

**Genworth Financial
Mortgage Insurance Pty
Limited**

ABN 60 106 974 305

Annual Financial Report
31 December 2020

Directors' report

The Directors present their report together with the financial statements of Genworth Financial Mortgage Insurance Pty Limited (the Company) for the year ended 31 December 2020 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:

Pauline Blight-Johnston (appointed on 2 March 2020)
David Foster
Ian MacDonald
Gai McGrath
Graham Mirabito (appointed on 10 August 2020)
Christine Patton (resigned on 9 August 2020)
Rajinder Singh (appointed on 9 September 2020)
Stuart Take
Gayle Tollifson (resigned on 15 March 2020)
Jerome Upton (resigned on 8 September 2020)
Andrea Waters (appointed on 16 March 2020)
Duncan West

Principal activities

The principal activity of the Company during the financial year was the provision of lenders mortgage insurance (LMI).

Review and result of operations

The Company reported a net loss after tax of \$107,698,000 compared to the \$119,952,000 net profit after tax in 2019. The loss was driven by an anticipated increase in future claims likely to occur from the economic impacts of COVID-19, which led to a write-down of deferred acquisition costs (DAC) of \$184.5 million at 31 March 2020 and an increase in claims reserving as a result of the refinement of the delinquency reserving methodology.

Corporate structure

Genworth Financial Mortgage Insurance Pty Limited is incorporated and domiciled in Australia. 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.

Genworth Financial Mortgage Insurance Pty Limited's registered office and principal place of business is Level 26, 101 Miller Street, North Sydney, NSW 2060.

Dividends

The Company paid an ordinary franked dividend per share of \$0.0221 amounting to \$31,000,000 to its shareholder, GMA on 18 March 2020. In 2019, the Company paid an ordinary franked dividend per share of \$0.0949 and \$0.050 amounting to \$133,000,000 and \$70,000,000 to its shareholder, GMA on 21 February 2019 and 21 August 2019 respectively. In addition, the Company also paid a special unfranked dividend per share of \$0.0714 amounting to \$100,000,000 to its shareholder GMA on 27 November 2019.

State of affairs

There were no significant changes in the state of affairs of the Company during the year.

Environmental regulations

The Company's operations are not subject to any significant environmental regulations under either Commonwealth or State legislation.

Events subsequent to reporting date

On 12 February 2021, the Directors determined that no dividend declaration would be made for the year ended 31 December 2020.

There are no events that have arisen since 31 December 2020 to the date of this report that, in the opinion of the Directors, have significantly affected or may significantly affect the operations of the Company or the state of affairs of the Company in future years.

Likely developments

Further information about likely developments in the operations of the Company and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the Company.

Indemnification and insurance of officers and auditors

During the financial year, the Company paid premiums to insure Directors and certain officers of the Company for the year ended 31 December 2020 and, since the end of the financial year, the Company has paid or agreed to pay premiums in respect of such insurance contracts for the year ending 31 December 2021. Such insurance contracts insure against liability (subject to certain exclusions) persons who are or have been Directors or officers of the Company.

The Directors have not included details of the nature of the liabilities covered or the amount of the premium paid as such disclosure is prohibited under the terms of the contracts.

The Company has not indemnified or made a relevant agreement for indemnifying against a liability any person who is or has been an auditor of the Company.

Directors' interests and benefits

Other than the aggregate remuneration paid or receivable by Directors included in the financial report, and remuneration as an executive paid or payable by the related body corporate, no Director has received or become entitled to receive any benefit because of a contract made by the Company or a related body corporate with a director or with a firm of which a Director is a member, or with an entity in which the Director has a substantial interest.

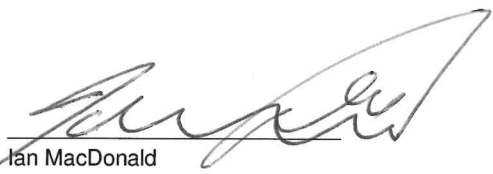
Rounding off

The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 dated 24 March 2016 and, in accordance with that Class Order, amounts in the financial statements and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

Lead auditor's independence declaration

The lead auditor's independence declaration is set out on page 5 and forms part of the Directors' report.

