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FIPS

Financial Institutions Performance Survey – Non-banks

Review of 2014

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An upward climb continues due to hard work in a competitive and regulated environment.

Contents

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John has been with KPMG's Financial Services audit team for 29-plus years, 16 of these as a partner working across a wide range of financial services audit clients, specialising in banks and finance companies.

John has a wealth of experience in auditing and accounting for banking products and services including treasury, retail offerings, corporate loans and loan provisioning. He is currently Head of KPMG's Financial Services team and Financial Services Audit and editor of this publication. John is also a Trustee of the Kidscan Charitable Trust.

Recently appointed deputy chairman of the New Zealand Auditing and Assurance Standards Board (NZAuASB), John is also a member of CAANZ, the Institute of Directors, FINSIA and INFINZ.

KPMG's Financial Services team

KPMG's Financial Services practice offers focused and practical audit, tax and advisory services to the retail banking, corporate and investment banking, investment management and insurance sectors.

Our team of professionals – led by senior partners with a wealth of client experience and relationships – has an in-depth understanding of the drivers, risks and issues facing our financial institutions. We provide independent assurance and insight that delivers objectivity that is both challenging and supportive while helping you identify your emerging risks.

We would welcome the opportunity to discuss how we could help you achieve your business objectives. To find out how we can work together, please contact one of the team.

Please find our contact information at the back of this document.

The Survey

Welcome to Part 1 of the 2014 edition of the Financial Institutions Performance Survey

Part 1 of the Financial Institutions Performance Survey (FIPS) focuses on the Non-bank financial institutions, while Part 2, to be published in February 2015 will focus on the registered banks. Our Non-bank Survey captures the annual balance dates between 1 October 2013 and 30 September 2014, with the exception of The Warehouse Financial Services Limited, whose financial statements were not available at the date of compilation and prior year financial statements are presented.

In prior editions of the Survey, we included separate analysis for the finance companies sector and savings institutions sector, however in the 2014 Survey we have decided to merge the finance companies and savings institutions sectors together due to the decrease in the number of savings institutions over the past few years, including the departure of previous sector giants Heartland Limited and PSIS (who are now included in the registered banks' Survey). As a result of this merger, we now have only one non-banking sector including finance companies and saving institutions. All comparatives have been amended to reflect this change in order to make prior year information comparable to the current year.

The non-banking sector has a total of 23 Survey participants, including the three individual GE entities which make up GE Capital, being GE Finance and Insurance Limited, GE Commercial Finance (USD) Limited, and GE Commercial Finance NZ Limited.

Ricoh New Zealand Limited is the latest company to be welcomed into the FIPS Survey this year, while Custom Fleet NZ has been amalgamated with GE Finance and Insurance Limited so is no longer stated separately. Prior numbers for GE Capital have remained unchanged. We continue to disclose the individual GE entities separately below our analysis table for information purposes.

Fisher & Paykel Finance Group have changed their balance date during the year from 31 March to 31 December. Therefore, the numbers disclosed for Fisher & Paykel Finance Group in this document are for the nine months ended 31 December 2013.

The threshold for inclusion in this year's Survey has remained unchanged at total assets of $75 million.

All the information used to compile this Survey is extracted from publicly available annual reports, disclosure statements and prospectuses for each financial institution, with the exception of employee numbers, which have been provided by the Survey participants. We thank the Survey participants for their continued and valued contribution and for making the time to meet with us.

TABLE 1: MOVEMENTS

	Who's out	Who's in
Non-banks Unchanged at 23	Acquired by GE Finance and Insurance: Custom Fleet	Included for the first year: Ricoh New Zealand Limited

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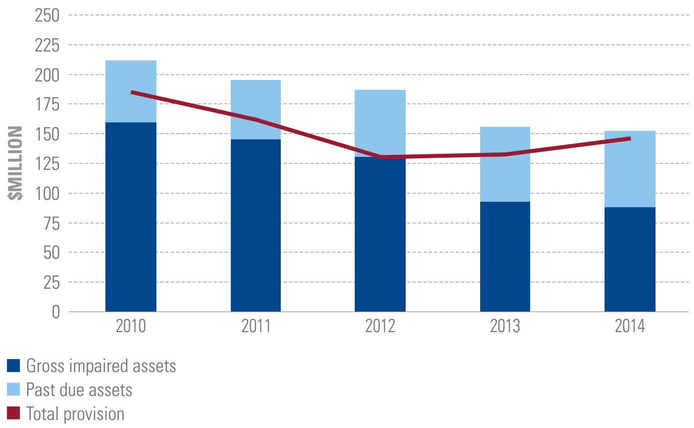
Industry overview

A very strong year for the non-banking sector

2014 has been another record year for the non-banking sector, with profits increasing by $133 million compared to the previous year, mainly driven by a large one-off expense in the prior year not recurring and good lending asset growth. The net profit after tax for the sector was $263 million which was an increase of 102.63% from the 2013 year. The non-banking sector also showed significant asset growth, increasing 8.4% from the previous year. Although at the headline level this indicates another strong year of growth, executives interviewed commented that the profit targets are getting harder to achieve due to both competitive pressures and further increases in operating expenses, driven principally by compliance costs.

1 GROSS IMPAIRED AND PAST DUE ASSETS



The current year has seen lower interest margins achieved by the sector as a result of pressure on lending rates; however, cheaper funding costs and strengthening loan book quality have helped the sector stay competitive and produce solid results. Asset quality shows some signs of deterioration; however, this is still significantly lower than the impairment charges shown between 2009 and 2011. Most sector participants have struggled to reduce operating expenses. However, the majority of participants were able to make up for this in improvements in non-interest income.

Improvements in economic conditions and a strengthening NZD has led to a growth in assets over the year. Motor vehicle leasing entities have fared particularly well, due to the fact that the majority of their vehicles to be leased are imported and the NZD is strong, and post the Global financial crisis (GFC) the New Zealand fleet had aged significantly as replacement was deferred.

Sector participants have acknowledged that the key to remaining competitive in this environment, where competition is tough and banks are still trying to entice their clients away, is to understand their customers, knowing how to provide them with exactly the nature of the finance they need, developing strong client relationships over time and sticking to their core business and not getting into products or market they do not normally operate.

> **Cheaper funding costs and strengthening loan book quality have helped the sector stay competitive and produce solid results.**

Margins under increasing pressure from banks and non-banking sector participants

Overseas wholesale markets have continued to be relatively stable and liquid over the Survey period. When combined with sustained deposit growth, funding costs have remained at prior year levels or even decreased compared to the prior year. While all sector participants do not have the scale to directly access the global wholesale markets, those that cannot have indirectly benefited from reduced rates passed down by their lenders such as the banks which act as an intermediary. Margins on the lending side continue to be under pressure due to the current competitive environment, but this has been offset on the borrowing side by a lower cost of funds. Sector participants acknowledged that they have been benefited by lower cost of funds although they have seen recently that these costs have started to increase. All in all, the result has been a decrease in the sector interest margin of 19 basis points (bps), driven by a decrease in the average lending rate partially offset by a reduction in the average cost of funds.

Competition is tough

A consistent theme coming from executives surveyed was that of extreme competition for lending and the consequential effect on margins, stemming from both industry incumbents and the intrusion of banks into the market.

The banks have proved to be quite agile, entering and exiting the market at will. Executives surveyed have indicated that the banks have not been afraid to act in a predatory manner by undercutting rates to secure lending, despite borrowers having pre-established relationships with non-bank participants. There is also the notion in the non-banking sector that, given the rate afforded to some borrowers without credit ratings, some of the lending is questionable as to whether it is sustainable. Sector participants agreed that this behaviour will

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probably have an impact on the industry once interest rates rise.

The intrusion of the banks appears to come from the desire to tap into growing segments offering better margins, given the significant competition between themselves in their more traditional segments of both mortgage and business lending, the desire to better leverage pre-existing relationships with customers, and an effort to both recover the business lost as a result of the loan to value ratio (LVR) restrictions and meet stretch growth targets. With the Reserve Bank of New Zealand (RBNZ or Reserve Bank) confirming LVR restrictions are to remain in place for the time being, credit growth in the mortgage market is likely to remain affected for some time further, fuelling the behaviour of the banks and driving down margins.

The one advantage the non-banking sector has is the ability to work with and offer flexibility to their customers. Comments by executives indicate that customers who have been attracted to the banks often find that when they go back to the bank for more money (as they often need to), they may not get it and then they need to go back to non-banks participants for this additional lending.

Sector participants believe that having supported their clients during the GFC and helping them through tough times has allowed them to utilise this loyalty to keep them. Sector participants said that their customers are now slowly understanding that they may get a better rate from the bank but it may not be as easy to renegotiate or increase their lending with the bank when the need arises.

Lastly, sector participants feel the banks lending model is based around a black box tool. If a loan fits within it, it can be executed quickly and efficiently by the bank, but where it doesn't fit into the box so well, the bank may decline the loan. These declines leave plenty of opportunity for the non bank lenders to service the customer. In addition, many have noted that the size and shape of the black box can change quite quickly.

Waves of regulation still coming

A common theme of the Survey over the past few editions has been the waves of regulation imposed on the sector with executives being critical of the substantial costs required to be borne by entities in order to establish compliance. Evidence from the current survey year suggests that the situation is much the same in the current period.

> **The one advantage the non-banking sector has is the ability to work with and offer flexibility to their customers.**

Throughout the survey year, there have been a number of high priority pieces of legislation coming into effect.

The Non-Bank Deposit Takers Act 2013 (NBDT Act) came into force on 1 May 2014 and covers finance companies, building societies and credit unions. Under the regime, Non-Bank Deposit Takers (NBDT) are required to be licensed after meeting certain requirements and also the imposition of conditions for specific entities.

The Act aims to bring regulation of NBDT's in line with that already implemented on both the banking and insurance sectors, with a view to prevent the collapses seen in 2008.

A one-year transition period is in place with entities given until 30 April 2015 to obtain a license, with applications received by the RBNZ from most existing institutions.

The Financial Markets Conduct Act (FMCA) represents a complete overhaul of financial markets regulation replacing both the Securities Act 1978 and Securities Markets Act 1988. With the first phase of the provisions of the FMCA already in force since 1 April 2014, the remainder of the Act comes into force on 1 December 2014, which is when new disclosure requirements and licensing obligations will begin to take effect. The FMCA looks to regulate financial products issued by entities and the ongoing responsibilities surrounding them.

FATCA is a law of the United States (US) aimed at preventing offshore tax abuses by US citizens. With the signing of the Intergovernmental Agreement (IGA) between New Zealand and the US in June and subsequent passing of the Taxation (Annual Rates, Employee Allowances and Remedial Matters) Bill, the legal framework for New Zealand financial institutions to comply with FATCA was established.

Under the FATCA requirements, New Zealand financial institutions are required to identify the accounts of US individuals and entities and report details of financial accounts to the US Internal Revenue Service (IRS). The information collection requirement began on 1 July with New Zealand financial institutions to begin reporting information to the IRS in April 2015. FATCA may not have had an impact on the non-banking sector, but it still requires appropriate risk management consideration.

