses arising from foreign exchange dealings are recognised immediately in profit or loss.

### (g) Other assets

Other assets includes the accrual of other service related income, and the payment in advance of the delivery of goods or the rendering of services.

### (h) Financial instruments

The Bank is a full service financial institution offering an extensive range of financial instruments. Financial instruments are transacted on a commercial basis to derive an interest yield / cost with terms and conditions having due regard to the nature of the transaction and the risks involved. All financial instruments are accounted for on a settlement date basis, except for derivatives which are accounted for on trade date.

The Bank recognises and classifies its financial instruments in accordance with NZ IFRS 9 which contains three principal classification categories for financial assets based on contractual cash flow characteristics and business model:

## 1. Statement of Compliance and General Accounting Policies (continued)

### (h) Financial instruments (continued)

**Financial assets**

— **Amortised cost** — applies to financial assets recognised and initially measured at fair value plus transaction cost that are managed within the business model whose objective is to hold to collect the contractual cash flows and their contractual terms give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI). Included in this category are cash and cash equivalents, loans and advances to customers and other assets.

- Cash and cash equivalents consist of cash, call deposits due from/to other banks and demand balances with the Reserve Bank. They are short-term, highly liquid instruments that are readily convertible to known amounts of cash and therefore subject to insignificant risk of changes in value. Cash and cash equivalents are used in the day-to-day cash management of the Bank.
- Loans and advances to customers: Refer to note 7. Loans and Advances to Customers.
- Other assets include the accrual of other service related income.

These assets are subsequently measured at amortised cost using the effective interest methods and the carrying value of these assets is adjusted for provision for impairment as described in the note below and note 16. Credit Risk Management and Asset Quality.

— **Fair value through other comprehensive income (FVOCI)** — applies to financial assets recognised and initially measured at fair value plus transaction cost that are held in a dual business model whose objective is achieved by both collecting contractual SPPI cash flows and selling the assets. This category includes investment securities (refer to note 8 for further information) and they are subsequently held at fair value. The fair value gains or losses accumulated are reported in other comprehensive income as changes of 'fair value reserve'. When the financial asset is derecognised, the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss.

— **Fair value through profit or loss (FVPL)** — includes the groups of trading assets or the assets managed on a fair value basis as the contractual cash flows are not SPPI on the principal amount outstanding. The Bank may designate financial assets at FVPL when doing so eliminate or significantly reduce measurement or recognition inconsistencies. Financial instruments at FVPL are recorded in the statement of financial position at fair value. Gains or losses arising from changes in fair value are recognised in other operating income. Included in the categories are derivative assets and derivative liabilities. Financial assets designated at FVPL cannot subsequently change their designation and therefore are not subject to the reclassification requirements of NZ IFRS 9.

**Business model:** the business model reflects how the Bank manages the assets in order to generate cash flows. That is whether the Bank's objective is to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. Factors considered by the Bank in determining the business model for a group of assets include past experience on how cash flows for these assets were collected. For example, the Bank's business model for the mortgage loan book is to hold to collect contractual cash flows. Another example is the liquidity portfolio of assets, which is held by the Bank as part of liquidity management and is generally classified within the hold to collect and sell business model.

**SPPI:** where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Bank assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending agreement i.e. interest primarily includes consideration for the time value of money and credit risk. Interest can also include consideration for administration and profit margin, consistently with a basic lending agreement.

**Financial liabilities**

— In accordance with NZ IFRS 9, the Bank records all financial liabilities initially at their fair value plus or minus, in the case of the financial liabilities not at fair value through profit or loss (FVPL), transaction costs and classifies them as subsequently measured at amortised cost using the effective interest method, except for financial liabilities at FVPL, financial guarantee contracts and commitments. Financial liabilities measured at amortised costs include deposits (refer to note 10. Deposits for further information) and other financial liabilities (refer to note 11. Other Liabilities for further information).

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Bank has transferred substantially all the risks and rewards of ownership. Financial liabilities are derecognised when its contractual obligations are discharged, cancelled or expire. The differences between the carrying amount of financial assets / liabilities measured at the date of derecognition and the consideration received / paid to the counterparty involved are recognised in profit or loss.

The Bank offsets financial assets and financial liabilities and reports the net balance in the statement of financial position where there is a legally enforceable right to set-off and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously. Details on how the fair value of financial instruments is determined are disclosed in note 12. Fair Value of Financial Instruments.

All in $000's

## 1. Statement of Compliance and General Accounting Policies (continued)

### (i) Changes in accounting policy

NZ IFRS 16 Leases became effective for TSB from 1 April 2019 and has been applied in the preparation of the financial statements. On adoption of NZ IFRS 16, TSB recognised right-of-use assets and lease liabilities in relation to leases which had previously been classified as operating leases under the principles of NZ IAS 17 Leases. The recognised right-of-use assets and lease liabilities all relate to property and equipment leases.

In adopting NZ IFRS 16, TSB has elected to use the simplified retrospective approach. Under this approach, no comparative information is restated, as permitted under the specific transition provisions in the standard. The lease liability is recognised at the present value of the remaining lease payments, discounted using an incremental borrowing rate.

The change in accounting policy affected the following items in the balance sheet on 1 April 2019:

• Property, plant and equipment - increase of $9.54m
• Other liabilities - increase by $9.54m

Lease payments previously included in other operating expense as premises occupancy are now classified to financing and amortisation costs under NZ IFRS 16. In the statement of cash flows, lease payments for the principal portion of the lease liability are classified within financing activities and the interest portion of the lease liability are classified as operating activities.

The lease liabilities as at 1 April 2019 can be reconciled to the operating lease commitments as at 31 March 2019 as follows:

| **Operating lease commitments disclosed** | **As at 31 March 2019** |
|---|---|
| Rental / lease commitments less than one year | 2,472 |
| Rental / lease commitments greater than one year | 8,266 |
| Total non-cancellable operating lease commitments | 10,738 |
| | |
| Discounting using the incremental borrowing rate* | (1,190) |
| Short-term leases not recognised as a liability | (6) |
| Low-value leases not recognised as a liability | - |
| **Finance lease liabilities recognised as at 31 March 2019** | **9,542** |

* The weighted average incremental borrowing rate applied to the lease liabilities on 1 April 2019 was 4.16%.

| **Lease liability recognised** | **As at 1 April 2019** |
|---|---|
| Current lease liabilities | 2,183 |
| Non-current lease liabilities | 7,359 |
| **Total operating lease commitments recognised as finance lease under NZ IFRS 16** | **9,542** |

## 1. Statement of Compliance and General Accounting Policies (continued)

### (j) Critical accounting estimates, assumptions and judgements

The preparation of financial statements in conformity with NZ IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in the relevant accounting policy or in the relevant note (further information in note 12. Fair Value of Financial Instruments and note 16.Credit Risk Management and Asset Quality).

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

**Implications of COVID-19 on allowance for expected credit loss (ECL)**

COVID-19 has had a significant impact on global and domestic economic conditions. The recent deterioration in the economy due to COVID-19,and the prospect of this worsening going forward, has resulted in a significant increase in TSB's provision for expected credit loss (ECL).

TSB measures the allowance for expected credit loss (ECL) using an expected credit loss impairment model in compliance with NZ IFRS 9 Financial Instruments. TSB's accounting policy for the recognition and measurement of the allowance for expected credit loss is described in Note 16 Credit Risk Management and Asset Quality.

The table below shows TSB's allowance for expected credit loss (refer note 16 for further information).

| | 1/03/2020<br>$m | 1/09/2019<br>$m | 1/03/2019<br>$m |
|---|---|---|---|
| Collectively assessed | 38.1 | 26.4 | 28.2 |
| Individually assessed | 9.6 | 1.5 | 0.4 |
| **Total** | **47.7** | **27.9** | **28.6** |

**Individually assessed**

For the year ended March 2020 the individually assessed allowance for expected credit loss increased by $9.2m. In estimating individually assessed ECL for Stage 3 exposures, TSB makes judgements and assumptions in relation to:

- expected repayments
- the realisable value of collateral
- the economic prospects for the customer
- competing claims; and
- the likely cost and duration of the work-out process.

Consideration has been given to the potential impact of COVID-19 which has been incorporated into the judgements and assumptions made regarding these matters.

**Collectively assessed**

For the year ended March 2020 the collectively assessed allowance for expected credit loss increased by $9.9m.

In estimating collectively assessed ECL, TSB makes judgements and assumptions in relation to:

- the development of a modelling methodology, noting that the modelling of TSB's ECL estimates is complex; and
- the selection of inputs for those models, and the interdependencies between those inputs.

There is uncertainty around the impact of COVID-19 on the New Zealand economy and how consumers, businesses and governments will respond. This uncertainty is incorporated in TSB's assessment of expected credit losses from its credit portfolio which are subject to a number of management judgements and estimates.

The following table summarises the key judgements and assumptions in relation to the model inputs, the interdependencies between those inputs and highlights significant changes during the current period.

## 1. Statement of Compliance and General Accounting Policies (continued)

### (j) Critical accounting estimates, assumptions and judgements (continued)

| Judgement/Assumption | Description | Changes and considerations during the year ended 31 March 2020 |
|---|---|---|
| Determining when a significant increase in credit risk (SICR) has occurred | In measuring ECL, judgement is required when setting the rules and trigger points used to determine when a SICR has occurred since the initial recognition of a loan. This is important in that it results in the financial asset moving from 'stage 1' to 'stage 2', and results in an increase in the ECL from an allowance based on the probability of default in the next 12 months, to an allowance for lifetime expected credit losses. Decrease in credit risk as a result of transitioning from stage 2 back to stage 1 can also result in a significant change to the ECL allowance. These examples highlight the importance and potential impact that setting these trigger points can have on the ECL allowance. | **Impact of COVID-19 restrictions of SICR**<br>As a response to the COVID-19 outbreak New Zealand and other governments around the world have implemented severe travel restrictions on individuals and operational restrictions on businesses. There still remains a considerable amount of uncertainty around the medium and long term economic impacts of these restrictions with various sectors of the economy being impacted differently. TSB has reviewed the publicly available information about the potential impact of these restrictions, as well as direct feedback from its customers, to shortlist certain industries that will be the most impacted by the restrictions. It then further divided these industries into two groupings. Industries where a structural shift in the economic prospects has occurred (impacted industries) and those where the impact is deemed to be short-term or still highly uncertain at the time of preparation of this report (watchlist industries). The impacted industries have been deemed to have experienced a SICR event and have been moved into the lifetime credit loss calculation methodology. TSB will continue to regularly evaluate industry prospects and will make appropriate adjustments to industry classifications as and when deemed appropriate.<br>**Impact of COVID-19 Support packages:**<br>In response to the immediate impact of COVID-19 on the economy TSB has rolled out COVID-19 support packages for its customers, including loan repayment deferrals for up to 6 months, designed to provide short term assistance during the time of most severe COVID-19 related restrictions. These packages are available to customers who have had their incomes impacted by COVID-19 and were current with their payments prior to the restrictions being implemented. Due to the short-term nature of these arrangements the customers who have taken advantage of these packages are not considered to have significant loan lifetime increase in credit risk. This is consistent with the IFRS 9 and COVID-19 guidance issued by the IASB. TSB will re-assess these customers economic lifetime economic prospects once these particular assistance packages expire and will make appropriate changes to their credit risk classifications if deemed necessary. |
| Measuring both 12-month and lifetime credit losses | ECL is a function of the probability of default (PD), the loss given default (LGD) and the exposure at default (EAD). These are point-in-time measures reflecting the relevant forward looking information determined by management. Judgement is involved in determining which forward-looking information variables are relevant for particular lending portfolios and for determining the sensitivity of the parameters to movements in these forward looking variables. | TSB has used probability weighted scenarios to determine the expected distribution of credit loss outcomes. The scenarios were developed based on external macroeconomic forecasts, including Treasury and RBNZ forecasts, TSB's internal modelling and management judgement. A view was taken on the probability of the forecasts eventuating. |

## 1. Statement of Compliance and General Accounting Policies (continued)

### (j) Critical accounting estimates, assumptions and judgements (continued)

| Judgement/Assumption | Description | Changes and considerations during the year ended 31 March 2020 |
|---|---|---|
| Management temporary adjustments | Management temporary adjustments to the ECL allowances are adjustments used when it is deemed that existing inputs, assumptions and model techniques do not capture all the risk factors relevant to our lending portfolios. The use of management temporary adjustments may impact the amount of ECL recognised. | TSB implemented a temporary model overlay to address some input data and modelling technique shortcomings which rendered TSB unable to capture all the risk factors relevant to the lending portfolio. As TSB works to enhance the model and incorporates outstanding risk factors the need for the overlay will be reassessed. |

**ECL sensitivity analysis**

Given the large amount of uncertainty in the current economic enviroment, expected credit losses should be considered as a best estimate within a range of possible estimates. TSB has elected to use a 50% base and 50% downside scenario in determining its ECL.

The table below illustrates the sensitivity of ECL to key macroeconomic factors used in determining it:

| ECL sensitivity - Weightings applied to forecast scenarios | Total ECL $m | Impact $m |
|---|---|---|
| 100% base scenario | 25.7 | (12.4) |
| 50% base scenario / 50% downside scenario | 38.1 | - |
| 100% downside scenario | 50.6 | 12.5 |

### (k) Standards and amendments issued but not yet effective

The following new standards have been issued but are not yet effective and have not been applied in the preparation of these financial statements:

NZ IFRS 17 Insurance Contracts was issued in August 2017 to replace NZ IFRS 4 and is not effective for the Bank until 1 April 2021. NZ IFRS 17 establishes principles for the recognition, measurement, presentation, and disclosure of insurance contracts. The Bank does not issue insurance or reinsurance contracts therefore NZ IFRS 17 is not expected to have a material impact on the Bank.

Management have considered amendments to NZ IFRS which became relevant for the Bank for the first time during the year ended 31 March 2020 and have concluded they have no material impact on the Bank's financial position or performance. No new standards, amendments or interpretations to existing standards that are not yet effective have been early adopted by the Bank in these financial statements.

All in $000's

# Financial Performance

## 2. Net Interest Income

Interest income is measured using the effective interest rate (EIR) method for all financial instruments measured at amortised cost.

Interest income on interest earning financial assets measured at fair value through other comprehensive income (FVOCI) under NZ IFRS 9 is also recorded by using the EIR method. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of a financial asset, except for the financial assets that are not purchased or originated credit-impaired but have subsequently become credit-impaired (refer to note 16.(b) for further information), or to the amortised cost of a financial liability.

When calculating the effective interest rate (EIR), the Bank estimates cash flows considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. The interest income or expense is allocated through the life of the instruments and is measured for inclusion in profit or loss by applying the effective interest rate to the instrument's amortised cost.

Interest expense on deposits from customers relates to financial liabilities measured at amortised cost.

| **Interest income** | **Financial assets measured at** | **2020** | **2019** |
|---|---|---|---|
| Cash and cash equivalents | Amortised cost | 1,145 | 1,609 |
| Loans and advances to customers [1] | Amortised cost | 264,896 | 258,941 |
| Investment securities | FVOCI | 41,096 | 52,064 |
| **Total interest income** | | **307,137** | **312,614** |
| | | | |
| **Interest expense** | **Financial liabilities measured at** | | |
| Deposits from customers [2] | Amortised cost | 162,497 | 173,533 |
| Wholesale deposits | Amortised cost | 1,374 | 954 |
| Lease liability | Amortised cost | 678 | 104 |
| **Total interest expense** | | **164,549** | **174,591** |
| **Net interest income** | | **142,588** | **138,023** |

[1] Includes interest income earned on the commercial loan due from TSB Group Limited (refer to note 22. Related Party Transactions and Balances for further information). Interest earned on impaired assets is $0.491m (2019: $0.245m).

[2] Includes interest expense on deposits from TSB Community Trust (refer to note 22. Related Party Transactions and Balances for further information).

## 3. Other Operating Income

Revenue is recognised to the extent that is probable that economic benefits will flow to the Bank and that revenue can be reliably measured. Included in other operating income are fee and commission income, gains or losses on financial instruments and other income.

### Fee and commission income

Fee and commission income from contracts with customers is measured based on the consideration specified in a contract with a customer. The Bank recognises revenue when it transfers control over a service to a customer.

The following table provides information about the nature and timing of the satisfaction of performance obligations in contracts with customers for fee and commission income.

| Type of service / products | Nature and timing of satisfaction of performance obligations | Revenue recogntion under NZ IFRS 15 |
|---|---|---|
| Account and card services | The Bank provides account and card services including account management, provision of overdraft facilities and debit/credit cards. Fee and commission income from account and card services represents the income arising from financial assets that are not at FVPL. It excludes amounts incorporated in determining the effective interest rate on such financial assets and financial liabilities.<br>Fees for ongoing account management are charged to the customer's account on a monthly basis. Card fees are charged on a six-monthly or annual basis. Transaction-based fees for interchange, and overdrafts are charged to the customer's account when the transaction takes place. | Revenue from account and card service fees is recognised when received given the short-term duration of the related performance obligations.<br>Revenue related to transactions is recognised at the point in time when the transaction takes place. |
| Foreign exchange services | The Bank provides foreign currency transactions services.<br>Transaction-based fees for foreign currency transactions are charged to the customer's account when the transaction takes place. | Revenue related to transactions is recognised at the point in time when the transaction takes place. |
| Fund and insurance products distribution | The Bank markets different products through its network, namely through the sale of asset management services provided by Fisher Funds (refer to note 22. Related Party Transactions and Balances for more information) and insurance products. The Bank receives commission income in return. | Ongoing marketing and promotional activities performed by the Bank means that there are ongoing performance obligations and the revenue should be recognised across the relevant period. |
| Real estate services | The Banks provides real estate services to its customers.<br>Real-estate commissions are charged to the customers when the transaction takes place. | Revenue related to transactions is recognised at the point in time when the transaction takes place. |

### Gains or losses on financial instruments

Included are net gains or losses from the movements in fair value of derivative financial instruments and cumulative gains or losses reclassified from accumulated other comprehensive income in the fair value reserve to profit or loss upon derecognition of investments securities (debt instruments) designated at fair value through other comprehensive income (FVOCI). Interest income and expense on these financial instruments are recognised within net interest income and do not form part of the fair value movements of the financial instruments.

### Other income

Included are gains or losses on sale of fixed assets and sundry income that includes the recoverable proportion of goods and services tax (GST) on expenses incurred . Refer to note 5. Taxation for more information on GST.

The receivables and contract liabilities from contracts with customers are deemed immaterial and have not been disclosed separately.

All in $000's

### 3. Other Operating Income (continued)

| | 2020 | 2019 |
|---|---|---|
| **Fee and commission income** | | |
| Account and card services | 9,269 | 8,329 |
| Foreign exchange services | 2,203 | 2,351 |
| Fund and insurance products distribution | 3,314 | 3,127 |
| Real estate services | 993 | 1,606 |
| Total fee and commission income | 15,779 | 15,413 |
| | | |
| **Gains / losses on financial instruments** | | |
| Gain / (loss) on derivative financial instruments (measured at FVPL) | 130 | 236 |
| Cumulative gains / (losses) transferred from fair value reserve (designated at FVOCI)* | 3,423 | 3,510 |
| Total other gains / losses | 3,553 | 3,746 |
| | | |
| **Other income** | | |
| Gain / (loss) on sale of fixed assets | (70) | (11) |
| Sundry income | 2,647 | 4,598 |
| **Total other operating income** | **21,909** | **23,746** |

* Includes recovery of $2.02m (2019: $2.1m) from Solid Energy (SENZ).