Signed in accordance with a resolution of the Directors:



Ian MacDonald
Chairman

Dated at Sydney, 26 February 2021



Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To the Directors of Genworth Financial Mortgage Insurance Pty Limited

I declare that, to the best of my knowledge and belief, in relation to the audit of Genworth Financial Mortgage Insurance Pty Limited for the financial year ended 31 December 2020 there have been:

- i. no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- ii. no contraventions of any applicable code of professional conduct in relation to the audit.

A stylized signature of the KPMG firm, written in black ink.

KPMG

A handwritten signature of David Kells, written in black ink.

David Kells

Partner

Sydney

26 February 2021

Financial statements

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Statement of comprehensive income

for the year ended 31 December 2020

	Note	2020 \$'000	2019 \$'000
Gross written premium	3.1	561,730	433,248
Movement in unearned premium		(192,674)	(77,814)
Outward reinsurance premium expense		(57,529)	(57,800)
Net earned premium		311,527	297,634
Net claims incurred	4.1	(289,821)	(151,127)
Acquisition costs	4.6	(198,820)	(46,858)
Other underwriting expenses	3.3	(59,033)	(58,232)
Underwriting result		(236,147)	41,417
Investment income on assets backing insurance liabilities	3.2	59,917	65,891
Insurance (loss)/profit		(176,230)	107,308
Investment income on equity holders' funds	3.2	34,763	76,459
Investment expense on equity holders' funds		(4,363)	(4,256)
Other income		1,330	1,258
Financing costs		(10,709)	(11,785)
(Loss)/profit before income tax		(155,209)	168,984
Income tax benefit/(expense)	3.5(a)	47,511	(49,032)
(Loss)/profit for the year		(107,698)	119,952
Total comprehensive (loss)/income for the year		(107,698)	119,952

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 2020

	Note	2020 \$'000	2019 \$'000
Assets			
Cash and cash equivalents	6.1	82,831	65,999
Accrued investment income		20,444	19,476
Investments	2.2(d)	3,286,132	3,008,227
Trade and other receivables	6.2	54,317	28,112
Prepayments		1,695	1,967
Non reinsurance recoveries	4.4	33,254	22,740
Deferred acquisition costs	4.2	40,264	182,878
Plant and equipment		4,301	5,120
Lease assets	6.3	5,955	11,166
Deferred tax assets	3.5(b)	54,153	9,055
Investment in controlled entity	7.4	27,598	27,598
Intangibles	6.4	6,490	7,340
Goodwill	6.5	7,490	7,490
Total assets		3,624,924	3,397,168
Liabilities			
Trade and other payables	6.6	48,692	38,456
Lease liabilities	6.3	12,324	16,430
Reinsurance payable		11,283	11,696
Outstanding claims	4.3	539,806	360,385
Unearned premiums	4.5	1,440,177	1,247,365
Employee benefits provision	6.7	7,645	7,096
Interest bearing liabilities	5.2	187,781	199,369
Total liabilities		2,247,708	1,880,797
Net assets		1,377,216	1,516,371
Equity			
Share capital	5.3(a)	1,401,559	1,401,559
Share-based payment reserve	5.3(b)	181	638
Other reserves	5.5	(603,268)	(603,268)
Retained earnings		578,744	717,442
Total equity		1,377,216	1,516,371

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

Statement of changes in equity

for the year ended 31 December 2020

	Share capital	Other reserves	Share-based payment reserve	Retained earnings	Total
	\$'000	\$'000	\$'000	\$'000	\$'000
Balance at 1 January 2019	1,401,559	(603,268)	639	900,411	1,699,341
Adjustment on initial application of AASB 16 Leases	-	-	-	79	79
Adjusted balance as at 1 January 2019	1,401,559	(603,268)	639	900,490	1,699,420
Profit after taxation	-	-	-	119,952	119,952
Dividend declared and paid	-	-	-	(303,000)	(303,000)
Share-based payment expense recognised	-	-	36	-	36
Share-based payment settled	-	-	(37)	-	(37)
Balance at 31 December 2019	1,401,559	(603,268)	638	717,442	1,516,371
Balance at 1 January 2020	1,401,559	(603,268)	638	717,442	1,516,371
Loss after taxation	-	-	-	(107,698)	(107,698)
Dividend declared and paid	-	-	-	(31,000)	(31,000)
Share-based payment expense recognised	-	-	(422)	-	(422)
Share-based payment settled	-	-	(35)	-	(35)
Balance at 31 December 2020	1,401,559	(603,268)	181	578,744	1,377,216

