

Members Equity Bank Limited

ABN: 56 070 887 679

**Interim Financial Statements
For the half-year ended 31 December 2014**

Members Equity Bank Limited

Directors' report

For the half-year ended 31 December 2014

The directors of Members Equity Bank Limited (the Company) submit herewith the interim financial statements of the Group (being the Company and its subsidiaries) for the half-year ended 31 December 2014, and the independent auditor's review report thereon.

Directors

The directors of Members Equity Bank Limited at any time during or since the end of the half-year and at the date of this report are:

G Weaven	Chairman (appointed to the Chair effective 5 February 2015)
C Christian	
G Combet	(appointed 7 November 2014)
A De Salis	
B Fraser	(retired 6 February 2015)
S Herman	
K Hodgson	
J Milne	
B Pollock	(retired 6 November 2014)

Principal activities

The principal activities of the Group comprised:

- provision of banking services under a banking licence;
- funding, management, and servicing of residential, consumer, and commercial lending portfolios; and
- carrying out associated funding activities for off balance sheet portfolios.

There were no significant changes during the period in the nature of the activities of the Group.

Dividends

No dividends have been paid or declared since the start of the financial year (2014: \$nil). The directors do not recommend the payment of a dividend in respect of the half-year ended 31 December 2014.

Review of operations and results

Profit for the half-year ended 31 December 2014 was \$40.2 million compared to \$25.9 million for the half-year ended 31 December 2013.

Significant items

The Group's pre-tax profit is impacted by the mark to market movement of interest rate swaps used to convert fixed rate home loan interest revenue into a floating interest rate. While the swaps are required to be revalued for accounting purposes, the fixed rate home loans are carried at cost. Until 30 June 2014, the revaluation of the interest rate swaps was recorded through profit or loss. From 1 July 2014, the Group adopted hedge accounting. The effective portion of the gain or loss on hedging instruments is initially recognised in equity in the cash flow hedge reserve. The cumulative unrealised loss as at 30 June 2014 will gradually reverse (or amortise) through the profit or loss statement as those hedges approach their maturity date. The result for the half-year ended 31 December 2014 includes an unrealised gain of \$11.1 million (post-tax) as a result of this treatment compared to an unrealised gain of \$0.4 million (post tax) for the half-year ended 31 December 2013.

Auditor independence

The auditor's independence declaration is included on page 3 of the interim financial statements.

Members Equity Bank Limited

Directors' report

For the half-year ended 31 December 2014

Subsequent events

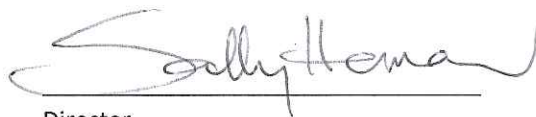
There have been no matters or circumstances which have arisen since the end of the financial half-year and up until the date of this report which significantly affect the operations of the Group, the results of those operations, or the state of affairs of the Group in subsequent years.

Rounding off of amounts

The Company is a company of the kind referred to in ASIC Class Order 98/0100, dated 10 July 1998, and in accordance with that Class Order amounts in the interim financial statements are rounded off to the nearest thousand dollars, unless otherwise indicated.

Signed in accordance with a resolution of the directors.

On behalf of the Directors

A handwritten signature in purple ink, appearing to read 'Sally Hewman', is written over a horizontal line.

Director

Melbourne, 5 March 2015

The Board of Directors
Members Equity Bank Limited
Level 28
360 Elizabeth Street
MELBOURNE VIC 3000

5 March 2015

Dear Board Members

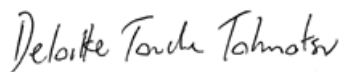
Members Equity Bank Limited

In accordance with section 307C of the Corporations Act 2001, I am pleased to provide the following declaration of independence to the directors of Members Equity Bank Limited.

As lead audit partner for the review of the Interim Financial Statements of Members Equity Bank Limited for the half-year ended 31 December 2014, I declare that to the best of my knowledge and belief, there have been no contraventions of:

- (i) the auditor independence requirements of the Australian Accounting Standards in relation to the review; and
- (ii) any applicable code of professional conduct in relation to the review.

Yours sincerely



DELOITTE TOUCHE TOHMATSU



Jamie C. J. Gatt
Partner
Chartered Accountant

Independent Auditor's Review Report to the Members of Members Equity Bank Limited

We have reviewed the accompanying Interim Financial Statements of Members Equity Bank Limited, which comprises the condensed consolidated statement of financial position as at 31 December 2014, and the condensed consolidated statement of profit or loss and other comprehensive income, the condensed consolidated statement of cash flows and the condensed consolidated statement of changes in equity for the half year ended on that date, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the end of the half-year or from time to time during the half-year as set out on pages 5 to 13.