### 4. Operating Expenses

All expenses are recognised in profit or loss on an accrual basis.

**Depreciation**

The cost of property, plant and equipment (excluding land) less the estimated residual value is depreciated over their useful lives (lease term for leased assets) on a straight line basis. The range of useful lives of the asset classes are:

| | |
|---|---|
| Buildings | 50 to 100 years |
| Furniture and Fittings | 5 to 10 years |
| Computer Equipment | 1 to 5 years |
| Leased Asset | Up to 30 years |

The assets' residual values, useful lives and depreciation methods are reviewed and adjusted if appropriate at each balance date.

The Bank has recognised new leased assets and corresponding lease liabilities of $9.54m at the date of initial application of NZ IFRS 16 and recorded them within property, plant and equipment and other liabilities, respectively. Refer to note 1.(i) Changes in accounting policy for further information.

Assets are reviewed for indications of impairment at least annually and whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Any impairment loss or write-down is recognised in profit or loss as an expense.

**Amortisation**

Amortisation is provided on intangible assets that consist of acquired computer software licences, naming rights and certain acquired and internally generated software.

Acquired computer software licences are capitalised on the basis of costs incurred to acquire and bring to use the specific software. These costs are amortised over their expected useful lives (two to four years) on a straight line basis.

All in $000's

## 4. Operating Expenses (continued)

### Amortisation (continued)

The identifiable and directly associated cost of acquiring and developing software are capitalised where the software is controlled by the Bank, and where it is probable that future economic benefits will flow from its use over more than one year. Intangible assets are amortised on a straight line basis over their expected useful lives (two to ten years). Costs associated with maintaining software are recognised as an expense as incurred. Intangible assets are subject to the same impairment review process as property, plant and equipment. Any impairment loss is recognised profit or loss as an expense.

### Personnel

Personnel includes expenses associated with employees' wages, salaries and other associated costs. The expense is recognised over the period the employee renders the service to receive the benefit.

| **Fees paid to auditor:** | **2020** | **2019** |
|---|---|---|
| Audit and review of financial statements [1] | 201 | 240 |
| Audit of TSB Realty Trust | 5 | 5 |
| Other services [2] | 292 | 182 |
| Total fees paid to auditor | 498 | 427 |
| | | |
| Depreciation | 5,686 | 3,235 |
| Amortisation of intangible assets | 3,226 | 2,386 |
| Directors' fees | 808 | 724 |
| Personnel | 42,022 | 40,861 |
| Defined contribution plan | 1,658 | 1,543 |
| Information technology | 13,403 | 12,228 |
| Premises occupancy | 2,135 | 4,615 |
| Marketing | 8,706 | 10,704 |
| Debit / Credit card expenses [3] | 6,694 | 5,571 |
| Other [4] | 17,842 | 12,661 |
| **Total operating expenses** | **102,678** | **94,955** |

[1] Included are fees for the audit of annual financial statements and review of interim financial statements.
[2] Other services include regulatory and risk advisory services $127k and $165k, respectively, totaling to $292k (2019: $182k).
[3] Debit / Credit card expenses are fee expenses arising from financial liabilities that are not at FVPL.
[4] Other includes an impairment loss of $2m on land.

All in $000's

## 5. Taxation

### Income tax

Income tax on the profit for the period comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in equity or other comprehensive income.

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at balance date after taking advantage of all allowable deductions under current taxation legislation and any adjustment to tax payable in respect of previous years.

Deferred tax is accounted for in respect of temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for tax purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at balance date.

In accordance with NZ IAS 12 Income Taxes, a deferred tax asset is recognised only to the extent that it is probable (i.e. more likely than not) that a future taxable profit will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

When the temporary differences cause the operating surplus to be higher than the taxable surplus, a deferred tax liability is recognised. When the operating surplus is lower than the taxable surplus, a deferred tax asset is recognised.

Movements in fair value (and deferred tax) related to investment securities, cash flow hedges and the revaluation of non-current assets (if applicable), are recognised in other comprehensive income and presented in shareholder's equity accordingly.

| **Reconciliation of net profit before tax to tax expense** | **2020** | **2019** |
|---|---|---|
| Net profit before tax | 41,457 | 62,578 |
| Tax at 28% | 11,608 | 17,522 |
| Adjustments to prima facie tax | (968) | 17 |
| **Tax expense** | **10,640** | **17,539** |
| | | |
| **Income tax recognised in profit or loss** | | |
| Current tax expense: | | |
| Current year | 18,399 | 18,246 |
| Prior period adjustments | (8) | 447 |
| Deferred tax expense: | | |
| Current year | (8,095) | (710) |
| Prior period adjustments | 344 | (444) |
| **Income tax expense** | **10,640** | **17,539** |
| | | |
| **Deferred tax recognised in profit or loss** | | |
| Depreciation | 1,073 | (77) |
| Amortisation of intangibles | 240 | (331) |
| Provision for impairment losses | 5,356 | 714 |
| Derivative financial instruments | (150) | 115 |
| Other temporary differences* | 1,232 | 733 |
| **Total deferred tax recognised in profit or loss** | **7,751** | **1,154** |
| | | |
| **Income tax recognised in other comprehensive income** | | |
| Deferred tax expense: | | |
| Cash flow hedge reserve | (331) | (434) |
| Fair value reserve | 911 | (1,816) |
| **Total deferred tax recognised in other comprehensive income** | **580** | **(2,250)** |

* Other temporary differences reflect adjustments for employee benefits.

All in $000's

### 5. Taxation (continued)

| | 2020 | 2019 |
|---|---|---|
| Deferred tax: | | |
| Balance at beginning of year | 4,319 | 5,137 |
| Balance adjusted for adoption of NZ IFRS 9 | - | 278 |
| Adjusted balance at beginning of year | 4,319 | 5,415 |
| Deferred tax recognised in profit or loss | 7,751 | 1,154 |
| Deferred tax recognised in equity | 580 | (2,250) |
| **Balance at end of year** | **12,650** | **4,319** |
| Deferred tax relates to: | | |
| Property, plant, and equipment | (11) | (1,084) |
| Amortisation of intangibles | (515) | (755) |
| Provision for impairment losses | 13,363 | 8,007 |
| Fair value adjustments for derivative financial instruments | 585 | 1,074 |
| Fair value movements on investment securities | (4,221) | (5,140) |
| Other temporary differences * | 3,449 | 2,217 |
| **Total deferred tax asset** | **12,650** | **4,319** |

* Other temporary differences reflect adjustments for employee benefits.

The imputation credits available to carry forward and utilise in future periods are $286.39m (31 March 2019: $267.55m).

**Goods and services tax (GST)**
Revenues, expenses and assets are initially recognised gross of the amount of goods and services tax (GST) unless stated otherwise. As the principal activity of the Bank is providing financial services, only a proportion of GST paid on inputs is recoverable from Inland Revenue Department. The recoverable proportion of GST is adjusted from the cost of acquisition of the asset or is recognised as other income.

### 6. Notes to the Cash Flow

The statement of cash flows has been prepared using the direct approach, including the netting of cash flows associated with deposits from customers, loans and advances to customers and investment securities.

The following are the definitions of the terms used in the statement of cash flows:
(a) Cash is considered to be cash on hand and current accounts in banks, net of bank overdrafts;
(b) Investing activities are those activities relating to the acquisition, holding and disposal of property, plant and equipment, intangible assets, and investment securities;
(c) Financing activities are those activities that result in changes in the size and composition of the capital structure of the Bank; and
(d) Operating activities include all transactions and other events that are not investing or financing activities.

| **Reconciliation of net profit after tax to net cash flows from operating activities** | 2020 | 2019 |
|---|---|---|
| **Net profit after tax** | **30,817** | **45,039** |
| **Add movements in statement of financial position items:** | | |
| Accounts payable | 8,537 | 6,951 |
| Current tax | (823) | (496) |
| Deposits from customers | 327,507 | 352,129 |
| Deferred tax asset | (7,751) | (1,154) |
| Accounts receivable | 1,189 | 928 |
| Lease liability | 2,219 | 61 |
| Derivative financial instruments | (558) | (211) |
| Loans and advances to customers | (357,754) | (488,173) |
| | **(27,434)** | **(129,965)** |
| **Add non - cash items:** | | |
| Amortisation of intangible assets | 3,226 | 2,386 |
| Depreciation | 5,686 | 3,235 |
| Credit impairment losses / (gains) | 20,362 | 4,236 |
| Other impairment losses / (gains) | 2,000 | - |
| | **29,274** | **9,857** |
| **Net cash flows from operating activities** | **34,657** | **(75,069)** |

All in $000's

## 7. Loans and Advances to Customers

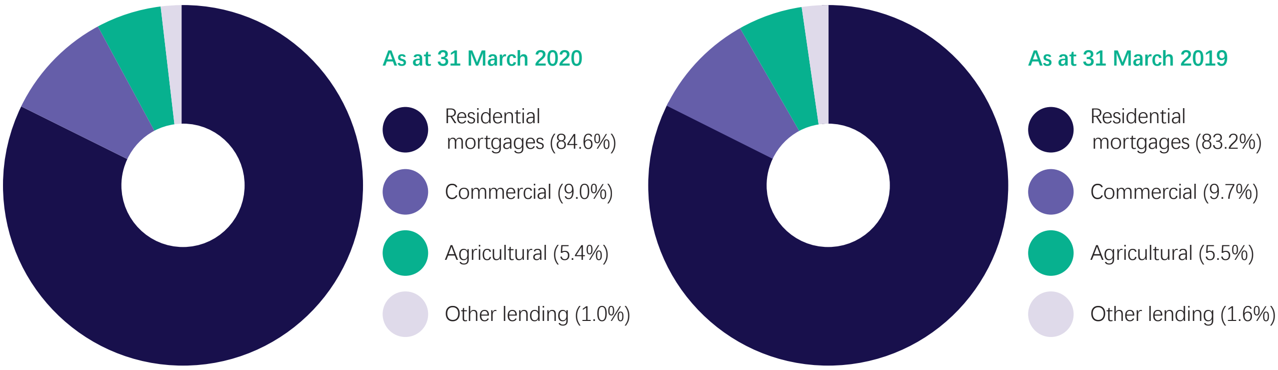
This covers all forms of lending to customers, and include mortgages, overdrafts, personal loans and credit card balances. Loans and advances to customers are recognised in the statement of financial position when cash is advanced to the customer and subsequently measured at amortised cost less allowance for impairment to reflect the estimated recoverable amounts. Refer to note 16. Credit Risk Management and Asset Quality for further information on provision for credit impairment.

Residential mortgages comprise 84.6% (31 March 2019: 83.2%) of the total loan portfolio and they are secured by a first mortgage over freehold dwellings. For overdrafts and credit card balances, some are unsecured as well as secured by obligation mortgages, which cover all undertakings with the Bank.

| | Note | 2020 | 2019 |
|---|---|---|---|
| Residential | 19.(d) | 5,222,565 | 4,844,453 |
| Commercial [1] | | 556,603 | 561,980 |
| Community | | 2,062 | 2,382 |
| Agricultural | | 331,038 | 317,281 |
| Personal [2] | | 43,338 | 72,745 |
| Others [3] | | 18,720 | 21,807 |
| **Total gross loans and advances to customers** | | **6,174,326** | **5,820,648** |
| Less provision for impairment | 16.(f) | (47,729) | (28,599) |
| **Total loans and advances to customers** | | **6,126,597** | **5,792,049** |

[1] Commercial includes a loan to TSB Group Limited (refer to note 22. Related Party Transactions and Balances for more information).
[2] Personal is inclusive of lending through Harmoney platform, other retail lending and credit card balances.
[3] Others include lending accruals and deferred acquisition costs.

Charts below show the percentage (%) breakdown of the loans and advances to customers.




## 8. Investment Securities

Included in this category are certificates of deposit, commercial paper and other debt securities measured at fair value through other comprehensive income (FVOCI) that are originated with a mixed objective that is both to collect the contractual cash flows and to sell the debt instruments, and that have contractual cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding. They are used to manage liquidity and may be sold prior to maturity. Interest earned whilst holding investment securities is recognised in the profit or loss using the effective interest method.

Unrealised gains and losses are recognised directly in other comprehensive income and presented in the fair value reserve within the statement of changes in equity, until the assets are sold or otherwise disposed of. On disposal the accumulated change in fair value is transferred to profit or loss and reported under other Income. Interest, premiums and discounts are amortised through profit or loss using the effective interest method.

| | 2020 | 2019 |
|---|---|---|
| Local authority securities | 128,719 | 235,603 |
| Government securities | 513,032 | 434,233 |
| Registered bank securities | 473,779 | 509,525 |
| Other investments * | 625,974 | 648,449 |
| **Total investment securities** | **1,741,504** | **1,827,810** |

* Other investments relate to investments in utility companies, SOE's and commercial paper, and Bonds of New Zealand corporates.

## 9. Derivative Financial Instruments

The Bank uses derivatives for risk management purposes as part of its asset and liability risk management activities to manage exposure to interest rate changes. Derivatives held for risk management purposes include hedges that either meet the hedge accounting requirements or hedges that are economic hedges, but do not meet the hedge accounting requirements. The treatment of changes in the derivatives' fair value depends on their classification. Provided certain criteria are met for hedge accounting under NZ IFRS 9, either fair value or cash flow hedge accounting can be applied. Hedge accounting is applied to remove the accounting mismatch between the hedging instrument and the hedged item.

For derivatives, any accrued interest is recognised and measured as part of the derivative's fair value. Derivatives are only used for economic hedging purposes and not as speculative investments. However, where derivatives do not meet the hedging criteria, they are classified as 'held for trading' for accounting purposes. Any derivative that is de-designated as a hedging derivative will be accounted for as held for trading from the time that it is de-designated, with all subsequent movements in fair value recognised in the profit or loss. The Bank has the following derivative financial instruments:

**Economic hedge**
Included under this classification are any derivatives entered into by the Bank in order to economically hedge its exposures for risk management purposes that do not meet the NZ IFRS 9 hedge accounting criteria.

**Cash flow hedge**
The main derivative type used by the Bank is interest rate swaps. Interest rate swaps relate to contracts taken out by the Bank with other counterparties. The Bank manages its cash flow interest rate risk by using:

(i) floating-to-fixed interest rate swaps to fix the income of a pool of floating rate assets (including loans and advances to customers and investment securities);

(ii) fixed-to-floating interest rate swaps to fix the cost of floating interest rate deposits.

During 2020, both the hedging derivatives and hedged items were all denominated in New Zealand dollars.

Under these swaps, the Bank agrees with other parties to exchange, at specified intervals (mainly quarterly or semi-annually), the difference between fixed contract rates and floating rate interest amounts calculated by reference to the agreed notional principal amounts.

The Bank's loans and advances to customers and the deposits are carried at amortised cost, whilst the investment securities are accounted for at FVOCI. These balance sheet items are contractually repriced from time to time and to that extent are also exposed to the risk of future changes in market interest rates.

The Bank documents, at inception of the transaction, the relationship between hedging instruments and hedged items, as well as the Bank's risk management objective and strategy for undertaking these hedge transactions. In addition, the documents outline how effectiveness will be measured throughout the life of the hedge relationship and its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedge transactions are highly effective in offsetting changes in cash flows of hedged items.

Method used to test hedge effectiveness and determine the hedge ratio is primarily based on regression analysis.

Hedge ineffectiveness may occur due to:
- the credit value/debit value adjustment on the interest rate swaps which is not matched by the hedged item; and
- differences in critical terms between the interest rate swaps and hedge items.

There was no ineffectiveness during 2020 in relation to the interest rate swaps (2019: nil).

The effective portion of changes in fair value of derivatives that are designated and qualify as cash flow hedges are recognised in other comprehensive income and presented in the cash flow hedge reserve in equity, while the gain or loss relating to any ineffective portion is recognised immediately in the profit or loss. The carrying value of the hedged item is not adjusted.

Amounts accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised in the profit or loss when the forecast transaction ultimately affects profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the profit or loss.

All in $000's

## 9. Derivative Financial Instruments (continued)

**Fair value hedge**
Changes in the fair value of derivatives associated with investment securities in a fair value hedge relationship are recorded in profit or loss, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

As at reporting date, there were no material fair value hedge relationships.

**FX forward exchange currency assets**
The Bank enters into forward exchange contracts (FEC) on its own and on behalf of customers with other banks. Where the contract is entered on behalf of customers, a separate contract is formed between the Bank and customers for any liability / asset that may arise as a result of the FEC. The fair value of these derivatives is obtained from observable market prices as at reporting date.

As at reporting date, there were no material holdings of foreign currency.

The Bank's risk management policy is included in note 17. Market Risk Management.

| | As at 31 March 2020 | | | As at 31 March 2019 | | |
|---|---|---|---|---|---|---|
| | Notional Amount | Fair Values Assets | Fair Values Liabilities | Notional Amount | Fair Values Assets | Fair Values Liabilities |
| **Interest rate swaps** | | | | | | |
| Derivatives held as economic hedges | 20,000 | - | 258 | 57,600 | - | 821 |
| Derivatives held as cash flow hedges | 1,243,000 | 13,942 | 17,541 | 868,000 | 6,519 | 11,296 |
| Derivatives held as fair value hedges | - | - | - | - | - | - |
| **Total interest rate swaps** | **1,263,000** | **13,942** | **17,799** | **925,600** | **6,519** | **12,117** |
| FX forward exchange currency assets | - | - | - | - | - | - |
| **Total derivative financial instruments** | **1,263,000** | **13,942** | **17,799** | **925,600** | **6,519** | **12,117** |

The notional amount, recorded gross, represents the quantity of the derivative contracts' underlying instruments.

The effects of the interest rate swaps related hedging instruments on the Bank's financial position and performance are as follows:

| | 2020 | 2019 |
|---|---|---|
| **Derivative financial instruments – interest rate swaps** | | |
| Change in fair value of outstanding hedging instruments | (3,857) | (5,598) |
| Change in value of hedged item used to determine hedge effectiveness | 3,857 | 5,598 |
| Hedge ratio | 1:1 | 1:1 |

The profile of the timing of the notional amount and average price of derivatives designated in cash flow hedge relationships is outlined in the following table:

| As at 31 March 2020 | 3 months or less | 3-12 months | 1-5 years | Over 5 years | Total |
|---|---|---|---|---|---|
| **Interest rate swaps** | | | | | |
| Pay fixed | 150,000 | 300,000 | 503,000 | 20,000 | **973,000** |
| Average fixed interest rate paid | 2.26% | 1.88% | 1.25% | 3.79% | 1.65% |
| Receive fixed | - | 10,000 | 260,000 | - | **270,000** |
| Average fixed interest rate received | 0.00% | 2.10% | 2.14% | 0.00% | 2.14% |
| **Total notional amount** | **150,000** | **310,000** | **763,000** | **20,000** | **1,243,000** |

All in $000's

### 10. Deposits

Deposits cover all forms of funding, and include savings, transactional accounts, term deposits and registered certificate of deposits (RCD's), apart from those classified as fair value through profit or loss. Wholesale deposits consist of registered certificates of deposit (RCD). Deposits including the amounts due to related entities are measured at amortised cost using the effective interest method.

| | 2020 | 2019 |
|---|---|---|
| Retail term deposits * | 3,940,007 | 3,899,785 |
| On call deposits bearing interest | 2,948,945 | 2,761,461 |
| On call deposits not bearing interest | 451,707 | 381,906 |
| Wholesale deposits bearing interest | 79,865 | 49,865 |
| **Total deposits** | **7,420,524** | **7,093,017** |

* Includes term deposits from TSB Community Trust. Refer to note 22. Related Party Transactions and Balances for more information.