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

Statement of cash flows

for the year ended 31 December 2020

	Note	2020 \$'000	2019 \$'000
Cash flows from operating activities			
Premiums received		621,779	496,095
Interest and other income		45,648	78,415
Claims paid		(123,930)	(133,957)
Interest paid		(12,190)	(9,931)
Outwards reinsurance premium expense paid		(57,941)	(57,800)
Cash payments in the course of operations		(153,971)	(153,096)
Income tax paid		(23,169)	(44,766)
Net cash provided by operating activities	3.4	<u>296,226</u>	<u>174,960</u>
Cash flows from investing activities			
Payments for plant and equipment and intangibles		(529)	(2,447)
Payment for purchase of investments		(3,425,821)	(2,333,834)
Proceeds from sale of investments		3,192,327	2,399,974
Proceeds from dividend income		542	749
Proceeds from sub-lease of property		1,629	946
Net cash (used in)/provided by investing activities		<u>(231,852)</u>	<u>65,388</u>
Cash flows from financing activities			
Net repayment of long-term borrowings		(12,434)	-
Payment of lease liabilities		(4,304)	(3,527)
Dividends paid		(31,000)	(303,000)
Net cash used in financing activities		<u>(47,738)</u>	<u>(306,527)</u>
Net increase/(decrease) in cash held		16,636	(66,179)
Effects of exchange rate changes on balances of cash held in foreign currencies		196	(2,187)
Cash and cash equivalent at the beginning of the financial year		<u>65,999</u>	<u>134,365</u>
Cash and cash equivalent at the end of the financial year	6.1	<u><u>82,831</u></u>	<u><u>65,999</u></u>

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 (the Company) is a company domiciled in Australia. The Company is a for-profit entity.

The financial statements were authorised for issue by the Board of Directors on 26 February 2021.

1.2 Significant accounting policies

(a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards adopted by the Australian Accounting Standards Board (AASB) and the *Corporations Act 2001*. International Financial Reporting Standards (IFRSs) form the basis of Australian Accounting Standards adopted by the AASB, being Australian equivalents to IFRS. The financial reports of the Company also comply with IFRS and interpretations adopted by the International Accounting Standards Board (IASB).

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 AASB 17 *Insurance Contracts* in an Australian context, that does include such criteria, with an effective date of 1 January 2023. At the time of implementation of AASB 17, AASB 9 *Financial Instruments* will be implemented as well given the Company meets the requirements for deferral under AASB 2016-6 *Amendments to Australian Accounting Standards – Applying AASB 9 Financial Instruments with AASB 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.

Selected explanatory notes are included to explain events and transactions that are significant to an understanding of the financial position and performance of the Company.

(b) Basis of preparation of the financial report

The financial report is presented in Australian dollars.

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 notes to the financial statements.

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

The Company does not prepare consolidated accounts for the consolidated entity comprising it and its controlled entity as the directors do not consider the consolidated entity to be a disclosing entity.

Consolidated accounts are prepared by the Company's parent entity, Genworth Mortgage Insurance Australia Limited.

(c) Accounting policies adopted

The accounting policies adopted in the preparation of this financial report have been applied consistently by the Company and are the same as those applied for the previous reporting year, unless otherwise stated. The significant accounting policies adopted in the preparation of this financial report are set out within the relevant notes to the financial statements.

(i) New and amended standards adopted by the Company

There are additional new accounting standards and interpretations, effective on or after 1 January 2020 (refer to the table below) which were adopted by the Company. The adoption of these standards did not have a material effect on the Company's financial statements.

	New standards, amendments and interpretations	Operative date
AASB 2018-6	Amendments to Australian Accounting Standards – Definition of a Business	1 January 2020
AASB 2018-7	Amendments to Australian Accounting Standards – Definition of Material	1 January 2020
AASB 2019-1	Amendments to Australian Accounting Standards – References to the Conceptual Framework	1 January 2020
AASB 2019-3	Amendments to Australian Accounting Standards – Interest Rate Benchmark Reform	1 January 2020
AASB 2019-5	Amendments to Australian Accounting Standards – Disclosure of the Effect of New IFRS Standards Not yet Issued in Australia	1 January 2020
AASB 2020-4	Amendments to Australian Accounting Standards - COVID-19 - Related Rent Concessions	1 June 2020

(ii) New accounting standards and amendments issued but not yet effective

There are various new accounting standards, amendments and interpretations noted below which are effective for annual periods beginning on or after 1 January 2021 and have not been applied in preparing these financial statements. An initial assessment of the financial impact of these standards and amendments has been undertaken and they are not expected to have a material impact on the Company's financial statements, except where noted below.

