

Southland Building Society
Annual Report & Financial Summary 2019



Highlights



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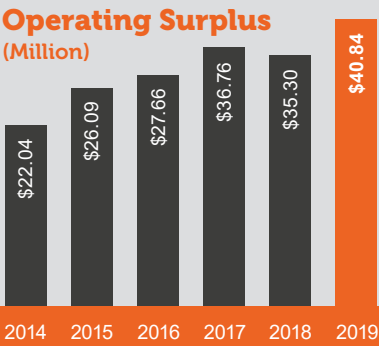
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Chairman's Report

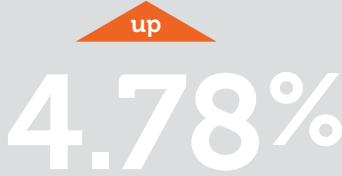
On behalf of the board, I'm extremely proud to present this annual report in our 150th year.



Operating Surplus
(Million)



Loan Advances



John Ward, Chairman

“I want to see people have security... I want to see humanity secure against poverty, secure in illness or old age.”

Michael Joseph Savage

Reaching 150 is a most extraordinary and rare achievement for any entity. As a ‘small fish in a big pond’ we have been up against so many challenges and naysayers and yet here we still are – bold and effective in a challenging environment.

History shows it's not about being the biggest player in a specific environment, but about striving to be the best. As our results show, we continue to be the little bank that capably performs within the markets that we operate in.

SBS Group (SBS Bank, FANZ, Finance Now, Southsure) has again performed strongly in extremely competitive markets. Our operating surplus of \$40.8 million was up on the 2018 result by 15.7%. That is, indeed, a most pleasing result. Members' Equity is subsequently up \$29.4 million or 10% on last year to \$324 million.

Our board has enjoyed connecting with Members at our 150th branch celebrations. It is made abundantly clear to us on these occasions that our people are the most important aspect in the SBS mix. We acknowledge with appreciation and gratitude the efforts of our Executive and staff over a challenging year. The way they, and those before them, have lived our Values has enabled SBS to emerge victoriously through 150 years and places us in a position to face the future with confidence.

I'd like to acknowledge the Directors for their contributions over the past year. There's no doubt each board member is committed to our future. As the complexity of the business grows, it is reassuring to have them all heavily involved in governance matters. Our subsidiaries are all major entities as are various committees that pertain to Audit, Risk and IT. You can be assured these people don't shirk their responsibilities, which are significant.

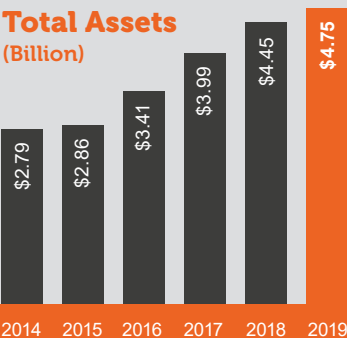
During the year Frank Spencer and Jeff Grant retired from the board. Both had significant roles within the SBS Group. Their commitment, capability and experience have been appreciated by other board members during their time and we all wish them well with their future endeavours. Former TSB Bank chief executive Kevin Murphy and former South Port chief executive Mark O'Connor have been appointed to the board and we look forward to their contributions.

The new board is working well, and our united goal remains the same: a strong future of profitable and sustainable growth for SBS that provides significant benefits for Members.

John Ward, Chairman

CEO's Report

In an ever-changing world, it is rare to celebrate 150 years. Marking our 150th birthday in our branches throughout the country has provided us with great opportunities for celebration, as well as reflection on how far SBS Bank has progressed.



Shaun Drylie, Group CEO

“True success is waking up every day with the feeling that the work you are doing will outlast you.”

Simon Sinek

We've reflected on the Values that provided the foundation for the organisation and recognised they're as important now as they were on that dark and stormy night in Invercargill on 23 March, 1869 when James Walker Bain and a group of passionate Southlanders founded this organisation.

Resilience has been a key component of our history – whether that's our creation, the various economic challenges or the proposed takeover by Westpac in the early 1990s – and it's clear that change and disruption will continue to be a driver well into the next 150 years.

The banking industry continues to experience change, but we're well placed to deal with that. The focus on conduct is intensifying, which again highlights the importance of Values to an organisation like SBS Bank.

The past 12 months have been significant. We launched our credit card through collaboration with our subsidiary Finance Now, introduced a digital onboarding option for term investments and the development of staff-assisted identification, as well as reducing the number of paper statements we send.

We continue to be involved in community sponsorship activities – Ronald McDonald Houses in Christchurch and Invercargill, the Volunteer Community at the NZ Golf Open, and the SBS Bank Tour of Southland are three that spring to mind – as we look to support the good work being done by our partners.

I'm excited about SBS Bank's future. We will build on our authentic service and continue to find ways in which you can interact with us in the way you want, to achieve the outcomes you desire.

In our 150th year, it's important to recognise and thank you, our Members. Everything we do is done with you in mind, but your support and loyalty over that time is equally powerful, so I thank you for your trust in this great institution.

Finally, I must thank every one of our team members, both past and present, for the work they do every day to ensure your bank continues to deliver on the promises it made 150 years ago.