**Concentrations of funding**
Concentrations of funding by geographic region and industry sector at balance date are as follows:

| | 2020 | 2019 |
|---|---|---|
| **Retail deposits** | | |
| Taranaki | 3,298,650 | 3,165,512 |
| Rest of New Zealand | 3,922,215 | 3,742,767 |
| Outside New Zealand | 199,659 | 184,738 |
| **Total funding by geographic region** | **7,420,524** | **7,093,017** |
| | | |
| Government and public authorities | 30,663 | 7,268 |
| Finance (wholesale deposits) | 79,865 | 49,865 |
| Households | 7,169,271 | 6,896,426 |
| Community | 53,733 | 52,839 |
| Commercial | 86,992 | 86,619 |
| **Total funding by industry sector** | **7,420,524** | **7,093,017** |

### 11. Other Liabilities

The Bank provides for the cost of employees' annual entitlements and long-service entitlements under the terms of their employment contracts. The liability for long-service entitlements is calculated as the present value of the expected future payments after allowing for salary reviews, years of service with the Bank, and other parameters affecting probability of payment. A provision is recognised for the amount expected to be paid and therefore recorded in other liabilities.

| | 2020 | 2019 |
|---|---|---|
| Employee entitlements | 10,285 | 9,256 |
| Dividend payable | - | 7,500 |
| Trade and other payables | 28,976 | 30,856 |
| Lease liabilities* | 15,854 | 6,089 |
| Other non-financial liabilities | 285 | 662 |
| **Total other liabilities** | **55,400** | **54,363** |

* Includes the lease liabilities of $9.54m recognised at the date of initial application of NZ IFRS 16. Refer to note 1.(i) Changes in accounting policy for further information.

All creditors and depositors are ranked equally.

## 12. Fair Value of Financial Instruments

**Fair value valuation methodology**
Certain financial instruments are carried on the statement of financial position at fair value. The best evidence of fair value is a quoted market price in an active market. Therefore, where possible, fair value is based on quoted market prices.

The following fair value hierarchy, as set out in NZ IFRS 13: Fair Value Measurement, has been used to categorise the inputs to valuation techniques used to measure the financial assets and financial liabilities which are carried at fair value:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the assets or liabilities, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the assets or liabilities that are not based on observable market data (unobservable inputs).

Where a quoted market price for an instrument is not available, the Bank uses its judgement to select a variety of methods and make assumptions depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instruments at each reporting date. Specific valuation techniques used to value financial instruments are described below in fair value estimates.

**Fair value estimates**
The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. The fair value of the Bank's financial insruments is estimated as follows:

Cash and cash equivalents
Included are cash and call deposits with the Reserve Bank. These assets are short term in nature and therefore the related carrying value is equivalent to their fair value.

Derivative assets and liabilities
Derivative financial instruments are classified in level 2 and their fair values are obtained from market yields and discounted cash flow models.

The fair values are estimated using present value or other market acceptable valuation techniques, using methods or assumptions that are based on observable market conditions and risks existing as at the reporting date.

Investment securities
Estimates of fair value for investment securities are based on quoted market prices or dealer price quotations for financial instruments traded in active markets, or by using valuation techniques. Where a market price in a liquid market is not readily available, the fair value is determined by reference to the market price available for a security with similar credit, maturity and yield characteristics or by using industry standard pricing models incorporating observable market inputs.

Loans and advances to customers
The fair value of loans and advances to customers is estimated using discounted cash flow models based on the interest rate repricing of the loans and advances. Discount rates applied in this calculation are based on the current market interest rates for loans and advances to customers with similar credit and maturity profiles. The current market interest rates are based on what the scheduled rate would be for a similar term and maturity profile as at reporting date.

Refer to the note 17. Market Risk Management for further information on interest rate repricing.

Other assets, deposits from customers and other liabilities
For non-interest bearing debt, call and variable rate deposits, the carrying amounts in the statement of financial position are a reasonable estimate of their fair value because all are short-term in nature. For other term deposits, fair value is estimated using discounted cash flow models based on the maturity of the deposits. The discount rates applied in this calculation are based on current market interest rates for similar deposits with similar maturity profiles. For all other assets, and other liabilities, the carrying amounts in the statement of financial position are a reasonable estimate of their fair value.

All of the Bank's financial instruments that are recognised and measured at fair value on a recurring basis sit within Level 2.

There were no transfers between Level 1 and Level 2 of the fair value hierarchy during the reporting period.

All in $000's

### 12. Fair Value of Financial Instruments (continued)

The following table summarises the carrying amounts and fair values of financial assets and financial liabilities.

| As at 31 March 2020 | Note | At amortised cost | At FVOCI | At FVPL | Fair value - hedging instruments | Total carrying amount | Fair value |
|---|---|---|---|---|---|---|---|
| Financial assets: | | | | | | | |
| Cash and cash equivalents | | 232,588 | - | - | - | 232,588 | 232,588 |
| Derivative financial instruments | 9 | - | - | - | 13,942 | 13,942 | 13,942 |
| Investment securities | 8 | - | 1,741,504 | - | - | 1,741,504 | 1,741,504 |
| Loans and advances to customers | 7 | 6,126,597 | - | - | - | 6,126,597 | 6,116,841 |
| Other assets | | 2,440 | - | - | - | 2,440 | 2,440 |
| **Total financial assets** | | **6,361,625** | **1,741,504** | **-** | **13,942** | **8,117,071** | **8,107,315** |
| Financial liabilities: | | | | | | | |
| Deposits | 10 | 7,420,524 | - | - | - | 7,420,524 | 7,372,049 |
| Derivative financial instruments | 9 | - | - | - | 17,799 | 17,799 | 17,799 |
| Other liabilities | | 55,115 | - | - | - | 55,115 | 55,115 |
| **Total financial liabilities** | | **7,475,639** | **-** | **-** | **17,799** | **7,493,438** | **7,444,963** |
| **As at 31 March 2019** | | | | | | | |
| Financial assets: | | | | | | | |
| Cash and cash equivalents | | 149,065 | - | - | - | 149,065 | 149,065 |
| Derivative financial instruments | 9 | - | - | - | 6,519 | 6,519 | 6,519 |
| Investment securities | 8 | - | 1,827,810 | - | - | 1,827,810 | 1,827,810 |
| Loans and advances to customers | 7 | 5,792,049 | - | - | - | 5,792,049 | 5,785,906 |
| Other assets | | 2,201 | - | - | - | 2,201 | 2,201 |
| **Total financial assets** | | **5,943,315** | **1,827,810** | **-** | **6,519** | **7,777,644** | **7,771,501** |
| Financial liabilities: | | | | | | | |
| Deposits | 10 | 7,093,017 | - | - | - | 7,093,017 | 7,054,997 |
| Derivative financial instruments | 9 | - | - | - | 12,117 | 12,117 | 12,117 |
| Other liabilities | | 53,701 | - | - | - | 53,701 | 53,701 |
| **Total financial liabilities** | | **7,146,718** | **-** | **-** | **12,117** | **7,158,835** | **7,120,815** |

## 13. Share Capital, Retained Earnings and Dividend Paid

All ordinary shares have equal voting rights and share equally in dividends and assets on winding up. All shares are held by the TSB Community Trust through the Trust's fully owned subsidiary, TSB Group Limited. Dividends are recognised in the financial year in which they are authorised and approved by the Board of Directors.

| **Share capital:** | 2020 | 2019 |
|---|---|---|
| Issued and fully paid up capital: | | |
| 20,000,000 ordinary shares | 10,000 | 10,000 |
| **Total share capital** | **10,000** | **10,000** |

| **Retained earnings:** | | |
|---|---|---|
| Opening balance | 632,080 | 597,756 |
| Balance adjusted for adoption of NZ IFRS 9 | - | (715) |
| Net profit after taxation (NPAT) | 30,817 | 45,039 |
| Retained earnings after NPAT | 662,897 | 642,080 |
| Dividends | (2,500) | (10,000) |
| **Retained earnings at end of period** | **660,397** | **632,080** |

| | 31 March 2020 | | 31 March 2019 | |
|---|---|---|---|---|
| **Dividend** | **$000** | **$ per share** | **$000** | **$ per share** |
| Interim | 2,500 | 0.125 | 2,500 | 0.125 |
| Special | - | - | - | - |
| Final | - | - | 7,500 | 0.375 |
| **Total** | **2,500** | **0.125** | **10,000** | **0.500** |

## 14. Reserves

The cash flow hedge reserve is used to recognise the effective portion of gains or losses on derivatives that are designated and qualify as cash flow hedges (refer to note 9. Derivative Financial Instruments for more details). The cumulative gain or loss relating to the ineffective portion is recognised immediately in profit or loss, within other operating income.

The Bank has investment securities measured at FVOCI and the changes in fair value of which are accumulated within the fair value reserve until the assets are derecognised or reclassified. As at the reporting date, the Bank has no investments in equity instruments designated as at FVOCI.

The following table shows a breakdown of the Bank's reserves and the movements in these reserves during the reporting period.

| **Cash flow hedge reserve** | Note | 2020 | 2019 |
|---|---|---|---|
| Opening balance | | (2,172) | (3,287) |
| Change in fair value of hedging instrument recognised in OCI for the year (effective portion) | | 1,314 | 1,785 |
| Cumulative gain / (loss) transferred to the profit or loss | 3 | (130) | (236) |
| Related tax | | (331) | (434) |
| Movement in cash flow hedge reserve | | 853 | 1,115 |
| **Closing balance** | | **(1,319)** | **(2,172)** |

| **Fair value reserve** | | | |
|---|---|---|---|
| Opening balance | | 13,217 | 8,546 |
| Gross changes in fair value | | 169 | 9,997 |
| Cumulative gain / (loss) transferred to the profit or loss | 3 | (3,423) | (3,510) |
| Related tax | | 911 | (1,816) |
| Movement in fair value reserve | | (2,343) | 4,671 |
| **Closing balance** | | **10,874** | **13,217** |

## 15. Risk Governance

The Bank is committed to the appropriate management of all risks arising from its activities, in accordance with the stated risk appetite approved by the Board of Directors. The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework, including the material risk domains and the associated risk appetite for each of the material risk domains.

Whilst there have been no material changes to the risk management policies, or material exposures to any new types of risk since publication of the previous Disclosure Statement, the Bank has identified a need for improved risk management policies, processes and models, including the control environment, monitoring, and assurance around material risks. The Bank is committed to taking appropriate steps to mature the risk environment as soon as practicable.

The Bank is in discussions with the Reserve Bank with respect to identified regulatory breaches. See Other Material Matters in General Information for further reference.

**(a) Risk governance and the role of the Board of Directors**

The Board of the Bank has the primary responsibility for effective risk management. These responsibilities are delegated to the Executive Management of the Bank through the Banks Delegated Authorities Framework.

The Bank's risk management framework embeds risk management accountability and responsibility throughout the Bank. The Banks' risk management framework is comprised of the following elements:

- A three lines of accountability model that defines the roles and responsibilities of individuals in relation to the effective management of risk;
- material risk domains and associated risk appetite statements and measurement mechanisms;
- policies and procedures covering risk identification, assessment, controls, treatment, monitoring, measurement and reporting; and
- mechanisms for the on-going review of systems, policies, and procedures, including independent review by Internal and External Audit.

The various Standing Committees of the Board (part (b) monitor performance against the risk appetite, policy and metrics. Executive management, including Standing Executive Management Committees, of the Bank ensure that policies are managed appropriately and provides assurance to the Standing Board Committees. The tactical implementation of policies through Executive Management ensures that operational processes are appropriately implemented and risks taken on by the organisation are effectively identified, assessed and managed in accordance with the risk appetite established by the Board.

**(b) Standing Committees of the Board and Executive Management**

Audit Committee (Board Committee)
The role of the Audit Committee is to assist the Board in discharging its oversight responsibilities by:

1.1 Overseeing the effectiveness and integrity of the Bank's financial controls; financial reporting process; and internal audit function;

1.2 Reviewing and recommending to the Board appropriate actions around the:
- appointment of external auditor;
- appointment of the co-sourced internal audit function;
- integrity of the financial statements and financial reporting systems;
- compliance with financial reporting regulatory requirements; and
- compliance with non-financial regulatory requirements.

1.3 Approving the:
- external audit plan; and
- internal audit plan;

Risk Committee (Board Committee)
The role of the Risk Committee is to assist the Board in discharging its oversight responsibilities by:

1.1 Ensuring that risk appetite is appropriate for the operating environment, aligned to the Banks strategic objectives and supported by the Banks capital allocation;

1.2 Inquiring into the effectiveness and integrity of the risk management framework and associated risk appetite, policies and procedures; and

1.3 Examining performance against risk appetite through risk reporting for each of the material risk domains.

People, Culture and Capability Committee (Board Committee)
The role of the People, Culture and Capability Committee is to assist the Board in discharging its responsibilities by:

1.1 Working with the Chairman of the Board in planning the Board composition, evaluating the competencies required of prospective directors, identifying those prospective directors, evaluating their independence and competencies, developing succession plans for the Board, setting Board remuneration policies and making recommendations to the Board accordingly;

1.2 Providing oversight surrounding Executive Management, people management processes, including specifically appointments, remuneration, performance assessments, succession management and making recommendations to the Board accordingly; and

1.3 Overseeing the effectiveness and integrity of people management policies of the Bank.

## 15. Risk Governance (continued)

### (b) Standing Committees of the Board and Executive Management (continued)

Asset and Liability Committee (Executive Committee)
The role of the Asset and Liability Committee (ALCO) is to:

1.1 Assist Management with its oversight responsibilities with respect to asset and liability management, liquidity and capital management, as well as the management of interest rate and FX market risk;

1.2 Oversee the implementation of an effective process for managing the Bank's FX and interest rate market risk (including pricing and product approval), liquidity risk, and Internal and Regulatory Capital risks relating to the Bank's balance sheet and associated activities, including the adoption from time to time of policies, risk limits and capital levels; and

1.3 Oversee the effective management of processes in relation to the credit risk arising from the Bank's investment and liquidity portfolio.

Management Operational Risk Committee (Executive Committee)
The role of the Management Operational Risk Committee is to:

1.1 Assist Management in providing effective governance over operational and compliance risk management;

1.2 Oversee the implementation of processes for effectively managing operational and compliance risk; and

1.3 Review key risk indicators, associated reporting and other monitoring outputs that determine the effectiveness and adequacy of controls for operational and compliance risks.

Credit Committee (Executive Committee)
The role of the Credit Committee is to:

1.1 Assist management in discharging its oversight responsibilities with respect to credit risk management;

1.2 Oversee the implementation of an effective process for managing credit risk relating to the Bank's retail, agribusiness, commercial and business lending portfolios; and

1.3 Where appropriate, exercise delegated authority to review and approve credit exposures outside of the CEO's delegated authority.

The terms of reference of this committee and its membership is set by the Risk Committee of the Board.

### (c) Areas of risk management

The primary risks arising from the activities of the Bank are credit risk, market risk (mainly interest rate risk and foreign currency risk), liquidity risk, and operational risk.

Credit risk
Credit risk is the potential risk for loss arising from the failure of a debtor or counterparty to meet their contractual obligations to the Bank. Credit risk principally arises within the Bank from its core business of providing lending facilities and comprises both on-balance sheet and off-balance sheet exposures. Details of credit risk management and asset quality are shown in note 16. Credit Risk Management and Asset Quality.

Market risk
Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates and equity prices. Details of market risk management are shown in note 17. Market Risk Management.

Liquidity risk
The Bank defines liquidity risk generally as the inability of the Bank to access the funds that it needs to meet its obligations when they become due. Liquidity can be in the form of cash on hand, securities available for sale, or borrowing arrangements that the Bank can utilise when required.

The Bank's business model gives rise to liquidity risk largely through its role in the maturity transformation between its assets (loans and investments) and its liabilities (deposits and other funding). The Bank acknowledges that it takes on liquidity risk as a core part of its business strategy and that the Bank's shareholder is unlikely to be able to provide additional liquidity support should it be required.

The liquidity risks faced by the Bank can be generally classified into three different types:

- Operational liquidity risk - the risk that the Bank does not have sufficient cash or collateral to make payments to its counterparties and customers as they fall due;
- Structural liquidity risk - the risk associated with longer term liquidity mismatches that might exist within the Bank's balance sheet and which may create an unnecessarily large funding need in the future; and
- Market liquidity risk - the risk that an asset cannot be sold in the market quickly, or if its sale is executed very rapidly, that this can only be achieved at a heavily discounted price.

Details of liquidity and funding risk management are shown in note 18. Liquidity and Funding Risk Management.

## 15. Risk Governance (continued)

### (c) Areas of risk management (continued)

Operational risk
Operational risk is defined as the risk of loss resulting from inadequate or failed processes, human error, system failures or from external events. This includes the risk of failure to comply with laws, regulations, contractual agreements, internal policies and operating processes. The Bank will seek to limit exposure to risk that will impinge on the Bank's ability to operate effectively and efficiently. Operational risk events can result in either direct loss, increased cost, or other indirect loss to the Bank (such as reduced revenue).

The Bank understands that efforts to reduce operational risk to zero could impact on ease of doing business and achieving strategic objectives and will therefore seek to minimise operational risk by either reducing the likelihood of an operational risk event occurring or the impact of the risk event occurring. It does not and cannot reasonably expect to eliminate all instances of operational risk.

The management of operational risk is a challenge due to its broad scope as operational risks arise from all activities conducted across the Bank. To address this challenge the Bank puts in place controls to manage and mitigate operational risks. Management benchmark practices against industry standards and, where appropriate, residual operational risk is transferred by the Bank, through its insurance programme.

The requirements for management of operational risks are equally applicable to all parts of the Bank. The Risk Committee of the Board provides oversight of operational risk management across the Bank. The Risk Committee, as well as the executive management team of the Bank receive quarterly reports on the Bank's operational risk profile and performance against operational risk metrics.

To implement its operational risk management approach, the Bank applies the three lines of accountability model. The first line of accountability is responsible for identifying and managing the inherent operational risks in business activities that they carry out. The second line of accountability is responsible for setting and maintaining policies that reflect the risk appetite set by the Board, monitoring adherence to policies and undertaking assurance activities. The third line of accountability is the co-sourced independent audit function, as well as the external auditors of the Bank.

Detailed policy parameters around operational risk are comprehensively detailed in the Banks suite of operational risk policies and procedures.

### (d) Risk management system review

The Bank operates a continuous cycle of review in relation to its risk management framework and its material risk domains. Policies for material risk domains are scheduled for internal review annually, to ensure that they remain relevant and risk appetite is appropriate for achieving the Banks strategic objectives. In addition, the Bank relies on advice from external third parties in relation to specific areas of managing operational risk, when required, for example when specific knowledge or expertise is not available internally.

### (e) Internal audit

Internal audit's role is to evaluate and suggest improvements to the effectiveness of governance, risk management and control processes and act as the third line of accountability. The internal audit function is co-sourced to PwC. The internal audit function reports directly to the Chairperson of the Audit Committee. In the performance of this role, the internal audit function adopts a risk based approach to selecting areas to undertake an audit. The risk-based approach is underpinned by the Bank's risk assessment matrix. Findings from internal audits are documented in management action plans and the implementation of management action plans is monitored and reported on by the internal audit function. Significant findings and the status of management action plans are reported quarterly to the Audit Committee.

## 16. Credit Risk Management and Asset Quality

### (a) Credit risk management

The Bank seeks to provide credit across its core customer base consisting of the retail, agribusiness, commercial and business sectors. The Bank does not seek to remove risks across this sector, rather it seeks to offer credit to sound customers that have the intent, willingness and ability to repay. Entry into new product or market segments is to be undertaken with caution, piloted as necessary to gain necessary experience and resource before significant growth is undertaken.