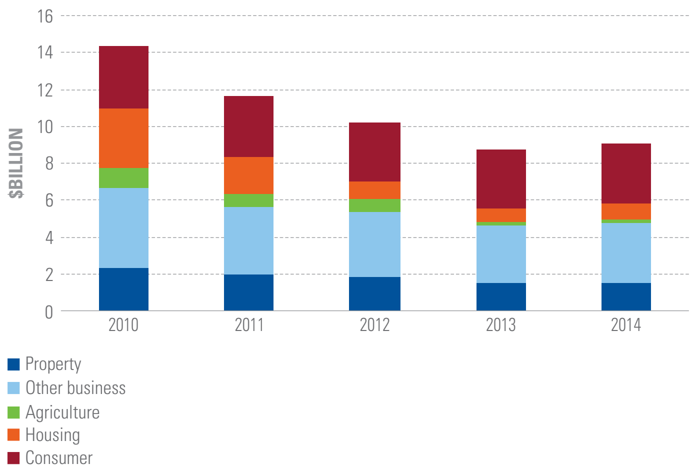
The Credit Contract and Consumer Finance Amendments (CCCFA) Act, which received royal assent in June, is primarily targeted at the likes of payday lenders and 'loan sharks'. Of most significance to sector participants will be the introduction of a "Responsible Lending Code" and the alteration of provisions relating to credit fees.

> **Sector participants acknowledge that compliance is taking a huge amount of time and money.**

The "Responsible Lending Code" will result in a much greater onus on participants to determine the appropriateness of lending, based on factors such as their ability to repay and the suitability of the financial products, in an overall effort to protect vulnerable consumers. Participants will also have great interest in the changes to the provisions regarding reasonable credit fees, especially given the ongoing Commerce Commission action against Motor Trade Finances Limited.

Despite receiving royal assent, the majority of the provisions are not

2 EXPOSURES OF NON-BANK LENDING INSTITUTIONS



Source: RBNZ SSR – T4

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yet in force, with the content of the "responsible lending code" still at discussion stage with an aim to be to be effective along with the remaining provisions by June 2015. One frequently voiced frustration from the sector was that still not enough was being done to remove loan sharks and payday loan providers from the market.

Sector participants acknowledge that compliance is taking a huge amount of time and money. They are not that impressed with the level of regulation that they are having to deal with, although they acknowledged that it is now embedded in their culture and part of the normal daily disciplines, has made for a better sector and may prevent unsustainable parties from entering the sector and limit the impact of disruptors in the market.

LVR – What is the result?

14 months since the introduction of the LVR requirements and with the RBNZ recently announcing they will remain in place for the time being, it is an appropriate time to look back and examine the associated impact in general and on the non-banks sector.

From all accounts it appears that the LVR requirements are having some of the desired effect to moderate housing market pressures. While house prices remain elevated especially in the Auckland and Canterbury regions due to supply issues, the policy has moderated the risks associated with house price inflation and a subsequent sharp correction in house prices. When the LVR restrictions were introduced, it was clear that the policy represented an opportunity for non-bank lenders who were not caught under the regulations to take advantage of an area of the market where the banks would be unable to effectively compete. The RBNZ has stated that such "regulatory leakage" appears to not have been material, although comments made by some executives indicate that some have used this advantage resulting in some good balance sheet growth. However, they also said that it needs to be managed carefully as this higher LVR lending represents more risk in a rising interest rate environment.

How long we see the LVR restrictions remain in place is open for debate, but it appears that the LVR speed limit is likely to stay in place a bit longer than the markets initially anticipated and until the RBNZ sees some further change in housing market growth rates. This is likely to continue to provide opportunities to the non-banks who offer home loans, as they are not constrained by the speed limits set by the RBNZ.

Potential industry disruption

A key theme that seemed to be on the mind of executives surveyed was the potential threat of a disrupter entering into the market and the consequential impact on incumbents. We have seen examples in industries such as retail and insurance where a disrupter has been able to come in and shake up the marketplace. Where, when and how a disrupter may manifest itself within the industry is still unclear to many of the executives, but they agree that it will probably come from someone who has access to customer and data information and have the ability to use this data.

With technology increasing significantly over the past few years, and this very likely to continue in the future, there are more and more methods being developed to capitalise on the "big data" captured by businesses, such as learning more about their customers and their habits, and using this information to provide additional and different products and services to their current customers. This provides an opportunity for a "disrupter" entering the sector, in the same capacity Amazon captured the retail market. It is yet to be seen in what form and what impact this entity may have, or when or if this would occur. But a real concern was identified around all the data that is moved around, and stored, as to exactly who does own it, the financial institution, the Telco, the payment system or the cloud storage entity.

One operator everyone is aware of and who is operating on the fringes is "Harmoney" which was issued the first licence by the Financial Markets Authority (FMA) to conduct peer to peer lending (P2P) under the Financial Markets Conduct Act.

> **"A real concern was identified around all the data that is moved around, and stored, as to exactly who does own it.**

P2P allows for the lending of money between unrelated individuals often taking place online through the platforms of peer to peer lending companies. In a typical scenario an investor will deposit cash with the peer to peer lending company which will then be broken up into many small blocks and lent out to many borrowers in an effort to diversify the credit risk of the investor.

While the impact of P2P lending overseas on the more traditional banks and lending institutions is not immediately clear, P2P appears to be growing overseas and the credibility of this market may be further enhanced by the implementation of regulation of the P2P market overseas.

What many executives noted was that all these entities have shown that an efficient and effective digital delivery tool is increasingly a critical platform from which to both lend and fund the business.

Organic or inorganic growth?

Over the past survey year, we have not seen any large transactions in the mergers and acquisitions space from the Survey participants. However, there has been two notable events worthy of mention.

Firstly, GE Capital, the sectors largest participant, notified the industry that its consumer finance division is up for sale. Given the substantial size of GE and its Trans-Tasman operation, we would expect that the number of potential purchasers maybe limited to the large banks, private equity firms, or specialist lenders who may look to bolster or create their presence in the consumer finance space.

The other notable event was the uninvited approach by Heartland Bank to acquire Motor Trade Finances (MTF). MTF, in a statement from July 2014, noted that Heartland's proposal was rejected by the MTF Board as the conditions and indicative price were not considered acceptable by MTF. It was also noted that Heartland's interest was subject to the resolution of the MTF court case regarding fees, which is subject to appeal in the Court of Appeal.

There continues to be consolidation in the credit union sector, especially with the smaller credit unions who have been amalgamating with the larger credit unions. Credit Union Bay Health merged with Credit Union Baywide in December 2013, and more recently, Credit Union Lakeland (also known as Credit Union Rotorua) announced that it will merge with First Credit Union. This shows that the levels of competition and regulation are forcing consolidation at the smaller end of the market, reflecting the higher costs that these entities are facing.

Of the executives surveyed, the common theme was many are on the lookout for potential acquisition targets to achieve growth and scale that cannot be obtained organically. It therefore appears that the lack of activity in this space is not down to a lack of will, but rather a lack of suitable acquisition targets at the right price.

We expect this momentum in the inorganic growth space to continue, as the growing costs due to regulation and pressure on margins due to increasing

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competition continue to indicate future consolidation of the sector is inevitable.

Securitisation – the not so new kid on the block

Over the past year, we have seen several sector participants enter into securitisation agreements for their receivables. This is being seen as an efficient way to manage the entity's capital and maximise returns, and is being driven by the demand from overseas institutions that are attracted to the relatively high yields being offered by the respective sector participants in a globally low yield environment.

While there have been issues with securitisation globally in the past, hard lessons have been learnt, and given the right risk profile and related returns, securitisation is proving its original purpose can be fulfilled where firstly, risks are appropriately recognised and measured, and secondly, where securitisation is designed to be an effective means to provide a product to the global market with good returns relative to a range of risk profiles. Based on the current global wholesale funding rates relative to New Zealand's domestic borrowing rates, especially in the non-banking sector, this is proving to be very attractive to overseas institutions. Until times where overall global yields begin to rise, this demand for high yielding products is likely to see other sector participants take advantage of securitisation of receivables, where it is appropriate for their funding mix.

> **"Global financial markets conditions continue to be favourable; however, there is an increased risk of volatility in some markets.**

The future – The overall economy

The Official Cash Rate (OCR) increases over the past year have stalled, on the back of the LVR speed limits slowing the housing markets and falls in commodity prices, a stubbornly strong New Zealand dollar and low inflation. This appears likely to stay flat for the near future, which will be good news for home owners. In other good news for current home owners, the national housing market continues to strengthen, albeit at a slower rate. This continues to centre around Auckland and Christchurch, with the LVR speed limits hitting the regional centres hard.

Global financial markets conditions continue to be favourable; however, there is an increased risk of volatility in some markets. The US economy appears to have come through the other side of their stimulus programme relatively unscathed, with a strengthened job market and investor sentiment rising. However, it is a different story in Europe and Japan. Europe looks again to further stimulus measures to ensure the area avoids deflation and recession, and Japan hasn't managed to avoid entering a recession, with the economy contracting in the third quarter of 2014. However, a raft of stimulus measures have been floated by the Japanese government, with investor sentiment of Japan very clearly demonstrated by the plummeting Japanese Yen. China's economic growth has slowed down, causing the New Zealand economy to become very vulnerable, particularly in the dairy sector, as dairy products are New Zealand's largest export to China.

Sector participants were optimistic about the future. They see the economy as stable, certainly not charging ahead, but starting to swing upwards, as employment is up and interest rates are low. Some executives said it is key to understand where their market is, where is it going and what they should do. Securitisation is likely to be a feature over the near future, with the attractive returns being made by sector participants leading to them being attractive participants for securitisation, especially whilst the demand, and the resulting pricing, is high.

Sector participants do not see credit quality worsening overly due to the level of employment nor do they see it improving as many feel its as good as it can get.

Competition has been intense over the past years and it is not expected to ease in the following year. With banks venturing into non-traditional markets, non-banks participants have experienced a dual relationship with the bank. First at an institutional level, providing funding to them, where they are happy with in terms of rate and tenure, and at the next level down, there is some frustration with banks coming in and taking customers from their areas of expertise. There is a continued concern in the industry around the level of regulation and the costs and time invested to comply with this. Some executives commented that with the current level of regulation, the regulator is under resourced, and once the regulation is issued, there is insufficient guidance, leaving a lot open to interpretation at the very time as they move into enforcement mode.

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Timeline of events

December 2013

11th Credit Union Bay Health merged with NZCU Baywide

January 2014

30th The Reserve Bank has left the Official Cash Rate (OCR) unchanged at 2.5 percent

February 2014

24th The Receivers of Lombard Finance & Investments Limited (Lombard) reached a $10 million settlement agreement with the directors of Lombard, their insurers and a third party.

March 2014

1st From 1 March 2014, registered charities will be exempted from the requirements of the Non-Bank Deposit Takers (NBDT) regime where they have outstanding debt securities offered to the public of under $15 million; or outstanding debt securities offered to the public of over $15 million, but outstanding loans of under $5 million.