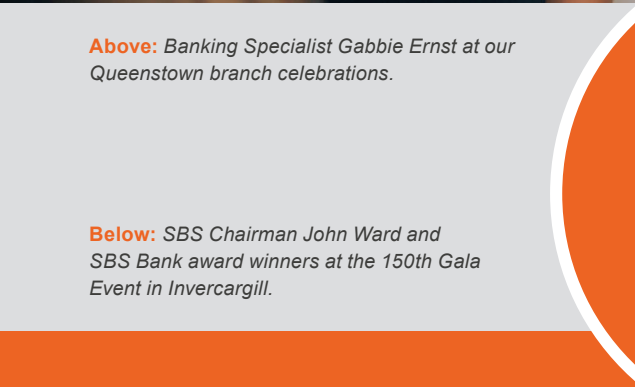
Shaun Drylie, Group CEO



Above: Banking Specialist Gabbie Ernst at our Queenstown branch celebrations.



Above: SBS Bank team member 150th Gala Event in Invercargill.



Below: SBS Chairman John Ward and SBS Bank award winners at the 150th Gala Event in Invercargill.



Your Board of Directors



Left to right: Mike Skilling, Kathryn Ball, Kevin Murphy, John Ward, Joe O'Connell, Mark O'Connor, Greg Mulvey, Anne McLeod.

John Ward BCom, Hon LLD (Otago), FCA, CFInstD
Chairman

John is a chartered accountant who stepped aside from public practice after being a partner and board member of KPMG and its ancillary practice Ward Wilson. He is a Fellow of the Institute of Chartered Accountants of Australia and New Zealand and a Chartered Fellow of the Institute of Directors.

He has served on the SBS Bank Board since 2002 and has been chairman since 2012. He chairs the wholly owned SBS subsidiary Finance Now, the Appointment Committee and is a member of both the Audit & Risk and Remuneration committees.

He currently chairs H&J Smith Holdings, Otago Innovation and the University of Otago Foundation Trust. He is a member of various other boards and was also University of Otago Chancellor from 2009 to 2017.

Kathryn Ball B Com, FCA, CMInstD
Deputy Chair

Kathryn is a chartered accountant with more than 30 years' experience in public practice. She is currently a self-employed consultant, principally to McIntyre Dick, Business Advisors and Chartered Accountants, based in Invercargill.

Kathryn was a partner/principal in McIntyre Dick and Partners for many years, and prior to that a partner in PricewaterhouseCoopers and Coopers and Lybrand.

A director of SBS Bank since 2006, she has been deputy chair since 2016 and chairs the Audit & Risk Committee. She is also a director of Stadium Southland. Kathryn served for several years as a Southern Institute of Technology (SIT) councillor, chairing the Audit & Finance Committee and serving a period as deputy chair. She was involved with SIT at the time the innovative "Zero Fees" scheme was introduced.

Kathryn is a fellow of Chartered Accountants Australia and New Zealand, and a Chartered Member of the Institute of Directors.

Mike Skilling BAgrSci, PGDipBank, CMInstD

Mike joined the SBS Board in August 2014. He is an independent director of various companies spanning funds management, insurance, mortgage broking, dairy/sheep/beef/crop/horticultural farming, consumer finance and early learning/preschool.

Mike has in-depth experience in retail, private, rural and business banking together with insurance, managed funds and finance companies. In previous roles, he has led both the Agribusiness and Business Banking arms of BNZ including Small Business, Medium/Large Business, International Trade, Property, Plant and Machinery Finance and Private Banking.

He is a Senior Fellow of the Financial Services Institute of Australasia (FINSIA) and a Chartered Member of the New Zealand Institute of Directors.

Kevin Murphy CA, FCAANZ, CMInstD

As managing director/CEO of TSB (previously TSB Bank), Kevin oversaw the bank's ambitious New Zealand-wide growth programme that had a focus on both branch presence and digital offerings.

He worked for more than 38 years at TSB, holding various roles that included accounting assistant, chief accountant and financial services manager before being appointed CEO in 2010.

Appointed to the SBS Board in November 2018, Kevin is also a director of Finance Now, Augusta Capital (chairing the Risk & Compliance Committee), and Adele Senior Living. He has been a trustee on Venture Taranaki since 2013, and a board member of the Taranaki Rugby Football Union since 2018.

He has continued to serve his community and has been a board member of New Plymouth Operatic since 1987 (also a life member), is a business advisor and life member of Musical Theatre New Zealand, chair of the New Plymouth Opera House Friends, and a committee member of the Dame Malvina Major Foundation.

Joe O'Connell B.Com, FCA, MInstD

A Fellow of the Institute of Chartered Accountants and a Member of the Institute of Directors, Joe joined the SBS Bank Board in 2017. He is an experienced director with a financial background that spans transportation, ready-mix concrete, timber processing, exploration piling and drilling, commercial property, fuel distribution, growing media, airports and electrical distribution networks.

Joe was Invercargill Airport chairman (2011-2016), overseeing the redevelopment of all land-side and terminal facilities as well as negotiating commercial terms for the company to secure its long-term viability.

He spent six years as general manager of finance for H W Richardson Group and during the past 12 years has focused on directorships and management consulting work with a large amount of time being spent with the K G Richardson group of companies, which has extensive interests in timber processing, property, drilling and transportation.

Joe currently sits on several boards, including Electricity Invercargill, PowerNet and Southfuels.

Mark O'Connor BCom, FCAANZ, FNZIM

Mark is a qualified accountant who has primarily been involved in senior management roles in the New Zealand port sector for more than 25 years. He is the former CEO of NZX-listed company South Port NZ, a position he held for 18 years.