The Bank aims to manage its credit exposures by focusing its activities on areas that it is most able to manage and influence, avoiding areas where the Bank has limited experience or knowledge.

Credit risk is managed through a framework that sets out policies and procedures covering the measurement and management of credit risk. There is clear segregation of duties between transaction originators in the business and approvers, apart from structural delegation processes in the retail portfolio. All credit exposure limits are approved within a defined credit approval authority framework and the Bank manages its exposures following the principle of diversification across products, regions, industries, collateral types and client segments.

Credit risk governance is managed through a delegation framework from the Board Risk Committee to the Credit Committee and CEO. The CEO delegates to the Chief Credit Officer (CCO). All have specific roles within the credit function. Regular meetings are undertaken and reports to the CEO, executive management and the Risk Committee are provided to ensure that risks arising from credit activities are within parameters set by the Board through the Risk Committee.

Overarching credit risk policies are approved by the Board and are consistent with the overall and specific Risk Appetite Statement (RAS) associated with the individual areas of credit risk. The principles of credit delegation are outlined in the credit policies and the Credit Committee is responsible for the oversight of these delegations, their performance, and overall portfolio performance.

Risk measurement plays a key role, along with judgement and experience, in informing risk taking and portfolio management decisions. A standard application credit scoring system is used to support and inform retail credit decisions. The Bank refers to external consumer scores from credit bureaus where these are available, but are not the only input used to determine retail risk grades. Lower grades are indicative of a higher probability of default. Risk grades are also assigned to non-performing and default loans as well as loans that have been restructured.

Agribusiness, commercial and business bank loans are also risk graded at initiation using standardised models, experience and data provided on application. These grades are updated at least annually for material exposures through an annual review process, which is independently reviewed by the second line credit risk function.

Credit risk is managed through the use of trained, competent lenders, structured approval processes considering the character, capacity, capability, collateral and condition applicable to the borrower; validation of this information; hindsight reviews; and portfolio and exposure performance management. Non-standard, non-retail lending activities are undertaken by specialist units within the Bank to ensure that the Bank's exposures are appropriately managed.

Loans which are showing signs of distress are managed by the Credit Solutions management function, which is responsible for taking action to minimise losses in the event of default or to realise securities where appropriate. All defaults are reported to credit bureaus via the bank's recoveries partners.

Wholesale counterparty credit arrangements in respect of the Bank's investment and liquidity portfolio are managed through an approved counterparty approach, derived from Board policy and delegations. This allows maximum limits in respect of credit risk associated with the counterparty relating to the credit rating of the counterparty, the type of instrument that has been issued by the counterparty, and the maturity profile of the counterparty.

Major credit exposures to individual counterparties, groups, connected persons, and portfolios of retail exposures are reviewed and approved by the Credit Committee.

All other credit approval authorities are delegated through the Risk Committee of the Board to the CEO who delegates to the Chief Credit Officer (CCO). The CCO has the ability to delegate further to individuals based upon their proven competence and experience, and the size and characteristics of the loan. Delegations are managed through a delegation framework and all decisions made through the delegation process are subject to independent hindsight review.

Credit concentration risk is managed through counterparty or group limits, industry limits (where appropriate), product limits, collateral type limits and regional exposure limits. Credit risk is further mitigated through the use of tools such as collateral, credit insurance and guarantees. The reliance that can be placed on such mitigating factors is assessed in the light of legal certainty and enforceability, market valuation, correlation and counterparty risk of the credit insurance provider. However, the existence of credit mitigations do not substitute for the ability of the borrower to pay, which is the primary consideration of any lending decision.

All credit risk is denominated in New Zealand dollars, and for non-wholesale credit exposure, is based in New Zealand.

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (b) Credit risk assessment and measurement

Credit risk is the risk that a customer or counterparty will default on its contractual obligations resulting in financial losses to the Bank.

The Bank is exposed to credit risks arising from the following groups of financial assets that are subject to impairment requirements of NZ IFRS 9.

| | | Estimated gross carrying amount | |
|---|---|---|---|
| **Types of financial assets** | **Measured at** | **2020** | **2019** |
| Cash and cash equivalent | amortised cost | 232,588 | 149,065 |
| Investment securities | FVOCI | 1,741,504 | 1,827,810 |
| Loans and advances to customers | amortised cost | 6,126,597 | 5,792,049 |
| Other assets | amortised cost | 2,440 | 2,201 |

The Bank has assessed the impairment requirements for cash and cash equivalents, investment securities and other assets. However, the identified impairment loss for the groups of assets was immaterial.

**Investment securities carried at FVOCI**
The Bank has reviewed its holdings of investment securities in terms of its counterparty credit policy and based on this review, and other information on hand, does not believe there is any evidence to indicate material impairment in this portfolio. The collective provision against this portfolio is assessed at each reporting date and whenever there is a significant change in the portfolio mix or change in the macro-economic factors and credit ratings. Furthermore, no specific provisions are being held against possible non-performance by any investment in this portfolio.

**Financial assets at fair value through profit or loss**
Financial assets at fair value through profit or loss are not assessed for impairment as their fair value reflects the credit quality of the instrument and changes in fair value are recognised in other income.

**Loans and advances to customers carried at amortised cost**
The majority of the Bank's provisions for impairment for lending assets are made on a collective basis. The credit quality of loans and advances to customers are continuously monitored since initial recognition and those that are neither past due or impaired can be assessed by reference to the Bank's internal credit risk rating system. At the origination of loans and advances to customers, loans are risk graded based on a number of characteristics that indicate Probability of Default (PD) and/or Loss Given Default (LGD). These risk grades are reviewed periodically for adverse changes during the life of the loan. Credit impairment allowance for loans and advances to customers carried at amortised cost are deducted from the gross carrying amount of the assets and impairment losses are presented as credit impairment losses in the statement of profit and loss.

## 16. Credit Risk Management and Asset Quality (continued)

### (c) Expected credit loss measurement

The Bank applies a three-stage model in accordance with NZ IFRS 9 to measures credit risk of a portfolio of assets using its internal credit risk model whose key inputs are probability of default (PD), loss given default (LGD), and exposure at default (ED). This is supplemented with forward-looking information on macroeconomic factors (refer to section C.4 below for further information).

The following diagram summarises the impairment requirements under NZ IFRS 9:

**Change in credit quality since initial recognition**

| Stage 1<br>12 month ECL | Stage 2<br>Lifetime ECL | Stage 3<br>Lifetime ECL |
|---|---|---|
| Initial recognition | Significant increase in credit risk since initial recognition | Credit impaired assets |

- 12 month ECL (Stage 1): applies to all items resulting from possible default events within 12 months after reporting date.
- Lifetime ECL (Stage 2 and 3): represents the ECL that result from all possible default events over the expected life of a financial instrument. If a financial instrument experiences a significant increase in credit risk since initial recognition then is moved to Stage 2 but is not yet deemed to be credit-impaired. When objective evidence of credit-impairment emerges with one or more events that have a detrimental impact on the estimated future cash flows of the financial assets then the asset is moved to Stage 3.

The change in the credit quality of a financial asset results in movements between the three stages.

The key judgments and assumptions adopted by the Bank in addressing the requirements of the standard are discussed below:

C.1. Significant increase in credit risk (SICR)
The Bank considers that a loan or advance to customers to have experienced a significant increase in credit risk when one or more of the quantitative, qualitative or backstop criteria have been met:

**Quantitative and qualitative criteria:**
Over the term of the loans and advances to customers, the Bank accounts for its credit risk by appropriately providing for ECL on a timely basis. In calculating the expected credit loss rates, the Bank considers historical loss rates for each category of customers that share similar risk characteristics, and adjusts for forward looking macroeconomic data. The Bank provides for credit losses against loans and advances to customers on both an individual and collective basis as follows:

| Category | Basis | Description and quantitative criteria for SICR | Recognition of interest revenue |
|---|---|---|---|
| **Stage 1<br>12 month ECL** | Collective | Customers with a low risk of default that have a strong capacity to meet contractual cash flows (interest and/or principal repayments). | Effective interest rate applied to the gross carrying amount |
| **Stage 2<br>Lifetime ECL** | Collective | Significant increase in credit risk is presumed if the loans and advances are more than 30 days past due in making a contractual payment or when there is reasonable and/or supportable information that there is an increase in the risk of a default occurring on the asset as at the reporting date. | Effective interest rate applied to the gross carrying amount |
| **Stage 3<br>Lifetime ECL** | Collective | Loans and advances are deemed credit impaired when they are over 90 days past due in making a contractual payment and/or when there is objective evidence of the events that indicate the borrower is in significant financial difficulty. | Effective interest rate applied to the amortised cost (net of collective provision)* |
| | Specific (Individual) | Loans and advances are deemed 'impaired' when the Bank has exhausted all options to rehabilitate a mortgage debt and/or expects to incur a loss. Impaired assets are specifically provided for on an individual basis. | Effective interest rate applied to the amortised cost (net of specific provision)* |
| **Write-off** | | Financial assets are written off when there is no reasonable expectation of recovery and customers fail to engage in a repayment plan with the Bank. Those financial assets that are written-off are still subject to enforcement activity. | None |

* When a financial asset becomes credit-impaired, the Bank calculates interest income by applying the effective interest rate to the net amortised cost of the financial asset. The Bank reverts to calculating interest income on a gross basis if the credit risk of the financial asset improves and deemed no longer credit-impaired.

## 16. Credit Risk Management and Asset Quality (continued)

### (c) Expected credit loss measurement (continued)

A significant increase in credit risk is also considered when the borrower meets one or more of the following criteria:
- In short-term forbearance
- Direct debit cancellation
- Extension of the terms granted
- Arrears within the last 12 months

Additionally, for the Commercial and Agricultural portfolios, a significant increase in credit risk is also considered if the borrower is under watch and/or the instrument meets one or more of the following criteria:
- Significant adverse changes in business, financial and/or economic conditions in which the borrower operates.
- Early signs of cashflow/liquidity problems such as delay in servicing of trade creditors/loans.

The assessment of SICR incorporates forward-looking information (refer to section C.4 below for further information) and is performed on a monthly basis at a portfolio level for all loans and receivables to customers held by the Bank.

**Backstop**
A backstop is applied and the financial instrument considered to have a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payment.

The Bank has not used the low credit risk exemption for any financial instrument in the year ended 31 March 2020.

C.2. Definition of default and credit-impaired assets
The Bank has defined a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

**Quantitative and qualitative criteria:**
- The borrowers are over 90 days past due in making a contractual payment
- There is objective evidence of the events that indicate the borrower is in significant financial difficulty
- The borrower is in long-term forbearance
- The borrower is insolvent
- The borrower is in breach of financial covenant(s)
- Concessions have been made by the lender relating to the borrower's financial difficulty
- It is becoming probable that the borrower will enter bankruptcy

The 90 days past due default definition used for the loans and advances to customers is consistent with the past due presumption under NZ IFRS 9 for the mortgage portfolio. However, this definition differs from that applied for impaired assets used for regulatory purposes as disclosed in section (h) Asset quality information. The adoption of this presumption will be monitored and reviewed by the Credit Risk department on an annual basis to ensure it remains appropriate.

An instrument ceases to be in default when it no longer exhibits arrears for a minimum period of four months.

C.3. Measuring ECL - Explanation of inputs, assumptions and estimation techniques
The ECL is measured on either a 12-month (12M) or lifetime basis depending on whether a significant increase in credit risk has occurred since the initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (ED) and Loss Given Default (LGD), defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation (as per "Definition of default and credit-impaired" above).
- ED is based on the amounts the Bank expects to be owed at the time of default, over the next 12 months (12M ED) or over the remaining lifetime (Lifetime ED).
- LGD represents the Bank's expectation of the extent of loss on a defaulted exposure. LGD is expressed as a percentage of loss per unit of exposure (ED). LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

The ECL is determined by projecting the PD, LGD and ED for each future period. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure was not prepaid or defaulted in an earlier period). This effectively calculates an ECL for each future period, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

## 16. Credit Risk Management and Asset Quality (continued)

### (c) Expected credit loss measurement (continued)

C.3. Measuring ECL - Explanation of inputs, assumptions and estimation techniques (continued)

The PD is developed by performing a linear regression based on the 12 months prior performance of the loans classified as impaired or 90 days or more in arrears. The regression is based on historical observed data and is performed separately for each product type. The Bank has used internal arrears information to regress against a list of macroeconomic factors to determine the PD. The following is the list of factors that have been considered during the analysis: gross domestic product, unemployment rate, dairy price, residential investment, 90-day interest rate, household debt and consumer price index.

The ED is primarily derived from the available balances at reporting date.

The LGD is determined using historical losses by observing the actual write-offs that have occurred over the past few years. For the unsecured portfolio, the Bank has decided to use a 100% LGD which aligns to their expectation of recoverability in the event of a default event.

The maximum period considered when estimating ECLs has been determined as the maximum between 4 years and the remaining contractual life. The ECL is probability-weighted and is discounted at the effective interest rate. The Bank has considered its historical loss experience for the last 3 years.

The following assumptions have been introduced in the ECL computation during the period:
- cooling-off period: the determination of the days in arrears has been modified to mitigate the volatility of the transfers between the different impairment stages.
- portfolio factors: whilst determining the PD, additional scalars have been incorporated, based on portfolio segmentation.

In instances where forward looking statistical analysis of TSB's portfolio and performance data produced ECL provisioning numbers that TSB management considers to be sufficient, model floors for ECL model factors based on industry publications were used.

C.4. Forward-looking information incorporated in the ECL models

The calculation of ECL incorporates forward-looking information. The Bank has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio. The forward-looking information includes macroeconomic factors such as forecast gross domestic product (GDP), interest rate and unemployment rate in measuring the provisions for expected credit losses (ECL) on groups of financial assets that share similar credit risk characteristics.

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political change, have also been considered, but are not deemed to have a material impact and therefore no adjustment has been made to the ECL for such factors.

**Significant estimates and judgements**
The provision for impairment are based on assumptions about risk of default and expected loss rates. The Bank uses judgement in making these assumptions and selecting the inputs to the calculation of impairment, based on the Bank's past history, existing market conditions and forward-looking estimates at each reporting date.

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (d) Credit risk exposure

D.1. Maximum exposure to credit risk - Financial instruments subject to impairment

The following table contains an analysis of the credit exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount and related lending commitments (refer to note 16.(i)) of the financial assets best represent the Bank's maximum exposure to credit risk on these assets.

| As at 31 March 2020 | Stage 1 12 month ECL | Stage 2 Lifetime ECL | Stage 3 Lifetime ECL | Specific Lifetime ECL | Total |
|---|---|---|---|---|---|
| Residential mortgage loans (gross) | 4,687,969 | 517,629 | 1,337 | 15,630 | **5,222,565** |
| Residential mortgage loans (net of provision) | 4,678,653 | 512,070 | 1,094 | 14,348 | **5,206,165** |
| Expected credit loss rate | 0.2% | 1.1% | 18.2% | 8.2% | 0.3% |
| Commercial mortgage loans (gross) | 352,730 | 193,921 | - | 12,014 | **558,665** |
| Commercial mortgage loans (net of provision) | 348,127 | 183,550 | - | 3,796 | **535,473** |
| Expected credit loss rate | 1.3% | 5.3% | 0.0% | 68.4% | 4.2% |
| Agricultural exposures (gross) | 290,651 | 35,991 | - | 4,396 | **331,038** |
| Agricultural exposures (net of provision) | 287,369 | 34,757 | - | 4,273 | **326,399** |
| Expected credit loss rate | 1.1% | 3.4% | 0.0% | 2.8% | 1.4% |
| Other exposures (gross) | 57,775 | 3,449 | 834 | - | **62,058** |
| Other (net of provision) | 55,474 | 3,033 | 53 | - | **58,560** |
| Expected credit loss rate | 4.0% | 12.1% | 93.6% | 0.0% | 5.6% |
| Cash and cash equivalent | 232,588 | - | - | - | **232,588** |
| Investment securities (gross) | 1,741,504 | - | - | - | **1,741,504** |
| Other assets | 2,440 | - | - | - | **2,440** |
| Expected credit loss rate | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |

| As at 31 March 2019 | Stage 1 12 month ECL | Stage 2 Lifetime ECL | Stage 3 Lifetime ECL | Specific Lifetime ECL | Total |
|---|---|---|---|---|---|
| Residential mortgage loans (gross) | 4,812,019 | 24,757 | 7,194 | 483 | **4,844,453** |
| Residential mortgage loans (net of provision) | 4,804,768 | 24,635 | 4,053 | 178 | **4,833,634** |
| Expected credit loss rate | 0.2% | 0.5% | 43.7% | 63.1% | 0.2% |
| Commercial mortgage loans (gross) | 551,680 | 12,682 | - | - | **564,362** |
| Commercial mortgage loans (net of provision) | 548,003 | 12,399 | - | - | **560,402** |
| Expected credit loss rate | 0.7% | 2.2% | 0.0% | 0.0% | 0.7% |
| Agricultural exposures (gross) | 275,884 | 38,066 | - | 3,331 | **317,281** |
| Agricultural exposures (net of provision) | 272,727 | 36,778 | - | 3,231 | **312,736** |
| Expected credit loss rate | 1.1% | 3.4% | 0.0% | 3.0% | 1.4% |
| Other exposures (gross) | 90,871 | 2,324 | 1,357 | - | **94,552** |
| Other (net of provision) | 83,881 | 1,727 | (331) | - | **85,277** |
| Expected credit loss rate | 7.7% | 25.7% | 124.4% | 0.0% | 9.8% |
| Cash and cash equivalent | 149,065 | - | - | - | **149,065** |
| Investment securities (gross) | 1,827,810 | - | - | - | **1,827,810** |
| Other assets | 2,201 | - | - | - | **2,201** |
| Expected credit loss rate | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (d) Credit risk exposure

D.2. Maximum exposure to credit risk - Financial instruments not subject to impairment

The following table contains an analysis of the maximum credit risk exposure from financial assets not subject to impairment (i.e. hedging instrument):

| Maximum exposure to risk | 2020 | 2019 |
|---|---|---|
| Derivative financial instruments | 13,942,260 | 6,518,930 |

D.3 Collateral and other credit enhancements
The Bank employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Bank has internal policies on the acceptability of specific classes of collateral or credit risk mitigation.

The Bank's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Bank since the prior period.

