Genworth Financial Mortgage Insurance Pty Limited New Zealand Branch

Annual Financial Report
31 December 2019

Directors' report

The directors of Genworth Financial Mortgage Insurance Pty Limited ("the Company") present their report together with the financial statements of Genworth Financial Mortgage Insurance Pty Limited New Zealand Branch ("the Branch") for the year ended 31 December 2019 and the auditor's report thereon.

Directors

The directors of the Company at any time during or since the end of the financial year are as follows:

David Foster
Ian MacDonald
Gai McGrath
Georgette Nicholas (ceased as a Director on 31 December 2019)
Christine Patton
Stuart Take
Gayle Tollifson
Jerome Upton
Duncan West

Principal activities

The principal activity of the Branch during the financial year was the provision of lenders mortgage insurance ("LMI"). The Branch ceased to write new business from 30 September 2011, and ceased writing top up policies from 30 September 2013. The Branch continues to manage the run-off portfolio.

Review and result of operations

The Branch's profit after income tax amounted to $467,578 (2018: $2,095,210).

Corporate structure

Genworth Financial Mortgage Insurance Pty Limited New Zealand Branch is a branch of an Australian company, Genworth Financial Mortgage Insurance Pty Limited (GFMI).

The parent entity of the Company is Genworth Mortgage Insurance Australia Limited (GMA). GMA's major shareholder is Genworth Financial International Holdings, LLC & Genworth Holdings, Inc. (as partners of the Genworth Australian General Partnership) representing 51.95% ownership. The ultimate parent entity of the Genworth Australian General Partnership is Genworth Financial Inc. (GFI) which is incorporated in Delaware, United States of America.

The Genworth Financial Mortgage Insurance Pty Limited New Zealand Branch's registered office is located at c/o Bell Gully, Vero Centre, 48 Shortland Street, Auckland.

Events subsequent to reporting date

Details of matters subsequent to the end of the financial year is set out below and in the events subsequent to reporting date note within the financial statements.

On 24 January 2020, the Company announced the appointment of Pauline Blight-Johnston as Chief Executive Officer and Managing Director effective 2 March 2020.

On 18 February 2020, the Company announced the retirement of Gayle Tollifson from the Board of Genworth effective 15 March 2020 and the appointment of Andrea Waters to the Board effective 16 March 2020. These changes were made as part of Genworth's Board renewal program.

Branch number

1493716

Auditors

KPMG

Bankers

Westpac Banking Corporation

Solicitors

Bell Gully
PO Box 4190
Auckland

Buddle Findlay
PO Box 1433
Auckland

The Board of Directors present their Annual Report, including financial statements of the New Zealand Branch, for the year ended 31 December 2019, and the auditor's report thereon.

The shareholder of the Company has exercised its right under Section 211(3) of the Companies Act 1993 and unanimously agreed that this Annual Report need not comply with any of paragraphs (a) and (e) to (j) of Section 211(1) of (the Act).

For and on behalf of the Board:

Ian MacDonald
Chairman

Gai McGrath
Director

Dated at Sydney, 26 February 2020

Financial statements

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Statement of comprehensive income

For the year ended 31 December 2019

	Note	2019 NZ$	2018 NZ$
Movement in unearned premium		36,103	61,525
Net earned premium		36,103	61,525
Net claims write back/(incurred)	4.1	218,036	(73,379)
Movement in unexpired risk liability	4.4	167,748	2,094,227
Other underwriting expenses	3.2	(31,991)	(15,273)
Profit from underwriting		389,896	2,067,100
Investment income	3.1	77,682	64,218
Other operating (expenses)		-	(36,108)
Profit before income tax		467,578	2,095,210
Income tax expense	3.4	-	-
Profit for the year		467,578	2,095,210
Total comprehensive income for the year		467,578	2,095,210

The statement of comprehensive income is to be read in conjunction with the notes to the financial statements.

Statement of financial position

As at 31 December 2019

	Note	2019 NZ$	2018 NZ$
Assets			
Cash and cash equivalents		2,054,509	1,944,710
Accrued investment income		8,860	9,736
Investments	2.1	1,500,000	1,500,000
Non reinsurance recoveries		11,340	18,932
Total assets		3,574,709	3,473,378
Liabilities			
Trade and other payables	6.1	16,582	-
Outstanding claims	4.2	267,295	446,273
Unearned premiums	4.4	38,648	74,751
Unexpired risk liability	4.5	546,501	714,249
Total liabilities		869,026	1,235,273
Head Office Account		2,705,683	2,238,105
Total liabilities and Head Office Account		3,574,709	3,473,378

The statement of financial position is to be read in conjunction with the notes to the financial statements.

Statement of movement in Head Office Account

For the year ended 31 December 2019

	2019 NZ$	2018 NZ$
Head Office Account at the beginning of the year	2,238,105	(562,958)
Capital contribution	-	705,853
Profit for the year	467,578	2,095,210
Head Office Account at the end of year	2,705,683	2,238,105

The statement of movement in head office account is to be read in conjunction with the notes to the financial statements.

Statement of cash flows

For the year ended 31 December 2019

	Note	2019 NZ$	2018 NZ$
Cash flows from operating activities			
Interest and other income		78,558	54,482
Claims recoveries received		46,650	52,013
Cash payments in the course of operations		(15,409)	(288,867)
Net cash provided by/(used in) operating activities	3.3	109,799	(182,372)
Cash flows from investing activities			
Payments for investments		6,000,000	(3,000,000)
Proceeds from sale of investments		(6,000,000)	1,500,000
Net cash used by investing activities		-	(1,500,000)
Net increase/(decrease) in cash held		109,799	(1,682,372)
Cash and cash equivalents at the beginning of the financial year		1,944,710	3,627,082
Cash and cash equivalents at the end of the financial year		2,054,509	1,944,710

The statement of cash flows is to be read in conjunction with the notes to the financial statements.