Appointed to the SBS Board in August 2018, Mark is also chairman of private equity fund Invest South and a director of Calvary Hospital Southland. He is also chairman of the Assurance & Risk Committee for NZ Customs and has been active in the Southland Regional Development (SoRDS) programme. He currently chairs the SoRDS Aquaculture Working Group and is a member of the SoRDS Transitional Advisory Group.

Greg Mulvey BCom, FCA, FNZIM

Greg is a qualified accountant with 40 years' experience in the corporate sector including 30 years as general manager of Invercargill Licensing Trust.

Appointed to the SBS Bank Board in 2004, he is chair of both the Remuneration and IT committees and is a member of the Audit & Risk Committee as well as a trustee of SBS Charitable Trust. Greg is also a director of Funds Administration New Zealand.

He is a trustee of the Southland Indoor Leisure Centre Charitable Trust, the entity that developed and owns ILT Stadium Southland.

Anne McLeod LLB, BCom, MInstD

Anne is a partner in the corporate commercial team at Anderson Lloyd in Dunedin.

Her legal expertise includes banking law, mergers and acquisitions and structuring advice. Anne also advises Anderson Lloyd's clients who are listed on the NZX and regularly advises on the offer of financial products. Given this experience she is a member of the Due Diligence Committee in relation to the bank's Capital Bond issues.

She joined the SBS Board in 2015 and chairs the bank's subsidiary Southsure Assurance. Anne is a Member of the Institute of Directors, RITANZ (Restructuring Insolvency and Turnaround Association New Zealand) and the Banking and Financial Services Law Association.

Subsidiaries

Over the past 12 months SBS' subsidiary companies, Finance Now, FANZ and Southsure, have continued to perform well, recording solid contributions for the SBS Group.

These subsidiary companies have increased in value significantly over the past 16 years with a combined enterprise value now in excess of \$210 million, based on independent valuations of these businesses conducted in March 2019.

We are pleased with the value generated within each of these businesses, representing up to \$133 million over the net assets of these entities. More than 98% of this value is attributable to Members of SBS Bank.

The \$324 million of equity attributable to Members as disclosed in the financial statements, excludes the revaluation of our subsidiaries.



Phil Ellison BMS
Finance Now CEO

Our focus throughout the 2018/2019 year was heavily weighted on development of our credit card products, culminating at the end of the financial year with the successful launch of the SBS Credit Card and development of long-term Interest Free integrated into our Purple Visa Card.

The SBS Credit Card involved great collaboration between Finance Now and SBS to deliver the card under tight deadlines on 19 March. This card will

enhance the SBS Bank product suite to members and new customers.

In parallel to the development of SBS Credit Card, the Finance Now team were also busy enhancing the existing Purple Visa Card to include an Interest Free product exclusively for Noel Leeming stores. This new offering was successfully launched in early April and will see significant growth in our Purple Visa customer base over the coming years.

Even with all these large project areas of focus, Finance Now's other areas of business continued to grow and deliver great results across all of our diversified product lines of Personal Loans, Retail, Motor Vehicle Dealer Finance, Retail Finance, Revolving Finance, Business Finance, and now Credit Card. The cumulative results of these areas enabled us to achieve our best financial profit year in our 18 years of trading.

Over the coming financial year, we will be enhancing our product offerings and processes to ensure we evolve to our customers' needs. This will ensure growth within our target markets as we deepen our customer experience and engagement.



Graham Duston NCFS, B.Com, P.G Dip, AFA
FANZ CEO

FANZ produced another strong year in terms of its financial results in the 12 months to March 31. This was driven off the back of continued strong growth in funds under management, solid returns for investors and strong financial management.

FANZ was pleased to see its total funds under management exceed \$1.25 billion and reach more than 20,000 clients over the financial year. FANZ also produced a record profit, which contributed to the Group's strong result.

FANZ continued to receive strong growth in the Lifestages KiwiSaver Scheme and the company continues to believe the KiwiSaver proposition will be a key part of this business now and for many years to come. KiwiSaver continues to be the cornerstone in helping people achieve financial security in retirement and to get that first step on the home ownership ladder.

The FANZ Private Wealth proposition continues to find favour with investors. During the year, we bought out our joint

venture partner, Staples Rodway, in the advice business, Staples Rodway Asset Management (SRAM). SRAM has been successfully integrated into the FANZ Private Wealth business, which means we are truly a nationwide Wealth business with staff from Invercargill to Auckland. FANZ Private Wealth continues to be one of the few Wealth firms in New Zealand that has no investments in receivership, default or under a liquidity moratorium.

We do note the increased compliance load that will arise as a result of the new

Adviser license regime, which will take effect from 1 April 2020. This compliance load will impact the entire FANZ business as the various parts of the business will be impacted by the requirement to obtain the relevant license from the FMA.

Our quality focus has meant FANZ continues to be one of New Zealand's fastest growing financial advisory firms. FANZ management is confident the philosophy of quality, a focus on delivering consistent returns and "no surprises" for investors will mean a bright future for all.



David Newman BCom, DipBank
Southsure Assurance CEO

Southsure recorded continued satisfactory growth in premium income and reported profit for the year ending 31 March 2019, driven by continued growth in core business lines and the distribution partnership established in March 2018 with NZCU South.

The company's growth was also supported by an increased contribution from its associate company Abbotts Insurance Brokers following its merger with I C Frith. However, the year was dominated by the joint Reserve Bank and Financial Markets Authority conduct and culture reviews of

the banking and insurance industries. These reviews were prompted by the findings of the Australian Royal Commission of Inquiry into Misconduct in the Banking, Superannuation and Financial Services Industry in Australia.