The Bank closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Bank will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

| Credit-impaired assets - 31 March 2020 | Gross exposure | Impairment allowance | Carrying amount | Fair value of collateral held |
|---|---|---|---|---|
| Residential mortgage loans | 16,967 | 1,525 | 15,442 | **28,338** |
| Commercial | 12,014 | 8,218 | 3,796 | **13,537** |
| Agricultural | 4,396 | 123 | 4,273 | **5,969** |
| Other | 834 | 781 | 53 | **265** |
| **Total credit-impaired assets** | **34,211** | **10,647** | **23,564** | **48,109** |

| Credit-impaired assets - 31 March 2019 | Gross exposure | Impairment allowance | Carrying amount | Fair value of collateral held |
|---|---|---|---|---|
| Residential mortgage loans | 7,677 | 3,446 | 4,231 | **17,405** |
| Commercial | - | - | - | **-** |
| Agricultural | 3,331 | 100 | 3,231 | **4,000** |
| Other | 1,357 | 1,688 | (331) | **-** |
| **Total credit-impaired assets** | **12,365** | **5,234** | **7,131** | **21,405** |

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (e) Loss allowance

The following table provides a reconciliation from the opening balance to the closing balance of provision for impairment and show movement between stages during the reporting period.

| 31 March 2020<br>Movements for credit impairment allowances | Stage 1 Collective provision<br>12 month ECL | Stage 2 Collective provision<br>Lifetime ECL | Stage 3 Collective provision<br>Lifetime ECL | Stage 3 Specific provision<br>Lifetime ECL | Total provision |
|---|---|---|---|---|---|
| **Residential mortgage loans** | | | | | |
| Opening balance | 7,251 | 122 | 3,141 | 305 | 10,819 |
| Transfers with no impact on profit or loss: | | | | | |
| Transferred to Stage 1 | 27 | (27) | - | - | - |
| Transferred to Stage 2 | (559) | 1,169 | (610) | - | - |
| Transferred to Stage 3 | (1) | (2) | 3 | - | - |
| Charged / (credited) to profit or loss | 2,591 | 4,297 | (2,291) | 966 | 5,563 |
| Amounts written off | 7 | - | - | 11 | 18 |
| Recovery | - | - | - | - | - |
| **Closing provision balance for residential mortgage loans** | **9,316** | **5,559** | **243** | **1,282** | **16,400** |
| **Commercial exposures** | | | | | |
| Opening balance | 3,677 | 283 | - | - | 3,960 |
| Transfers with no impact on profit or loss: | | | | | |
| Transferred to Stage 1 | 15 | (15) | - | - | - |
| Transferred to Stage 2 | (684) | 684 | - | - | - |
| Transferred to Stage 3 | - | - | - | - | - |
| Charged / (credited) to profit or loss | 1,595 | 9,419 | - | 8,218 | 19,232 |
| Amounts written off | - | - | - | - | - |
| Recovery | - | - | - | - | - |
| **Closing provision balance for commercial exposures** | **4,603** | **10,371** | **-** | **8,218** | **23,192** |
| **Agricultural exposures** | | | | | |
| Opening balance | 3,157 | 1,288 | - | 100 | 4,545 |
| Transfers with no impact on profit or loss: | | | | | |
| Transferred to Stage 1 | - | - | - | - | - |
| Transferred to Stage 2 | (114) | 114 | - | - | - |
| Transferred to Stage 3 | (2) | - | 2 | - | - |
| Charged / (credited) to profit or loss | 241 | (168) | (2) | 23 | 94 |
| Amounts written off | - | - | - | - | - |
| Recovery | - | - | - | - | - |
| **Closing provision balance for agricultural exposures** | **3,282** | **1,234** | **-** | **123** | **4,639** |
| **Other exposures** | | | | | |
| Opening balance | 6,990 | 597 | 1,688 | - | 9,275 |
| Transfers with no impact on profit or loss: | | | | | |
| Transferred to Stage 1 | 2 | (2) | - | - | - |
| Transferred to Stage 2 | (31) | 31 | - | - | - |
| Transferred to Stage 3 | (2) | - | 2 | - | - |
| Charged / (credited) to profit or loss | (4,846) | (215) | (920) | - | (5,981) |
| Amounts written off | 188 | 5 | 11 | - | 204 |
| Recovery | - | - | - | - | - |
| **Closing provision balance for other exposures** | **2,301** | **416** | **781** | **-** | **3,498** |
| **Total provision** | **19,502** | **17,580** | **1,024** | **9,623** | **47,729** |

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (e) Loss allowance (continued)

| 31 March 2019<br>Movements for credit impairment allowances | Collective provision | Stage 1 Collective provision 12 month ECL | Stage 2 Collective provision Lifetime ECL | Stage 3 Collective provision Lifetime ECL | Stage 3 Specific provision Lifetime ECL | Total provision |
|---|---|---|---|---|---|---|
| **Residential mortgage loans** | | | | | | |
| Opening balance | 19,570 | - | - | - | 205 | 19,775 |
| Restated for adoption of NZ IFRS 9 | (19,570) | 4,581 | 101 | 2,141 | - | (12,747) |
| Transfers with no impact on profit or loss: | | | | | | |
| Transferred to Stage 1 | - | 523 | (26) | (497) | - | - |
| Transferred to Stage 2 | - | (15) | 15 | - | - | - |
| Transferred to Stage 3 | - | (4) | (3) | 7 | - | - |
| Charged / (credited) to profit or loss | - | 2,166 | 35 | 1,490 | - | 3,691 |
| Amounts written off | - | - | - | - | 101 | 101 |
| Recovery | - | - | - | - | (1) | (1) |
| **Closing provision balance for residential mortgage loans** | **-** | **7,251** | **122** | **3,141** | **305** | **10,819** |
| **Commercial exposures** | | | | | | |
| Opening balance | 2,995 | - | - | - | - | 2,995 |
| Restated for adoption of NZ IFRS 9 | (2,995) | 3,468 | 234 | 3,897 | - | 4,604 |
| Transfers with no impact on profit or loss: | | | | | | |
| Transferred to Stage 1 | - | 3,238 | (47) | (3,191) | - | - |
| Transferred to Stage 2 | - | (41) | 41 | - | - | - |
| Transferred to Stage 3 | - | - | - | - | - | - |
| Charged / (credited) to profit or loss | - | (2,988) | 55 | (706) | - | (3,639) |
| Amounts written off | - | - | - | - | - | - |
| Recovery | - | - | - | - | - | - |
| **Closing provision balance for commercial exposures** | **-** | **3,677** | **283** | **-** | **-** | **3,960** |
| **Agricultural exposures** | | | | | | |
| Opening balance | 1,847 | - | - | - | 100 | 1,947 |
| Restated for adoption of NZ IFRS 9 | (1,847) | 3,092 | 1,832 | - | - | 3,077 |
| Transfers with no impact on profit or loss: | | | | | | |
| Transferred to Stage 1 | - | 38 | (38) | - | - | - |
| Transferred to Stage 2 | - | (20) | 20 | - | - | - |
| Transferred to Stage 3 | - | - | - | - | - | - |
| Charged / (credited) to profit or loss | - | 47 | (526) | - | - | (479) |
| Amounts written off | - | - | - | - | - | - |
| Recovery | - | - | - | - | - | - |
| **Closing provision balance for agricultural exposures** | **-** | **3,157** | **1,288** | **-** | **100** | **4,545** |
| **Other exposures** | | | | | | |
| Opening balance | 340 | - | - | - | - | 340 |
| Restated for adoption of NZ IFRS 9 | (340) | 5,173 | 4 | 1,222 | - | 6,059 |
| Transfers with no impact on profit or loss: | | | | | | |
| Transferred to Stage 1 | - | 1 | (1) | - | - | - |
| Transferred to Stage 2 | - | (190) | 190 | - | - | - |
| Transferred to Stage 3 | - | - | - | - | - | - |
| Charged / (credited) to profit or loss | - | 2,006 | 404 | 466 | - | 2,876 |
| Amounts written off | - | - | - | - | - | - |
| Recovery | - | - | - | - | - | - |
| **Closing provision balance for other exposures** | **-** | **6,990** | **597** | **1,688** | **-** | **9,275** |
| **Total provision** | | **21,075** | **2,290** | **4,829** | **405** | **28,599** |

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (e) Loss allowance (continued)

The following explains how significant changes in the gross carrying amount of financial assets during the year have contributed to the changes in the provision for credit impairment. Provision for credit impairment reflects Expected Credit Losses (ECL) measured using the three-stage approach under NZ IFRS 9.

The overall increase in the provision for credit impairment for the year was $19.13m. The two main drivers of this increase were lending book growth and an increase in provisions due to deterioration of the anticipated macro and micro economic prospects of TSB's customers associated with the COVID-19 related economic downturn. The increase includes a $5.55m increase in provision for loans in the residential lending portfolio and $19.23m provision in the Commercial portfolio, partially offset by a $5.75m provision decrease in the Personal lending portfolio as TSB exited the riskier exposure of this customer segment. Agri portfolio provisions are largely unchanged year on year.

Updated management assumptions that reflect the changing nature of the underlying portfolio and their relationship to external factors also impacted the total value of provisions held across the entire lending book.

Detailed information regarding the changes are as follows:

- Collective Provision 12 month ECL (Stage 1) decreased by $1.57m due to the balance transfer to Lifetime ECL provision stage for industries impacted by COVID-19 which, in management's view experienced a structural shift in economic prospects. The impact of the transfer was partially offset by lending book growth during the year.
- Collective Provision Lifetime ECL not credit impaired (Stage 2) increased by $15.29m. This was primarily due to a $10.07m collective provision increase in the Commercial portfolio, driven by a transfer of loan balances from Stage 1 as a result of COVID-19 impacted industries being deemed to have experienced a significant increase in Credit Risk, and a $5.44m collective provision increase in the Residential Lending portfolio also driven by COVID-19 related industry restaging. This was offset by a $0.18m release of Stage 2 provisions across Personal segments.
- Collective Provision Lifetime ECL credit impaired (Stage 3) decreased by $3.81m, driven by a decrease in loan balances of this stage of $6.38m.
- Specific provision lifetime ECL credit impairment increased by $9.22m driven by an increase in balances of $28.23m and a change in the quality of collateral for accounts that are individually assessed for specific provision purposes.

Refer to Note 1 (j) for information on ECL sensitivity analysis.

Note: Personal lending includes both Personal and Harmoney segments.

### (f) Movement in balances of credit impairment allowances

| As at 31 March 2020 | Residential mortgage loans | Commercial exposures | Agricultural exposures | Other exposures | Total Credit exposures |
|---|---|---|---|---|---|
| **Specific provision for impairment** | | | | | |
| Balance at beginning of period | 305 | - | 100 | - | 405 |
| Add new provisions | 988 | 8,218 | 23 | - | 9,229 |
| Current year amounts written off | (11) | - | - | - | (11) |
| Reversal of previously recognised provision | - | - | - | - | - |
| **Specific provision balance at end of period** | **1,282** | **8,218** | **123** | **-** | **9,623** |
| **Collective provision for impairment** | | | | | |
| Balance at beginning of period | 10,514 | 3,960 | 4,445 | 9,275 | 28,194 |
| Recognised in profit or loss | 4,604 | 11,014 | 71 | (5,777) | 9,912 |
| **Collective provision balance at end of period** | **15,118** | **14,974** | **4,516** | **3,498** | **38,106** |
| **Total provision for impairment loss** | **16,400** | **23,192** | **4,639** | **3,498** | **47,729** |

The Bank's total provision for credit impairment was $47.7m (2019: $28.6m) at balance date representing 0.77% (2019: 0.49%) of the total loans and advances to customers.

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (f) Movement in balances of credit impairment allowances (continued)

| As at 31 March 2019 | Residential mortgage loans | Commercial exposures | Agricultural exposure | Other exposures | Total credit exposures |
|---|---|---|---|---|---|
| **Specific provision for impairment** | | | | | |
| Balance at beginning of period | 205 | - | 100 | - | 305 |
| Add new provisions | 322 | - | - | - | 322 |
| Current year amounts written off | (221) | - | - | - | (221) |
| Reversal of previously recognised provision | (1) | - | - | - | (1) |
| **Balance of specific provision at end of period** | **305** | **-** | **100** | **-** | **405** |
| **Collective provision for impairment** | | | | | |
| Balance at beginning of period | 19,570 | 2,995 | 1,847 | 340 | 24,752 |
| Balance adjusted for adoption on NZ IFRS 9 | (12,747) | 4,604 | 3,077 | 6,059 | 993 |
| Recognised in profit or loss | 3,691 | (3,639) | (479) | 2,876 | 2,449 |
| **Collective provision balance at end of period** | **10,514** | **3,960** | **4,445** | **9,275** | **28,194** |
| **Total provision for impairment loss** | **10,819** | **3,960** | **4,545** | **9,275** | **28,599** |

| Impairment losses recognised in profit or loss | 2020 | 2019 |
|---|---|---|
| Individual impairment expenses | 1,232 | 1,687 |
| Movement in specific provision | 9,218 | 100 |
| Movement in collective provision | 9,912 | 2,449 |
| **Impairment losses – loans and advances** | **20,362** | **4,236** |

The estimated fair value of collateral and other charges related to financial assets that are individually impaired (specific loans stage 3 lifetime ECL) is $8.341m (2019: $4.018m).

### (g) Lending commitments and guarantees

For loan commitments and financial guarantee contracts, the loss allowance is recognised as a provision. The Bank however cannot separately identify the ECL on the undrawn commitment component from those on the loan component and thus they are recognised together with the loss allowance for the loan.

### (h) Asset quality information

The Bank has disclosed certain components of its loan portfolio as impaired assets according to the classifications below:

Impaired assets
The impaired assets consist of restructured assets, assets acquired through the enforcement of security and other individually impaired assets.

A restructured asset is any credit exposure for which:
(a) The original terms have been changed to grant the counterparty a concession that would not otherwise have been available, due to the counterparty's difficulties in complying with the original terms;
(b) The revised terms of the facility are not comparable with the terms of new facilities with comparable risks; and
(c) The yield on the asset following restructuring is equal to, or greater than, the Bank's average cost of funds, or a loss is not otherwise expected to be incurred.

Assets acquired through the enforcement of security are where the Bank assumes ownership of an asset (primarily real estate) in settlement of all or part of the debt. Other individually impaired assets means any credit exposures for which an impairment loss is required to be recognised in accordance with NZ IFRS 9.

Past due asset
A past due asset is any credit exposure where a counterparty has failed to make payment when contractually due, and which is not a restructured asset, other individually impaired asset, or a financial asset acquired through the enforcement of security. A 90-day past due asset is a financial asset which has not been operated by the counterparty within its contractual payment terms for at least 90 days and which is not a restructured asset, other individually impaired asset, or a financial asset acquired through the enforcement of security.

Asset under administration
An asset under administration is any credit exposure which is not an individually impaired asset or a past due asset but which is to a counterparty:
(a) who is in receivership, liquidation, bankruptcy, statutory management or any form of administration in New Zealand; or
(b) who is in any other equivalent form of voluntary or involuntary administration in an overseas jurisdiction.

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (h) Asset quality information (continued)

The majority of the Bank's provisions for impairment are made on a collective basis. The table below shows the credit quality information for loans and advances to customers.

| As at 31 March 2020 | Note | Residential mortgage loans | Commercial exposures | Agricultural exposures | Other exposures | Total credit exposures |
|---|---|---|---|---|---|---|
| **Neither past due or impaired** | | **5,137,821** | **554,281** | **324,638** | **60,005** | **6,076,745** |
| **Past due assets not impaired:** | | | | | | |
| Less than 30 days | | 62,876 | 1,591 | 2,003 | 1,401 | 67,871 |
| 30 to 59 days | | 7,328 | 53 | - | 1,461 | 8,842 |
| 60 to 89 days | | 1,177 | - | - | 426 | 1,603 |
| 90 days and over | | 801 | - | - | 827 | 1,628 |
| **Balance of past due but not impaired assets at end of period** | | **72,182** | **1,644** | **2,003** | **4,115** | **79,944** |
| **Movements in individually impaired assets:** | | | | | | |
| Balance at beginning of period | | 482 | - | 3,332 | - | 3,814 |
| Additions | | 15,510 | 678 | 1,137 | - | 17,325 |
| Amounts written off / loans closed out | | (11) | - | - | - | (11) |
| Transfer back to loans and advances to customers | | (3,419) | - | (72) | - | (3,491) |
| **Balance of impaired assets at end of period** | | **12,562** | **678** | **4,397** | **-** | **17,637** |
| **Total gross loans and advances to customers** | 7 | **5,222,565** | **556,603** | **331,038** | **64,120** | **6,174,326** |
| **Less provision for impairment** | 16.(f) | 16,400 | 23,192 | 4,639 | 3,498 | 47,729 |
| **Total loans and advances to customers** | | **5,206,165** | **533,411** | **326,399** | **60,622** | **6,126,597** |

| As at 31 March 2019 | Note | Residential mortgage loans | Commercial exposures | Agricultural exposures | Other exposures | Total credit exposures |
|---|---|---|---|---|---|---|
| **Neither past due or impaired** | | **4,768,631** | **558,896** | **311,393** | **90,737** | **5,729,657** |
| **Past due assets not impaired:** | | | | | | |
| Less than 30 days | | 58,334 | 3,084 | 1,456 | 2,557 | 65,431 |
| 30 to 59 days | | 10,385 | - | 1,100 | 1,835 | 13,320 |
| 60 to 89 days | | 1,660 | - | - | 448 | 2,108 |
| 90 days and over | | 4,961 | - | - | 1,357 | 6,318 |
| **Balance of past due but not impaired assets at end of period** | | **75,340** | **3,084** | **2,556** | **6,197** | **87,177** |
| **Movements in individually impaired assets:** | | | | | | |
| Balance at beginning of period | | 968 | - | 3,432 | - | 4,400 |
| Additions | | 487 | - | - | - | 487 |
| Amounts written off / loans closed out | | (129) | - | - | - | (129) |
| Transfer back to loans and advances to customers | | (844) | - | (100) | - | (944) |
| **Balance of impaired assets at end of period** | | **482** | **-** | **3,332** | **-** | **3,814** |
| **Total gross loans and advances to customers** | 7 | **4,844,453** | **561,980** | **317,281** | **96,934** | **5,820,648** |
| **Less provision for impairment** | 16.(f) | 10,819 | 3,960 | 4,545 | 9,275 | 28,599 |
| **Total loans and advances to customers** | | **4,833,634** | **558,020** | **312,736** | **87,659** | **5,792,049** |

**Undrawn balances on lending commitments to counterparties**
Undrawn balances on lending commitments to counterparties for whom drawn balances are classified as individually impaired total $82k at reporting date (2019: $1k).

**Restructured asset**
At 31 March 2020, the Bank had lending restructured assets totalling $1,622k (2019: $532k). Interest foregone on lending restructured assets throughout the year was nil (2019: $nil).

**Other assets under administration**
The Bank does not have any assets under administration (2019: $nil).
There was an asset of $166k acquired through the enforcement of security at reporting date ($2019: $nil).

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (i) Concentrations of credit exposures

Concentrations of credit exposures arise where the Bank is exposed to risk in activities or industries of a similar nature.

Credit exposure is calculated on the basis of selected items on and off-balance sheet. The exposures shown below are based on net carrying amounts as reported in the statement of financial position without taking account of any collateral held. Off-balance sheet exposures include undrawn lending commitments. Refer to note 21. Commitments and Contingent Liabilities for more information on commitments.