Notes to the financial statements

Section 1 – Basis of preparation

1.1 Reporting entity

Genworth Financial Mortgage Insurance Pty Limited New Zealand Branch ("the Branch") is registered to carry on insurance in New Zealand as a foreign Branch. The principal activity is the provision of lenders mortgage insurance ("LMI"). The Branch is a for-profit entity.

The financial statements were authorised for issue by the Board of Directors on 26 February 2020.

1.2 Significant accounting policies

(a) Statement of compliance

The financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice ("NZ GAAP"). They comply with the New Zealand Equivalents to International Financial Reporting Standards ("NZ IFRS") and other applicable Financial Reporting Standards as appropriate to profit generating entities. The Branch is a reporting entity in terms of the Financial Markets Conduct Act 2013 and the financial statements have been prepared in accordance with the requirements of that Act and the Financial Reporting Act 2013.

The current IFRS standard for insurance contracts does not include a comprehensive set of recognition and measurement criteria. The IASB has issued a new standard (*IFRS 17 Insurance Contracts* – adopted as NZ IFRS 17 *Insurance Contracts* in a New Zealand context) that does include such criteria, the effective date of 1 January 2021 has been deferred to 1 January 2022 subject to being approved by the New Zealand Accounting Standards Board, at which time NZ IFRS 9 *Financial Instruments* will be implemented as well given the Branch meets the requirements for deferral under the amendment to NZ IFRS 4 *Applying NZ IFRS 9 Financial Instruments with NZ IFRS 4 Insurance Contracts.* Until this standard takes effect, the financial reports of insurers in different countries that comply with IFRS may not be comparable in terms of the recognition and measurement of insurance contracts.

(b) Basis of preparation

These financial statements are presented in New Zealand dollars.

Genworth Financial Mortgage Insurance Pty Limited New Zealand Branch is a branch of Genworth Financial Mortgage Insurance Pty Limited ("the Company") and is a separate reporting entity in terms of the Financial Markets Conduct Act 2013 and the Financial Reporting Act 2013. The branch and head office are one legal entity and therefore the Branch's financial statements should be read in conjunction with the Company's. The Company has a strong financial position and will provide necessary financial support when it is required to meet any future claims obligations of the Branch and any deficit in the Head Office Account. Based on this the directors are satisfied that the going concern assumption is appropriate.

The statement of financial position has been prepared using the liquidity format of presentation, in which the assets and liabilities are presented broadly in order of liquidity. The assets and liabilities comprise both current amounts (expected to be recovered or settled within 12 months after the reporting date) and non-current amounts (expected to be recovered or settled more than 12 months after the reporting date). For those assets and liabilities that comprise both current and non-current amounts, information regarding the respective current and non-current amounts is disclosed in the relevant note to the financial statements.

Items included in the financial statements are measured using the currency of the primary economic environment in which the Branch operates. The financial statements are presented in New Zealand dollars, which is the Branch's functional and presentation currency.

The Branch has applied the amendment to NZ IFRS 4 *Applying NZ IFRS 9 Financial Instruments with NZ IFRS 4 Insurance Contracts* from 1 January 2018, and has made the required disclosures in its 2019 financial statements in relation to the deferral of NZ IFRS 9 *Financial Instruments*.

The mandatory application of NZ IFRS 17 *Insurance Contracts* ("NZ IFRS 17") has been deferred to 1 January 2022 subject to approval of the proposed one-year delay.The Branch continuing to work through the detailed impact assessment of the new standard. NZ IFRS 17 is likely to have significant impact on the Branch's recognition and measurement of insurance contracts and their disclosure in the financial statements.

A number of other new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2020, and have not been applied in preparing these financial statements. An initial assessment of these standards and amendments has taken place and the application of these standards is not expected to have material impact on the Branch's accounting policies.

The financial report is prepared on the historical cost basis except for investments being stated at fair value and outstanding claims and the related reinsurance recoveries on unpaid claims being stated at present value.

(c) Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held at call with financial institutions and other short-term and highly liquid investments with maturity from date of acquisition of three months or less that are readily convertible to known amounts of cash, that are subject to an insignificant risk of change in fair value and which are used to meet short-term cash commitments.

(d) Earned and unearned premium revenue

Premiums have been brought to account as income from the date of attachment of risk over periods up to twelve years based on an actuarial assessment of the pattern and period of risk. The earned portion of premiums received is recognised as revenue. The balance of premium received is carried as an unearned premium reserve.

(e) Comparative figures

Comparative figures have been adjusted, where necessary, to conform to the basis of presentation and the classification used in the current year.

Change in the presentation of the claims development in Note 4.1(b)
A new claims development attribution methodology for "current year" and "prior years" presentation has been introduced effective 1 January 2019 to reflect the substance of the underlying claims event. This involves claims incurred but not recorded being attributed to the year of actual incident (i.e. the year in which the loan first went into 30+ days in arrears).

As a result, the 2018 comparatives have been updated reducing the "current year" net claims incurred from $378,624 to $292,105 and a corresponding increase in the "prior years" net claims incurred from ($305,245) to ($218,726), with no change to total net claims incurred.