Directors' Responsibility for the Interim Financial Statements

The directors of the company are responsible for the preparation of the Interim Financial Statements that gives a true and fair view in accordance with Australian Accounting Standards and for such internal control as the directors determine is necessary to enable the preparation of the Interim Financial Statements that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

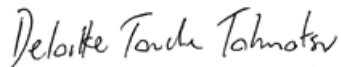
Our responsibility is to express a conclusion on the Interim Financial Statements based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the Interim Financial Statements is not in accordance with Australian Accounting Standards including: giving a true and fair view of the Members Equity Bank Limited's financial position as at 31 December 2014 and its performance for the half-year ended on that date. As the auditor of Members Equity Bank Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the review of the annual financial report.

A review of an Interim Financial Statements consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain

assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, which is not an audit, nothing has come to our attention that causes us to believe that the 31 December 2014 Interim Financial Statements of Members Equity Bank Limited do not present fairly, in all material respects, the bank's financial position as at 31 December 2014 and of its financial performance for the period ended on that date in accordance with *Australian Accounting Standards*.



DELOITTE TOUCHE TOHMATSU



Jamie C. J. Gatt

Partner

Chartered Accountants

Melbourne, 5 March 2015

Members Equity Bank Limited

Directors' declaration

The directors declare that:

- (a) in the directors' opinion there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable; and
- (b) in the directors' opinion, the attached financial statements and notes thereto comply with accounting standards and giving a true and fair view of the financial position and performance of the consolidated entity.

Signed in accordance with a resolution of the directors:

A handwritten signature in dark ink, appearing to read 'Sally Thomas', written over a horizontal dashed line.

Director

Melbourne, 5 March 2015

Members Equity Bank Limited

Condensed consolidated statement of profit or loss and other comprehensive income

For the half-year ended 31 December 2014

	Note	Half-year ended	
		31 Dec 2014 \$'000	31 Dec 2013 \$'000
Interest and similar income		608,436	492,193
Interest and similar expense		(474,288)	(375,251)
Net interest income		134,148	116,942
Funds management fee income		9,793	13,176
Other operating income		34,962	12,862
Total net operating income		178,903	142,980
Expenses			
Operating expenses		108,797	92,252
Impairment losses		7,987	7,221
Project expenses		7,522	6,474
Total operating expenses		124,306	105,947
Profit before income tax		54,597	37,033
Income tax expense	4	14,384	11,132
Profit for the period		40,213	25,901
Other comprehensive income			
Items that will not be reclassified subsequently to profit or loss		-	-
Items that may be reclassified subsequently to profit or loss			
Net gain on available-for-sale financial assets, net of tax		675	(2,122)
Cash flow hedges – effective portion of changes in fair values, net of tax		(43,936)	-
Total comprehensive income		(3,048)	23,779

Notes to the consolidated financial statements are included on pages 10 to 13.

Members Equity Bank Limited

Condensed consolidated statement of financial position

As at 31 December 2014

	31 Dec 2014 \$'000	30 Jun 2014 \$'000
Assets		
Cash and cash equivalents	284,074	360,414
Investments	2,839,384	2,461,801
Derivatives	12,234	10,019
Trade and other receivables	3,466	8,255
Loans and advances	16,415,787	14,916,724
Plant and equipment	37,910	35,602
Intangible assets	71,238	58,192
Deferred tax assets	29,344	19,336
Other assets	7,219	5,113
Total assets	19,700,656	17,875,456
Liabilities		
Amounts due to other financial institutions	3,907	30,897
Deposits and other borrowings	18,413,623	16,897,526
Derivatives	88,262	39,271
Trade and other payables	34,912	29,996
Current tax liabilities	3,999	12,343
Provisions	18,537	24,371
Subordinated debt	332,315	32,903
Total liabilities	18,895,555	17,067,307
Net assets	805,101	808,149
Equity		
Issued capital	699,995	699,995
Reserves	(18,032)	21,683
Retained earnings	123,138	86,471
Total equity	805,101	808,149
Book value per share	\$82.20	\$82.51

Notes to the consolidated financial statements are included on pages 10 to 13.

Members Equity Bank Limited

Condensed consolidated statement of changes in equity

For the half-year ended 31 December 2014

	Issued capital \$'000	Retained earnings \$'000	General Reserve for credit losses \$'000	Investment Revaluation reserve \$'000	Cash- flow hedge reserve \$'000	Total \$'000
As at 1 July 2013	570,101	69,511	3,874	5,810	-	649,296
Issue of share capital	59,999	-	-	-	-	59,999
Transfer to/(from) general reserve for credit losses	-	(1,810)	1,810	-	-	-
Other comprehensive income for the period	-	-	-	(2,122)	-	(2,122)
Profit for the period	-	25,901	-	-	-	25,901
As at 31 December 2013	630,100	93,602	5,684	3,688	-	733,074
As at 1 July 2014	699,995	86,471	15,079	6,604	-	808,149
Transfer to/(from) general reserve for credit losses	-	(3,546)	3,546	-	-	-
Other comprehensive income for the period	-	-	-	675	(43,936)	(43,261)
Profit for the period	-	40,213	-	-	-	40,213
As at 31 December 2014	699,995	123,138	18,625	7,279	(43,936)	805,101

Notes to the consolidated financial statements are included on pages 10 to 13.