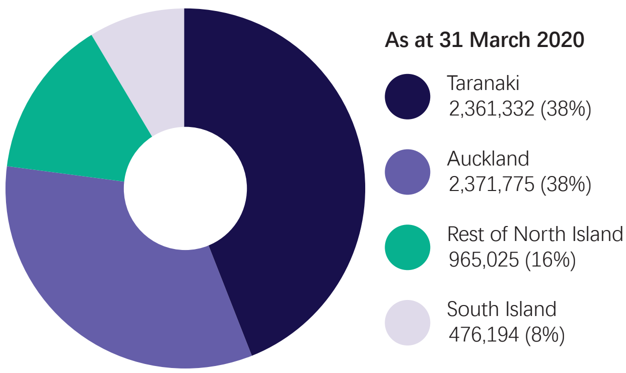
| (i) On and off-balance sheet | Note | 2020 | 2019 |
|---|---|---|---|
| On balance sheet: | | | |
| Cash and cash equivalents | | 232,588 | 149,065 |
| Investment securities | 8 | 1,741,504 | 1,827,810 |
| Loans and advances to customers | 7 | 6,126,597 | 5,792,049 |
| Off balance sheet: | | | |
| Lending commitments | 21 | 764,042 | 748,759 |
| **Total Credit Exposures** | | **8,864,731** | **8,517,683** |

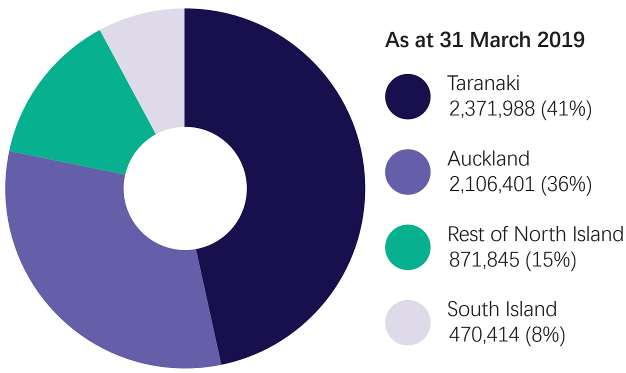
Australian and New Zealand Standard Industrial Classification ("ANZSIC") codes have been used as the basis for disclosing customer industry sectors. An analysis of financial assets by geographic region and industry sector as at balance date is as follows:

### (ii) Concentration of credit exposure by geographic region

| As at 31 March 2020 | Note | Cash and cash equivalent | Investment securities | Loans and advances to customers | Off-balance sheet | Total credit exposures |
|---|---|---|---|---|---|---|
| New Zealand total | | 232,588 | 1,216,694 | 6,174,326 | 764,042 | 8,387,650 |
| Outside New Zealand | | - | 524,810 | - | - | 524,810 |
| Provision for impairment | 16.(f) | - | - | (47,729) | - | (47,729) |
| **Total credit exposure** | | **232,588** | **1,741,504** | **6,126,597** | **764,042** | **8,864,731** |
| **As at 31 March 2019** | | | | | | |
| New Zealand total | | 149,065 | 1,425,974 | 5,820,648 | 748,759 | 8,144,446 |
| Outside New Zealand | | - | 401,836 | - | - | 401,836 |
| Provision for impairment | 16.(f) | - | - | (28,599) | - | (28,599) |
| **Total credit exposure** | | **149,065** | **1,827,810** | **5,792,049** | **748,759** | **8,517,683** |

Charts below show the percentage (%) breakdown of the loans and advances to customers.



All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (i) Concentrations of credit exposures (continued)

#### (iii) Concentration of credit exposure by industry sector

| | Note | 2020 | 2019 |
|---|---|---|---|
| Cash on hand | | 21,966 | 22,666 |
| Local government lending and investments | | 180,434 | 366,590 |
| New Zealand registered banks | | 473,779 | 509,525 |
| Multilateral development banks and other international institutions | | 370,272 | 321,404 |
| Other financial institutions | | 127,474 | 38,921 |
| Sovereigns and Central Bank | | 723,654 | 560,632 |
| Food product and beverages | | - | 18,484 |
| Utilities | | 128,228 | 140,786 |
| Transport, postal and warehousing | | - | 31,983 |
| Information media and telecommunications | | - | 30,291 |
| Agricultural lending | | 350,072 | 338,343 |
| Residential lending | | 5,729,666 | 5,334,932 |
| Personal and other lending | | 170,124 | 217,190 |
| Community lending | | 4,881 | 5,131 |
| Commercial lending | | 631,910 | 609,404 |
| Provision for impairment loss | 16.(f) | (47,729) | (28,599) |
| **Total credit exposure** | | **8,864,731** | **8,517,683** |

### (j) Concentration of credit exposures to individual counterparties

The following disclosures show the number of individual counterparties or groups of closely related counterparties where the period end and peak end-of-day credit exposures equalled or exceeded 10% of the Bank's Common Equity Tier 1 (CET1) capital as at balance date (excluding exposures to connected persons, central government of any country with a long-term credit rating of A- or A3 or above, or its equivalent, and any supranational or quasi-sovereign agency with a long-term credit rating of A- or A3 or above, or its equivalent). The peak aggregate end of day credit exposure is the largest daily actual credit exposure for the most recent quarter. 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.

| **% of Shareholders equity** | Year ended 31 March 2020 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Number of bank counterparties | | | | Number of non-bank counterparties | | | |
| As at Balance date | "A" Rated | "B" Rated | Unrated | Total | "A" Rated | "B" Rated | Unrated | Total |
| 10% - 15% | 4 | - | - | 4 | 3 | - | - | 3 |
| 15% - 20% | 1 | - | - | 1 | - | - | - | - |
| **Total** | **5** | **-** | **-** | **5** | **3** | **-** | **-** | **3** |
| Peak exposure | "A" Rated | "B" Rated | Unrated | Total | "A" Rated | "B" Rated | Unrated | Total |
| 10% - 15% | 3 | - | - | 3 | 3 | - | - | 3 |
| 15% - 20% | 2 | - | - | 2 | - | - | - | - |
| **Total** | **5** | **-** | **-** | **5** | **3** | **-** | **-** | **3** |

Note:
"A" Rated - those counterparties that have a long-term credit rating of A- or A3 or above, or its equivalent.
"B" Rated – those counterparties that have a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent.
Unrated – those counterparties that do not have a long-term credit rating.

All in $000's

## 16. Credit Risk Management and Asset Quality (continued)

### (k) Concentration of credit exposures to connected persons

Credit exposure concentrations are disclosed on the basis of actual credit exposures and calculated on a gross basis (net of specific provisions and excluding advances of a capital nature). The Bank only has credit exposures to non-bank connected persons. Peak end-of day credit exposures to non-bank connected persons are calculated using the Bank's tier one capital at the end of the period. The rating contingent limit, which is applicable to the Bank as at balance date, is 30%. There have been no rating-contingent limit changes during the last year. Within the rating-contingent limit there is a sub-limit of 15%, which applies to non-bank connected persons. All limits on aggregate credit exposure to all connected persons and non-bank connected persons in the Bank's Conditions of Registration have been complied with at all times over the last quarter. The information on credit exposures to connected persons has been derived in accordance with the Reserve Bank of New Zealand document entitled "Connected Exposures Policy (BS8)" dated November 2015.

There are no specific provisions against credit exposures to connected persons as at 31 March 2020 (31 March 2019: $nil).

| | 2020 | 2019 |
|---|---|---|
| Credit exposures to non-bank connected persons at period end | 83,600 | 83,600 |
| Credit exposures to non-bank connected persons at period end (expressed as % of total tier one capital) | 12.80% | 13.02% |
| Peak credit exposures to non-bank connected persons during the period | 83,600 | 83,600 |
| Peak credit exposures to non-bank connected persons during the period (expressed as % of total tier one capital) | 12.80% | 13.02% |

### (l) Maximum exposure to credit risk

The Bank does not have any material exposures on which balances have been netted. As such, the carrying amount of loans and advances (gross of provisions), investment securities, plus commitments are as set out in note 21. Commitments and Contingent Liabilities represent the Bank's maximum exposure to credit risk for on and off-balance sheet financial instruments.

### (m) Coverage provided by collateral held on loans

The table below presents the maximum exposure to credit risk for balance sheet financial instruments before taking account of the financial effect of any collateral held, unless such collateral meets the offsetting criteria in NZ IAS 32 Financial Instruments: Presentation.

The most common types of acceptable collateral include security over real estate, cash deposits, and other security over business assets.

| | As at 31 March 2020 | | | As at 31 March 2019 | | |
|---|---|---|---|---|---|---|
| Balance sheet position | Maximum exposure to credit risk | Financial effect of collateral | Unsecured portion of credit exposure | Maximum exposure to credit risk | Financial effect of collateral | Unsecured portion of credit exposure |
| Cash and cash equivalents | 232,588 | 232,588 | - | 149,065 | 149,065 | - |
| Derivative financial instruments | 13,942 | - | 13,942 | 6,519 | - | 6,519 |
| Investment securities | 1,741,504 | 203,458 | 1,538,046 | 1,827,810 | 302,183 | 1,525,627 |
| Loans and advances to customers | 6,126,597 | 6,083,259 | 43,338 | 5,792,049 | 5,719,304 | 72,745 |
| Other financial assets | 2,440 | 2,440 | - | 2,201 | 2,201 | - |
| **Total exposure to credit risk** | **8,117,071** | **6,521,744** | **1,595,327** | **7,777,644** | **6,172,753** | **1,604,891** |

## 17. Market Risk Management

### Interest rate risk

Interest rate risk (IRR) refers to the risk to the Bank's economic value or earnings arising from adverse movements in interest rates. The Bank has a preference for stability of earnings, which is consistent with the Shareholder's expectations of stable dividend payments over time.

When interest rates change, the present value and timing of future cash flows change. This in turn changes the underlying value of the bank's assets, liabilities and off-balance sheet instruments and in turn, their economic value. Changes in interest rates also affect the bank's earnings by altering interest rate-sensitive income and expenses, affecting its net interest income (NII).

The Bank measures and manages its interest rate risk using a combination of economic value and earnings-based measures.

Under the economic value approach, the measure of interest rate risk is the theoretical change in the market value of the entire balance sheet. The economic value for both on and off-balance sheet items is derived from their contractual cash flows, which are discounted to reflect current market rates.

Under the earnings-based measure, the focus is on the impact of changes in interest rates on future reported net interest income (NII). This focus reflects both the importance of NII the bank's overall earnings and the direct link to changes in interest rates.

All in $000's

## 17. Market Risk Management (continued)

### Interest rate risk (continued)

The Bank is exposed to IRR from mismatches in the repricing dates, or differences in the repricing characteristics of its assets and liabilities. The Bank closely monitors the repricing behaviour of its assets and liabilities and ensures that any mismatches remain within policy limits. This may be done with the use approved derivative transactions. The Bank does not seek to eliminate interest rate risk, rather to limit downside variability in NII.

### Foreign currency risk

Foreign currency risk is the risk to the Bank's earnings or market value caused by movements in foreign exchange rates.

The Bank provides foreign exchange services via its branch network and offers foreign currency deposit accounts to customers via a third party.

Limits are in place to control the amount of foreign currency exposure. The Bank's policy is to maintain minimal levels of foreign currency cash balances and therefore foreign currency exposure is immaterial. The Bank also ensures customers who have foreign currency deposit accounts with the Bank are aware that they could be exposed to foreign currency fluctuations in their own right.

### (a) Interest rate repricing schedule

The interest rate repricing schedule of on-balance sheet financial assets and financial liabilities has been prepared on the basis of contractual maturity or next repricing date, whichever is earlier.

| As at 31 March 2020 | 0-3 months | 3-6 months | 6-12 months | 1-2 years | Over 2 years | Non-interest sensitive | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and cash equivalents | 210,622 | - | - | - | - | 21,966 | 232,588 |
| Investment securities | 818,564 | 43,365 | 115,530 | 263,000 | 456,651 | 44,574 | 1,741,504 |
| Loans and advances to customers | 1,824,474 | 528,842 | 1,400,407 | 1,921,250 | 480,633 | (29,009) | 6,126,597 |
| Other financial assets [1] | - | - | - | - | - | 16,382 | 16,382 |
| **Total financial assets** | **2,853,660** | **572,207** | **1,515,757** | **2,184,250** | **937,284** | **53,913** | **8,117,071** |
| **Liabilities** | | | | | | | |
| Deposits | 4,293,520 | 963,610 | 910,639 | 573,078 | 227,970 | 451,707 | 7,420,524 |
| Lease liabilities | 562 | 568 | 1,129 | 1,783 | 11,812 | - | 15,854 |
| Other financial liabilities [2] | - | - | - | - | - | 57,060 | 57,060 |
| **Total financial liabilities** | **4,294,082** | **964,178** | **911,768** | **574,861** | **239,782** | **508,767** | **7,493,438** |
| **Lending commitments** | **764,042** | **-** | **-** | **-** | **-** | **-** | **764,042** |
| **Derivative notional principals (net)** | **633,305** | **(15,305)** | **(275,000)** | **(525,000)** | **182,000** | **-** | **-** |
| **Interest sensitivity gap** | **(43,075)** | **(407,276)** | **328,989** | **1,084,389** | **879,502** | **(454,854)** | **1,387,675** |

| As at 31 March 2019 | 0-3 months | 3-6 months | 6-12 months | 1-2 years | Over 2 years | Non-interest sensitive | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and cash equivalents | 126,399 | - | - | - | - | 22,666 | 149,065 |
| Investment securities | 899,909 | 100,680 | 176,750 | 238,547 | 384,150 | 27,774 | 1,827,810 |
| Loans and advances to customers | 1,765,208 | 577,251 | 1,373,205 | 1,698,761 | 384,416 | (6,792) | 5,792,049 |
| Other financial assets [1] | - | - | - | - | - | 8,720 | 8,720 |
| **Total financial assets** | **2,791,516** | **677,931** | **1,549,955** | **1,937,308** | **768,566** | **52,368** | **7,777,644** |
| **Liabilities** | | | | | | | |
| Deposits | 4,139,471 | 913,679 | 957,556 | 402,959 | 297,446 | 381,906 | 7,093,017 |
| Lease liabilities | 22 | 23 | 46 | 95 | 5,903 | - | 6,089 |
| Other financial liabilities [2] | - | - | - | - | - | 59,729 | 59,729 |
| **Total financial liabilities** | **4,139,493** | **913,702** | **957,602** | **403,054** | **303,349** | **441,635** | **7,158,835** |
| **Lending commitments** | **748,759** | **-** | **-** | **-** | **-** | **-** | **748,759** |
| **Derivative notional principals (net)** | **421,905** | **(20,305)** | **(108,600)** | **(420,000)** | **127,000** | **-** | **-** |
| **Interest sensitivity gap** | **(177,313)** | **(256,076)** | **483,753** | **1,114,254** | **592,217** | **(389,267)** | **1,367,568** |

[1] Other financial assets include receivables and derivative financial instruments.
[2] Other financial liabilities include accounts payable, provision for dividend and derivative financial instruments.

All in $000's

## 17. Market Risk Management (continued)

### (b) Sensitivity analysis

In accordance with NZ IFRS 7, an assessment has been undertaken of the market risk sensitivity of net interest income and shareholder's equity based on fluctuations in interest rates.

The primary objective of the Bank's framework for the management of interest rate risk is to minimise the impact of changes in wholesale interest rates on the Bank's earnings. The Risk Framework includes limits for both earnings at risk and economic value, as well as repricing gap analysis.

**Next 12 months net interest earnings**

The figures in the table below indicate the outcome of the earnings at risk measure for the current period.

| Scenarios | Change in net Interest Earnings ($m) | |
|---|---|---|
| | 31 Mar 2020 | 31 Mar 2019 |
| -2.0% | 0.8 | 5.3 |
| -1.0% | 0.8 | 2.6 |
| 1.0% | (2.9) | (3.6) |
| 2.0% | (6.5) | (7.5) |

The earnings at risk measure looks at the sensitivity of net interest earnings over the next twelve months to potential changes in interest rates and is measured on a monthly basis.

Earnings at risk is measured assuming immediate one percent and two percent parallel movement in interest rates across the yield curve. Sensitivity of net interest earnings is measured using a model that takes into account current and projected future changes in terms of asset and liability levels as well as product mix.

**Economic value of shareholder's equity (EVE)**

The figures in the table below indicate the outcome of the EVE measure for the current period.

| Scenarios | Change in EVE ($m) | |
|---|---|---|
| | 31 Mar 2020 | 31 Mar 2019 |
| -2.0% | 15.2 | 29.8 |
| -1.0% | 12.7 | 15.3 |
| 1.0% | (18.7) | (17.2) |
| 2.0% | (37.8) | (34.7) |

The economic value of shareholders equity (EVE) risk measure looks at the sensitivity of the economic value of the Bank to changes in wholesale interest rates and is measured on a monthly basis.

The current economic value for both on and off-balance sheet assets and liabilities is derived from their contractual cash flows, which are discounted to reflect current market rates. The sensitivity of the EVE is measured assuming immediate one percent and two percent parallel movements in interest rates across the yield curve.

## 18. Liquidity and Funding Risk Management

### (a) Core liquid assets

The Bank maintains a portfolio of highly marketable and diverse assets that are assumed to be easily liquidated in the event of an unforeseen interruption in cash flow. The table below lists the Bank's core liquid assets.

| | 2020 | 2019 |
|---|---|---|
| **Cash and cash equivalents** | **232,588** | **149,065** |
| **Investment securities:** | | |
| Local authority securities | 128,718 | 235,602 |
| Government securities | 513,032 | 434,233 |
| Registered bank securities | 473,779 | 509,525 |
| Other investments | 625,.974 | 489,002 |
| **Total investment securities** | **1,741,503** | **1,668,362** |
| **Total core liquid assets** | **1,974,091** | **1,817,427** |

All in $000's

## 18. Liquidity and Funding Risk Management (continued)

### (b) Contractual cash flows

The following tables analyse the Bank's financial liabilities into relevant maturity groupings based on the remaining period as at balance date to the contractual maturity date. The amounts disclosed in the tables are the contractual undiscounted cash flows and include principal and future interest cash flows, and therefore will not agree to the carrying values on the statement of financial position.

| As at 31 March 2020 | On demand | 0-1 months | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|---|
| **Liabilities:** | | | | | | | |
| Deposits | 3,480,517 | 590,196 | 826,764 | 1,822,497 | 803,990 | - | 7,523,964 |
| Lease liabilities | - | 243 | 486 | 2,166 | 8,230 | 11,426 | 22,550 |
| Other financial liabilities * | - | 30,945 | 17,642 | 2,932 | 5,331 | 210 | 57,060 |
| **Total financial liabilities** | **3,480,517** | **621,384** | **844,892** | **1,827,595** | **817,551** | **11,636** | **7,603,574** |
| **Lending commitments (off-balance sheet)** | **764,042** | **-** | **-** | **-** | **-** | **-** | **764,042** |
| **As at 31 March 2019** | | | | | | | |
| **Liabilities:** | | | | | | | |
| Deposits | 3,193,232 | 625,114 | 859,114 | 1,806,432 | 733,173 | - | 7,217,065 |
| Lease liabilities | - | 33 | 67 | 299 | 1,596 | 9,812 | 11,807 |
| Other financial liabilities * | - | 26,605 | 16,861 | 3,412 | 6,217 | 916 | 54,011 |
| **Total financial liabilities** | **3,193,232** | **651,752** | **876,042** | **1,810,143** | **740,986** | **10,728** | **7,282,883** |
| **Lending commitments (off-balance sheet)** | **748,759** | **-** | **-** | **-** | **-** | **-** | **748,759** |

* Other financial liabilities include accounts payable, provision for dividend and derivative financial instruments.

### (c) Current and non-current assets and liabilities

Assets and liabilities are classified as current if it is expected they will be realised, consumed or settled within 12 months of the reporting date.