12th The Financial Markets Authority (FMA) consented to an $18.9 million settlement between the receiver of Bridgecorp, the Bridgecorp directors, and their liability insurers. The FMA agreed to end its own civil proceedings against the Bridgecorp directors once the settlement sum has been paid. Bridgecorp Ltd and Bridgecorp Investments Ltd were placed in receivership in July 2007 with approximately $459 million owing to 14,500 investors.

13th The Reserve Bank raises the OCR by 0.25 to 2.75 percent

21st The Financial Markets Authority filed charges under the Crimes Act and under the Companies Act against directors and another of Viaduct Capital Limited and Ex-MFL Limited (formerly Mutual Finance Limited). The companies went into receivership in 2010. At the time of receivership, Viaduct owed $7.8 million to investors and Mutual owed $9.3 million to investors.

April 2014

24th The Reserve Bank raises the OCR by 0.25 to 3 percent.

30th The Reserve Bank released a consultation paper on its review of the prudential regime for NBDT.

May 2014

1st The Non-Bank Deposit Takers Act comes into force, requiring all NBDTs to be licensed by the Reserve Bank. A one-year transition period will enable existing NBDTs to meet the new licensing rules. As part of the licensing process, the Reserve Bank will assess an applicant's ability to comply with the requirements of the NBDT Act. The Bank will also assess the suitability of directors and senior officers of the applicant.

16th Hugh Edward Staples Hamilton was found guilty on 14 charges arising out of the collapse of Belgrave Finance Limited. The charges related to loans, with a value of more than $12 million, made by Belgrave Finance to various related companies between June 2005 and March 2008.

June 2014

5th The FMA and the Receivers of Strategic Finance Limited (Strategic), John Fisk and Colin McCloy of Pricewaterhouse Coopers, announced that they have finalised a settlement with the directors and auditors of Strategic. Under the terms of the settlement the directors and auditors will pay to the Receivers of Strategic $22 million, enabling the Receivers to make a further distribution to investors.

12th The Reserve Bank raises the OCR by 0.25 to 3.25 percent.

12th New Zealand has signed an Intergovernmental Agreement (IGA) with the United States to implement the FATCA (Foreign Account Tax Compliance Act) in New Zealand. This will require New Zealand financial institutions to identify customers and investors that are US persons and report this to the IRD. The IRD will exchange the information with the US IRS (Internal Revenue Service) and receive information about New Zealanders with Investments in US financial institutions.

30th The Cabinet agreed to declare a number of entities out of the NBDT regime, such as intergroup funding vehicles, payment facility providers, small charitable or religious organisations that act as NBDTs, and special purpose vehicles established by registered banks for the purpose of raising regulatory capital.

30th The Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 comes into force which implements the FATCA in New Zealand. FATCA starts on 1 July 2014.

July 2014

4th Lawyer Hugh Edward Staples Hamilton, who was found guilty of fraud in relation to the collapse of Belgrave Finance Limited, was sentenced to four years and nine months' imprisonment.

8th The FMA issued its first peer-to-peer lending service licence under the Financial Markets Conduct Act 2013 to Auckland-based Harmoney.

22nd Heartland Bank show intentions of acquiring Motor Trade Finances Limited (MTF). The shareholders of MTF rejected an intial takeover bid from Heartland's financing arm, MARAC.

24th Commerce Minister Craig Foss announced that changes are underway to update the legislation for Credit Unions, in order to give them greater legal status and reduce operating and compliance costs. One of the key changes will be the ability for Credit Unions to offer loans directly to small businesses owned by their members. This will avoid the current law's cumbersome process of making the loan to a member of the credit union who then on-lends it to the organisation.

24th The Reserve Bank raises the OCR by 0.25 to 3.5 percent.

August 2014

12th The Strategic Finance Limited settlement agreement became unconditional, and the first payment of $10 million was received. Two further instalments of $6 million were due at the end of August and November 2014, which would then enable further distributions to be made.

26th On announcing their 30 June 2014 annual results, Heartland Bank announced that they will investigate potential acquisition opportunities that were "ROE-accretive".

September 2014

11th The Reserve Bank leaves the OCR unchanged at 3.5%.

12th GE Capital announced that it intends to sell its New Zealand and Australia consumer finance businesses, including GE Money, GE CreditLine, GEM Visa card and the Countdown OneCard Visa credit card.

15th The Reserve Bank published a consultation document on its review of the credit rating exemption threshold for NBDTs. NBDTs are exempt from the requirement to have a credit rating when they are part of a borrowing group with consolidated liabilities of less that $20 million, or are not part of a borrowing group, and have consolidated liabilities of under $20 million. The consultation document seeks feedback on options for possible changes to this $20 million threshold.

17th Standard & Poor's lowered the credit rating of Medical Securities Limited (MSL) from A- to BB+. However, the outlook remains stable. This was based on their assessment of strategic importance reducing to "core" from "strategically important". It was also noted that MSL still continue to exhibit a "sound financial profile, stemming from its strong capitalisation, very sound asset quality, and good liquidity coverage".

October 2014

30th The Reserve Bank leaves the OCR unchanged at 3.5%.

November 2014

6th NZCU Steelsands becomes the first NBDT to be licenced by the Reserve Bank under the NBDT Act 2013.

December 2014

11th The Reserve Bank leaves the OCR unchanged at 3.5%.

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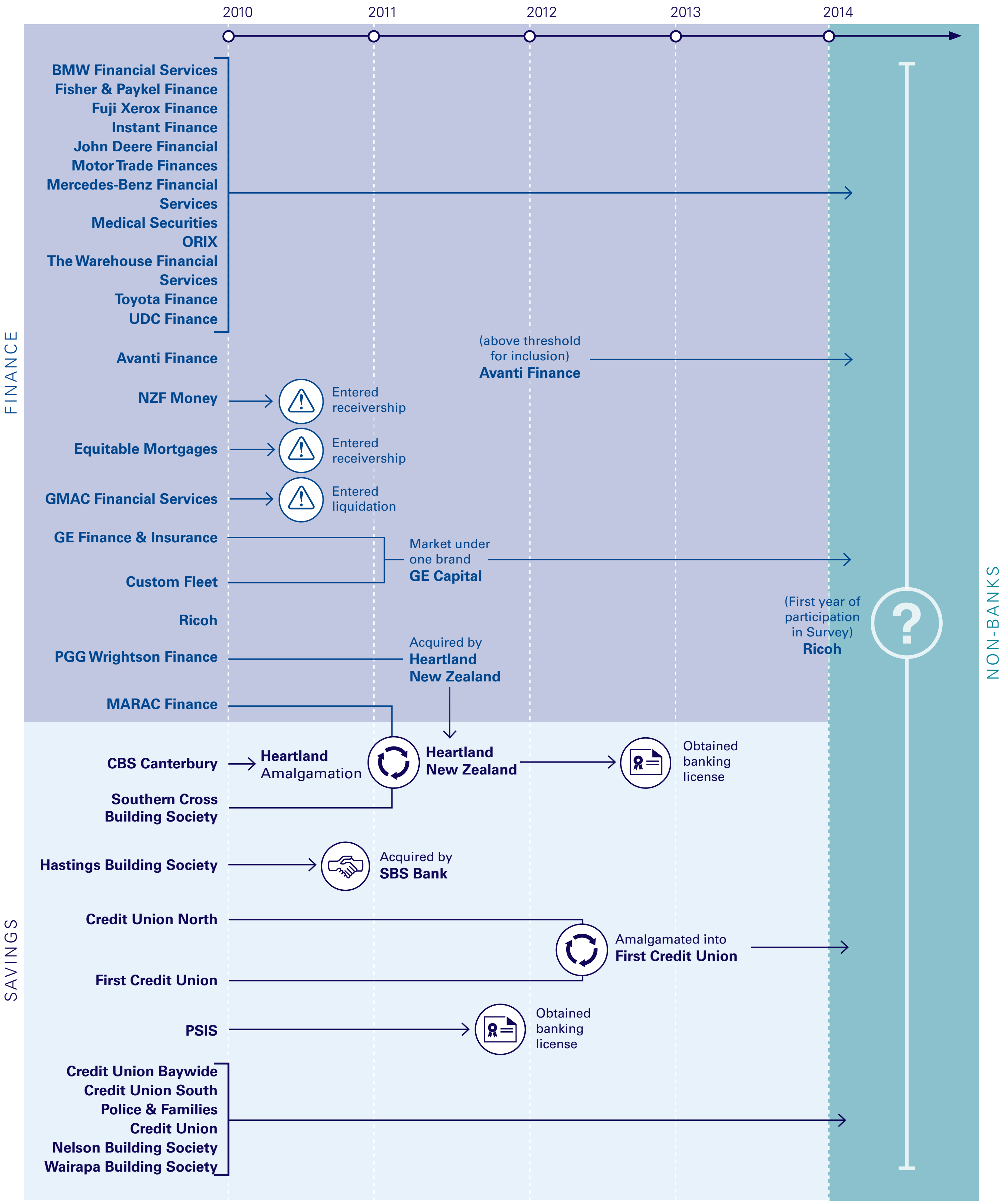
Looking back at the sector



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Intense competition has shrinking effect

We probably haven't seen the end of the M& A activity

Gary Ivory | Partner | Corporate Finance | KPMG

The number of participants in the New Zealand banking and finance sector is continuing to decline despite the prevailing optimum trading conditions in the sector. In this article, we examine the trends that are driving the reduction in the number of sector participants (both those covered by the Survey and those which fall outside the greater than $75 million asset threshold adopted by KPMG for Survey reporting).

Gary is a partner within KPMG's corporate finance team and he leads KPMG New Zealand's Mergers & Acquisitions practice and Debt Advisory practice. Gary also assists with the interviews for and compilations of KPMG's FIPS Survey.

His primary role is to assist New Zealand and international clients with the acquisition; sale; merger; public takeover; and financing of businesses and the provision of related advice – including privately owned, publicly listed and cooperatively owned entities.

Gary and his team have been and are currently are actively involved in providing advice to and undertaking transactions in the New Zealand financial services sector.

Please contact Gary to see how he can assist your business.

Predictably, the impact of the GFC and the resultant collapse of a number of sector participants (predominantly public issuers with a weighting towards property lending) led to a fall in numbers in the period from 2007 through to 2010. But since 2010, there has been, and we foresee, a further decline in sector participant numbers.

From an onlooker's perspective, market conditions appear optimal with solid levels of reported profitability and near all-time low levels of bad debts and impairments. You might expect therefore that we would be seeing visible growth in participant numbers as new entrants come into the market attracted by these favourable market conditions – rather than the decline we are seeing in participant numbers.

By our analysis, there is a single driving factor for this decline in numbers – intense competition – but impacting in several ways.

Firstly, the registered bank sector remains increasingly competitive and in recent times has seen the arrival of three new foreign participants from China, all of whom are yet to stamp their mark in the banking arena.

With growth targets on average exceeding the current growth in credit demand, the banking sector (particularly the Australian owned banks) has continued to more aggressively grow in areas also serviced by other sector participants such as credit unions (home mortgages and personal loans) and finance companies (asset financing).