	New standards, amendments and interpretations	Operative date
AASB 17 / AASB 2020-5	Insurance Contracts / Amendments to Australian Accounting Standards – Insurance Contracts	1 January 2023
AASB 9	Financial Instruments	1 January 2023 (subject to exemption)
AASB 2017-5	Amendments to Australian Accounting Standards – Effective Date of Amendments to AASB 10 and AASB 128 and Editorial Corrections	1 January 2022
AASB 2020-1	Amendments to Australian Accounting standards – Classification of Liabilities as Current or Non-current	1 January 2022
AASB 2020-3	Amendments to Australian Accounting Standards – Annual Improvements 2018-2020 and Other Amendments	1 January 2022
AASB 2020-6	Amendments to Australian Accounting Standards – Classification of Liabilities as Current or Non-current – Deferral of Effective Date	1 January 2022
AASB 2020-7	Amendments to Australian Accounting Standards – COVID-19 - Related Rent Concessions: Tier 2 Disclosures	1 July 2021
AASB 2019-8	Amendments to Australian Accounting Standards – Interest Rate Benchmark Reform – Phase 2	1 January 2021

AASB 17 Insurance Contracts

AASB 17 (including amendments within AASB 2020-5), the new accounting standard for insurance contracts, was adopted by the Australian Accounting Standards Board in July 2020. Various implementation and interpretation matters are still being discussed by various stakeholders at the AASB 17 Transition Resource Group. At this stage, it is not expected that those discussions will lead to further changes to AASB 17.

The first applicable annual reporting period for the Company will be the year ending 31 December 2023, with the comparative period for the year ending 31 December 2022 and the Statement of Financial Position at 1 January 2022. The standard introduces a new general measurement model for accounting for insurance contracts, with the application of a simplified approach permitted in certain circumstances. The Company has completed a detailed impact assessment of the new standard and has determined that the vast majority of insurance contracts underwritten by the Company will not meet the requirements of the simplified approach due to their long-term coverage period.

It is expected that the timing of recognition of profit will change under the new standard. As AASB 17 is to be applied retrospectively, a different valuation method for the insurance liability and a different model for the recognition of profit could lead to significant changes in the net asset position between 31 December 2021 (under the current insurance accounting standard) and 1 January 2022 (to be determined under AASB 17 in the Company's financial statements as at 31 December 2023). AASB 17 will require substantial changes to the presentation and disclosures of the financial statements.

To achieve those changes, significant modifications to systems and processes are required. The Company will also consider revising the key performance indicators relevant for its employee incentive schemes.

In November 2020, the Australian Prudential Regulation Authority (APRA) has issued a Quantitative Impact Study to be completed by a sample of insurance companies in Australia, as part of its ongoing work to update its prudential and reporting standards, in light of the adoption of AASB 17. APRA has indicated that those updates were not intended to alter the minimum capital levels required to be held by an insurance company.

AASB 9 Financial Instruments

AASB 9 applies to annual reporting periods beginning on or after 1 January 2018. The Company is allowed to apply the temporary exemption from AASB 9 as it has not previously adopted any version of AASB 9 and its activities are predominantly connected with insurance, as prescribed by AASB 4 *Insurance Contracts* (i.e. at 31 December 2015, the carrying amount of the Company's insurance liabilities, including insurance debt instruments, was significant compared to the total carrying amount of all its liabilities and the percentage of the total carrying amount of its liabilities connected with insurance relative to the total carrying amount of all its liabilities was greater than 90%).

The AASB (in line with the IASB) extended the temporary exemption from the adoption of AASB 9 to reporting periods beginning 1 January 2023, for companies meeting this criteria. The Company, having met the relevant criteria, has deferred the adoption of AASB 9 and is expecting to adopt AASB 9 at the same time as AASB 17.