Members Equity Bank Limited
Condensed consolidated statement of cash flows
For the half-year ended 31 December 2014

	Half-year ended	
	31 Dec 2014	31 Dec 2013
	\$'000	\$'000
Cash flows from operating activities		
Profit before tax	54,597	37,033
Adjustments for:		
Change in operating assets	(1,952,086)	(1,466,012)
Change in operating liabilities	1,537,003	1,459,249
Non-cash items included in profit before tax	21,485	17,984
Income tax payments	(14,196)	(10,115)
Net cash (used in)/provided by operating activities	(353,197)	38,139
Cash flows from investing activities		
Purchase of plant and equipment	(7,761)	(9,466)
Purchase of intangible assets	(14,794)	(18,476)
Proceeds from sale of plant and equipment	-	2,173
Net cash used in investing activities	(22,555)	(25,769)
Cash flow from financing activities		
Proceeds from issue of shares	-	59,999
Net proceeds from issue of subordinated debt	299,412	-
Net cash provided by financing activities	299,412	59,999
Net (decrease)/increase in cash and cash equivalents	(76,340)	72,369
Cash and cash equivalents at the beginning of the period	360,414	281,169
Cash and cash equivalents at the end of the period	284,074	353,538

Notes to the consolidated financial statements are included on pages 10 to 13.

Members Equity Bank Limited

Condensed notes to consolidated financial statements

1. General information

The interim financial statements of Members Equity Bank Limited (the Company) and its subsidiaries (collectively, the Group) for the half-year ended 31 December 2014 were authorised for issue in accordance with a resolution of the directors made on 5 March 2015.

The Company is a limited company, incorporated and domiciled in Australia. The Group's principal activities are: provision of banking services under a banking licence, funding, management, and servicing of residential, consumer, and commercial lending portfolios and carrying out associated funding activities for off balance sheet portfolios.

2. Basis of preparation

The interim financial statements are a general purpose financial report prepared in accordance with AASB 134 'Interim Financial Reporting'. Compliance with AASB 134 ensures compliance with international Financial Reporting Standard IAS 34 'Interim Financial Reporting'. The interim financial statements do not include notes of the type normally included in an annual financial report and shall be read in conjunction with the most recent annual financial report.

The interim financial statements have been prepared on the basis of historical cost, except for the revaluation of financial instruments. Cost is based on the fair values of the consideration given in exchange for assets. All amounts are presented in Australian dollars, unless otherwise stated.

The Company is a company of the kind referred to in ASIC Class Order 98/100, dated 10 July 1998, and in accordance with that Class Order amounts in the interim financial statements are rounded off to the nearest thousand dollars, unless otherwise stated.

3. Significant accounting policies

The accounting policies and methods of computation adopted in the preparation of the half-year financial report are consistent with those adopted and disclosed in the Company's 2014 annual financial report for the financial year ended 30 June 2014, except as described below.

Hedge accounting

From 1 July 2014, the Group designates certain derivatives held for risk management as hedging instruments in qualifying cash flow hedging relationships in accordance with AASB 139 'Financial Instruments: Recognition and Measurement'. On initial designation of the hedge, the Group formally documents the relationship between the hedging instruments and hedge items, including the risk management objective and strategy in undertaking the hedge, together with the method that will be used to assess the effectiveness of the hedging relationship.

The Group makes an assessment, both at inception of the hedge relationship and on an ongoing basis, of whether the hedging instruments are expected to be highly effective in offsetting the changes in the cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80-125%. The effective portion of the gain or loss on the hedging instrument is initially recognised directly in equity in the cash flow hedge reserve. The ineffective portion of the gain or loss on the hedging instrument is recognised immediately in other operating income in the statement of profit or loss.

Members Equity Bank Limited

Condensed notes to consolidated financial statements

3. Significant accounting policies (continued)

When the hedged forecasted variable cash flow affects the profit or loss statement, the gain or loss on the hedging instrument is transferred from equity to the corresponding income or expense line of the income statement. When a hedging instrument expires, or is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss that has been recognised in other comprehensive income at that time remains in other comprehensive income and is recognised when the hedged forecast transaction is ultimately recognised in the statement of profit or loss. When a forecast transaction is no longer expected to occur, the gain or loss accumulated in equity is recognised immediately in profit or loss.