> **There is a single driving factor for this decline in numbers – intense competition.**

At the next level down, this competition is intensified for both deposit taking and lending activity and the ability to compete is impacted by lack of scale as regulatory compliance costs and other operating costs continue to increase in the face of declining net interest margins. Most affected are the mutuals as their funding and lending options are more limited, being a function of the regulatory environment in which they operate. Consequently, we are seeing, and will continue to see, merger activity occurring amongst the mutuals, and perhaps some demutualisation as entities are absorbed into other financial institutions where there is a preferred regional or cultural fit.

At the finance company level, the field has been thinned considerably since the GFC with the majority of those remaining operating in niche areas of the market and enjoying high levels of profitability. Many of these are no longer public issuers, instead relying on wholesale funding provided by the banks. Given the high growth objectives of the other market participants, these finance companies are seen by some market participants as attractive acquisition targets and we are observing a new level of acquisition activity which, in some instances, is at price levels equating to pre-GFC levels.

> **We expect to see a net reduction in the number of financial services sector participants.**

A topic of discussion in many boardrooms is the upcoming sale of GE Money's consumer finance interests in both New Zealand and Australia, which may well see another major participant absorbed into the operations of another with plenty of speculation afoot as to who the likely acquirers may be.

Consequently, in the ensuing 12-24 months, we expect to see a net reduction in the number of financial services sector participants with the number of participants exiting through merger and acquisition activity exceeding the number of new entrants coming into the market as market conditions remain intensely competitive.

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Practical responses to increased regulation

Where to next for you?

Ceri Horwill | Partner | Advisory | KPMG

Globally there is increasing pressure to complete and enforce regulation of the shadow banking sector. This regulation has been developed globally to ensure that systemic risks aren't created by driving lending activity away from banks towards entities that facilitate or offer credit and that are traditionally less regulated.

Ceri is a specialist in financial services advisory, accounting for financial services businesses and financial services regulation. Using her detailed knowledge of the industry combined with her technical, regulatory and risk management experience, Ceri has a strong ability to understand the business impacts of accounting and regulatory change.

Ceri is the leader of KPMG New Zealand's Financial and Regulatory Risk Management practice. She provides regulatory, risk, accounting and compliance advice for financial service clients. Ceri has a deep and detailed knowledge of financial products, financial services businesses and financial risk and a strong ability to explain complicated concepts in simple and easy to understand language. She is responsible for leading KPMG's roll out of some of the complex new accounting, regulatory and capital requirements which will impact the financial services industry over the next few years (IFRS 9, Capital Requirements, FATCA, AML etc.) and frequently presents on these topics.

Please contact Ceri to discuss ways you can optimise your approach and management of your regulatory portfolio.

In New Zealand the RBNZ is responsible for monitoring systemic risks to the economy. According to the RBNZ's November 2014 Financial Stability Report the non-banking sector accounts for just 3% of intermediated credit outstanding; it states that the sector is no longer a significant source of funding for property development and although NBDTs are not subject to the new bank mortgage LVR restrictions "there is no evidence of any material 'regulatory leakage' arising from the policy."

However, with the new NBDT Act that came into force on 1 May, New Zealand non-bank financial institutions are certainly not feeling like they are at the lighter end of the regulatory scale. They are feeling the regulatory pressure of the one year NBDT Act transition period, the recent implementations of the Financial Advisors Act (FAA), FATCA, AML and FMCA, planning for the Responsible Lending Code, other CCCFA reform and a host of other regulation.

With increased regulation both nationally and globally here to stay, what can you, an NBDT, do to practically respond to increased regulatory pressure and turn it to your advantage or at least drive efficient responses that work for your business?

Engage with the regulator

The more relevant information that you can communicate to your regulator, the better they can understand your business and evaluate your approach to compliance. As non-bank financial institutions have started applying new regimes, communication with the regulator has inevitably stepped up. This should form part of your overall regulatory compliance strategy.

A regulatory compliance strategy should include a plan for when and how to communicate with the regulator, an approach to dealing with a regulatory compliance event, regulatory remediation plans where problems occur, as well as steps for keeping the regulator abreast of changes in the business. An important part of this is providing feedback to your regulator and actively commenting on their proposals.

> “
>
> **Many businesses are finding themselves developing multiple compliance programmes which are different for each latest piece of legislation.**

The RBNZ's recently announced "regulatory stocktake" is a fantastic opportunity to do this. The RBNZ's objective is to improve "the efficiency, clarity and consistency of regulatory requirements" as well as to "identify improvements to the RBNZ's current process for introducing or amending prudential requirements". The public consultation period is planned to commence between June and September 2015 and NBDTs should be preparing to make an active contribution to the process.

> “
>
> **This concept of root cause analysis is critical to ensure you remediate issues appropriately and prevent issues from recurring.**

Identify the root causes of challenges

Think about recent regulation implemented in your business, was it smooth sailing? What was your regulator's feedback? Where your business has experienced challenges in implementing new regulation or where the regulator has provided feedback or required remediation, you need to think honestly about the underlying problems that caused those issues. This concept of root cause analysis is critical to ensure you remediate issues appropriately and prevent issues from recurring. Was it due to the compliance programme in your risk framework being weak, a result of your staff's poor attitude to implementation, a result of there being holes in your three lines of defence framework or you simply didn't have enough budget or buy in to do it properly?

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Identify synergies

Businesses should look for ways to drive synergies in regulatory compliance; learning from prior implementations, looking across regulation for consistent approaches, as well as learning from other industries. Increasingly, new pieces of legislation demand a more formal compliance programme to help meet requirements. However, smaller financial service businesses are really only starting to develop line two as part of their three lines of defence framework and many haven't got a formal compliance framework in place.

Many businesses are finding themselves developing multiple compliance programmes which are different for each latest piece of legislation. A business' baseline approach to compliance should be the same across all areas of regulation: identify obligations, risk assess, develop controls, assign responsibility, train and monitor, report and remediate and ultimately continually improve. Once this basic framework is set up then tailor the compliance programme to each piece of regulation.

> **This concept of root cause analysis is critical to ensure you remediate issues appropriately and prevent issues from recurring.**

It is important not to overlook the need for tailoring compliance programmes and critically for risk frameworks. Your risk profile is unique to your business. Some of the early comments from the RBNZ whilst reviewing NBDT risk frameworks were around boiler plate risk frameworks which hadn't been tailored to the business.

To really drive efficiency, businesses should consider common aspects to multiple regulations; for example, identifying conduct risks in your business and driving a consistent and aligned approach to conduct, coupled with conduct angles of CCCFA reform and enforcement, FMCA and FAA.

Understand the critical judgements

Just after you have implemented a piece of legislation is the best time to sit back and work out where all the effort was expended. Similarly, talking to colleagues in other industries who have been through a similar process can help focus your work. For example, what did the insurance industry do well when developing their risk frameworks and what could you learn from them?

Businesses should look at the lifecycle of their products and work out where the risk is, what aspects of previous implementations took up the most time and what the most critical areas of judgement were. This will set you up to succeed next time, streamline your compliance approach and help you focus on the most risky areas and important judgements – e.g. is it point of sale that you really need to focus on or is it product development?

Regulation – a disruptor?

Once you have got basic compliance in place and are driving efficiency in your approach, you can turn your attention to looking for ways to turn regulation to your advantage. Non-banks have had success in New Zealand by specialising in differentiating themselves from banks. They have done this, for example, by focusing on customer loyalty, better rates, more flexible credit. Similarly, where digital disruptors have succeeded globally is where players have moved on new developments quickly and aren't constrained by old ways of thinking, systems or processes. This lens can also be applied to regulation and businesses across the world who are starting to work out how to differentiate themselves and be more nimble to gain advantage. For example, where global regulators are focussed on restoring trust in the financial markets and improving the conduct of market participants, business are increasingly marketing themselves accordingly; not only complying with the legislation, but looking to be a leader in that space. Some of the advertising campaigns and practices coming out of the UK at the moment demonstrate this: "#1 financial brand for fairness", "150 years building trust", "truth and banking" and "measuring complaints".

It's all about attitude ...

Finally – it's all about attitude. Remember, while your regulator is looking at technical compliance, they are also assessing the spirit of your approach to the legislation as well as your risk culture and level of buy in to risk and compliance at a senior level. This point came up when the New Zealand Productivity Commission released their report on regulatory institutions and practices in July 2014:

Where regulation focuses on an industry with relatively few firms, it is generally easier for the regulator to identify regulated parties and to develop closer regulatory relationships with them. This allows more opportunity for the regulator to gauge the regulated party's attitude to compliance.

> **Non-banks have had success in New Zealand by specialising in differentiating themselves from banks.**

Risk culture is critical to the regulators assessment of you and it needs to be demonstrated across the business from Board level to front line sales staff. A two fold approach is therefore required: firstly, looking for ways to "do regulation well", and secondly, demonstrating a positive attitude and your businesses' commitment to doing it well.

KPMG deals with many financial institutions globally and has the insight and proven capabilities to help your business know and implement best practice holistically and effectively.

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Video killed the radio star

The Impact of Digital Disrupters in New Zealand

Philip Whitmore | Partner | IT Advisory | KPMG

Advances in communications and associated technology are rapidly changing the financial services sector, and financial services organisations, payment companies and electronic payment start-ups are all vying for leadership. Although the consumer spending benefits are clear, the winning proposition among so many entrants has yet to emerge.

A partner within KPMG's IT Advisory team, Philip leads KPMG's technology risk, security advisory services and data analytics practices.

Philip helps organisations gain insights from their data, maximising the benefits presented by 'big data', and managing their IT-related risks, including around cyber security. His detailed IT advisory and assurance knowledge and experience is complemented by his internal audit, fraud and business process controls background.

Philip sits on the boards and steering committees for a range of professional bodies, including the Institute of Internal Auditors, the Information Systems Security Certification Consortium (ISC)2, the Information Systems Audit and Control Association (ISACA), and the Cloud Security Alliance.

Philip works with organisations to help them understand the impact of new technology on their business and how to mitigate risks posed.

Please contact Philip to discuss how he can assist your business.

How the payment services industry is changing

The last two years in the payment services industry have seen tremendous upheaval, particularly in mobile banking and payments. Several global factors are driving change in the once-staid payment services sector:

- **Cashless purchases:** Consumers in North America, Western Europe and Asia are catching up with New Zealand, and now make only small purchases with cash. They have traded in their cheques for payment cards and other cash-free payment methods.
- **High merchant fees:** Retailers are increasingly unsatisfied with paying credit card companies two to five percent of their gross sales, fees that up until now have been seen as a necessary cost to bear.
- **Small business limitations:** Small businesses such as tradespeople need a streamlined, low-cost way to accept payment beyond cash or cheques.
- **Expanding marketplace:** With new payment technology start-ups entering the market, financial services organisations and credit card companies are feeling threatened and scrambling to innovate in order to satisfy industry demand.

Hardly a month passes without a new product or platform announcement, a new industry partnership or a new entrant promising a radically new approach. With Apple launching its new Apple Pay mobile payment and digital wallet service in the US in October this year, it is still unclear whether there will be wide adoption of the service. Apple's technology is essentially nothing new, and there have been multiple previous unsuccessful efforts to build mobile payments services. Its differing business model may see it succeed where others failed

> **The last two years in the payment services industry have seen tremendous upheaval, particularly in mobile banking and payments.**

however, due to the benefits it offers all participants in the payments process – consumers, merchants, issuers and credit card brands.