The Company's investments are currently designated at fair value through profit and loss on initial recognition and are subsequently remeasured to fair value at each reporting date, reflecting the business model applied by the Company to manage and evaluate its investment portfolio. Under the Company's business model, the adoption of AASB 9 could result in a portion of the investment portfolio being revalued through other comprehensive income. The Company is evaluating the elections to be made to its portfolios of investments, in conjunction with the implementation of AASB 17.

(d) Rounding off

The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 dated 24 March 2016 and, in accordance with that Class Order, amounts in the financial statements and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

(e) Critical accounting estimates and judgements

The preparation of a financial report requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable in the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

These estimates and underlying assumptions are reviewed on an ongoing basis and actual results may vary from estimates. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of Australian Accounting Standards that have a significant effect on the financial report and estimates with a significant risk of material adjustment are discussed in note 4.8.

Coronavirus (COVID-19) pandemic

The ongoing COVID-19 pandemic has increased the estimation uncertainty in the preparation of these financial statements. The Company has developed various accounting estimates in these financial statements based on forecasts of economic conditions which reflect expectations and assumptions as at 31 December 2020 about future events that the Directors believe are reasonable in the circumstances. There is a considerable degree of judgement involved in preparing these forecasts. The underlying assumptions are also subject to uncertainties which are often outside the control of the Company. Accordingly, actual economic conditions may be different from those forecast since anticipated events may not occur as expected, and the effect of those differences may significantly impact accounting estimates included in these financial statements.

The significant accounting estimates particularly impacted by these associated uncertainties are predominantly related to the valuation of the outstanding claims liability including the estimates of future claims and related expenses for the preparation of the liability adequacy test, recoverable amount assessments of non-financial assets and fair value measurement of investments.

The impact of the COVID-19 pandemic on accounting estimates is discussed further below and in the relevant notes to the financial statements.

Outstanding claims liability

Responses to COVID-19 such as government stimulus and repayment deferrals are delaying the development and progression of delinquencies and claims and increasing uncertainty around potential claims emergence. The Company has allowed for those factors in its reserving process, which led to the outstanding claims liability increasing from \$360.4 million as at 31 December 2019 to \$539.8 million as at 31 December 2020. This movement includes the estimated impact of the delayed claims progression of claims and a refinement of the reserving methodology for future re-reporting of cured delinquencies, as well as an increase in the risk margin to reflect the elevated uncertainty. Refer to notes 4.3 and 4.8 for more detail.

In addition to the COVID-19 specific element reflected in the outstanding claims provision, any COVID-19 underwriting exposure related to unexpired risk has been incorporated within the estimation of premium liabilities and, as a result, in the calculation of the Company's regulatory capital position. Refer to note 4.6 and note 4.9 for further details on liability adequacy test (LAT) and capital adequacy position respectively.

Goodwill and intangible assets impairment

The assumptions underpinning the value-in-use calculations used to evaluate the recoverability of goodwill and intangible assets were adjusted to reflect reasonable estimates of the impact of COVID-19 and the increased risks associated with the estimated cash flows. Whilst there is no impairment in relation to the cash-generating unit at 31 December 2020, there is a heightened level of uncertainty around key assumptions in the current environment. This has the potential to materially impact the value-in-use

assessment moving forward and potentially the carrying value of the respective intangible assets and goodwill. Refer to note 6.4 and note 6.5 for further details on intangible assets and goodwill respectively.

Fair value measurement of investments

The Company's investments are designated at fair value through profit and loss, and for the vast majority of the investments, the fair value is determined based on observable market data. This measurement basis has not changed as a result of COVID-19. The investments which are subject to valuation using unobservable inputs are disclosed in the Company's fair value hierarchy. Refer to note 2.2(d) for further details on investments.

(f) Comparative figures

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

Section 2 Risk management

This note presents information about the Company's objectives, policies and processes for measuring and managing risk.

2.1 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 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 ongoing operation of the Company's Risk Management Framework. The Risk 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 assess 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.

Risk is managed primarily through appropriate pricing, product design, risk selection, appropriate investment strategies, financial strength ratings and reinsurance. It is vital that the Company closely monitors and responds to any changes in the general economic and commercial environment in which it operates.

In Australia, the majority of mortgages are originated through the country's four largest banks. The lenders representing 10% or more of the Company's gross written premium (GWP) are included in the table below:

Lender customer	2020 GWP	2019 GWP
Largest customer	56.9%	55.0%
Second largest customer	11.0%	12.0%

The second largest customer's contract with the Company was not renewed and expired on 20 November 2020.