Considerable internal resources were necessarily diverted to participate in and respond to these reviews. While the Insurance Industry Review found little evidence of systemic misconduct, it did highlight major weaknesses in insurers' systems, processes and controls for managing conduct risks. As a result, the

regulators have given the industry clear expectations and definitive timeframes to improve the management of conduct and culture risks.

Significant industry change will flow from these reviews. Implementing this change will dominate developments and workstreams over the coming year as insurers focus on ensuring they have improved compliance systems and processes in place to be satisfied they are delivering consistently good customer outcomes by managing conduct and culture risks adequately.

Operationally, economic conditions continued to be challenging with the low interest environment prevailing throughout the year and further falls in interest rates negatively impacting results by reducing investment earnings and necessitating higher transfers to Policy Liability Reserves.

Confirming the company's strong Capital Adequacy and Solvency position, Southsure's Investment Grade BBB+ Insurer Financial Strength Rating was reaffirmed in November 2018 by Fitch Ratings Agency.



Corporate Responsibility



“SBS has a duty and a desire to consider the wider community and the part the organisation can play as a good corporate citizen.”

Shaun Drylie Group CEO

Above: SBS Group CEO Shaun Drylie and Queenstown Lakes District councillor John MacDonald with the Housing Affordability Taskforce report.

SBS is committed to putting our Members' needs first and ensuring their banking experience with us provides good outcomes for them. We have a duty and a desire to provide the best products and service so that all Member interactions are easy, effortless and enjoyable.

But SBS also has a duty and a desire to consider the wider community and the part the organisation can play as a good corporate citizen.

We are committing to do more through our Corporate Social Responsibility (CSR) and sponsorship programmes and to how we can support those people or organisations doing good things in the communities we operate in.

Our background is obviously in “bricks and mortar” – we’ve been helping Kiwis get into homes for 150 years. That’s why we partner with the likes of the Queenstown Lakes Community Housing Trust to help families find homes, when the thought of home ownership had previously been unlikely. The Welcome Home Loan, offered by SBS and supported by Housing New Zealand, is an initiative to make access to home ownership even easier for New Zealanders. Last year we helped Kiwis into 1,220 new homes through this scheme.

Our Group CEO, Shaun Drylie, is chairman of the Southland Housing Action forum, a group of people and organisations committed to ensuring the housing needs of Southlanders, across all spectrums, are understood and addressed.

In the past 12 months, SBS has rolled out a resilience and a personal health and well-being programme designed to provide tools to enable our team members find that right work-life balance. We believe it will bring value and help our team. While that’s been an internal project, we believe there are some wider opportunities to help our Members navigate their way around the areas of financial literacy and good conduct with money.

This is all predicated on being a Values and Member-based organisation that contributes to our Members and the communities they belong to.

Finally, one of our major projects this year has been reducing significantly the amount of paper statements that are printed.

The Future

There are five “planks” to the strategy that guide our direction, so over the coming year we will:

- 1

Strengthen our brand position as a genuine NZ bank focused on sustainable return and support of the communities we operate in. In essence doing more good stuff, as well as telling NZ about what we do.
- 2

Continue to make it easier for Members to access “their” bank, physically, virtually, digitally – ‘any channel any time’.
- 3

Refine our product offer and service to ensure great Member outcomes. This includes ensuring products and services are fit for your needs and introducing new and simplified products. A key focus for this coming year will be addressing everyday transaction banking needs.
- 4

Continue to leverage the power of our group through offering competitive solutions that meet your needs in wealth accumulation, personal and property protection and consumer finance.
- 5

Improve our internal processes and infrastructure to make SBS faster and nimbler.

We’ve had 150 years to cement the foundations for SBS Bank. Our key organisational themes of Simplicity, Benefit and Synergy (SBS) remain at the core of everything we do, with our overall aim to deliver a great banking experience to our Members.

Simplicity is based on our commitment to making banking easy to use, easy to understand and easy to do business with. Benefit is about giving value to Members through our products and services and providing tangible Member benefits. Our focus on Synergy allows us to leverage the strength of our subsidiaries by offering a full suite of banking services such as insurance products, investment options and personal finance.

Last year we told you we were planning to expand our digital and product offering to make banking with SBS easier, more accessible and more appealing. And we’ve delivered on this promise: we’ve launched a credit card (orange, of course), and made it possible for Members to apply for and open term investments online.

Now we’re looking to capitalise on the knowledge obtained from those projects and use it elsewhere among our products – we are working on a major project to introduce same-day inter-bank payments, meaning money moved in and out of SBS Bank will be accessible in the same day as opposed to waiting for overnight processing.

Notwithstanding an ever-increasingly competitive banking environment, as well as external regulatory forces and changes, SBS Bank’s strategy largely remains unchanged with the focus to reinforce and deliver on our core purpose of providing sustainable value to Members.