Change in the presentation of the current outstanding claims balance Note 4.2
A new claim payments attribution methodology for "current" and "non-current" outstanding claims liability has been introduced effective 1 January 2019 to reflect the underlying probability that delinquencies, including incurred but not reported delinquencies, will be paid in the next 12 months, based on the underlying characteristics of the delinquency.

As a result the 2018 comparatives have been updated, reducing the "current" outstanding claims liability from $354,361 to $195,563 and a corresponding increase in the "non-current" liability from $91,912 to $250,710 with no change in the total outstanding claims balance.

Section 2 - Risk management

2.1 Financial risk management

(a) Risk management framework

The Board has overall responsibility for the establishment and oversight of the risk management framework. The Board has established a Risk Committee, Audit Committee and a Capital and Investment Committee. The Risk Committee is responsible for developing and monitoring the Company's risk management policies, and reports regularly to the Board on its activities. Furthermore, the Committee assists the Board in providing an objective non-executive review and oversight of the implementation and on-going operation of the Company's Risk Management Framework. The Committee works closely with other Board Committees that have oversight of some material risks to ensure that all risks are identified and adequately managed.

The Audit Committee assists the Board in providing an objective non-executive review of the effectiveness of the risk management framework, in relation to the management of material financial risks. Similarly, the Capital and Investment Committee assists the Board in monitoring compliance with the Risk Management Framework, in relation to the execution of the Company's capital and investment strategy.

The Company's risk management policies are established to identify and analyse the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed to reflect changes in market conditions and the Company's activities. The Company, through its management policies and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

(b) Market risk

Market risk is the risk that the market price of assets change and the potential for such change to result in the actual market value of Genworth's assets being adversely impacted.

Cash flow and fair value interest rate risk

The Branch is exposed to interest rate risk arising on interest bearing assets. Assets with floating rate interest expose the Branch to cash flow interest rate risk. Fixed interest rate assets expose the Branch to fair value interest rate risk. The Branch's strategy is to invest in high quality, liquid fixed interest securities and cash and to actively manage duration. The investment portfolios are actively managed to achieve a balance between cash flow interest rate risk and fair value interest rate risk bearing in mind the need to meet the liquidity requirements of the insurance business.

The potential impact of movements in interest rates on the Branch's profit or loss and equity resulting from a 1% increase/decrease in interest rates on interest bearing assets, assuming all other variables remain constant, are shown below.

	2019	2018
	NZ$	NZ$
+1% increase in interest rates	27,871	35,848
-1% decrease in interest rates	(27,871)	(35,848)

(c) Credit risk exposures

Credit risk is the risk of default by borrowers and transactional counterparties as well as the loss of value of assets due to deterioration in credit quality. The Branch's credit risk arises predominantly from investments and the amounts are as indicated by the carrying amounts of the financial assets.

The Branch's investment portfolio comprises 100% (2018: 100%) cash and term deposits $3,554,509 (2018: $3,444,710) with counterparties having a rating of AA based on the lower equivalent rating of either Standard & Poor's or Moody's. The Branch does not expect any investment counterparties to fail to meet their obligations given their strong credit ratings.

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if available) or to historical information about counterparty default rates. As at balance date there were no assets past due.

As an eligible insurer, the Branch is required to present the credit risk rating of its financial assets with contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding ("SPPI assets"). All the financial assets of the Branch at 31 December 2019 and 31 December 2018 are SPPI assets, with a low credit risk. These assets are carried at face value, as a proxy for fair value. As such, there is no change in fair value in 2019 and 2018.

(d) Liquidity risk

Liquidity risk is the risk of there being insufficient cash resources to meet payment obligations without affecting the daily operations or the financial condition of the Branch. The Company has a strong financial position and will provide necessary financial support when it is required to meet any future claims obligations of the Branch and any deficit in the Head Office Account.

Management of liquidity risk includes asset and liability management strategies. The assets held to back insurance liabilities consist of highly rated money market securities. The assets are managed so as to effectively match the maturity profile of the assets with the expected pattern of claims payments.
The money market securities are restricted to investment grade securities with concentrations of investments managed as per the investment mandate.

The only financial liabilities are payables of $16,582 which has a term of less than one year (2018: Nil).

(e) Fair value measurements

Accounting policies

The valuation methodology of assets valued at fair value is summarised below:

- Term deposits, cash assets and bank overdrafts are carried at face value of the amounts deposited or drawn.

The Branch's financial assets and liabilities are carried in the statement of financial position at amounts that approximate fair value.

The Branch investments carried at fair value have been classified under the three levels of the IFRS fair value hierarchy as follows:

Level 1 - Quoted prices in an active market: Fair value investments which are quoted in active and known markets. The quoted prices are those at which transactions have regularly and recently taken place within such markets.

Level 2 - Valuation techniques with observable parameters: Fair value investments using inputs other than quoted prices within Level 1 that are observable either directly or indirectly.

Level 3 - Valuation techniques with significant unobservable parameters: Fair value investments using valuation techniques that include inputs that are not based on observable market data.

All investments (short term deposits) of $1,500,000 (2018: $1,500,000) are considered Level 1 assets.

Section 3 – Results for the year

3.1 Investment income

Accounting policies

Interest revenue

Interest revenue is recognised as it accrues, taking into account the coupon rate on investments and interest rates on cash and cash equivalents, net of withholding tax paid or payable.

	2019 NZ$	2018 NZ$
Interest	77,682	64,218
	77,682	64,218

3.2 Other underwriting expenses

	2019 NZ$	2018 NZ$
Operating expenses	31,991	15,273
	31,991	15,273

The Branch ceased underwriting new policies from 30 September 2011, and ceased writing top up policies from 30 September 2013. The Branch continues to manage the run-off portfolio.