In New Zealand our already high adoption of cashless payments through the likes of EFTPOS means that the drivers for adoption of new payments technologies are not the same as other parts of the world. While we will continue to see changes to how we make payments, with mobile payment products the most likely to feature, unless significant benefits are provided to the different stakeholders, the impact to the financial services sector is unlikely to be significant in the short to moderate term.

Digital currency

Digital currency such as Bitcoin is one of the emerging technologies that may impact the sector, but whether they are adopted widely as payment in the next few years depends on the country or region.

> **New Zealanders are, however, unlikely to be high users of digital currencies in the foreseeable future.**

With the Asia Pacific region generally being an early adopter of mobile payments, it may be that we see the common place adoption of digital currencies in this part of the world first. China in particular is one of the innovators in the payments' sector. With the massive rise of the consumer in China, significant innovations are taking place.

New Zealanders are, however, unlikely to be high users of digital currencies in the foreseeable future. While the focus on Bitcoin saw the unveiling of New Zealand's first Bitcoin ATM this year, it also saw one of the Bitcoin ATM operators rapidly shutting its doors due to lack of

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support from banks. For Bitcoin to gain any traction in the market, it will need the support of banks, which looks unlikely at present.

Everyone a banker?

Technology is also changing the way we fund our businesses, with the introduction of online crowd-funding platforms presenting new opportunities. The growing use of crowd-funding in New Zealand is changing the way businesses raise cash. While crowd-funding opens up new sources of funding not previously available, it is still unknown as to whether the impact will be significant.

> **The growing use of crowd-funding in New Zealand is changing the way businesses raise cash.**

Non-equity crowd-funding has been in New Zealand for over two years with the likes of PledgeMe, whereas equity-based crowd-funding – where investors receive an ownership stake in a company – was only legalised on 1 April this year. To date this has seen three crowd-funders licensed. When Snowball Effect launched New Zealand's first equity crowd-funding online service in August, craft brewery Renaissance Brewing successfully raised $700,000 in 13 days. Equity-based crowd-funding has tended to be the fastest growing sector of crowd-funding in the developed world, and there is every indication that the trend should continue to accelerate in New Zealand.

But the risk to investors – who are often left to their own devices to separate a good investment from a bad one – is certainly real and it presents investors with a strong motivation for remaining with traditional investment advisors. While a robust vetting process by the crowd-funding platforms and the regulation implemented around equity crowd-funding should help mitigate this, it may also lead to costs rising to a point where equity-based crowd-funding becomes just as expensive as traditional borrowing.

Skipping the middle man

Another potential disruptor to traditional finance models is peer-to-peer lending where lenders are connected directly to borrowers looking to finance anything from debt consolidation to an engagement ring. July this year saw Harmoney become the first licensed peer-to-peer lender in New Zealand.

> **The biggest flight risk for traditional providers of finance may be small businesses.**

The biggest flight risk for traditional providers of finance may be small businesses. While there are a wide range of funding options for small businesses, peer-to-peer lending has the potential to provide more accessible funding options.

If you can't beat them ...

So should traditional financial services organisations in New Zealand be afraid of increasing democratised financial markets? With it being so new, the jury is still out. While there are certainly under-served market segments that may abandon traditional finance providers in favour of crowd-funding, there are few signs that equity investors are currently in the mood to take on more risk.

That is not to say that crowd-funding and peer-to-peer lending will not disrupt the growth in the financial services sector, particularly amongst non-banks, but the disruption is likely to be the strongest in other countries where banking infrastructure can be sparse.

If traditional financial services organisations do start to feel the heat, there are certainly opportunities for traditional financial services organisations to take a role in the crowd-funding and peer-to-peer lending value chain.

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Non-banking sector performance

Overview of results

On a first look, net profit for the sector appears to have seen a substantial increase of 102.63%, from $130 million to $263 million. As can be seen from figure 3, the sector showed favourable movements in all main income statement categories, except impaired asset expense.

TABLE 2		Total
Increase in total assets		8.4%
Increase in net profit after tax		102.6%
Movement of impaired asset expense (% of loans and advances)	bp	18
Decrease in interest margin	bp	-19

Profits continue on the rise

Reductions in operating expenses has had the most significant impact on improved profitability; however, this reduction relates to normalisation after a large one off payment made in the prior year by sector powerhouse GE Capital (with a $138 million related party compensation payment in the 2013 Survey). Taking out this prior year non-recurring item (and acknowledging that we have not taken into account any other one-offs), this gives us a very different picture for operating expenses, as they would have in fact increased over the year by 11%, and reduced net profit by $5 million, a 2% contraction.

However there are still plenty of positives to be taken out of the sector's performance this year. Despite competition heating up, which has tightened margins, interest income still managed to increase by $10 million and interest expense managed to decrease by $9 million, leading to an overall increase in net interest income of $19 million, a 2.8% improvement over the prior year. 16 out of the 23 sector participants improved their net interest income, despite the majority of participants having tighter net interest margins, showing that the increase mainly came off the back of asset growth.

Non-interest income has also seen a strong improvement over the year. This is mostly attributable to new-comer Ricoh New Zealand Limited making an $18.9 million increase in revenue from its non-financing business, while Toyota Finance New Zealand Limited had a significant turn-around from its prior year loss on the fair value of interest rate derivative instruments from a $12.9 million loss in 2013 to a $4.9 million gain in 2014. The large majority of the other Survey participants also improved their non-interest earnings, with only six participants worsening over the year.

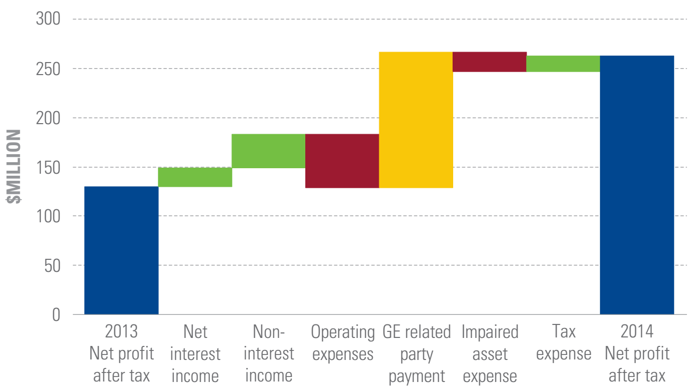
As a whole, asset quality appears to have deteriorated, as impaired asset expense has gone up. However, GE Capital had a major impairment charge over the year, which makes the sector look worse than it really is for the majority of participants. The motor vehicle leasing industry appears to have generally improved asset quality to a greater extent than the other Survey participants.

Tax expense has reduced over the year. This is partly due to Fuji Xerox Finance paying a $50 million subvention payment to Fuji Xerox New Zealand Limited in the prior year.

Asset quality

Overall the sector has shown a $19 million increase in impaired asset expense over the year from $65 million to $84 million. This is driven by large impairment charge increases made by the two largest sector participants, GE Capital and UDC, of $14.7 million and $4.6 million respectively. However at a high level, we are seeing a far more normalised level of impairment expense for the sector, with $67 million, $65 million, and now $84 million over the

3 MOVEMENT IN NET PROFIT AFTER TAX



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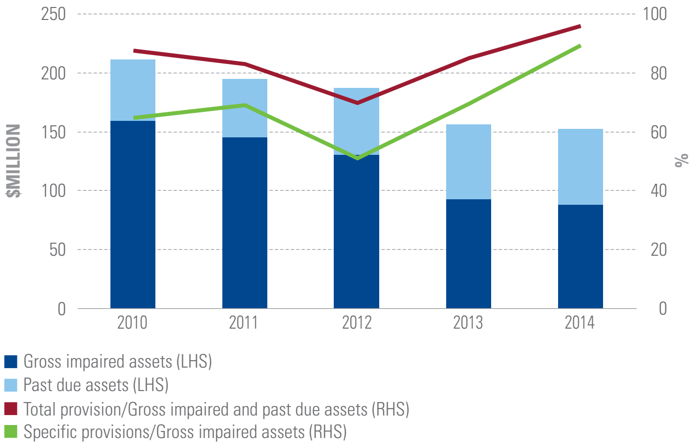
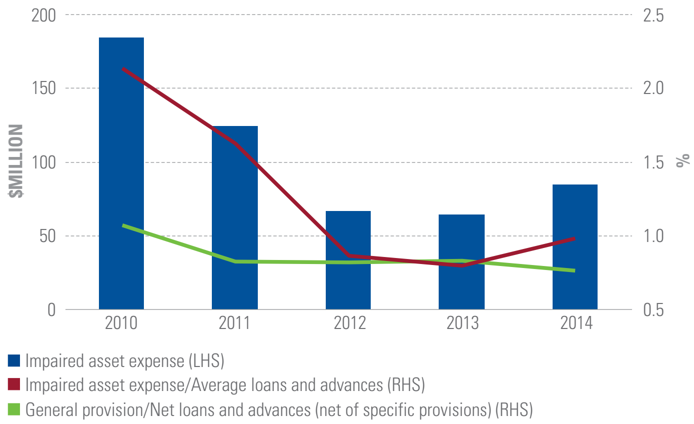
4 GROSS IMPAIRED AND PAST DUE ASSETS WITH PROVISIONS



5 IMPAIRED ASSET ANALYSIS



past three years, compared with $184 million and $124 million in 2010 and 2011 respectively, when we were still experiencing some of the hangover effects caused by the GFC.

Survey participants in the motor vehicle financing segment showed the best improvement in impaired asset expenses, as four out of the five motor vehicle financing companies managed a decrease. This may be related to the strong value of residuals in the second hand car market.

Compared to the increase in impaired asset expense, gross impaired assets have continued to show favourable results and have now reduced for the fifth consecutive year. UDC led the way in terms of dollar movement, as they were able to reduce their impaired assets by $5.4 million, a 22% reduction.

Collective provisions over net loans and advances has remained consistent over the past four years, only dropping 7 bps in the current year. However, impaired asset expense as a percentage of average loans and advances has increased by 18 bps over the year. Again this was mostly influenced by GE, whose ratio worsened by 72 bps.

Total assets on the growth

Total assets for the sector achieved significant growth from the prior year with an 8.41% increase to $11 billion. This rapid rate of growth reflects asset growth experienced by 19 of the 23 participants surveyed and is underpinned by growth in net loans and advances of 7% for the sector over the year. Motor Trade Finances was the best performing entity with increases in both categories above 20%.

These movements in the asset pool and loan book are aligned with comments expressed by the Survey participants regarding improved economic conditions with heightened business confidence and increased levels of investment and expenditure post the GFC. These traits have flowed to the non-banking sector, leading to an increased willingness for businesses to invest, in plant and equipment for example. This is assisted by the increased margin pressure on the lending side, making it cheaper for customers to do so, and at a time when interest rates are in a relatively low period. Replacement and purchase of fleet vehicles has also grown, driven by the strength of the NZD throughout the year and the fact the majority of these vehicles are imported.