Southland Building Society Summary Financial Statements
Summary Income Statement – Banking Group for the year ended 31 March 2019

	31/03/19 \$000	31/03/18 \$000
Interest income	246,803	225,417
Interest expense	26,191	25,761
Dividends on redeemable shares	104,851	93,631
	131,042	119,392
Net interest income	115,761	106,025
Net fee and commission income	24,450	21,188
Other income	12,369	10,601
Total operating income	152,580	137,841
Operating expenses	96,299	87,596
Provision for credit impairment	15,443	14,920
Operating surplus	40,838	35,298
Net gain/(loss) from financial instruments at fair value through profit or loss	193	76
Share of associates and joint ventures profit net of tax	1,202	1,066
Surplus before income tax	42,233	36,440
Less income tax expense	11,415	9,777
Net surplus	30,818	26,663
Attributable to:		
Members' interests	30,503	25,801
Non-controlling interests	315	862
	30,818	26,663

Summary Statement of Comprehensive Income – Banking Group for the year ended 31 March 2019

Net surplus for the year	30,818	26,663
Other comprehensive income		
Net change in reserves, net of tax	(1,599)	2,464
Total comprehensive income for the year	29,219	29,127
Attributable to:		
Members' interests	28,904	28,281
Non-controlling interests	315	846
	29,219	29,127

Summary Statement of Changes in Equity – Banking Group for the year ended 31 March 2019

Equity at beginning of the year	296,997	274,918
Balance adjusted for adoption of accounting standards	490	-
Net surplus for the year	30,818	26,663
Other comprehensive income for the year	(1,599)	2,464
Total comprehensive income for the year	29,219	29,127
Dividends	(210)	(357)
Change in capital of non-controlling interests	(1,163)	(6,691)
Total equity at end of the year	325,333	296,997
Equity represented by:		
Revaluation reserves	(6,176)	(4,708)
Retained earnings	330,536	299,707
Total equity attributable to members' interests	324,360	294,999
Non-controlling interests	973	1,998
Total equity at end of the year	325,333	296,997

Southland Building Society Summary Financial Statements
Summary Statement of Financial Position – Banking Group as at 31 March 2019

	31/03/19 \$000	31/03/18 \$000
Assets		
Liquid assets and securities	686,451	573,557
Advances to customers	3,977,488	3,796,045
Other assets	90,579	85,608
	4,754,518	4,455,210
Liabilities		
Redeemable shares	3,236,987	3,087,614
Deposits from customers	144,106	145,716
Commercial paper	298,417	278,521
Due to other financial institutions	538,694	486,538
Subordinated redeemable shares	132,003	88,345
Other liabilities	78,978	71,479
	4,429,185	4,158,213
Equity		
Attributable to members of the society	324,360	294,999
Attributable to non-controlling interests	973	1,998
	325,333	296,997

Summary Statement of Cash Flows – Banking Group for the year ended 31 March 2019

Net cash flows provided by/(used in) operating activities	122,537	88,632
Net cash flows provided by/(used in) investing activities	(74,413)	(80,402)
Net cash flows provided by/(used in) financing activities	(6,569)	(11,181)
Net increase/(decrease) in cash held	41,555	(2,951)
Add opening cash and cash equivalents	97,749	100,700
Closing cash and cash equivalents	139,304	97,749



Chairman
J F Ward



Deputy Chair
K J Ball

28 May 2019

1. Accounting Policies

Southland Building Society (SBS) was established in 1869, is incorporated under the Building Societies Act 1965, and is registered as a bank under the Reserve Bank of New Zealand Act 1989. The summary financial statements presented here are consolidated statements for the reporting entity of the Banking Group comprising SBS and its subsidiaries.

These summary financial statements have been prepared in compliance with FRS-43: Summary Financial Statements and comply with New Zealand Generally Accepted Accounting Practice (NZ GAAP) as it relates to summary financial statements. The specific disclosures included in the summary financial statements have been extracted from the full financial statements dated 28 May 2019. The full financial statements from which the summary financial statements have been produced have been audited by KPMG, who expressed an unmodified opinion in relation to those financial statements as at 29 May 2019. These summary financial statements have been examined by KPMG for consistency with the full financial statements.

Users of the summary financial statements should note that the information contained therein cannot be expected to provide as complete an understanding as provided by the full financial statements of the Banking Group.

Users who require additional information are encouraged to access the SBS Disclosure Statement and Annual Financial Statements on the SBS website at www.sbsbank.co.nz. Alternatively a hard copy of the SBS Disclosure Statement and Annual Financial Statements can be requested by any person and will be dispatched within two working days after the day on which the request is made at no charge.

The full financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 2013 and under 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 and the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended). The financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB).

The functional and presentation currency of the Banking Group is New Zealand dollars. All amounts contained in the summary financial statements are presented in thousands of New Zealand dollars, unless otherwise stated.

All accounting policies are consistent with those used in previous periods, except for the implementation of NZ IFRS 9 Financial Instruments and NZ IFRS 15 Revenue from Contracts with Customers. The effect of implementation of these accounting standards are set out in the full financial statements.

2. Critical Estimates and Judgements Used in Applying Accounting Policies

The full financial statements upon which the summary financial statements are based have been prepared in accordance with stated accounting policies which are based on New Zealand equivalents of International Financial Reporting Standards (NZ IFRS) and other authoritative accounting pronouncements. Notwithstanding the existence of relevant accounting standards, there are a number of critical accounting treatments which include complex or subjective judgements and estimates that may affect the reported amounts of assets and liabilities. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

An explanation of the judgements and estimates made by the Banking Group in the process of applying its accounting policies, that have the most significant effect on the amounts recognised in the financial statements are set out in the full financial statements.

3. Risk Management Policies

SBS's objective is to appropriately manage all the risks that arise from its activities. SBS does not naturally seek treasury and financial risk from its involvement in the financial markets and consequently minimises risks wherever possible. Reviews of risk management policies, systems and reporting are conducted on a regular basis.