3.3 Net cash provided by operating activities

This note reconciles the operating profit to the cash provided by operating activities per the cash flow statement.

	2019 NZ$	2018 NZ$
Profit after income tax	467,578	2,095,210
Net cash provided by operating activities before change in assets and liabilities	467,578	2,095,210
Change in assets and liabilities during the financial year:		
Decrease/(Increase) in receivables	8,468	(15,556)
(Decrease)/Increase in outstanding claims liability	(178,978)	131,213
Increase/(Decrease) in payables	16,582	(943,340)
(Decrease)/Increase in unexpired risk reserve	(167,748)	(2,094,227)
Decrease in unearned premiums	(36,103)	(61,525)
Capital contribution	-	705,853
Net cash provided/(used) in operating activities	109,799	(182,372)

3.4 Income tax

Accounting policies

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity.

Current tax is expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the statement of financial position date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the statement of financial position method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Temporary differences for the initial recognition of assets or liabilities that affect neither accounting nor taxable profit are not provided for. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the statement of financial position date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Income tax expense

	2019 NZ$	2018 NZ$
Income tax expense	-	-
	-	-

Reconciliation of income tax benefit to prima facie tax payable

	2019 NZ$	2018 NZ$
Prima facie income tax expense calculated at 28% (2018: 28%) on profit	130,922	586,659
(Decrease) in income tax expense due to:		
Recognition of prior period tax losses not previously brought to account	(130,922)	(586,659)
Income tax expense on profit	-	-

At the statement of financial position date the Branch had tax losses carried forward of $78,329,422 (2018: $78,629,253). The tax losses will be available to carry forward to offset against future profits of the Branch. No deferred tax asset has been recognised in respect of these tax losses due to insufficient certainty of future profits to utilise the losses.

Section 4 – Insurance Contracts

4.1 Net claims incurred

Accounting policies

Classification of insurance contracts

Contracts under which an entity accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary are classified as insurance contracts. Insurance risk is a risk other than financial risk.

(a) Claims analysis

	2019	2018
	NZ$	NZ$
Gross claims write back/(incurred)	171,385	(155,440)
Reinsurance and other recoveries revenue	46,651	82,061
Net claims incurred	218,036	(73,379)

(b) Claims development

	2019			2018		
	Current Year	Prior Years	Total	Current Year[2]	Prior Years[2]	Total
	NZ$	NZ$	NZ$	NZ$	NZ$	NZ$
Gross claims write back/(incurred)						
Direct	(32,111)	203,496	171,385	(292,105)	136,665	(155,440)
Gross claims write back/(incurred)[1]	(32,111)	203,496	171,385	(292,105)	136,665	(155,440)
Reinsurance and other recoveries revenue						
Reinsurance and other recoveries	-	46,651	46,651	-	82,061	82,061
Net claims write back/ (incurred)	(32,111)	250,147	218,036	(292,105)	218,726	(73,379)

[1] including reinsurance and other recoveries provision movement

[2] refer to note 1(e) for details on the adjustment to comparative figures

Current year amounts relate to risks borne in the current financial year. Prior year amounts relate to a reassessment of the risks borne in all previous financial years.

The prior year incurred losses and current year development continue to exhibit favourable experience in 2019, reflecting the nature of a run-off portfolio and continued stable economic and favourable housing conditions in 2019.

4.2 Outstanding claims

Accounting policies

Claims expense and a liability for outstanding claims are recognised in respect of direct business. The liability covers claims reported and outstanding, IBNR and the expected direct and indirect costs of settling those claims. Outstanding claims are assessed by estimating the ultimate cost of settling delinquencies, which includes IBNR and settlement costs, using statistics based on past experience and trends. Changes in outstanding claims are recognised in profit or loss in the reporting period in which the estimates are changed.

The provision for outstanding claims contains a risk margin to reflect the inherent uncertainty in the central estimate, the central estimate being the expected value of outstanding claims.

	2019 NZ$	2018 NZ$
Central estimate	235,862	393,793
Risk margin	31,433	52,480
Gross outstanding claims	267,295	446,273

Reconciliation of changes in outstanding claims

	2019 NZ$	2018 NZ$
Balance at 1 January	446,273	315,060
Current year net claims incurred	(218,036)	73,379
Movement in non reinsurance recoveries	(7,592)	5,821
Claims recoveries received	46,650	52,013
Balance at 31 December	267,295	446,273
Comprising[1]:		
Current	127,766	195,563
Non-current	139,529	250,710
	267,295	446,273

[1] refer to note 1(e) for details on the adjustment to comparative figures

4.3 Non reinsurance recoveries

Accounting policies

Non-reinsurance recoveries receivable on paid claims, reported claims not yet paid and IBNR claims are recognised as revenue. Recoveries receivable on paid claims are presented as part of non-reinsurance recoveries receivable net of any provision for impairment based on objective evidence for individual receivables. Recoveries receivable are assessed in a manner similar to the assessment of outstanding claims. Reinsurance does not relieve the Branch of its liabilities to policyholders and reinsurance recoveries are, if applicable, presented as a separate asset on the statement of financial position. The following table presents non-reinsurance recoveries.

4.4 Unearned premiums

Accounting policies

Earned and unearned premium revenue

Premiums have been brought to account as income from the date of attachment of risk over periods up to twelve years based on an actuarial assessment of the pattern and period of risk. The earned portion of premiums is recognised as revenue. The balance of premium received is carried as an unearned premium reserve.