2.2 Financial risk management

The Company has exposure to market, credit and liquidity risks relating to its use of financial instruments.

(a) Market risk

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

(i) Currency risk

Currency risk is the risk of loss arising from an unfavourable movement in market exchange rates. The Company is exposed to currency risk on its investments in debt securities, in receivables and payables denominated in a currency other than Australian dollars and the net investment in foreign branch operations. The currencies giving rise to the risk are United States dollars, Euros and New Zealand dollars.

The Company used forward foreign exchange contracts to mitigate currency risk arising from fixed interest securities denominated in United States dollars and Euros. The risk management processes required both Board and regulatory approvals. Transactions are subject to close senior management scrutiny in addition to the regular risk management and monitoring processes. Derivatives are used only for approved purposes and are subject to delegated authority levels provided to management. The level of derivative exposure is reviewed on an ongoing basis. Appropriate segregation of duties exists with respect to derivative use and compliance with policy, limits and other requirements are closely monitored.

The potential impact on the Company's profit or loss resulting from a 10% depreciation or appreciation of the Australian dollar (AUD) compared with selected currencies, net of related derivatives at the reporting date, assuming all other variables remain constant, is shown below.

	2020		2019	
	+10%	-10%	+10%	-10%
	\$'000	\$'000	\$'000	\$'000
New Zealand dollar	(79)	79	(260)	260
United States dollar	(185)	185	102	(102)
Euros	201	(201)	67	(67)

(ii) Cash flow and fair value interest rate risk

The Company is exposed to interest rate risk primarily arising from interest bearing assets. Assets with floating rate interest expose the Company to cash flow interest rate risk. Fixed interest rate assets expose the Company to fair value interest rate risk.

The Company's strategy is to invest in high quality, liquid debt securities and cash and to actively manage the 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 Company has exposure to interest rate risk on its term subordinated notes. The interest rate on these notes is reset quarterly.

The potential impact of movements in interest rates on the Company's profit or loss resulting from 50 basis points increase or decrease in interest rates on interest bearing assets, assuming all other variables remain constant, are shown below:

	2020		2019	
	+50bps	-50bps	+100bps	-100bps
	\$'000	\$'000	\$'000	\$'000
Interest bearing assets	(42,167)	42,167	(63,440)	66,310

(iii) Equity price risk

Price risk is the risk that the fair value of a financial asset will fluctuate because of changes in market prices, rather than changes in interest rates and/or exchange rates. These price movements may be caused by factors specific to the individual financial asset or its issuer, or factors affecting all similar financial assets traded on the market. The Company has exposure to equity price risk through investment in equities and equity unit trusts.

The potential impact of movements in price risk on the Company's profit and loss (before tax) as resulting from 10% increase or decrease in value of equity securities at reporting date are shown below.

	2020		2019	
	+10%	-10%	+10%	-10%
	\$'000	\$'000	\$'000	\$'000
Investments – unit trusts equity securities	11,631	(11,631)	7,885	(7,885)
Investments – unlisted equities	967	(967)	400	(400)

(b) Credit risk

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 Company's credit risk arises predominantly from investment activities and the amounts are as indicated by the carrying amounts of the financial assets.

The Company's investment portfolio comprises 80% (2019: 81%) of total securities and cash with counterparties having a rating of A- or better. The Company 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 is 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.

The ratings in the following table are the lower equivalent rating of either Standard & Poor's or Moody's.

	2020	2019
	\$'000	\$'000
Cash at bank and short-term deposits		
AAA	13,176	1,598
AA	143,147	102,777
A	23,975	72,737
BBB	-	46,434
	180,298	223,546
Investments (excluding short-term deposits)		
AAA	1,037,638	1,253,623
AA	906,963	579,999
A	583,671	493,868
BBB	519,831	424,113
BB	14,590	16,231
	3,062,693	2,767,834
Accrued interest receivable		
AAA	5,407	7,243
AA	8,178	5,706
A	2,529	3,098
BBB	3,315	2,896
BB	200	266
Not rated	815	267
	20,444	19,476
Trade and other receivables		
<i>Premium receivables</i>		
AA	11,394	16,794
A	-	600
<i>Other receivables</i>		
A	33,834	6,069
Not rated	9,089	4,649
	54,317	28,112

(c) Liquidity risk

Liquidity risk is the risk of having insufficient cash resources to meet payment obligations to policyholders and creditors without affecting the daily operations or the financial condition of the Company.