Non-current assets include property, plant and equipment and intangible assets as well as financial assets of a long term nature. Noncurrent liabilities include financial and non-financial liabilities which are expected to be settled after twelve months from reporting date. For the purposes of this disclosure, the fair value of derivatives has been classified as current.

| | As at 31 March 2020 | | | As at 31 March 2019 | | |
|---|---|---|---|---|---|---|
| | Current | Non-current | Total | Current | Non-current | Total |
| **Assets** | | | | | | |
| Cash and cash equivalents | 232,588 | - | 232,588 | 149,065 | - | 149,065 |
| Derivative financial instruments | 13,942 | - | 13,942 | 6,519 | - | 6,519 |
| Investment securities | 704,137 | 1,037,367 | 1,741,504 | 733,996 | 1,093,814 | 1,827,810 |
| Loans and advances to customers | 2,601,400 | 3,525,197 | 6,126,597 | 2,566,377 | 3,225,672 | 5,792,049 |
| Deferred tax asset | - | 12,650 | 12,650 | - | 4,319 | 4,319 |
| Property, plant and equipment | - | 34,150 | 34,150 | - | 28,072 | 28,072 |
| Intangible assets | - | 15,404 | 15,404 | - | 9,010 | 9,010 |
| Other assets * | 2,440 | - | 2,440 | 2,201 | - | 2,201 |
| **Total assets** | **3,554,507** | **4,624,768** | **8,179,275** | **3,458,158** | **4,360,887** | **7,819,045** |
| **Liabilities** | | | | | | |
| Deposits | 6,617,355 | 803,169 | 7,420,524 | 6,390,425 | 702,592 | 7,093,017 |
| Derivative financial instruments | 17,799 | - | 17,799 | 12,117 | - | 12,117 |
| Current tax liability | 5,600 | - | 5,600 | 6,423 | - | 6,423 |
| Lease liabilities | 2,259 | 13,595 | 15,854 | 91 | 5,998 | 6,089 |
| Other liabilities | 33,929 | 5,617 | 39,546 | 42,674 | 5,600 | 48,274 |
| **Total liabilities** | **6,676,942** | **822,381** | **7,499,323** | **6,451,730** | **714,190** | **7,165,920** |

* Other assets include receivables, prepayments and sundry debtors.

All in $000's

## 18. Liquidity and Funding Risk Management (continued)

### (d) Regulatory liquidity ratios

The Reserve Bank of New Zealand's Liquidity Policy (BS13) sets regulatory minimums for liquidity risk that the Bank is required to meet as part of its conditions of registration. As part of its over-arching risk management practices, the Bank has adopted a conservative approach to liquidity management and aims for liquidity to be well in excess of the minimum regulatory requirements. The Bank's Treasury Policy, which is approved by the Board of Directors, sets out the minimum internal liquidity requirements for the Bank as well as providing guidance for the Bank's portfolio of liquid assets.

The Bank manages its liquidity risk through a combination of forward looking cash flow management, as well as maintaining a portfolio of high quality liquid assets that can be realised quickly if required. The Bank also closely monitors a series of potential leading indicators for liquidity risk, including term deposit reinvestment rates and the weighted average term of funding.

In the event of a severe liquidity event, the Bank has a contingency funding plan in place which outlines the actions the Bank would take in order to manage the situation.

Liquidity ratios below were calculated at the close of each working day in the periods specified in accordance with the conditions of registration relating to liquidity-risk policy and management.

| | Three month period ending on 31 March 2020 | Three month period ending on 31 December 2019 |
|---|---|---|
| One-week mismatch ratio | 13.9% | 13.5% |
| One-month mismatch ratio | 20.3% | 19.8% |
| Core funding ratio | 117.2% | 117.3% |

## 19. Capital Adequacy

The Bank is subject to regulation by the 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. These requirements define what is acceptable as capital and provide for methods of measuring the risks incurred by the Bank. The Bank must comply with RBNZ minimum capital adequacy ratios under its Conditions of Registration.

The Bank's objectives for the management of Capital Adequacy are to comply at all times with the regulatory capital requirements set by the Reserve Bank of New Zealand (RBNZ); to maintain a strong capital base to cover the inherent risks of the business in excess of that required by rating agencies to maintain an investment credit grading; and to support the future development and growth of the business to maximise shareholder's value.

Total regulatory capital is divided into Tier 1 and Tier 2 capital. Tier 1 capital comprises Common Equity Tier 1 ("CET1") capital and Additional Tier 1 ("AT1") capital. Tier 1 capital primarily consists of shareholder's equity and other capital instruments acceptable to the RBNZ, less intangible assets, cash flow hedge reserve, deferred tax assets and a deduction for any advances of a capital nature to connected persons. Tier 2 Capital comprises capital instruments as defined by the RBNZ.

Regulatory capital adequacy ratios are calculated by expressing capital as a percentage of risk weighted exposures. Risk weighted exposures are derived by assigning a risk weight percentage to certain categories of exposures, including statement of financial position assets (excluding intangible assets and capital deductions for investments in subsidiaries not wholly owned or funded), and off-balance sheet assets. The risk weighting categories range from 0% - 150%. It should be noted that the regulatory risk weightings may not be consistent with the loss experience of the Bank.

As a Condition of Registration, the Bank must comply with the following minimum requirements set by the RBNZ:

- Total capital must not be less that 8% of risk weighted exposure.
- Tier 1 capital must not be less than 6% of risk weighted exposure.
- Common Equity Tier One capital must not be less than 4.5% of risk weighted exposure.
- Capital must not be less than NZ$30m.
- Buffer ratio must be not less than 2.5%.

The Board of Directors has ultimate responsibility for capital adequacy, and approves capital policy and minimum capital levels and limits. These are typically at a higher level than required by the Regulator to reduce the risk of breaching Conditions of Registration. The Bank monitors its Capital Adequacy and reports this on a regular basis to the Board and on a monthly basis to the RBNZ.

All in $000's

## 19. Capital Adequacy (continued)

In November 2019, the Bank identified that it had incorrectly applied "Capital Adequacy Framework (Standardised Approach (BS2A) when calculating its risk weighted assets and regulatory capital. The incorrect application of BS2A did not result in non-compliance with condition of registration 1 after 31 December 2018, as a new version of that condition took effect from 1 January 2019. The details of the incorrect application are as follows:

1. The Bank used loan-to-value ratios calculated at origination, as opposed to recalculating them for each reporting period.
2. The Bank also identified several credit data classification discrepancies.

Due to the size and complexity involved in implementing fixes for the identified issues, calculations are yet to be reperformed. It is anticipated the impact of these corrections will result in an increase to the Bank's minimum capital requirement of up to $6 million. The Bank currently holds $263 million of capital in excess of the minimum capital requirement. The impact equates to a reduction in the Banks regulatory capital ratios of up to 25 basis points.

A project has been established to resolve these issues and remediation is ongoing.

The capital adequacy tables set out on the following pages summarise the composition of regulatory capital and the Capital Adequacy ratios for the Bank for the year ended 31 March 2020.

### (a) Capital Adequacy Ratios

Total capital adequacy ratios for the Bank at balance date are:

| | RBNZ Minimum ratio requirement | 2020 31 Mar Unaudited Basel III | 2019 31 Mar Unaudited Basel III |
|---|---|---|---|
| Common Equity Tier 1 capital ratio | 4.50% | 14.32% | 14.57% |
| Tier 1 capital ratio | 6.00% | 14.32% | 14.57% |
| Total capital ratio | 8.00% | 14.32% | 14.57% |
| Buffer ratio | 2.50% | 6.32% | 6.57% |

### (b) Regulatory Capital

| | 2020 Basel III Unaudited | 2019 Basel III Unaudited |
|---|---|---|
| **Tier 1 capital** | | |
| **Common Equity Tier 1 ("CET1") capital** | | |
| Issued and fully paid up share capital | 10,000 | 10,000 |
| Retained earnings | 632,080 | 597,756 |
| Balance adjusted for adoption of NZ IFRS 9 | - | (715) |
| Current period's audited retained earnings | 28,317 | 35,039 |
| Fair value reserve | 10,874 | 13,217 |
| Cash flow hedge reserve | (1,319) | (2,172) |
| | **679,952** | **653,125** |
| **Less Deductions from CET1 capital** | | |
| Intangible assets | 15,404 | 9,010 |
| Cash flow hedge reserve | (1,319) | (2,172) |
| Deferred tax assets | 12,650 | 4,319 |
| Implicit risk adjustment* | 57,000 | - |
| | **83,735** | **11,157** |
| **Total CET 1 capital** | **596,217** | **641,968** |
| Additional Tier 1 ("AT1") Capital | - | - |
| **Total Tier 1 capital** | **596,217** | **641,968** |
| **Tier 2 capital** | | |
| Unrealised revaluation on security holdings at 45% | - | - |
| **Total capital** | **596,217** | **641,968** |

*Implicit risk adjustment has been made in accordance with Condition 1C of the Bank's conditions of registration.

All in $000's

## 19. Capital Adequacy (continued)

### (c) Credit risk

#### (i) On-balance sheet exposures

| As at 31 March 2020 | Total exposure after risk mitigation | Risk weighting | Risk weighted exposure | Minimum pillar one capital requirement |
|---|---|---|---|---|
| Cash | 9,390 | 0% | - | - |
| Sovereigns & RBNZ | 723,655 | 0% | - | - |
| Multilateral development banks | 349,582 | 0% | - | - |
| Multilateral development banks | 20,690 | 20% | 4,138 | 331 |
| Public sector entities | 145,283 | 20% | 29,057 | 2,325 |
| Banks | 156,286 | 20% | 31,257 | 2,501 |
| Banks | 330,068 | 50% | 165,034 | 13,203 |
| Corporate | 187,932 | 20% | 37,586 | 3,007 |
| Corporate | - | 50% | - | - |
| Corporate | 912,074 | 100% | 912,074 | 72,966 |
| Residential mortgages not past due: | | | | |
| Non-property investment <80% LVR * | 3,350,394 | 35% | 1,172,638 | 93,811 |
| Non-property investment 80%<90% LVR * | 328,920 | 50% | 164,461 | 13,157 |
| Non-property investment 90%<100% LVR * | 49,890 | 75% | 37,418 | 2,993 |
| Non-property investment >100% LVR * | 846 | 100% | 846 | 68 |
| Property investment <80% LVR * | 1,371,252 | 40% | 548,500 | 43,880 |
| Property investment 80%<90% LVR * | 7,939 | 70% | 5,557 | 445 |
| Property investment 90%<100% LVR * | 645 | 90% | 580 | 47 |
| Property investment >100% LVR * | 319 | 100% | 319 | 26 |
| Welcome home <80% LVR * | 2,325 | 35% | 814 | 65 |
| Welcome home 80%<90% LVR * | 47,397 | 35% | 16,589 | 1,327 |
| Welcome home 90%<100% LVR * | 29,277 | 50% | 14,639 | 1,171 |
| Welcome home >100% LVR * | 2,418 | 100% | 2,418 | 193 |
| Reverse mortgages <60% LVR * | 8,907 | 50% | 4,454 | 356 |
| Reverse mortgages 60%<80% LVR * | 128 | 80% | 102 | 8 |
| Reverse mortgages >80% LVR * | 21 | 100% | 21 | 2 |
| Past due residential mortgages * | 5,487 | 100% | 5,487 | 439 |
| Other past due assets | 52 | 100% | 52 | 4 |
| Other past due assets | 1,126 | 150% | 1,689 | 135 |
| Other lending | 58,386 | 100% | 58,386 | 4,671 |
| Other assets | 50,532 | 100% | 50,532 | 4,043 |
| Non-risk weighted assets | 28,054 | 0% | - | - |
| **Total on-balance sheet exposures** | **8,179,275** | | **3,264,648** | **261,174** |

* Total exposure of residential mortgages is $5,206,165.

All in $000's

## 19. Capital Adequacy (continued)

### (c) Credit risk

#### (ii) Off-balance sheet exposures

| As at 31 March 2020 | Total exposure | Credit conversion factor | Credit equivalent amount | Average risk weight | Risk weighted exposure | Minimum Pillar one capital requirement |
|---|---|---|---|---|---|---|
| Commitments that can be cancelled unconditionally | 624,988 | 0% | - | N/A | - | - |
| Commitment with certain drawdown | 135,836 | 100% | 135,836 | 43% | 58,634 | 4,691 |
| Market related contracts: | 3,218 | 50% | 1,609 | 100% | 1,609 | 129 |
| Foreign exchange contracts | - | Various | - | 0% | - | - |
| Interest rate contracts* | 1,263,000 | Various | 18,107 | 35% | 6,414 | 513 |
| Credit valuation adjustment (CVA) | - | | - | - | 4,880 | 390 |
| **Total off-balance sheet exposures** | **2,027,042** | | **155,552** | | **71,537** | **5,723** |

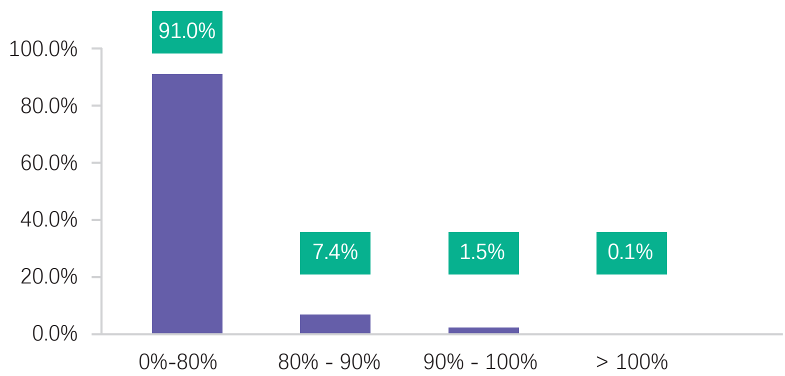
* The credit equivalent amount for market related contracts (which are all interest rate contracts) were calculated using the current exposure method.

### (d) Residential mortgages by loan-to-valuation (LVR) ratio

As at 31 March 2020

| LVR Range | Note | 0%-80% | 80% - 90% | 90% - 100% | > 100% | Total |
|---|---|---|---|---|---|---|
| **On-balance sheet exposures** | | 4,747,284 | 385,374 | 80,038 | 3,596 | 5,216,292 |
| Past due and impaired | | 5,402 | 559 | - | 312 | 6,273 |
| **Total value of on-balance sheet exposures** | 7,16 | **4,752,686** | **385,933** | **80,038** | **3,908** | **5,222,565** |
| Less provisions: | | | | | | |
| Collective | | 13,825 | 1,055 | 225 | 13 | 15,118 |
| Specific | | 939 | 172 | 1 | 170 | 1,282 |
| **Total residential mortgages** | | **4,737,922** | **384,706** | **79,812** | **3,725** | **5,206,165** |
| **Off-balance sheet exposures** | | 493,909 | 8,799 | 4,318 | 75 | 507,101 |
| **Total residential mortgages** | | **5,231,831** | **393,505** | **84,130** | **3,800** | **5,713,266** |

The bar graph represents the percentage (%) of residential mortgage by LVR



All in $000's

## 19. Capital Adequacy (continued)

### (e) Market risk

In accordance with clause 9 of Schedule 9 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014, peak end-of-day aggregate capital charge and peak end-of-day aggregate capital charge as a percentage of the Bank's equity at the end of the period, are derived by following the risk methodology for measuring capital requirements within Part 10 of - Capital Adequacy Framework (Standardised Approach) (BS2A).

| As at 31 March 2020 | | Implied risk weighted exposure | Aggregate capital charge |
|---|---|---|---|
| End of period capital charges | Interest risk | 316,542 | 25,323 |
| Peak end of day capital charges | Interest risk | 329,810 | 26,385 |

### (f) Risk weighted exposure and total capital requirements

| As at 31 March 2020 | Total exposure after credit risk mitigation | Risk weighted exposure or Implied RWE | Capital requirement |
|---|---|---|---|
| Total credit risk plus equity | 8,306,932 | 3,336,185 | 266,894 |
| Operational risk | N/A | 509,424 | 40,754 |
| Market risk | N/A | 316,542 | 25,323 |
| **Total** | **8,306,932** | **4,162,151** | **332,971** |

### (g) Capital for other material risks (Pillar II)

Pillar 2 is intended to ensure that banks have adequate capital to support all risks in their business, and includes the requirement on banks to have an "Internal Capital Adequacy Assessment Process (ICAAP)" for assessing their overall Capital Adequacy in relation to risk profile and a strategy for maintaining adequate capital to support risk. The Bank's ICAAP has identified other areas of risk not covered by Pillar I (credit risk, market risk, and operational risk) and assigned a level of capital to them. These risks include but are not limited to strategic risk, reputational risk, environmental risk, liquidity risk, investment portfolio risk, sector and regional concentration risk, natural disaster risk, brand risk and ownership structure.

The Bank has made an internal capital allocation of $61.7m (2019: $61.9m) to cover these identified risks.

### (h) Credit Risk Mitigation

The Bank determines whether it requires security to mitigate credit risk associated with the loans and investments that it makes in the course of its business.

The Bank's loan portfolio comprises predominantly of residential mortgages (85%) which are secured by first-ranking registered mortgages over residential property. As at 31 March 2020, $81m of these loans are underwritten by Housing New Zealand Corporation, a Statutory Crown Corporation, as part of its Welcome Home Loan programme.

Other lending, in the form of overdrafts and credit cards, is unsecured.

As at 31 Mar 2020, the Bank has total securities of $1.7 billion for the liquidity management purpose. These securities have been issued by the New Zealand Government and other Crown entities, domestic banks, multilateral development banks, supranational organisations and domestic corporate entities on the basis of their high financial standing and credit ratings. The Bank holds no guarantees or credit derivatives against them.

The Bank does not hold collateral in the form of cash or other securities to mitigate credit risk relating to the derivatives it has entered into for the purpose of interest rate risk management.

All in $000's

## 20. Securitisation, Funds Management, Other Fiduciary Activities and Marketing and Distribution of Insurance Products

The Bank has no involvement with any securitisation, custodial, or other fiduciary activities. The Bank does not conduct any insurance business, however general insurance, life insurance, and KiwiSaver products are marketed through the Bank's branch network. These have been provided at arm's length terms and conditions. The Bank provides no funding to the entities on whose behalf the insurance products are marketed. External third party insurance companies underwrite these. The Bank markets Fisher Funds KiwiSaver products through the Bank's branch network. Refer to note 22. Related Party Transactions and Balances in regards to the related party loan to TSB Group Limited and commission income from Fisher Funds Management Limited.

TSB Bank Limited is the manager and promoter of the TSB Bank PIE Unit Trust, and the New Zealand Guardian Trust Company Limited is the trustee. Units in the fund do not directly represent deposits or other liabilities of the Bank. However, the Trust Deed stipulates that the TSB Bank PIE Unit Trust is invested exclusively in TSB Bank debt securities.

As at 31 March 2020, the TSB Bank PIE Unit Trust had $11.1m (31 March 2019: $15.4m) invested with the Bank.

## 21. Commitments and Contingent Liabilities

The Bank is involved in a range of transactions that give rise to contingent and/or future liabilities. The Bank discloses a contingent liability when it has a possible obligation arising from past events that will be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the Bank's control. A contingent liability is disclosed when a present obligation is not recognised because it is not probable that an outflow of resources will be required to settle an obligation, or the amount of the obligation cannot be measured with sufficient reliability.

The Bank issues commitments to extend credit and other credit facilities. These financial instruments attract service charges in line with market process for similar arrangements. They are not sold or traded. The items generally do not involve cash payments other than in the event of default. The service charges are set as part of the broader customer credit process and reflects the probability of default. They are disclosed as commitments at their face value.

| | 2020 | 2019 |
|---|---|---|
| **Lending commitments:** | | |
| Commitments approved to advance less than one year | 108,002 | 107,137 |
| Commitments approved to advance greater than one year[1] | 656,040 | 641,622 |
| **Total lending commitments** | **764,042** | **748,759** |
| **Other commitments:** | | |
| Rental / lease commitments less than one year[2] | 10 | 2,472 |
| Rental / lease commitments greater than one year[2] | 23 | 8,266 |
| Capital commitments | 4,210 | 3,035 |
| **Total other commitments** | **4,243** | **13,773** |
| **Total commitments** | **768,285** | **762,532** |

[1] Includes $30.8m (31 March 2019: $10.44m) related to the facility granted to TSB Group Limited, a related entity.
[2] There was a significant reduction in total non-cancellable operating lease commitments consequent to the adoption of NZ IFRS 16. The rental/lease commitments disclosed in this note are related to leases that meet the exemption criteria of NZ IFRS 16. Refer to note 1(i) Changes in accounting policy for further information.