The three largest entities, being GE Capital, Toyota Finance and UDC, maintained their positions as industry leaders with their combined market share remaining at just under 60% of the sector's total assets for 2014. Between these three entities, total assets grew an accumulated $458 million at an average of 8% from prior year.

As forecast at the beginning of the year, the non-banking sector has seen an increase in competition through pricing with margins squeezed in response to the additional pressure from industry competitors as well as banks encroaching on this sector. This is something that will need to be monitored closely going forward considering the risk of overcrowding an industry that already hosts a large number of participants.

Net interest margin

The non-banking sector has experienced a decrease in net interest margin of 19 bps from 6.97% in 2013 to 6.78% in the current survey year. The result comes on the back of cheaper costs of funding, which has been fully eroded by extensive competitive pressures across all sectors.

Wholesale debt funding costs have continued to decline over the survey period and are now at levels pre-GFC in 2008. When combined with strong retail deposits for deposit taking entities, participants have seen further savings on the expense side of their net interest margin, with interest expense having reduced by 2.54% in the current survey year from $361 million to $352 million, despite an increase in interest bearing liabilities of 9%. Comments made by executives surveyed indicate that even those entities without direct access to wholesale debt markets obtaining funding through intermediaries such as banks, and securitisation agreements have also benefited from lower funding costs originated in wholesale being passed down.

On the income side, participants have been under extreme competitive pressures from the banks and others in the sector. This has been particularly pronounced in the finance companies where the majority of entities have experienced a decrease in net interest margin as they have needed to reduce rates to retain business. The largest observed decreases have been experienced by Fisher & Paykel Finance and Ricoh, with movements of 218 bps and 204 bps respectively. Moving against the trend were Orix, BMW Financial Services and UDC which all managed to increase their interest margins by greater than 40 bps. Further reflective of the competitive pressures has been the deterioration of yield (net interest income to average interest earning assets ratio) of 10.70% to 10.22% in the current survey year, the lowest level seen since 2009, showing the competition is forcing the entities to pass on the lower funding costs and sometimes more.

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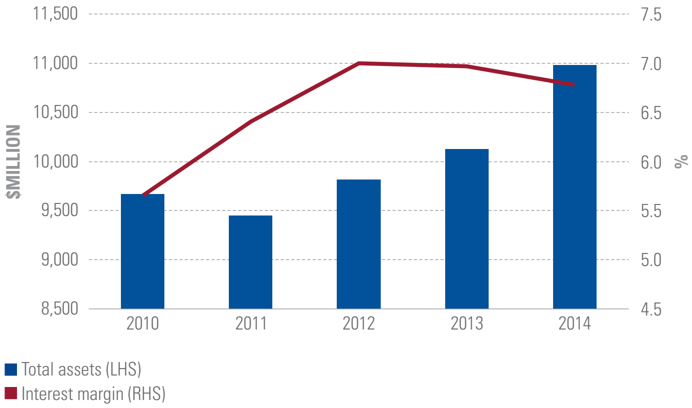
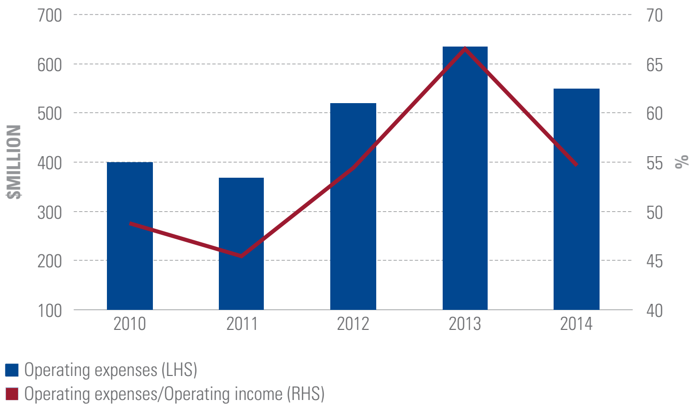
6 TOTAL ASSETS VS INTEREST MARGIN



7 OPERATING EXPENSES VS OPERATING EXPENSES / OPERATING INCOME



Whilst the competition in the mortgage market for the savings institutions has also been noticeable and is particularly fierce in the <80% LVR space, the impact on the savings institutions appears to be less dramatic with a mix of increases and decreases. Credit Union South had the most positive experience with an increase in interest margin of 36 bps to 8.42%. While the mixed impact could be attributed to a multitude of factors, it may potentially be the result of the LVR rules opening up a whole new market where good margins can be made due to the banks inability to compete as fiercely given they can only write up to 10% of new lending above 80% LVR. The RBNZ recently announced the continuation of the LVR restrictions, which will have been welcome news for the savings institutions which will continue to be shielded in the high LVR lending space.

With consumer confidence still high and unemployment continuing to decline, it is expected that consumer's appetite for credit to fund non-essential luxury items will continue. If so, there will be a boom for the finance companies which will also present further opportunity for the banks to intrude into the market and drive margins down.

Operating expenses

The non-banking sector has seen a substantial drop in operating expenses as a proportion of operating income with the ratio falling from 66.51% in 2013 to 54.67% in 2014. This points to a higher degree of operational efficiency with larger returns on investment across the board. However, these results must be taken with a grain of salt for a number of reasons.

Operating expenses during 2013 were exceptionally high due to a number of one off expenses that did not impact the current year results. GE Capital in particular were subject to these inflated expenses as a result of a related party settlement of around $138 million. Excluding GE Capital from our calculations we in fact see a 5% increase in operating expenses and a stable fluctuation of the income cost ratio with only a slight drop of 2% from 2013 to 56% in 2014.

This provides a more accurate representation of operational efficiency across the sector and indicates that the industry continues to run at an efficient rate even with higher operational expenses factored in. This is welcome news given the increased pressure and costs associated with conforming to a heavily regulated industry that requires constant adapting to new and updated legislation.

From discussions held with the Survey participants there was a clear and consistent message that keeping up to date with regulation has proved to be an expensive task and is the driving force behind the increased operating expenses.

Overall, there has been positive signs to emerge when looking at operational efficiency across the sector. With the skewed results of GE Capital backed out it can be seen that although operational expenses have increased on the back of additional regulation expenses, operational income has risen at a higher rate which is indicative of a productive and efficiently resourced industry.

TABLE 3: GROSS LOANS Entity	2014 $'000	2013 $'000	Movement $'000	Movement %
Avanti Finance Limited	106,340	93,616	12,724	14%
BMW Financial Services New Zealand Limited	347,799	297,792	50,007	17%
Credit Union Baywide	197,262	164,418	32,844	20%
Credit Union South	83,381	71,722	11,659	16%
First Credit Union	144,320	133,435	10,885	8%
Fisher & Paykel Finance Group	598,262	624,338	-26,076	-4%
Fuji Xerox Finance Limited	350,969	294,147	56,822	19%
GE Capital	2,013,839	2,035,576	-21,737	-1%
Instant Finance Limited	83,777	82,520	1,257	2%
John Deere Financial Limited	129,246	113,057	16,189	14%
Medical Securities Limited	170,112	173,416	-3,304	-2%
Mercedes-Benz Financial Services New Zealand Limited	448,497	381,164	67,333	18%
Motor Trade Finances Limited	489,293	397,381	91,912	23%
Nelson Building Society	318,826	289,347	29,479	10%
ORIX New Zealand Limited	33,046	37,339	-4,293	-11%
Police & Families Credit Union	63,746	55,701	8,045	14%
Ricoh New Zealand Limited	88,487	73,057	15,430	21%
The Warehouse Financial Services Limited	68,490	71,316	-2,826	-4%
Toyota Finance New Zealand Limited	765,330	736,115	29,215	4%
UDC Finance Limited	2,304,090	2,102,780	201,310	10%
Wairarapa Building Society	88,936	85,564	3,372	4%
Total	**8,894,048**	**8,313,801**	**580,247**	**7%**

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Analysis of financial statements