Management of liquidity risk includes asset and liability management strategies. The assets held to back insurance liabilities consist predominantly of highly rated fixed income securities which can generally be readily sold or exchanged for cash. The assets are managed to effectively match the interest rate maturity profile with the expected pattern of claims payments.

The money market securities are restricted to investment grade securities with concentrations of investments managed in accordance with investment mandates.

2020	Less than 1 year	1 - 5 years	Total
Financial liabilities	\$'000	\$'000	\$'000
Trade and other payables	47,750	942	48,692
Reinsurance payable	11,283	-	11,283
Lease liabilities	4,978	7,346	12,324
	64,011	8,288	72,299

2019	Less than 1 year	1 - 5 years	Total
Financial liabilities	\$'000	\$'000	\$'000
Trade and other payables	37,370	1,086	38,456
Reinsurance payable	11,696	-	11,696
Lease liabilities	4,790	11,640	16,430
	53,856	12,726	66,582

Interest bearing liabilities which is classified as financial liabilities are separately disclosed in note 5.2.

(d) Fair value measurements

Accounting policies

The valuation methodologies of assets valued at fair value are summarised below:

- *Cash assets and bank overdrafts* are carried at face value of the amounts deposited or drawn.
- *Interest bearing securities* are initially recognised at fair value, determined as the quoted cost at date of acquisition. They are subsequently remeasured to fair value at each reporting date. For securities traded in an active market, fair value is determined by reference to published bid price quotations. For securities not traded and securities traded in a market that is not active, fair value is determined using valuation techniques with the most common technique being reference to observable market data using the fair values of recent arm's length transactions involving the same or similar instruments. In the absence of observable market information, unobservable inputs which reflect management's view of market assumption are used. Valuation techniques maximise the use of observable inputs and minimise the use of unobservable inputs.
- *Unlisted unit trusts securities* are valued using quoted current unit prices as advised by the responsible entity, trustee or equivalent of the investment vehicle.

Financial assets backing general insurance liabilities

The assets backing general insurance liabilities are those assets required to cover the technical insurance liabilities (outstanding claims and unearned premiums) plus an allowance for capital adequacy.

The Company has designated the assets backing general insurance activities based on their function. Initially insurance technical balances are offset against the required assets with any additional assets required being allocated based on liquidity.

In accordance with the Company's investment strategy, the Company actively monitors the average duration of the notional assets allocated to insurance activities to ensure sufficient funds are available for claim payment obligations.

The Company accounts for financial assets and any assets backing insurance activities at fair value through profit and loss, with any resultant unrealised profits and losses recognised in the statement of comprehensive income.

Financial assets not backing general insurance liabilities

Investments not backing insurance liabilities are designated as financial assets at fair value through profit and loss on the same basis as those backing insurance liabilities.

Derivative financial instruments

The Company used forward foreign exchange contracts to hedge currency exposures arising from interest bearing securities denominated in currencies other than Australian dollars, with both the foreign exchange and derivatives impact reported through profit and loss. Derivatives are used solely to manage risk exposure and are not used for trading or speculation.

Derivatives are initially recognised at trade date at fair value; attributable transaction costs are recognised in profit and loss as incurred. Subsequent to initial recognition, derivatives are measured at fair value through

profit and loss. The investment related derivatives are presented together with the underlying investments or as payables when the fair value is negative. Forward foreign exchange contracts are determined using observable inputs (level 2 in the fair value hierarchy).

Investments

	2020 \$'000	2019 \$'000
<i>Fixed interest rate</i>		
Short-term deposits	97,216	123,274
Australian government and state government bonds	1,433,219	1,327,689
Corporate bonds and others	864,136	672,344
	<u>2,394,571</u>	<u>2,123,307</u>
<i>Floating interest rate</i>		
Short-term deposits	251	34,273
Corporate bonds and others	747,867	757,768
	<u>748,118</u>	<u>792,041</u>
<i>Derivatives</i>		
Investment related derivatives	17,471	10,033
<i>Equity securities</i>		
Unlisted unit trust	116,306	78,846
Unlisted equities	9,666	4,000
	<u>125,972</u>	<u>82,846</u>
Total investments	<u>3,286,132</u>	<u>3,008,227</u>
Comprising:		
Current	364,977	608,606
Non-current	2,795,183	2,316,775
Equities	125,972	82,846
	<u>3,286,132</u>	<u>3,008,227</u>

For further details on the impact from COVID-19 refer to note 1.2(e).