Risk Governance Structure

The Board has responsibility for reviewing all aspects of risk management. The Board receives comprehensive monthly reporting covering each area of risk management. In addition SBS has specific policies in relation to liquidity and capital management which contain trigger points at which Board involvement is required. The following committees also report into the Board.

Audit and Risk Committee - responsible for overseeing the effectiveness and integrity of the internal control environment and the quality of financial information presented to the Board;

Lending Committee - responsible for reviewing and approving all lending proposals in excess of \$5 million;

IT Committee - responsible for monitoring and reviewing risks associated with IT and for formulating and developing SBS's IT strategy;

Asset and Liability Committee (ALCO) - responsible for all aspects of balance sheet risk management and strategy including interest rate, liquidity, funding, credit and margin;

Credit Risk Committee (CRC) - responsible for monitoring and reviewing exposure to credit risks in SBS's lending portfolios;

Operational Risk Committee (ORC) - responsible for monitoring and reviewing exposure to operational risks arising from SBS's day to day activities;

Internal Audit - SBS's internal audit function conducts independent reviews that assist the board of directors and management to meet their statutory and other obligations. The internal audit function has been carried out by the Dunedin based firm of Chartered Accountants, Deloitte.

Liquidity risk management

Liquidity risk is the risk that, under certain conditions, cash outflows can exceed cash inflows in a given period. Liquidity risk is managed on a cash flow mismatch and also core funding basis. To meet both expected and unexpected patterns in operating cash flows, SBS maintains a stock of core liquid assets to adequately meet day to day operational requirements. This includes committed wholesale funding facilities and utilisation of securitisation vehicles. The Banking Group's liquidity risks are governed by a Board approved liquidity strategy that defines policy, systems and procedures for measuring, assessing, reporting and managing liquidity. This also includes a formal contingency plan for dealing with a liquidity crisis. This also meets the RBNZ liquidity policy requirements.

Credit risk management

Credit risk is the risk of loss arising from the non-performance of a counterparty to an instrument or facility. Credit risk arises when funds are extended, committed, invested or otherwise exposed through contractual arrangements, and encompasses both on and off-balance sheet instruments. Credit risk is controlled through a combination of approvals, limits, reviews and monitoring procedures that are carried out on a regular basis, the frequency of which is dependent on the level of risk. Credit risk management involves a thorough evaluation of the credit risk associated with potential borrowers, the taking of security against the loan and close ongoing monitoring of account performance. Loans which show signs of adverse performance are managed by the credit risk management function, which is responsible for the collections and recovery process. For wholesale arrangements, credit risk is managed with reference to specific limits as outlined in detailed treasury management policies and reported to the Board on a monthly basis.

Interest rate risk management

Interest rate risk is the risk of loss arising from adverse changes in interest rates. Management's objective is to produce strong and stable net interest income over time. Interest rate risk management focuses on mismatches between the repricing dates of interest bearing assets and liabilities. Interest rate risk is managed using financial instruments to manage the risks within set limits as defined by SBS treasury policy. Regular reporting of interest rate risk against limits is provided to the Board.

Currency risk management

Currency risk results from the mismatch of foreign currency assets and liabilities. The Banking Group has a policy of hedging all foreign currency borrowing into New Zealand dollars.

Operational risk management

Operational risk is the risk arising from day to day operational activities which may result in direct or indirect loss. These losses may result from failure to comply with policies, procedures, laws and regulations, from fraud or forgery, from a breakdown in the availability or integrity of services, systems and information, or damage to SBS's reputation. Examples include failure to comply with policy and legislation, human error, natural disasters, fraud and other malicious acts. SBS aims to minimise the impact of operational risks by ensuring the appropriate risk management policies, controls, systems, staff and processes are in place. Where appropriate, risks are mitigated by insurance.

4. Advances – Banking Group

	31/03/19 \$000	31/03/18 \$000
Gross advances	4,005,988	3,822,147
Provisions for credit impairment	(29,304)	(28,261)
Deferred fee revenue and expenses	804	2,159
Total net advances	3,977,488	3,796,045

5. Provision for Credit Impairment – Banking Group

	31/03/19 \$000	31/03/18 \$000
Individual provisions against advances and loans		
Balance at beginning of the year	2,420	2,841
New provisions during the year	429	1,090
Balances written off during the year	(157)	(1,371)
Recoveries / reversals of previously recognised provision	(750)	(140)
Balance at end of the year	1,942	2,420
Collective provisions against advances and loans		
Balance at beginning of the year	25,841	18,297
Adoption of accounting standard	(859)	-
Charged to income statement	2,380	1,504
Acquired in business acquisition	-	6,040
Balance at end of the year	27,362	25,841
Total provisions for credit impairment	29,304	28,261
Reconciliation of provision movements		
Bad debts written off during the year	13,081	12,466
Individual provisions	(321)	950
Collective provision	2,683	1,504
Provision for credit impairment to income statement	15,443	14,920

6. Asset Quality – Banking Group

	31/03/19 \$000	31/03/18 \$000
Advances to customers		
Neither past due or impaired	3,916,492	3,741,269
Individually impaired	3,600	6,638
Past due	86,700	76,399
Provision for credit impairment	(29,304)	(28,261)
Total carrying amount	3,977,488	3,796,045

7. Liquidity Risk – Banking Group

Liquidity risk is the risk that the Banking Group will encounter difficulty in meeting commitments associated with its financial liabilities. The Banking Group manages its exposure to liquidity risk on a cash flow mismatch and also core funding basis and maintains sufficient liquid funds to meet its commitments. The following maturity profile of liabilities, derivatives and commitments show cash flows prepared on a contractual maturity basis as at balance date. These have been created using a run-off scenario which assumes no further origination of liabilities. Further detail on this maturity profile and the contractual undiscounted maturity profile, including the assumptions underlying them, can be obtained from the full financial statements. Note that the contractual maturity profile is not indicative of future cash flows.