ANALYSIS OF CONSOLIDATED ACCOUNTS OF NON-BANKS[a]				Size & strength measures					Growth measures		
	Rank by total assets	Balance date	Year	Total assets[d] $000	Net assets $000	Gearing %	Net loans and advances[e] $000	Number of employees[f]	Increase in net profit after tax %	Increase in underlying profit %	Increase in total assets %
Avanti Finance Limited	18	31-Mar	2014	108,927	20,741	19.04	106,180	63	10.49	10.42	17.90
			2013	*92,387*	*35,453*	*38.37*	*93,461*	*57*	*23.54*	*22.97*	*10.17*
BMW Financial Services New Zealand Limited	9	31-Dec	2013	359,711	21,195	5.89	342,572	17	5.99	4.61	17.03
			2012	*307,375*	*13,163*	*4.28*	*295,388*	*16*	*27.13*	*27.58*	*23.20*
Credit Union Baywide	10	30-Jun	2014	252,021	34,943	13.87	195,944	103	41.41	41.33	10.19
			2013	*228,714*	*32,824*	*14.35*	*162,597*	*102*	*2.61*	*4.70*	*4.64*
Credit Union South	17	30-Jun	2014	112,885	19,877	17.61	83,343	93	111.36	120.45	4.45
			2013	*108,072*	*18,644*	*17.25*	*71,679*	*86*	*-67.57*	*-67.57*	*-5.93*
First Credit Union	11	30-Jun	2014	249,216	39,994	16.05	142,782	93	-11.53	-11.53	7.68
			2013	*231,436*	*38,459*	*16.62*	*132,124*	*97*	*97.83*	*97.83*	*97.98*
Fisher & Paykel Finance Group	4	31-Dec	2014	704,808	89,346	12.68	598,262	239	-31.89	-29.92	-4.52
			2013	*738,189*	*98,017*	*13.28*	*624,338*	*226*	*33.35*	*25.68*	*-4.46*
Fuji Xerox Finance Limited	8	31-Mar	2014	361,341	37,014	10.24	350,969	n/d	138.23	27.55	22.02
			2013	*296,123*	*22,218*	*7.50*	*294,147*	*n/d*	*-476.74*	*27.76*	*13.18*
GE Capital[b]	1	31-Dec	2013	2,829,296	372,410	13.16	1,955,746	853	809.65	1,115.36	6.96
			2012	*2,645,286*	*205,279*	*7.76*	*1,991,861*	*794*	*-92.00*	*-93.92*	*4.08*
Instant Finance Limited	20	31-Mar	2014	88,529	24,415	27.58	83,777	140	1.28	0.29	2.77
			2013	*86,142*	*23,142*	*26.86*	*82,520*	*136*	*0.33*	*-0.64*	*0.88*
John Deere Financial Limited	15	31-Oct	2013	135,584	12,603	9.30	129,246	n/d	42.52	42.60	13.32
			2012	*119,648*	*9,593*	*8.02*	*113,057*	*n/d*	*6.67*	*6.58*	*20.12*
Medical Securities Limited	13	31-Oct	2014	202,860	37,170	18.32	170,079	31	-10.34	-8.75	-7.46
			2013	*219,221*	*50,498*	*23.04*	*173,388*	*32*	*-34.62*	*-36.26*	*-5.69*
Mercedes-Benz Financial Services New Zealand Limited	6	31-Mar	2013	464,252	37,481	8.07	448,497	26	-1.85	-4.53	17.56
			2012	*394,923*	*28,345*	*7.18*	*381,164*	*26*	*21.80*	*25.10*	*-0.12*
Motor Trade Finances Limited	5	31-Dec	2014	540,910	80,676	14.91	489,291	51	-24.82	-16.13	22.94
			2013	*439,996*	*77,101*	*17.52*	*397,357*	*49*	*75.80*	*47.15*	*7.83*
Nelson Building Society	7	30-Sep	2014	414,210	26,155	6.31	318,366	36	42.96	46.47	10.10
			2013	*376,204*	*22,000*	*5.85*	*289,247*	*36*	*-8.25*	*-5.71*	*10.68*
ORIX New Zealand Limited	12	31-Mar	2014	229,576	131,810	57.41	33,046	63	0.81	0.66	2.10
			2013	*224,864*	*114,429*	*50.89*	*37,313*	*64*	*-3.89*	*0.57*	*-20.42*
Police & Families Credit Union	19	31-Mar	2014	98,434	17,284	17.56	63,729	13	33.44	37.62	9.70
			2013	*89,727*	*15,671*	*17.47*	*55,692*	*14*	*-8.35*	*-4.40*	*2.51*
Ricoh New Zealand Limited	14	30-Jun	2014	136,401	49,554	36.33	88,487	369	0.58	13.98	17.87
			2013	*115,720*	*30,123*	*26.03*	*73,057*	*336*	*11.07*	*-21.55*	*3.14*
The Warehouse Financial Services Limited	21	30-Sep	2013	82,543	12,621	15.29	68,490	n/d	-5.37	-5.35	-9.14
			2012	*90,844*	*14,669*	*16.15*	*71,316*	*n/d*	*-9.09*	*-11.99*	*-1.20*
Toyota Finance New Zealand Limited	3	31-Mar	2014	1,138,883	158,377	13.91	763,923	84	114.73	92.94	8.72
			2013	*1,047,516*	*143,103*	*13.66*	*734,397*	*83*	*-34.68*	*-37.80*	*-4.83*
UDC Finance Limited	2	30-Sep	2014	2,354,448	341,412	14.50	2,293,481	144	19.94	20.29	8.42
			2013	*2,171,656*	*314,869*	*14.50*	*2,089,816*	*168*	*13.24*	*13.76*	*2.72*
Wairarapa Building Society	16	31-Mar	2014	114,160	16,006	14.02	88,849	9	133.88	11.11	10.38
			2013	*103,426*	*15,707*	*15.19*	*85,514*	*9*	*-51.79*	*10.82*	*-0.62*
Non-banking sector total[c]				**10,978,995**	**1,581,084**	**14.40**	**8,815,059**	**2,426**	**102.63**	**45.47**	**8.41**
				10,127,469	***1,323,307***	***13.07***	***8,249,433***	***2,330***	***-49.30***	***-30.95***	***3.20***
Custom Fleet NZ		*31-Dec*	*2012*	*1,088,207*	*58,187*	*5.35*	*618,681*	*n/d*	*-12.05*	*-17.44*	*-1.12*
GE Finance and Insurance Limited		31-Dec	2013	2,677,503	326,795	12.21	1,900,060	853	307.61	314.43	91.21
			2012	*1,400,298*	*103,928*	*7.42*	*1,257,368*	*794*	*-170.13*	*-168.46*	*5.76*
GE Commercial Finance NZ Limited		31-Dec	2013	134,247	45,003	33.52	42,270	n/d	111.89	37.81	-4.55
			2012	*140,652*	*43,168*	*30.69*	*100,763*	*n/d*	*-53.34*	*-41.65*	*38.48*
GE Commercial Finance (USD) NZ Limited[d]		31-Dec	2013	17,546	612	3.49	13,416	n/d	-1,846.02	-4,427.37	8.79
			2012	*16,129*	*n/a*	*n/a*	*15,049*	*n/d*	*-781.82*	*350.00*	*4.75*

Key: n/a = not available/applicable; n/d = not disclosed.

Footnotes

Changes in accounting policy that have an immaterial impact on the financial statements have not been detailed in the following footnotes. The effect of the changes listed below has been to impact certain ratios, or to lead to the omission of certain ratios.

(a) Where applicable, consolidated Group numbers have been used.

(b) GE Management made the decision to go to market under one brand, showing all of their business operations which operate together in New Zealand as GE Capital. Operationally this has occurred, however, they legally operate as separate entities. These include the entities GE Finance and Insurance (parent), Custom Fleet NZ, GE Commercial Finance NZ and GE Commercial Finance (USD) NZ. We note that GE Finance and Insurance acquired Custom Fleet NZ in the year ended 31 December 2013, so from that point, Custom Fleet is reported as part of GE Finance and Insurance.

(c) Companies with total tangible assets less than $75 million are excluded from all sector totals.

(d) As at its prior year balance date, GE Commercial Finance (USD) NZ had goodwill and other intangible assets which exceeded its equity. In accordance with the Survey definitions, total assets and net assets are adjusted to exclude goodwill. We do not believe it is appropriate to present negative net tangible assets or gearing ratios; therefore, where they arise, they have been excluded.

(e) Net loans and advances exclude operating lease assets.

(f) Employee numbers are on a full time equivalent basis (including casuals and contracting staff) at the annual balance date and the prior balance date.

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Analysis of financial statements

ANALYSIS OF CONSOLIDATED ACCOUNTS OF NON-BANKS[a]		Credit quality measures					Profitability measures						Efficiency measures	
	Year	Impaired asset expense $000	Provision for doubtful debts/ Gross loans and advances %	Past due assets $000	Gross impaired assets $000	Impaired asset expense/Average loans and advances %	Interest margin %	Interest spread %	Non-interest income/Average total assets %	Net profit after tax $000	Net profit after tax/Average net tangible assets %	Underlying profit $000	Operating expenses/Average total assets %	Operating expenses/ Operating income %
Avanti Finance Limited	2014	1,247	3.50	628	11,817	1.25	13.53	10.99	9.83	9,238	32.88	12,838	9.57	40.61
	2013	945	3.86	71	11,720	1.06	13.66	9.55	9.78	8,361	24.92	11,627	9.44	39.81
BMW Financial Services New Zealand Limited	2013	107	1.50	n/d	n/d	0.03	7.52	7.14	0.32	8,032	46.75	11,105	4.40	56.68
	2012	191	0.81	n/d	n/d	0.07	7.03	6.69	0.32	7,578	42.40	10,616	3.40	46.71
Credit Union Baywide	2014	1,497	0.75	0	3,985	0.83	5.29	4.78	1.36	1,721	5.08	1,826	5.21	79.04
	2013	1,391	1.18	0	4,080	0.86	5.47	4.93	1.50	1,217	3.78	1,292	5.71	82.64
Credit Union South	2014	1,118	1.42	0	2,828	1.44	8.42	7.84	5.15	279	1.45	291	12.22	90.55
	2013	1,115	1.45	0	2,393	1.52	8.06	7.47	4.74	132	0.71	132	11.63	91.23
First Credit Union	2014	835	1.60	1,430	5,065	0.60	4.12	3.46	2.18	1,535	3.91	1,535	5.24	84.17
	2013	325	1.84	360	3,631	0.32	4.68	3.93	2.57	1,735	5.79	1,735	5.97	83.47
Fisher & Paykel Finance Group	2014	8,388	0.00	55,870	30,028	1.37	8.76	8.41	2.79	16,942	18.08	30,590	5.17	48.91
	2013	10,393	0.00	55,486	25,650	1.71	10.94	10.41	4.02	24,873	25.99	43,653	6.54	47.76
Fuji Xerox Finance Limited	2014	1,651	0.00	n/d	n/d	0.51	5.49	5.34	1.51	14,796	49.96	16,495	1.43	20.63
	2013	1,726	0.00	n/d	n/d	0.63	6.66	6.39	0.36	-38,699	-93.10	12,932	1.68	24.26
GE Capital[b]	2013	49,155	2.88	n/d	n/d	2.43	9.02	8.57	2.66	69,891	24.20	100,951	5.65	50.74
	2012	34,455	2.15	n/d	n/d	1.71	9.23	8.67	2.91	7,683	3.16	8,306	9.99	85.84
Instant Finance Limited	2014	2,242	3.77	0	6,087	2.70	20.06	16.79	18.85	6,426	27.02	9,278	25.22	65.66
	2013	2,343	3.80	0	5,616	2.86	20.28	16.80	18.13	6,345	27.47	9,251	24.43	64.38
John Deere Financial Limited	2013	0	0.00	n/d	n/d	0.00	5.04	4.89	0.01	3,010	27.12	4,181	1.71	34.33
	2012	0	0.00	n/d	n/d	0.00	4.65	4.44	0.09	2,112	24.74	2,932	2.03	43.13
Medical Securities Limited	2014	211	0.31	0	0	0.12	3.49	2.58	0.42	1,673	3.82	2,326	2.70	69.22
	2013	80	0.31	6	0	0.04	3.54	2.41	0.26	1,866	3.76	2,549	2.62	69.27
Mercedes-Benz Financial Services New Zealand Limited	2013	951	1.46	0	0	0.23	4.49	4.05	0.00	9,016	27.39	12,505	1.39	30.70
	2012	-758	1.81	28	4,887	-0.20	4.42	3.93	0.00	9,186	32.94	13,099	1.33	29.92
Motor Trade Finances Limited	2014	-180	1.00	0	243	-0.04	9.32	8.33	2.57	6,143	7.79	10,682	9.58	81.73
	2013	293	1.00	176	235	0.08	9.79	8.62	3.73	8,171	11.01	12,737	10.21	76.86
Nelson Building Society	2014	455	0.27	0	1,424	0.15	2.50	2.27	0.25	2,193	9.11	3,218	1.79	65.82
	2013	256	0.14	33	0	0.09	2.42	2.19	0.21	1,534	7.30	2,197	1.92	73.72
ORIX New Zealand Limited	2014	-35	2.21	n/d	0	-0.10	12.00	9.14	6.14	16,684	13.55	23,170	7.25	41.58
	2013	-262	2.02	n/d	28	-0.63	11.05	9.73	5.44	16,550	15.60	23,017	6.92	43.57
Police & Families Credit Union	2014	-22	0.23	3	17	-0.04	4.58	4.05	0.29	1,612	9.78	1,734	3.03	62.48
	2013	9	0.28	0	17	0.02	4.46	3.92	0.23	1,208	8.02	1,260	3.25	69.40
Ricoh New Zealand Limited	2014	368	0.00	54	1,488	0.46	3.11	2.74	94.56	6,561	16.47	10,453	88.01	91.11
	2013	0	0.00	135	1,451	0.00	5.15	4.87	88.01	6,523	23.19	9,171	83.48	91.21
The Warehouse Financial Services Limited	2013	2,447	3.75	0	2,568	3.50	11.58	11.03	6.10	6,452	47.28	8,964	4.70	26.31
	2012	1,782	3.79	0	2,705	2.46	11.49	10.86	5.67	6,818	43.26	9,471	5.02	28.98
Toyota Finance New Zealand Limited	2014	2,176	2.99	23	2,986	0.29	5.21	4.57	1.17	28,591	18.97	36,525	2.87	44.74
	2013	3,087	2.92	2	5,452	0.44	5.24	4.65	-0.50	13,315	9.08	18,931	2.71	56.95
UDC Finance Limited	2014	11,733	1.38	5,172	19,436	0.53	4.85	4.14	0.20	51,543	15.71	71,768	1.38	27.27
	2013	7,123	1.78	6,778	24,814	0.34	4.42	3.69	0.12	42,975	14.05	59,664	1.44	31.62
Wairarapa Building Society	2014	37	0.10	598	516	0.04	2.22	1.95	0.56	283	1.78	330	2.21	86.75
	2013	50	0.06	287	0	0.06	2.32	2.05	0.64	121	0.77	297	2.37	87.63
Non-banking sector total[c]	**2014**	**84,381**	**1.64**	**63,778**	**88,488**	**0.98**	**6.78**	**6.18**	**2.94**	**262,621**	**18.08**	**370,765**	**5.20**	**54.67**
	2013	**64,544**	**1.60**	**63,362**	**92,679**	**0.80**	**6.97**	**6.29**	**2.80**	**129,604**	**9.60**	**254,869**	**6.36**	**66.51**
Custom Fleet NZ	2012	7,731	1.57	n/d	n/d	1.21	7.34	7.01	1.59	40,571	110.03	53,493	3.16	36.09
GE Finance and Insurance Limited	2013	49,591	2.97	n/d	n/d	3.05	11.99	11.40	3.43	69,880	32.45	100,892	7.23	49.48
	2012	26,728	2.62	n/d	n/d	2.10	11.35	10.62	4.20	-33,660	-20.59	-47,052	16.25	110.11
GE Commercial Finance NZ Limited	2013	-87	0.00	n/d	n/d	-0.12	2.84	1.88	2.00	1,835	4.16	2,493	2.78	61.36
	2012	-4	0.00	n/d	n/d	0.00	3.51	2.81	0.76	866	2.03	1,809	2.16	59.23
GE Commercial Finance (USD) NZ Limited	2013	-349	0.00	n/d	n/d	-2.45	2.65	2.63	1.20	-1,824	-599.69	-2,434	20.32	536.33
	2012	0	0.00	n/d	n/d	0.00	3.50	3.49	0.32	-94	-220.59	56	3.45	90.63