Application of new and revised accounting standards

The Group has adopted all of the new and revised accounting standards that are relevant to its operations and effective for the half-year. None of the new and revised standards had a material impact on the Group.

4. Income tax

The Group calculates the period income tax expense using the tax rate that would be applicable to the expected total annual earnings. The major components of income tax expense in the interim statement of profit or loss are:

	Half-year ended	
	31 Dec 2014	31 Dec 2013
	\$'000	\$'000
Income taxes		
Current income tax expense	26,408	10,165
Adjustment recognised in the current year in relation to the current tax of prior years	(2,014)	(276)
Deferred income tax expense / (income) related to origination and reversal of deferred taxes	(10,008)	1,243
Income tax expense recognised in statement of profit or loss	14,384	11,132

5. Investment in controlled entities

During the six months ended 31 December 2014, the Group has formed two additional trusts as part of its securitisation program. Both trusts were formed in Australia, and the Group holds 100% of the residual income units of the trusts. The names of the trusts are SMHL Series Securitisation Fund 2014-1 and SMHL Series Private Placement 2014-2.

6. Deposits and other borrowings

In November 2014, the Group issued \$200 million unsecured floating-rate notes with the contractual maturity date on 17 November 2017.

7. Subordinated debt

In August 2014, the Company issued 30,000 subordinated notes with a par value of \$10,000 per note which will mature in August 2024. The notes were issued off the Company's \$1 billion subordinated notes program. Under the terms of the program, the principal on these notes will be converted into ordinary equity (without voting rights) or, if that is not legally possible, written off, partially or in full, in the event that the Australian Prudential Regulation Authority (APRA) notifies the Company that:

- (i) without such conversion or write-off the Company would become non-viable, or
- (ii) without a public sector injection of capital (or equivalent capital support) being made, the Company would become non-viable.

The subordinated notes qualify as Tier 2 capital under Basel III.

Members Equity Bank Limited

Condensed notes to consolidated financial statements

8. Financial instruments

Carrying amounts and fair value

The following table shows the carrying amounts and fair values of financial instruments, other than cash and cash equivalents, held by the Group as at 31 December 2014.

	At amortised cost	Loans & receivables	Available- for-sale	Fair value through profit or loss	Fair value through OCI	Total fair value
31 December 2014						
Financial assets						
<u>Measured at fair value</u>						
Investments	-	-	2,839,384	-	-	2,839,384
Derivatives	-	-	-	12,006	228	12,234
<u>Not measured at fair value</u>						
Trade & other receivables	-	3,466	-	-	-	3,466
Loans & advances	-	16,415,787	-	-	-	16,485,889
Financial liabilities						
<u>Measured at fair value</u>						
Derivatives	-	-	-	-	88,262	88,262
<u>Not measured at fair value</u>						
Deposits & other borrowings	18,413,623	-	-	-	-	18,418,039
Trade & other payables	34,912	-	-	-	-	34,912
Subordinated debt	332,315	-	-	-	-	333,632
30 June 2014						
Financial assets						
<u>Measured at fair value</u>						
Investments	-	-	2,461,801	-	-	2,461,801
Derivatives	-	-	-	10,019	-	10,019
<u>Not measured at fair value</u>						
Trade & other receivables	-	8,255	-	-	-	8,255
Loans & advances	-	14,916,724	-	-	-	15,024,606
Financial liabilities						
<u>Measured at fair value</u>						
Derivatives	-	-	-	39,271	-	39,271
<u>Not measured at fair value</u>						
Deposits & other borrowings	16,897,526	-	-	-	-	16,900,057
Trade & other payables	29,996	-	-	-	-	29,996
Subordinated debt	32,903	-	-	-	-	34,419

Members Equity Bank Limited

Condensed notes to consolidated financial statements

8. Financial instruments (continued)

The following table shows the levels in the fair value hierarchy for financial instruments measured at fair value.

	31 December 2014			30 June 2014		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Financial assets						
Investments	-	2,839,384	-	-	2,461,801	-
Derivatives	-	12,234	-	-	10,019	-
Financial liabilities						
Derivatives	-	88,262	-	-	39,271	-

There were no transfers between level 1 and level 2 measurements during the period.

Risk management activities – cash flow hedges of floating rate liabilities

The Group uses interest rate swaps to hedge the interest rate risks arising from its floating-rate liabilities (refer note 3). The fair values of the interest rate swaps designated as cash flow hedges are as follows:

	31 Dec 2014		30 Jun 2014	
	Assets \$'000	Liabilities \$'000	Assets \$'000	Liabilities \$'000
Interest rate swaps	228	88,262	-	-

9. Subsequent events

There have been no matters or circumstances which have arisen since the end of the financial half-year and up until the date of this report which significantly affect the operations of the Group, the results of those operations, or the state of affairs of the Group in subsequent years.