Refer to Note 4.6 Accounting estimates and judgements for further detailed information.

	2019 NZ$	2018 NZ$
Balance at 1 January	74,751	136,276
Premiums earned during the year	(36,103)	(61,525)
Balance as at 31 December	38,648	74,751
Comprising:		
Current	20,783	40,868
Non-current	17,865	33,883
	38,648	74,751

4.5 Liability adequacy test

Accounting policies

Unexpired risk liability

Provision is made for unexpired risks arising from lenders mortgage insurance business where the expected value of claims and expenses attributed to the unexpired period of policies in force at the statement of financial position date exceeds the unearned premiums provision in relation to such policies after the deduction of any deferred acquisition costs and deferred reinsurance.

The provision for unexpired risk is calculated separately for each group of contracts subject to broadly similar risks and managed together as a single portfolio.

Any unexpired risk liability remaining after writing off deferred acquisition costs and deferred reinsurance premium is recognised immediately in the statement of comprehensive income.

Liability adequacy test

The liability adequacy test ("LAT") has been conducted using the central estimate of premium liabilities together with the appropriate margin for uncertainty for each portfolio of contracts that are managed as a single portfolio and are subject to broadly similar risks. The test is based on prospective information and so is heavily dependent on assumptions and judgements.

The LAT undertaken as at the balance date identified a deficit of $546,501 (2018: $714,249). The decrease in the unexpired risk liability of $167,748 (2018: $2,094,227 decrease) has been recognised in the statement of comprehensive income.

The probability of adequacy (POA) adopted in performing the liability adequacy test is set at the 70th percentile (2018: 70th percentile). The 70% PoA represented by the LAT differs from the 75% represented by the outstanding claims liability as the former is reflective of experience, whereas the latter is a measurement accounting policy used in determining the carrying value of the outstanding claims liability.

The continuing recognition of the deficiencies in unexpired risk liability is to reflect the tail experience related to older underwriting years. The deficiency continues to decline as premium liabilities decrease as a result of the Branch's book seasoning, with no new business written.

4.6 Accounting estimates and judgements

Critical accounting estimates and judgements

The Branch makes judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The areas where critical accounting estimates and judgements are applied are noted below.

Estimation of premium revenue and unearned premiums (Note 4.4)

Premium is earned over periods of up to twelve years. The principle underlying the earning recognition is to derive a premium earning scale which recognises the premium in accordance with the incidence of claims risk.

The review of the premium earning scale is based on an annual analysis of a number of factors including the historical pattern of claims incurred, the pattern of policy cancellations, economic outlook and policyholder risk profile. The estimate for unearned premiums is established on the basis of this earning scale. Changes to earnings curve assumptions, which in turn impact the timing of the recognition of unearned premium and DAC, are recognized prospectively. Changes are recommended by the Appointed Actuary when the results of the annual analysis indicate an ongoing change in the pattern of emergence of risk.

Estimation of outstanding claims liabilities (Note 4.2)

Provision is made for the estimated claim cost of reported delinquencies at the statement of financial position date, including the cost of delinquencies incurred but not yet reported to the Branch.

The estimated cost of claims includes direct expenses to be incurred in settling claims gross of expected third party recoveries. The Branch takes all reasonable steps to ensure that it has appropriate information regarding its claims exposure. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

The risk margin is an additional allowance for uncertainty in the ultimate cost of claims over and above the central estimate determined on the bases set out above. The overall margin adopted by the Branch is determined after considering the uncertainty in the portfolio, industry trends, the Branch's risk appetite and the margin corresponding with that appetite.

The estimation of IBNR is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Branch, where more information about the claim event is generally available. IBNR claims may often not be apparent to the insured or notified to the Branch until some time after the events giving rise to the claims have happened.

In calculating the estimated cost of unpaid claims, the Branch uses a variety of estimation techniques, generally based upon statistical analysis of historical experience of the Company and the Branch, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortion in the underlying statistics or which might cause the cost of unsettled claims to increase or decrease when compared with the cost of previously settled claims.

Provisions are calculated gross of any recoveries. A separate estimate is made of the amounts that will be recoverable from lenders under specified arrangements. Estimates are also made for amounts recoverable from borrowers and property valuers, based upon the gross provisions.

4.7 Actuarial assumptions and methods

(a) Outstanding claims

The Branch internally values the outstanding claims liabilities at the reporting date. The valuation approach is consistent with that recommended by the Company's Appointed Actuary.

The valuation methods used are based on the underlying attributes of the claims portfolio. The Branch establishes provisions for outstanding claims in two parts:

- Delinquent loans advised to the Branch by lenders as being 90 days delinquent at the valuation date.

- IBNR, being loans delinquent between 30 and 90 days, or not otherwise advised to the Branch by lenders.

The provision in respect of delinquent loans not in possession by the mortgagee is determined according to the following formula:

- Outstanding loan amount multiplied by frequency factor multiplied by severity factor.

In applying this formula:

- The outstanding loan amount insured is the total outstanding amount on those loans advised to the Branch;

- The frequency and severity factors are based on a review of historical claims and delinquency experience performed by the Appointed Actuary for the Company and adopted by the Branch.

Actuarial assumptions and process

Historical information relating to arrears and claims history for the Branch is provided to the Appointed Actuary in order to determine the underlying assumptions.

The Appointed Actuary examines all past underwriting years, including the mix of business by loan to value ratio ("LVR") and loan size band, the region in which the mortgaged property is located, product types, loan purpose and arrears duration.