7. Liquidity Risk – Banking Group (continued)

Contractual maturity profile	31/03/19			31/03/18		
	Current Liabilities \$000	Non-current Liabilities \$000	Total \$000	Current Liabilities \$000	Non-current Liabilities \$000	Total \$000
Liabilities						
Redeemable shares	3,031,289	205,698	3,236,987	2,858,082	229,532	3,087,614
Other deposits	488,778	492,439	981,217	435,427	475,348	910,775
Subordinated redeemable shares	39,124	92,879	132,003	-	88,345	88,345
Other monetary liabilities	32,891	-	32,891	34,425	-	34,425
	3,592,082	791,016	4,383,098	3,327,934	793,225	4,121,159
Net derivative cash flows	(12,236)	(12,504)	(24,740)	(8,298)	2,599	(5,699)
Unrecognised loan commitments	28,255	-	28,255	30,727	-	30,727

The following table outlines the liquid investments and committed funding lines that are available to SBS to meet both expected and unexpected fluctuations in operating cash flows. Included within total liquidity are residential mortgage backed securities ('RMBS') that are eligible under the Reserve Bank of New Zealand liquidity management arrangements.

	31/03/19 \$000	31/03/18 \$000
Asset liquidity ²	663,260	530,216
Committed and undrawn funding lines	130,107	180,198
Eligible RMBS collateral (less haircut ¹)	117,252	114,516
Total liquidity	910,619	824,930

¹A haircut is a percentage that is subtracted from the par value of the assets that are being used as collateral. The size of the haircut reflects the perceived risk associated with holding the assets.

²As at 31 March 2019 investment securities of \$23.2 million (31 March 2018: \$43.3 million) that are encumbered through repurchase agreements have been excluded in the above table as they are not held for liquidity management purposes.

8. Capital Adequacy

The Banking Group's objectives in relation to the management of capital adequacy are to comply at all times with the regulatory capital requirements set out by the Reserve Bank of New Zealand (RBNZ); to maintain a strong capital base to cover the inherent risks of the business and maintain a targeted credit rating; and to support future business development and growth.

The Banking Group 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 Banking Group. The Banking Group must comply with RBNZ minimum capital adequacy ratios as determined in its Conditions of Registration which are as follows:

- Total capital ratio of the banking group is not less than 8%
- Tier 1 capital ratio of the banking group is not less than 6%
- Common equity tier 1 capital ratio of the banking group is not less than 4.5%
- Total capital of the banking group is not less than NZ \$30 million

Regulatory capital adequacy ratios are calculated by expressing capital as a percentage of risk weighted assets. Risk weighted assets are derived by assigning risk weight percentages to certain material risk categories of exposures. These exposures are measured or estimated from selected balance sheet assets and off balance sheet exposures and market contracts. It should be noted that the regulatory risk weightings may not necessarily be consistent with the loss experience of the Banking Group.

The Banking Group has adopted the Basel III methodology as per the RBNZ's "Capital Adequacy Framework (Standardised Approach)" (BS2A) document to calculate regulatory capital requirements. Basel III consists of 3 pillars - Pillar One covers the capital requirements for banks for credit, operational, and market risks. Pillar Two covers all other material risks not already included in Pillar One, and Pillar Three relates to market disclosure.

	Minimum ratio requirement	31/03/19 Unaudited	31/03/18 Unaudited
Regulatory Capital Ratios			
Common equity tier 1 capital ratio	4.50%	11.38%	10.87%
Tier 1 capital ratio	6.00%	11.41%	10.92%
Total capital ratio	8.00%	14.18%	12.84%
Buffer ratio	2.50%	5.41%	4.84%

9. Directors' Fees	31/03/19 \$000	31/03/18 \$000
Amounts received, or due and receivable by directors:		
JF Ward (Chairman)	146	144
KJ Ball (Deputy Chair)	77	73
GJ Mulvey	81	77
JJ Grant (resigned 30 June 2018)	16	67
FE Spencer (resigned 30 September 2018)	45	67
MJ Skilling	89	72
AL McLeod	77	69
AJ O'Connell (appointed 1 June 2017)	88	56
MP O'Connor (appointed 21 August 2018)	47	-
KJ Murphy (appointed 1 November 2018)	29	-
	695	625
Provision for directors' retiring allowance	24	10
GST on directors' fees	15	10
	734	645

10. Investments in Subsidiaries, Associates and Joint Ventures

On 30 June 2017, the Bank increased its shareholding in its subsidiary Southsure Assurance Limited from 80% to 90%. On 11 September 2017, the Bank increased its shareholding in its subsidiary Finance Now Limited from 95% to 100%. In accordance with International Financial Reporting Standards, as the Bank has had no change in effective control, the acquisition price was recorded through equity to reflect transactions amongst shareholders. No adjustments have been made to the fair value of the assets and liabilities of Southsure Assurance Limited or Finance Now Limited in the consolidated accounts of the Bank in accordance with IFRS, and the associated premiums (reflecting the future earnings potential of the entities) are recorded as an adjustment to equity.