Key: n/a = not available/applicable; n/d = not disclosed.

Footnotes

Changes in accounting policy that have an immaterial impact on the financial statements have not been detailed in the following footnotes. The effect of the changes listed below has been to impact certain ratios, or to lead to the omission of certain ratios.

(a) Where applicable, consolidated Group numbers have been used.

(b) GE Management made the decision to go to market under one brand, showing all of their business operations which operate together in New Zealand as GE Capital. Operationally this has occurred, however, they legally operate as separate entities. These include the entities GE Finance and Insurance (parent), Custom Fleet NZ, GE Commercial Finance NZ and GE Commercial Finance (USD) NZ. We note that GE Finance and Insurance acquired Custom Fleet NZ in the year ended 31 December 2013, so from that point, Custom Fleet is reported as part of GE Finance and Insurance.

(c) Companies with total tangible assets less than $75 million are excluded from all sector totals.

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Definitions

Terms and ratios used in this Survey	Definitions used in this Survey
Gearing	Net assets divided by total assets.
Gross impaired assets	Includes all impaired assets, restructured assets, assets acquired through the enforcement of security, but excludes past due assets.
Impaired asset expense	The charge to the Profit and Loss Account for bad debts and provisions for doubtful debts, which is net of recoveries (where identifiable).
Interest bearing liabilities	Customer deposits (including accrued interest payable where identifiable), balances with banks, debt securities, subordinated debt and balances with related parties.
Interest earning assets	Cash on hand, money on call and balances with banks, trading and investment securities, net loans and advances (including accrued interest receivable where identifiable), leased assets net of depreciation and balances with related parties.
Interest expense	Includes all forms of interest or returns paid on debt instruments.
Interest margin	Net interest income divided by average interest earning assets.
Interest spread	Difference between the average interest rate on average interest earning assets, and the average interest rate on average interest bearing liabilities.
Loans and advances	Includes loans and advances, lease receivables (net of unearned income) and accrued interest receivable (where identifiable), but excludes amounts due from banks, marketable securities, loans to related parties, sundry debtors and prepayments.
Net assets	Total assets less total liabilities.
Net interest income	Interest income (including net income from acting as a lessor) less interest expense.
Net loans and advances	Loans and advances, net of individual provisions for doubtful debts.
Net profit after tax	After minority interests, adjusting for the impact of subvention payments.
Operating expense	Includes all expenses charged to arrive at net profit before tax (excluding interest expense, impaired asset expense, subvention payments, depreciation of leased assets where a lessor and amortisation/write-off of goodwill and other intangibles).
Operating income	Net interest income and income from all other sources net of depreciation of leased assets, but excludes subvention receipts.
Past due assets	Includes any asset which has not been operated by the counterparty within its key terms for 90 days and which is not an impaired or restructured asset.
Provision for doubtful debts	Includes both collective and individual provisions for bad and doubtful debts.
Total assets	Excludes goodwill assets (unless specifically defined).
Total liabilities	Includes subordinated debt, but excludes minority interest.
Ultimate shareholding	Identifies the ultimate holding company rather than any intermediate holding companies.
Underlying profit	Operating income less operating expense and impaired asset expense. Items of a non-recurring nature, unrelated to the ongoing operations of the entity, are excluded.

Ownership

(as at 30 November 2014)

Non-bank entity	Ultimate shareholding	%
Avanti Finance Limited	Various investment/nominee companies	100
BMW Financial Services New Zealand Limited	BMW AG	100
Credit Union Baywide	Various depositors	100
Credit Union South	Various depositors	100
First Credit Union	Various depositors	100
Fisher & Paykel Finance Group	Haier (Singapore) Management Holding Co. Pte. Limited	100
Fuji Xerox Finance Limited	Fuji Xerox Co. Ltd (Japan)	100
GE Capital	General Electric Company	100
Instant Finance Limited	Various Private Shareholders	100
John Deere Financial Limited	Deere & Company (USA)	100
Medical Securities Limited	Medical Assurance Society New Zealand Limited	100

Non-bank entity	Ultimate shareholding	%
Mercedes-Benz Financial Services New Zealand Limited	Daimler AG	100
Motor Trade Finances Limited	Various Licensed Motor Vehicle Dealers	100
Nelson Building Society	Various depositors	100
ORIX New Zealand Limited	ORIX Corporation	100
Police & Families Credit Union	Various depositors	100
Ricoh New Zealand Limited	Ricoh Co. Ltd (Japan)	100
The Warehouse Financial Services Limited	Westpac Banking Corporation, The Warehouse Group Limited	100
Toyota Finance New Zealand Limited	Toyota Motor Corporation (Japan)	100
UDC Finance Limited	Australia and New Zealand Banking Group	100
Wairarapa Building Society	Various depositors	100

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Credit ratings

(as at 30 November 2014)

Entity Name	Name of credit rating agency and rating							
	Standard & Poor's		Fitch Ratings		Moody's		Rating and Investment	
	Rating	Outlook	Rating	Outlook	Rating	Outlook	Rating	Outlook
Avanti Finance Limited	BB	Positive						
BMW Financial Services New Zealand Limited[a]	A+	Stable			A2	Stable		
Credit Union Baywide	BB	Negative						
Credit Union South	BB-	Developing						
First Credit Union	BB	Negative						
Fisher & Paykel Finance Group	BB+	Stable						
Fuji Xerox Finance Limited[b]							AA	Stable
GE Capital[c]	AA+	Stable			A1	Stable		
Instant Finance Limited								
John Deere Financial Limited[d]					A2	Stable		
Medical Securities Limited	BBB+	Stable						
Mercedes-Benz Financial Services New Zealand Limited[e]	A-	Stable			A3	Stable		
Motor Trade Finances Limited								
Nelson Building Society			BB+	Stable				
ORIX New Zealand Limited[f]	A-	Stable	A-	Stable	Baa2	Stable	A+	Stable
Police & Families Credit Union	BB+	Stable						
Ricoh New Zealand Limited[g]	A	Stable					AA-	Negative
The Warehouse Financial Services Limited								
Toyota Finance New Zealand Limited	AA-	Stable			Aa3	Stable		
UDC Finance Limited	AA-	Stable						
Wairarapa Building Society			BB+	Stable				

Long-term credit rating grades assigned by Standard & Poor's	Description of the steps in the Standard & Poor's credit rating grades for the rating of the long-term senior unsecured obligations payable in New Zealand, in New Zealand dollars.
AAA	Extremely strong capacity to meet financial commitments. Highest rating.
AA	Very strong capacity to meet financial commitments.
A	Strong capacity to meet financial commitments, but somewhat susceptible to adverse economic conditions and changes in circumstances.
BBB	Adequate capacity to meet financial commitments, but more subject to adverse economic conditions.
BB	Less vulnerable in the near term, but faces major ongoing uncertainties to adverse business, financial and economic conditions.
B	More vulnerable to adverse business, financial and economic conditions, but currently has the capacity to meet financial commitments.
CCC	Currently vulnerable and dependent on favourable business, financial and economic conditions to meet financial commitments.
CC	Currently highly vulnerable.
Plus (+) or Minus (-)	The ratings AA to CCC may be modified by the addition of a plus (+) or minus (-) sign to show relative standing with the major rating categories.
BB, B, CCC, and CC	Borrowers rated BB, B, CCC and CC are regarded as having significant speculative characteristics. BB indicates the least degree of speculation and CC the highest. While such borrowers will likely have some quality and protective characteristics, these maybe outweighed by large uncertainties or major exposures to adverse conditions.
Assigned by Moody's Investor Service	Moody's Investors Service appends numerical modifiers 1, 2 and 3 in each generic rating classification from Aa through Caa. The modifier 1 indicates the obligation ranks in the higher end of its generic category; the modifier 2 indicates a mid range ranking; and the modifier 3 indicates the lower end of that generic category.
Assigned by Fitch Ratings	Fitch Ratings applies 'investment grade' rates 'AAA' to 'BBB' to indicate relatively low to moderate credit risk, while those in the 'speculative' or 'non-investment grade' categories which have either signalled a higher level of credit risk or that a default has already occurred, Fitch Ratings applies a 'BB' to 'D' rating. The modifiers '+' or '-' may be appended to a rating to denote relative status within the major rating categories. Credit ratings express risk in relative rank order, which to say they are ordinal measures of credit risk and not predictive of a specific frequency of default or loss.

Footnotes

(a) Rating of parent company BMW AG
(b) Rating of parent company Fuji Xerox Co. Ltd
(c) Rating of parent company GE Capital Corporation
(d) Rating of John Deere Financial Limited Australia
(e) Rating of parent company Daimler AG
(f) Rating of parent company ORIX Corporation
(g) Rating of parent company Ricoh Co Ltd

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