Statistical modelling was used to identify significant explanatory factors affecting outcomes for frequency and severity based on historical claims experience.

The Appointed Actuary identifies significant explanatory factors affecting outcomes and incorporates this information into models for frequency and severity. The models incorporate past and anticipated movements in key variables to determine appropriate assumptions for reserving. The actuarial assumptions used in determining the outstanding claims liabilities, other than MIPs, are:

Frequency

While the propensity for a delinquent loan to become a claim varies for many explanatory factors (as determined by the Appointed Actuary's analyses), the frequency basis is summarised on any given balance date and expressed so that it varies by LVR band, housing price appreciation (HPA) and number of payments in arrears taking into account the average mix of effects of the other explanatory factors on the balance date. Additional loadings may be placed on these factors with the aim of adjusting for shorter term expectations of frequency.

Severity

Claim severity varies according to the geographic region of the properties secured by the mortgages and mortgagor groups. Claim severity is expressed as a percentage of the outstanding loan amount at the arrears date.

The following average frequency and severity factors were used in the measurement of outstanding claims:

- Average frequency factor is 31% (2018: 32%)
- Average severity factor is 30% (2018: 30%)

Incurred But Not Reported (IBNR)

The IBNR provision is estimated by analysing the historical pattern of reported delinquencies.

Risk Margin

The risk margin is an additional allowance for uncertainty in the ultimate cost of claims over and above the central estimate determined on the bases set out above. The overall margin adopted by the Branch is determined after considering the uncertainty in the portfolio, industry trends, the Branch's risk appetite and the margin corresponding with that appetite.

The Appointed Actuary reviews the factors impacting the portfolio to establish a recommended risk margin at the level required by the Branch and APRA. Factors considered include:

- Variability of claims experience of the portfolio.
- Quality of historical data.
- Uncertainty due to future economic conditions.
- Diversification within the portfolio.
- Increased uncertainty due to future legislative changes.

A risk margin for outstanding claims of 14% (2018: 14%) of net central estimate has been assumed and is intended to achieve a 75% PoA.

No discounting has been applied to non-current claims on the basis that the effect is immaterial.

The weighted average term to settlement is approximately 22 months (2018: 19 months).

Sensitivity Analysis

The results of the NZ actuarial valuation are subject to various degrees of uncertainty depending on economic experience and the volatility of claim experience over time. The valuation result is within expectations and not significant in dollar terms given this portfolio has been in run-off since 2013 and the net outstanding claims provision is $255,955 (2018: $427,341). The NZ portfolio is also less sensitive to future economic conditions as the book is ageing and the level of embedded home equity in the portfolio remains strong.

Claims handling expenses

Claims handling expenses are estimated after considering historical actual expenses and management's projected costs of handling claims over the weighted average term to settlement.

(b) Unearned premium

The assessment of future recognition of unearned premium is an inherently uncertain process involving assumptions concerning the discontinuance and pattern of the incidence of risk. When deciding an appropriate earning pattern to apply at the start of an underwriting year, consideration is given to:

- The emergence of claims and their cost for historical underwriting years.
- The economic outlook for key economic variables (interest rates, house prices and unemployment) at the time the policy was written.
- Policyholder risk profile, determined by characteristics such as location, LVR at underwriting, type of dwelling, loan type and type of interest repayment.

Over the term of a policy, changes in economic conditions invariably lead to a difference between the expected and actual risk emergence pattern. Over time, these differences may be sizeable and, as business is cyclical, these may build up over successive periods. The earnings curves is revised when experience indicates such differences are ongoing.

Section 5 – Capital management

5.1 Capital management

Under the New Zealand Insurance (Prudential Supervision) Act 2010, insofar as it relates to the Company, insurance entities operating in New Zealand are required to meet minimum solvency standards. The Branch has a section 59 exemption which, subject to certain requirements, means the Company is deemed to comply with the minimum solvency standards set out in the Act, provided it meets the corresponding APRA solvency requirements in Australia. The Company is in a strong financial position and will provide necessary financial support to the New Zealand branch when required to maintain any minimum solvency standards.

Under NZ legislation, the Company is required to maintain a solvency margin which is pursuant to an exemption granted by RBNZ is calculated in accordance with Australian solvency requirements.

The solvency information for the Company as at 31 December 2019 using RBNZ published exchange rate AUD = 1.044 NZD (2018: AUD = 1.052NZD) are detailed below:

	2019	2018
	NZ$'000	NZ$'000
Actual solvency capital	1,706,958	1,994,695
Minimum solvency capital	897,465	1,047,987
Solvency margin	809,493	946,708
Solvency ratio	190%	190%

To improve policyholder and market understanding of the capital adequacy of the company, the following table summarised the Australian Prudential Regulatory Authority's Prudential Standard GPS 110 Capital Adequacy requirements:

	2019 A$'000	2018 A$'000
Tier 1 capital		
Paid-up ordinary shares	1,401,559	1,401,559
Other reserves	(602,630)	(602,628)
Retained earnings	717,442	900,412
Less: Deductions	(36,956)	(34,622)
Net surplus(deficit) relating to insurance liabilities	(44,398)	31,377
Net Tier 1 capital	1,435,017	1,696,098
Tier 2 capital	200,000	200,000
Total capital base	1,635,017	1,896,098
Insurance risk charge	284,375	245,302
Insurance concentration risk charge	469,360	651,088
Asset risk charge	125,109	123,723
Asset concentration risk charge	-	-
Operating risk charge	36,192	31,962
Aggregation benefit	(55,395)	(55,890)
Total prescribed capital amount	859,641	996,185
Prescribed Capital Amount coverage	1.90x	1.90x

