

24 August 2017

KINA SECURITIES FIRST HALF 2017 RESULTS

Kina delivers profit, dividend and key projects.

Financial highlights

- underlying profit of PGK10.0m
- statutory profit of PGK3.0m
- interim dividend of AUD\$0.02 cents/PGK 0.05 toea per share.

Kina Securities Limited (KSL) has reported a statutory profit of PGK3.0m and an underlying profit of PGK10.0m for the half year to June 2017. The statutory profit has been calculated in accordance with International Financial Reporting Standards and reflects a lease termination expense of PGK7.0m.

The financial result compares with a profit of PGK20.5m in the corresponding six months to June 2016 (H1 2016) and PGK20.5m in the half year to December 2016 (H2 2016). The drop in earnings has largely been attributed to lower income from foreign currency trading as a result of the withdrawal of Kina's USD correspondent banking partner in FY 2016.

Kina recently announced it has established a new USD correspondent banking arrangement with leading ASEAN bank, CIMB Bank.

The one-off profit adjustment related to an agreement for the Group to relocate to a new building, Kina Haus. The arrangement was entered into prior to Kina's plans to list on the ASX. The Board took the decision to terminate the arrangement and for the Group to remain in its present location, as a relocation no longer aligned with its future business direction or represented the best value for the company.

However, Kina is presently in discussions with its landlord regarding the renewal of its current lease, with a view to negotiating terms which will recover the termination expense over the term of the new lease.

Kina continued to grow all of its businesses during H1 2017, excluding the impact of the decline in FX income.

The Group achieved the following operational highlights:

- Grew loan market share from 3.7% in H1 2016 to 5.6% at the end of H1 2017
- Achieved 57% growth in loans compared with June 2016 including 13% in H1 2017.
- Lending growth has been moderated in H1 2017 to keep loan to deposit ratio within target range of 60-70%
- Delivered a 13.8% increase in Business lending and Personal lending growth of 10.1%, with total loans now recorded at PGK685m compared with December 2016.

- The realignment of customer deposit base from high cost to low cost was a priority for H1 2017. This was to ensure the cost of funds remains within 2-3% for the year and will continue to be the focus in H2 2017
- Increased the number of transactional accounts by 10% with the number of Term Deposits remaining stable compared with December 2016
- Opening the new Vision City retail outlet in May 2017 which has generated growth of new to bank customers.
- Successfully delivered agreement to become PNG's first bank to sign a trade finance agreement with the Asian Development Bank (ADB). The deal will assist Kina's local importing and exporting business customers by providing access to ADB's Trade Finance Program (TFP).

Kina Managing Director Syd Yates said the result reflected a solid underlying performance with solid contributions from its key Banking and Wealth Management businesses.

"Asset quality remains sound and our underlying capital position remains strong," Mr Yates said.

"After the reporting period, Kina delivered on a number of key projects including the agreement to establish a new USD correspondent banking arrangement with leading ASEAN bank, CIMB Bank, and the Nasfund funds under administration transaction. The performance of these arrangements will generate additional revenues in the second half and provide confidence in Kina's ability to deliver on its strategies in the future."

"For Kina, technology is the key to providing simpler, more affordable and easier to access products and the Group continues to focus on its technology transformation.

"Kina continued to enhance its banking systems and technology during the half year to support business growth. This includes upgrading and modernising the Core Banking systems, which has enabled new products to be added, on-line services expanded and new synergies between the Banking and Wealth Management businesses. This project is expected to continue in 2017 with further investment in systems to deliver new business growth."

"While the PNG operating environment remains challenging across the banking sector well positioned to weather the recent slowing in economic growth.

"With the PNG Election now over and the promise of political stability, PNG's economy appears to be undergoing a slight recovery in 2017 and there appears to be improving business sentiment. These factors provides a more favourable backdrop for Kina's operations."

Kina Bank

Kina Bank recorded net interest income of PGK33.6m for the half year, up 7% from H1 2016. This was achieved by driving loan book growth while ensuring careful management of cost of funds and yield on interest earning assets.

Total non-interest income was impacted in H1 2017 after the withdrawal of the bank's previous USD Correspondent bank partner in FY2016. As advised to the market in May 2017, the impact in H1 2017 is PGK10.7m compared to the same period last year. The acquisition of a new correspondent banking partner will assist in returning foreign exchange income to normal levels in H2 2017 and beyond.