Effective 11 September 2017, the Banking Group via its subsidiary Finance Now Limited, purchased 100% of the shares in The Warehouse Group Financial Services ("TWGFS"). As part of the purchase, FNL agreed to receive a "claw-back amount" and pay a "debt recovery payment". A final "claw-back amount" of \$1,480k was received on 24 August 2018. One year after completion date, the debt recovery payment was calculated based on 50% of all monies recovered on or prior to the anniversary of the completion date in respect of bad debt, net of usual fees and expenses. The final amount received for the debt recovery payment was \$59k. Due to the differences between the estimated and final payment, the final fair value of identifiable net assets has been calculated as \$18.642m, with software fair value increasing by \$2.125m and deferred tax decreasing by \$0.595m.

On 31 October 2017, the Bank increased its indirect interest in Abbott Insurance Brokers Limited by 5% to 37.5%. During January 2018, the Abbott group restructured, with a new entity established as holding entity, named Abbott NZ Holdings Limited. Abbott NZ Holdings Limited is the 100% shareholder of Abbott Insurance Brokers Limited. Southsure's shareholding diluted from 37.5% to 22.99% due to this restructure. This investment is still being accounted for as an associate company under the equity method of accounting as the Banking Group does not have control over the financial and operating policies.

During March 2018, the Banking Group established the SBS Warehouse Trust No.2, a special purpose vehicle holding securitised loans assigned from SBS and funded through wholesale funding lines.

On 13 June 2018, the Banking Group acquired via FANZ, the remaining shares of SRAM, previously held as a joint venture, for \$2.325m. FANZ obtained \$172k of identifiable net assets and \$4.013m goodwill and other intangible assets. Net cash flow relating to the transaction was \$2.229m. The fair value of the joint venture before acquisition was \$1.860m, with \$25k gain on equity interest included in other income in the income statement.

During July 2018, the Banking Group increased its shareholding in FANZ from 85% to 100%. In accordance with International Financial Reporting Standards, as the Bank has had no change in effective control, the acquisition price was recorded through equity to reflect transactions amongst shareholders. No adjustments have been made to the fair value of the assets and liabilities of FANZ in the consolidated accounts of the Bank in accordance with IFRS, and the associated premiums (reflecting the future earnings potential of the entities) are recorded as an adjustment to equity.

During August 2018 TW Money Limited changed its name to SBS Money Limited.

As at 31 March 2019, total investments in associates and joint ventures recognised by the Banking Group was \$6.9 million. Further information on investments in subsidiaries, associates and joint ventures is set out in the full financial statements.

11. Subsequent Events

There have been no material subsequent events after 31 March 2019.

Independent Auditor's Report



To the Members of Southland Building Society

Report on the summary consolidated financial statements

Opinion	
In our opinion, the accompanying summary consolidated financial statements of Southland Building Society (the Bank) and its subsidiaries (the Banking Group) on pages 10 to 16:	The accompanying summary consolidated financial statements comprises:
i. Have been correctly derived from the audited Banking Group's financial statements for the year ended on that date; and	- the summary consolidated statement of financial position as at 31 March 2019;
ii. Are a fair summary of the Banking Group's financial statements, in accordance with FRS 43 Summary Financial Statements.	- the summary consolidated income statement, statements of comprehensive income, changes in equity and cash flows for the year then ended; and
	- notes, including a summary of significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standard on Auditing (New Zealand) (ISA (NZ)) 810 (Revised), *Engagements to Report on Summary Financial Statements*.

Our firm has also provided other services to the Banking Group in relation to the review of the Banking Group's half-year Disclosure Statement, regulatory compliance, and taxation compliance. Subject to certain restrictions, partners and employees of our firm may also deal with the Banking Group on normal terms within the ordinary course of trading activities of the business of the Banking Group. These matters have not impaired our independence as auditor of the Banking Group. The firm has no other relationship with, or interest in, the Banking Group.

Use of this Independent Auditor's Report

This report is made solely to the members as a body. Our audit work has been undertaken so that we might state to the members 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 members as a body for our audit work, this report, or any of the opinions we have formed.

Responsibilities of the Directors for the summary consolidated financial statements

The Directors, on behalf of the Banking Group, are responsible for:

- the preparation and fair presentation of the summary consolidated financial statements in accordance with FRS 43 Summary Financial Statements; and
- implementing necessary internal control to enable the preparation of a summary consolidated set of financial statements that is correctly derived from the audited consolidated financial statements.

Auditor's Responsibilities for the summary consolidated financial statements

Our responsibility is to express an opinion on whether the summary consolidated financial statements are consistent, in all material respects, with (or are a fair summary of) the audited consolidated financial statements based on our procedures, which were conducted in accordance with International Standard on Auditing (New Zealand) (ISA (NZ)) 810 (Revised), *Engagements to Report on Summary Financial Statements*.

We expressed an unmodified audit opinion on the consolidated financial statements in our audit report dated 29 May 2019.

The summary consolidated financial statements do not contain all the disclosures required for a full set of consolidated financial statements under generally accepted accounting practice in New Zealand. Reading the summary consolidated financial statements, therefore, is not a substitute for reading the audited consolidated financial statements of the Banking Group.



Christchurch
29 May 2019

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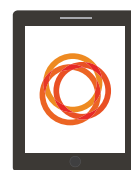
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To view this Annual Report online go to **sbsbank.co.nz**



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