The Company has a strong financial position and will provide necessary financial support when it is required to meet any future claims obligations of the Branch and any deficit in the Head Office Account. On 31 May 2019, Standard & Poor's Ratings Services (S&P) reaffirmed Genworth Financial Mortgage Insurance Pty Limited's (GFMI) financial strength rating at 'A+' and outlook as 'negative'. S&P subsequently, on 1 July 2019, published revised criteria for rating insurance companies. On 25 July 2019 S&P announced that due to revisions to its rating criteria it has changed GFMI's financial strength rating to 'A' with a 'stable' outlook. GFMI holds an APRA capital adequacy multiple of 1.90x at 31 December 2019 (2018: 1.90x).

5.2 Capital commitments and contingencies

There were no capital commitments and contingent liabilities as at 31 December 2019 (31 December 2018: Nil)

Section 6 – Operating assets and liabilities

6.1 Trade and other payables

Accounting policies

Liabilities are recognised for amounts to be paid in the future for goods or services received. Trade accounts payable are normally settled within 30-60 days. The carrying amount of accounts payable approximates fair value.

	2019	2018
	NZ$	NZ$
Trade and other payables	16,582	-
Current	16,582	-

Section 7 – Other disclosures

7.1 Remuneration of auditors

	2019	2018
	NZ $	NZ $
Audit of financial reports	10,666	10,305
	10,666	10,305

Fees for the Branch are paid by the head office of the Company.

7.2 Related party disclosures

Transactions with related parties are undertaken on normal commercial terms and conditions.

7.3 Events subsequent to reporting date

Details of matters subsequent to the end of the financial year is set out below and in the events subsequent to reporting date note within the financial statements.

On 24 January 2020, the Company announced the appointment of Pauline Blight-Johnston as Chief Executive Officer and Managing Director effective 2 March 2020.

On 18 February 2020, the Company announced the retirement of Gayle Tollifson from the Board of Genworth effective 15 March 2020 and the appointment of Andrea Waters to the Board effective 16 March 2020. These changes were made as part of Genworth's Board renewal program.

Directors' declaration

In the opinion of the directors of Genworth Financial Mortgage Insurance Pty Limited, the financial statements and notes of the New Zealand Branch on pages 4 to 22:

(i) comply with New Zealand Generally Accepted Accounting Practice and give a true and fair view of the financial position of the Branch as at 31 December 2019 and the results of its operations for the year ended on that date; and

(ii) have been prepared using appropriate accounting policies, which have been consistently applied and supported by reasonable judgements and estimates.

The directors believe that proper accounting records have been kept which enable, with reasonable accuracy, the determination of the financial position of the Branch and facilitate compliance of the financial statements with the Financial Markets Conduct Act 2013 and the Financial Reporting (Amendments to Other Enactments) Act 2013 .

The directors consider that they have taken adequate steps to safeguard the assets of the Branch, and to prevent and detect fraud and other irregularities. Internal control procedures are also considered to be sufficient to provide reasonable assurance as to the integrity and reliability of the financial statements.

For and on behalf of the Board:

Ian MacDonald
Chairman

Gai McGrath
Director

Dated at Sydney, 26 February 2020.

Independent Auditor's Report

To the shareholder of Genworth Financial Mortgage Insurance Limited - New Zealand Branch

Report on the audit of the financial statements

Opinion

In our opinion, the accompanying financial statements of Genworth Financial Mortgage Insurance Limited - New Zealand Branch (the 'Branch') on pages 4 to 22:

i. present fairly in all material respects the Branch's financial position as at 31 December 2019 and its financial performance and cash flows for the year ended on that date; and

ii. comply with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

We have audited the accompanying financial statements which comprise:

— the statement of financial position as at 31 December 2019;

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

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

Basis for opinion

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

We are independent of the Branch in accordance with Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ('IESBA Code'), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our responsibilities under ISAs (NZ) are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

Other than in our capacity as auditor we have no relationship with, or interests in, the Branch.

Key audit matters

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

KPMG

The key audit matter	How the matter was addressed in our audit

Valuation of Gross Outstanding Claims Liability - NZ $267K

Refer to accounting policy in Note 4.1 Net claims incurred, Note 4.2 Outstanding Claims, Note 4.5 Accounting estimates and judgements and Note 4.6 Actuarial assumptions and methods.

The valuation of gross outstanding claims liability is a key audit matter as it is highly judgemental and requires assumptions to be made with inherent estimation uncertainty. These assumptions can have significant impacts on the valuation. This complexity requires us to exercise judgement when evaluating the methodology and assumptions adopted.

The Branch's insurance policies are similar in nature. As a result our audit focused on the Branch's consistent identification and application of common characteristics to segment the stages of claim emergence when applying frequency and severity (size) factors to determine the gross outstanding claims liability. These common characteristics include region, loan originator, outstanding loan size, and loan-to-value ratio. As a result of these factors, the estimation of the liability is highly dependent on the integrity of the underlying data.

The gross outstanding claims liability reflects the Branch's internal actuarial experts' assessment of future expected outcomes. These outcomes are influenced by a number of factors, including macroeconomic ones, which are subject to a wide range of views and interpretations. The valuation methodology requires the Branch to make assumptions in respect of these factors including:

- the uncertainty in the timing of claim payments and recoveries;
- the frequency at which claims emerge, and the subsequent severity of those claims. Frequency and severity is likely to be influenced by changes in macroeconomic factors such as interest rates, unemployment, property prices, house price movements and performance of industry and geographic segments;
- the timing of receipt of information from lenders indicating a delinquency or claim has occurred; and
- past claims experience being an appropriate predictor of future experience.