In H1 2017, bank fees and commissions income grew by 9%, compared to December 2016, reflecting growth in lending and retail customer segments. This assisted in cushioning the impact from the drop in foreign exchange income.

Wealth Management

The Wealth Management division delivered growth in the funds management, stockbroking and trustee businesses. However, foreign exchange income (realised and unrealised) adversely impacted the division's net profit for the current year.

The division contributed PGK2.2m to the H1 2017 result, compared with PGK3.6m in H1 2016 primarily due to currency revaluation losses and higher initial staffing costs for the forthcoming Nasfund project. The success of Kina's Funds Administration service in signing the agreement to provide services to one of PNG's largest superannuation fund, Nasfund was a highlight for the division in H1 2017. This agreement went live in August 2017 and this contract is expected to increase revenue by PGK3.6m by end of H2 2017.

Importantly, this contract will lift Kina's funds under administration to PGK4b to PGK10b. This means Kina has the opportunity to offer targeted wealth management and banking products to a customer base in excess of 700,000 superannuation members.

Asset quality

Overall asset quality remains sound. The loan impairment expense decreased to PGK1.3m in H1 2017, from PGK2.5m in H1 2016. Impairment expense as a proportion of Gross Loans and Advances (GLA) remained low at 0.2%. Gross non-performing loans were just PGK2.8m, equal to 0.4% of GLA.

The Coverage ratio stands at 115% as at 30 June 2017 and is at similar levels to June 2016. Kina adopts the industry standard methodology of measuring loan loss provision cover against the balance of greater than 90 days impaired balances.

Operating Expenses

Operating expenses from ordinary activities for H1 2017, excluding the one-off lease termination expense, grew by 12% compared to H1 2016 reflecting the growth in core business. Overall costs were managed and staffing costs remain at 47% of total costs and business operating costs including IT spend remain at 25% of total cost.

Cost to income ratio excluding the one-off lease termination expense in H1 2017 was 67%, up from 48% in H1 2016. The increase in the cost to income ratio was largely due to a drop in foreign exchange income. If the FX income had been as in previous year, the ratio would have been similar to H1 2016.

Capital

The capital of the business remains strong, with regulatory capital (T1+T2) at 28% of risk weighted assets (RWA), compared with a regulatory required minimum of 12%.

Outlook

PNG's economy appears to be undergoing a slight recovery in 2017 following a period of slow expansion. This has been reflected in the positive sentiment of executives polled in the Oxford Business Group's (OBG) inaugural *OBG Business Barometer: PNG CEO Survey* released in July

2017. More than 60% of survey respondents have positive or very positive expectations for business conditions. OBG said some weak headline numbers, depreciation of the kina and a shortage of US dollars have slowed imports and led to pockets of local strength. The Group also reported robust activity in the small and medium-sized enterprise segment.

According to the Asian Development Bank, the PNG economy is expected to grow by 2.5% in 2017 and, with the hosting of the Asia-Pacific Economic Cooperation Leaders' Meeting, by 2.8% in 2018.

Despite some challenges in PNG's operating environment, improving economic conditions and business sentiment provide a more favourable backdrop for Kina's operations.

In a country such as PNG with a geographically dispersed population, technology is opening up new opportunities for businesses to provide services to customers.

Key strategic priorities

Kina set a number of key operational priorities for the year in January 2017. The Board and management continued to pursue these priorities including:

- Completing the bank's technology transformation. This includes expanding Kina's suite of personal and business banking products and services such as mobile applications for retail customers and mobile applications and internet banking for corporate clients
- Continuing to provide increased convenience for our customers by pursuing options to launch new branches in strategic locations within PNG
- Ongoing delivery of profitable, quality lending growth
- Achieving continued growth in the low-cost deposit base
- Maintaining a strong prudential position and conservative capital adequacy
- Maintain a net interest margin in target range of 7-9%
- Ongoing focus on reducing the cost to income ratio in a target range of 45%-50%, by efficient cost control and growing other income streams.
- Leveraging key superannuation fund relationships to facilitate cross-selling opportunities. The ability to leverage PNG's three largest superannuation funds provides a significant database of large and affluent members which can be offered a suite of Banking and Wealth products and services.

SYD YATES, OBE

Chief Executive Officer & Managing Director

For further information, please contact;

CHETAN CHOPRA

CFO & Company Secretary

+675 7004 6615

Chetan.Chopra@kina.com.pg