There are no material contingent liabilities and outstanding claims that are not provided for as at 31 March 2020.

All in $000's

## 22. Related Party Transactions and Balances

The Bank is wholly owned by the TSB Community Trust (the Trust) through the Trust's fully owned subsidiary, TSB Group Limited. During the period the Trust operated bank account facilities which were on normal customer terms and conditions.

The Bank markets Fisher Funds KiwiSaver products through the Bank's branch network and receives commission income in return. TSB Group Limited together with its subsidiaries, TSB Capital Limited and TSB Group Investment Limited, hold 66.01% (2019: 66.01%) shareholding of Fisher Funds Management Limited.

The following table shows the outstanding balances and transactions between TSB group entities that arose from the ordinary course of business and carried out at normal commercial rates.

| | | 2020 | | | 2019 | | |
|---|---|---|---|---|---|---|---|
| Recognised in | Note | TSB Community Trust | TSB Group Limited | Fisher Funds | TSB Community Trust | TSB Group Limited | Fisher Funds |
| **Statement of Financial Position** | | | | | | | |
| Loan balance | 7 | - | 52,803 | - | - | 73,161 | - |
| Deposit balance | 10 | 7,603 | - | - | 21,203 | - | - |
| **Statement of Changes in Equity** | | | | | | | |
| Dividends | 13 | - | 2,500 | - | - | 10,000 | - |
| **Statement of Comprehensive Income** | | | | | | | |
| Interest income | 2 | - | 2,484 | - | - | 3,103 | - |
| Interest expense | 2 | 479 | - | - | 671 | - | - |
| Commission income | | - | - | 724 | - | - | 559 |

During the reporting period, subvention payments were made to TSB Group Limited of $1.375m (2019: $1.377m), TSB Group Capital Limited of $0.014m (2019: $0.164m) and TSB Group Investments Limited of $0.893m (2019: $1.328m).

### Transactions with directors and key management personnel

Key management personnel are defined as the directors, trustees and senior management of TSB Bank – those persons having the authority and responsibility for planning, directing and controlling the activities of the entity. Loans made to and deposits held by the key management personnel are made in the course of ordinary business on normal terms and conditions, other than some loans made to key management personnel, which are made with an interest rate at a discount to market.

| | 2020 | 2019 |
|---|---|---|
| **Key management compensation:** | | |
| Short-term employee benefits | 3,584 | 3,937 |
| Other long-term benefits | (3) | (19) |
| Termination benefits | 285 | 881 |
| Retirement benefits | - | 1,020 |
| **Total key management compensation** | **3,866** | **5,819** |
| **Loans to directors and key management personnel:** | | |
| Balance at beginning of period | 3,476 | 2,914 |
| Net loans / (repaid) during the period | (781) | 562 |
| **Balance at end of period** | **2,695** | **3,476** |
| **Deposits from directors and key management personnel:** | | |
| Balance at beginning of period | 825 | 528 |
| Net deposits received / (repaid) during the period | 2,321 | 297 |
| **Balance at end of period** | **3,146** | **825** |

Loans and deposits to directors and key management personnel include the directors of the TSB Group and TSB Community Trust.

## 23. Subsequent Events

Subsequent to 31 March 2020, TSB's Conditions of Registrations were modified by RBNZ. The amendments can be summarised as follows:

*Effective 2 April 2020*

- The current restrictions on distributions that apply in increasing steps once the buffer ratio falls below 2.5% have been replaced with a full restriction on distributions.
- The minimum requirement for the core funding ratio has been reduced from 75% to 50%.

*Effective 1 May 2020*

- Previously imposed loan-to-valuation ratio limits on new residential mortgage lending have been removed.

TSB paid an interim dividend of $2.5m to its shareholder, the TSB Community Trust, however will not be paying a final dividend as a result of this modification to its Conditions of Registration.

As part of the response to Covid-19, a number of initiatives have been undertaken to assist customers who have been impacted financially. These include;

- the home-loan deferral scheme, established in March 2020, is a scheme under which banks, including TSB, are now offering the deferral of mortgage payments for principal and interest for up to six months. As at 30 June 886 TSB customers had taken up this deferral, totalling $407m in lending.
- the Business Finance Guarantee Scheme, established in April 2020, is a scheme under which the Government will guarantee 80% of the risk of lending to small and medium-size businesses. Borrowers are still liable and must pay back the debt, with interest, in the usual way. TSB is a registered participant in the Business Finance Guarantee Scheme, and as at 30 June, had issued 20 loans under the scheme totalling $1.5m.
- TSB are of the opinion that there were no material changes to these numbers since 30 June.

# Conditions of Registration

**These conditions will apply on and after 31 December 2019.**

**The registration of TSB 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,—

   Except to the extent modified by Condition 1C, "Total capital ratio", "Tier 1 capital ratio", "Common Equity Tier 1 capital ratio" and "Total capital" 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;

   "Total capital" has the same meaning as in Part 2 of 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 group's buffer ratio:

| Banking group's buffer ratio | Percentage limit to distributions of the Bank's 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, except to the extent modified by Condition 1C — "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.

1C. That when calculating the banking group's Common Equity Tier 1 capital ratio, Tier 1 capital ratio and Total capital ratio for the purposes of Condition 1, and the banking group's buffer ratio for the purposes of Condition 1B, in addition to the amounts deducted in calculating Common Equity Tier 1 capital in accordance with subsection 7(3) of BS2A, the Bank must deduct an additional amount of $57 million for the implicit risk arising from the bank's association with Fisher Funds Management Limited ("FFML").

   For the purposes of this condition of registration, "BS2A" means the Reserve Bank of New Zealand document "Capital Adequacy Framework (Standardised Approach)" (BS2A) dated November 2015.

1D. That the Bank, in every full year and half year disclosure statement that it is required to publish, discloses the deduction for implicit risk required by Condition 1C as a separate item within the required disclosure of deductions from Common Equity Tier 1 capital.

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.

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 |

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

   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 exposure 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).

   For the purposes of this condition of registration, "non-executive" and "independent" have 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 or to the deputy 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, "non-executive" and "independent" have the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014.

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 per cent at the end of each business day;
   (b) the one-month mismatch ratio of the banking group is not less than zero per cent at the end of each business day; and
   (c) the one-year core funding ratio of the banking group is not less than 75 per cent 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 January 2018 and "Liquidity Policy Annex: Liquid Assets" (BS13A) dated October 2018.

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.

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 9 am 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" (BS17) dated September 2013.

    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.

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 70%, 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 20% 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 TSB 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 January 2019:

"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 June 2019.

# Conditions of Registration

### Changes in Conditions of Registration

The following changes, effective from 31 December 2019, have been made to the Bank's Conditions of Registration since the reporting date of the Bank's previous disclosure statement pursuant to section 74(2) of the Reserve Bank of New Zealand Act 1989:

- Condition 1C has been amended to reflect the change made to the calculation of Bank's capital adequacy in terms of the implicit risk arising from the Bank's related party, Fisher Funds Management Limited (FFML).
- Condition 1D has been modified to support the change made in condition 1C.

There have been no other changes to the Bank's Conditions of Registration.

# Independent Auditor's Report

To the shareholder of TSB Bank Limited

**Report on the disclosure statement**

## Opinion

In our opinion, the accompanying financial statements (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements) of TSB Bank Limited (the Bank) on pages 38 to 90:

i. give a true and fair view of the Bank's financial position as at 31 March 2020 and its financial performance and cash flows for the year ended on that date; and

ii. comply with New Zealand Generally Accepted Accounting Practice, which in this instance means New Zealand Equivalents to International Financial Reporting Standards ("NZIFRS") and International Financial Reporting Standards.

In our opinion, the supplementary information (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements) that is required to be disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order") and is included within notes 15, 16, 19 and 21 of the disclosure statement:

i. has been prepared, in all material respects, in accordance with the guidelines issued pursuant to section 78(3) of the Reserve Bank of New Zealand Act 1989 and any conditions of registration;

ii. is in accordance with the books and records of the Bank in all material respects; and

iii. fairly states the matters to which it relates in accordance with those Schedules.

We have audited the accompanying financial statements and supplementary information (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements) which comprise:

— the statement of financial position as at 31 March 2020;

— the statements of comprehensive income, changes in equity and cash flows for the year then ended;

— notes, including a summary of significant accounting policies and other explanatory information; and

— the information that is required to be disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order.

## Basis for Opinion

We conducted our Audit in accordance with International Standards on Auditing (New Zealand) (ISA's (NZ)). We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Bank in accordance with Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board and the

International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our responsibilities under ISA (NZ) are further described in the auditor's responsibilities for the audit of the financial statements (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements) section of our report.

Our firm has also provided other services to the Bank in relation to risk and regulatory advisory services. Subject to certain restrictions, partners and employees of our firm may also deal with the Bank on normal terms within the ordinary course of trading activities of the business of the Bank. These matters have not impaired our independence as auditor of the Bank.

## Materiality

The scope of our audit was influenced by our application of materiality. Materiality helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole. The materiality for the financial statements as a whole was set at $3.22 million determined with reference to a benchmark of the Bank's Profit before tax. We chose the benchmark because, in our view, this is a key measure of the Bank's performance.

## Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements in the current period.  We summarise below those matters and our key audit procedures to address those matters in order that the shareholder as a body may better understand the process by which we arrived at our audit opinion. Our procedures were undertaken in the context of and solely for the purpose of our statutory audit opinion on the financial statements as a whole and we do not express discrete opinions on separate elements of the financial statements

### Key changes in the assessment of audit risks

### Covid-19

The Covid-19 pandemic has created significant additional risks across a number of areas of the business, particularly the assessment of the provision for credit impairments.  All forward looking assumptions are inherently more uncertain during these unprecedented times. While the key audit matter "Provisions for Credit Impairment", detailed below, is unchanged from last year, the underlying audit risk has increased which impacted the extent and nature of audit evidence that we had to gather.

### The key audit matter

### Provision for credit impairment

Refer to Note 16 to the Disclosure Statement.

The collective and specific expected credit loss ("ECL") provision is a key audit matter owing to the financial significance of loans and advances and the high level of judgement and complexity involved in estimating impairment provisions against these loans.

Due to COVID-19 and New Zealand entering into a Government imposed lockdown just prior to year-end, this judgement and complexity is heightened in respect of assessing the immediate impact of the pandemic and the path to recovery from the lockdown. This is reflected in the increased uncertainty in relation to judgements about future cashflows, security values and the underlying assumptions made to estimate expected credit losses.

For loans that have been identified as impaired, judgement is involved primarily with estimating the timing and proceeds from the future sale of assets securing the loans.

For loans not currently impaired, judgement is required as the collective impairment provision is forward-looking and involves estimating the likelihood that these loans will default in the future and the amount of loss if they do default.

### How the matter was addressed in our audit

Our audit procedures for the specific and collective provision for credit impairment included:

**Provisions against specific individual loans (specific provision)**

- Testing of lending related controls, including testing the approval of new lending facilities and monitoring of loans in arrears.
- Re-performing the specific impairment provision calculations for a sample of individual loans. We challenged the Bank's assessment of loan recoverability and the impact on the provision. To do this, we reviewed the information on the Bank's loan file including third party valuations, discussed the case with management and performed our own assessment of recoverability;
- Performed credit assessments of a sample of loans, focusing on larger exposures, areas of emerging risk and loans in arrears, to determine whether the loans have been appropriately monitored and provided for if necessary.

**Provisions estimated for the loan portfolio as a whole (collective provision)**

- Assessing the Bank's methodology used in the Expected Credit Loss (ECL) model to calculate the collective provision against the requirements of NZ IFRS 9: *Financial Instruments* ("NZ IFRS 9") and industry practice;
- Testing the accuracy of key inputs into the ECL model by checking a sample of balances to source systems and historic data (both internal and external data sources);
- Assessing forward-looking economic assumptions and the development of economic scenarios against external economic information and the application into the ECL model. Given the degree of uncertainty in respect of forecast macroeconomic inputs in a COVID-19 scenario, this included benchmarking managements estimates to a range of different market forecasts;
- Testing the accuracy of the model calculations;
- Assessing the Bank's significant accounting policies and disclosures in the financial statements against the requirements of NZ IFRS 9;

## The key audit matter

## Operation of IT systems and controls

The Banking Group is heavily dependent on IT systems for the processing and recording of a large volume of transactions each day, as well as other core banking activity. Given this, there are some areas of our audit where we seek to place reliance on IT systems, automated controls, and system generated reports. The ability to rely on IT is dependent on the Bank's General IT environment being designed, implemented, and operating effectively. This includes controls relevant to system changes and development, IT operations, developer and user access controls.

### How the matter was addressed in our audit

Our audit procedures, for the Bank, amongst others, included:

- Gaining an understanding of business processes, key controls, and IT systems relevant to our planned audit approach;
- Testing the design and operating effectiveness of the General IT control environment, including core banking IT systems, in-scope automated controls, and in-scope reports; and
- Evaluating General IT controls relevant to IT system changes, IT operations, developer and user access controls.

## Other information

The Directors, on behalf of the Bank, are responsible for the other information included in the Bank's Annual Report. Other information includes the Highlights, Messages from Chair and CEO and information required to be included in the Disclosure Statement in accordance with Schedule 2 of the Order and is included on pages 2 to 37 and 91 to 95. Our opinion on the disclosure statement does not cover any other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the disclosure statement our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the disclosure statement or our knowledge obtained in the audit or otherwise appears materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## Report on other legal and regulatory requirements

In accordance with the requirements of clauses 2(1)(d) and 2(1)(e) of Schedule 1 of the Order, we report that:

- we have obtained all the information and explanations we have required; and
- in our opinion, proper accounting records have been kept by the Bank, as far as appears from our examination of those records.

## Responsibilities of Directors for the financial statements and supplementary information (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements)

The Directors, on behalf of the Bank, are responsible for:

- the preparation and fair presentation of the financial statements in accordance with Clause 24 of the Order, NZIFRS and International Financial Reporting Standards;
- the preparation and fair presentation of supplementary information (excluding the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements), in accordance with Schedules 2, 4, 7, 13, 14, 15 and 17 of the Order;
- implementing necessary internal control to enable the preparation of financial statements that are fairly presented and free from material misstatement, whether due to fraud or error; and
- assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.

## Auditor's responsibilities for the audit of the financial statements and supplementary information (excluding supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements)

Our objective is:

- to obtain reasonable assurance about whether the disclosure statement, including the financial statements prepared in accordance with Clause 24 of the Order, and supplementary information (excluding the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements), in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order as a whole is free from material misstatement, whether due to fraud or error; and

— to issue an independent Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (New Zealand) will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial statements.

A further description of our responsibilities for the audit of these financial statements is located at the External Reporting Board (XRB) website at:

https://www.xrb.govt.nz/assurance-standards/auditors-responsibilities/audit-report-2/

This description forms part of our independent auditor's report.

## Review conclusion on the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements

Based on our review, nothing has come to our attention that causes us to believe that the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements, disclosed in notes18(d) and 19 to the disclosure statement, is not, in all material respects:

i. prepared in accordance with the Bank's conditions of registration; and

ii. disclosed in accordance with Schedule 9 of the Order.

We have reviewed the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements, as disclosed in notes 18(d) and 19 of the disclosure statement for the year ended 31 March 2020. The supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements comprises the information that is required to be disclosed in accordance with Schedule 9 of the Order.

## Basis for conclusion on the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements

A review of the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements 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, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. Our responsibilities under that standard are further described in the Auditor's Responsibilities for the Review of the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements section of our report.

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

## Responsibilities of Directors for the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements

The directors are responsible for the preparation of supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements that is required to be disclosed under Schedule 9 of the Order and prepared in accordance with the Capital Adequacy Framework (Standardised Approach) (BS2A) and described in notes 18(d) and 19 to the disclosure statement.

## Auditor's responsibilities for the review of the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements

Our responsibility is to express a conclusion on the Capital Adequacy and Regulatory Liquidity Requirements based on our review. We conducted our review in accordance with NZ SRE 2410 Review of Financial Statements Performed by the Independent Auditor of the Entity ("NZ SRE 2410") issued by the New Zealand External Reporting Board. As the auditor of TSB Bank Limited, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements, and plan and perform the review to obtain limited assurance about whether the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements is, in all material respects:

- prepared in accordance with the Bank's conditions of registration; and
- disclosed in accordance with Schedule 9 of the Order.

A review of the supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

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 supplementary information relating to Capital Adequacy and Regulatory Liquidity Requirements disclosures.

## Use of this independent auditor's report

This independent auditor's report is made solely to the shareholder as a body. Our work has been undertaken so that we might state to the shareholder those matters we are required to state to them in the independent auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the shareholder as a body for our work, this independent auditor's report, or any of the opinions or conclusions we have formed.

The engagement partner on the audit resulting in this independent auditor's report is Brent Manning.

For and on behalf of

KPMG

KPMG
Wellington

3 July 2020

# Abbreviations

**The following abbreviations are used throughout the report.**

| | |
|---|---|
| AT1 | Additional Tier 1 |
| CET1 | Common Equity Tier 1 |
| ECL | Expected credit loss |
| ED | Exposure at default |
| FVOCI | Fair value through other comprehensive income |
| FVPL | Fair value through profit or loss |
| IRR | Interest rate risk |
| IDR | Issuer default rating |
| LVR | Loan-to-valuation ratio |
| LGD | Loss given default |
| NII | Net Interest Income |
| NZ IAS | New Zealand equivalent to International Accounting Standards |
| NZ IFRS | New Zealand equivalents to International Financial Reporting Standards |
| PD | Probability of default |
| RBNZ | Reserve Bank of New Zealand |
| RCD | Registered Certificate of Deposits |
| SICR | Significant increase in credit risk (SICR) |
| SPPI | Solely payments of principal and interest on the principal amount outstanding |
| UCO | Under criteria observation |

# Directory

### Directors

J.J. (John) Kelly, Chair
M.I. (Murray) Bain, MCom (Hons), BSc, C.F.Inst.D, Deputy Chair
M.A. (Anne) Blackburn, MA, BA
N. (Natalie) Pearce, BCom
P.M. (Peter) Schuyt, BCom, C.F.Inst.D
D.J. (Dion) Tuuta
H.F. (Harvey) Dunlop, BCom (Ag)
P.S. (Peter) Dalziel, MBA, C.M.Inst.D

### Executive Management

D. (Donna) Cooper, BBus, MA, MIntBus, CEO
R.G. (Roddy) Bennett, BSc, CA, GM Finance
H. (Herman) Visagie, BCom, LLB, Chief of Staff & General Counsel
J.S. (Justine) St John, BCom, GM Marketing & Customer Experience
H. (Hamish) Archer, BE (E&E), GM Technology
C. (Chris) Boggs, BCom, MBM, GM People & Strategy
T. (Tracey) Berry, PGDPFP, GM Customer Solutions & Service
S. (Sean) Edwards , MBA, MHSc (Psych), GM Risk (Acting)

### Registered Office

Level 5, TSB Centre, 120 Devon St East, New Plymouth, 4310

### Principal Solicitors to the Company

Auld Brewer Mazengarb & McEwen
9 Vivian Street, New Plymouth

### Auditor

KPMG
10 Customhouse Quay, Wellington

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TSB