The assumptions adopted have a significant impact on the financial performance of the Branch, and therefore, are a focus of our audit attention. As a result, we involved senior audit team members, including specialists, who collectively understand the valuation methodology, the Branch's business, its industry and the economic and regulatory environment it operates in.

Our procedures included:

We tested the key controls designed and operated by the Branch for gross outstanding claims liabilities.

Along with our IT specialists, we assessed the key controls for significant data inputs used to determine the outstanding claims liability. Our assessment included testing specific reconciliation controls and interfaces from key IT systems that provide data used in the actuarial valuation processes underlying the outstanding claims liability.

We focused on the assumptions and valuation methodology used in estimating the gross outstanding claims liability. In so doing we challenged the methodology and the assumptions used in the valuation. We were assisted by our actuarial specialists in this regard and in our consideration of the work and findings of the Branch's internal actuarial experts, including their competency, objectivity, and scope of work. We considered the valuation methodology and assumptions for consistency between reporting periods, as well as for indicators of possible bias.

Our challenge focused on the assumptions applied to delinquencies and claims data. We did this by:

- evaluating underlying documentation. For example, we considered actual versus expected claims data and the timing of claims payments and recoveries using historical data;
- considering external information available (e.g. macroeconomic assumptions such as forecast interest rates, unemployment, property prices) and investigating significant variances. Specifically, we have considered the impact of recent trends in housing prices on the selected assumptions;
- identifying and analysing key changes in frequency and severity assumptions by comparing selected assumptions to experience exhibited to date; and
- assessing the consistency of information, such as claims experience and trends across the Branch's operations.

The key audit matter	How the matter was addressed in our audit

Valuation of Unexpired Risk Liability - (NZ $622K), Unearned Premium Liability (NZ $39K) and Net Earned Premium (NZ $36K), Movement in Unexpired Risk Reserve - (NZ $93K)

Refer to the accounting policy in Note 4.3 Unearned premium, Note 4.4 Liability Adequacy Test, Note 4.5 Accounting estimates and judgements, and Note 4.6 Actuarial assumptions and methods.

The Branch receives payment for its insurance policies upfront, however it is their policy to recognise this premium revenue over time. The timing pattern for recognition of premiums earned and the resulting valuation of the unearned premium liability (the proportion of the premium revenue not yet recognised), is determined by the Branch applying actuarial modelling techniques to develop an earnings curve. In this way, the timing of revenue recognition is dependent on the way in which claims are expected to emerge.

As the Branch ceased writing new business in 2011, the remaining unearned premium liability relates to policies written in 2011 and prior.

Provision is made for unexpired risks arising from business where the expected value of claims and expenses attributed to the unexpired period of policies in force at balance sheet date exceeds the unearned premiums provision in relation to these policies.

Net earned premiums and the unearned premium liability are a key audit matter due to the complexity of the actuarial methodology used to model the earnings curve and the significant level of judgment applied in assessing the assumptions adopted. The unexpired risk liability and movement in unexpired risk reserve are further included in this key audit matter due to its correlation with the unearned premium liability and the significant level of judgment applied in assessing the assumptions adopted in the performance of the liability adequacy test.

As a result the complexities noted in the key audit matter on *'Valuation of Gross Outstanding Claims Liability'* are also relevant to our work over the valuation of the unearned premium liability and the unexpired risk liability.

The assumptions adopted have a significant impact on the financial performance of the Branch. As a result, we involved senior audit team members, including specialists, who collectively understand the valuation methodology, the Branch's business and the economic and regulatory environment it operates in.

Our procedures included:

Along with our IT specialists, we assessed the key controls for significant data inputs. This included testing specific reconciliation controls, including those over the reliability of data used in the actuarial modelling processes and interfaces from key IT systems used in the valuation of the unearned premium liability. We further tested the key controls designed by management for the valuation of unearned premiums reserve and unexpired risk liability.

With the assistance of our Actuarial specialists, we focused on the assumptions and valuation methodology used by the Branch in their assessment.

We performed additional procedures to consider possible management bias. These included:

- an assessment of consistency in the adopted pattern of risk emergence;
- an assessment of sensitivity of the adopted earnings curve to more recent experience in key model assumptions; and
- consideration of the impact of more recent experience on the applied earnings curve.

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Other information

The Directors, on behalf of the Branch, are responsible for the other information included in the Annual Financial Report. Other information includes the Directors' Report. Our opinion on the financial statements does not cover any other information and we do not express any form of assurance conclusion thereon.

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

Use of this independent auditor's report

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

Responsibilities of the Directors for the financial statements

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

— the preparation and fair presentation of the financial statements in accordance with generally accepted accounting practice in New Zealand (being New Zealand Equivalents to International Financial Reporting Standards) and International Financial Reporting Standards;

— implementing necessary internal control to enable the preparation of a set of financial statements that is fairly presented and free from material misstatement, whether due to fraud or error; and

— assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.

Auditor’s responsibilities for the audit of the financial statements

Our objective is:

— to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error; and

— to issue an independent auditor’s report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs NZ will always detect a material misstatement when it exists.

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

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

http://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-2/

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

The engagement partner on the audit resulting in this independent auditor's report is David Kells

For and on behalf of

KPMG

KPMG Sydney

26 February 2020