The following additional disclosure is required for eligible insurers which met the criteria of the temporary exemption of deferring the adoption of AASB 9. It presents the fair value and the change in the fair value of the Company's financial assets as at 31 December 2020, showing separately the fair value of financial assets with contractual terms that give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI) and the fair value of financial assets that do not give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding (Non-SPPI):

2020	SPPI		Non-SPPI	
	Fair value	Change in fair value	Fair value	Change in fair value
Financial assets	\$'000	\$'000	\$'000	\$'000
Short-term deposits	97,467	(71)	-	-
Bonds	3,006,202	(6,694)	39,020	275
Derivatives	-	-	17,471	-
Unlisted equities	-	-	9,666	5,666
Unlisted unit trusts	-	-	116,306	(2,540)
	3,103,669	(6,765)	182,463	3,401

2019	SPPI		Non-SPPI	
	Fair value	Change in fair value	Fair value	Change in fair value
Financial assets	\$'000	\$'000	\$'000	\$'000
Short-term deposits	157,547	(76)	-	-
Bonds	2,742,455	57,526	15,346	156
Derivatives	-	-	10,033	-
Unlisted equities	-	-	4,000	-
Unlisted unit trusts	-	-	78,846	(1,164)
	2,900,002	57,450	108,225	(1,008)

Trade and other receivables are financial assets which are in the scope of AASB 9 and are SPPI assets. These assets amounted to \$54,317,000 at 31 December 2020 (2019: \$28,112,000). These assets are measured at their present value less any impairment loss for any doubtful accounts (no doubtful account at 31 December 2020 and 31 December 2019) which approximates fair value.

The credit risk ratings of SPPI financial assets at 31 December 2020 is set out in the table below:

2020	Credit Risk	Fair value	Fair value
		\$'000	%
Bonds and short-term investments			
AAA	Low	1,050,570	33.8
AA	Low	949,807	30.6
A	Low	607,647	19.6
BBB	Low	481,055	15.5
BB	Other	14,590	0.5
		3,103,669	100.0

2019	Credit Risk	Fair value	Fair value
		\$'000	%
Bonds and short-term investments			
AAA	Low	1,254,690	43.3
AA	Low	645,406	22.3
A	Low	527,934	18.2
BBB	Low	456,408	15.7
BB	Other	15,556	0.5
		2,900,002	100.0

Trade and other receivables at 31 December 2020 have the following credit rating: AA with low credit risk \$11,394,000 (2019: \$16,794,000), A with low credit risk \$33,834,000 (2019: \$6,669,000) and not rated credit risk \$9,089,000 (2019: \$4,649,000).

Fair value hierarchy

The Company investments carried at fair value have been classified under the three levels of the AASB 13 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. This category includes unlisted equities. The fair value has been supported based on a discounted cash flow analysis performed utilising the latest available cash flows from the entity.

2020	Level 1	Level 2	Level 3	Total
	\$'000	\$'000	\$'000	\$'000
Financial instruments				
Australian government and state-government bonds	-	1,433,219	-	1,433,219
Corporate bonds and others	-	1,612,003	-	1,612,003
Short-term deposits	97,467	-	-	97,467
Derivative assets	-	17,471	-	17,471
Unlisted unit trusts	-	116,306	-	116,306
Unlisted equities	-	-	9,666	9,666
Total	97,467	3,178,999	9,666	3,286,132

2019	Level 1	Level 2	Level 3	Total
	\$'000	\$'000	\$'000	\$'000
Financial instruments				
Australian government and state-government bonds	-	1,327,689	-	1,327,689
Corporate bonds and others	-	1,430,112	-	1,430,112
Short-term deposits	157,547	-	-	157,547
Derivative assets	-	10,033	-	10,033
Unlisted unit trusts	-	78,846	-	78,846
Unlisted equities	-	-	4,000	4,000
Total	157,547	2,846,680	4,000	3,008,227

There have not been any transfers between levels during the current and prior years.

The reconciliation from the beginning balances to the ending balances for fair value measurements in Level 3 of the fair value hierarchy is set out in the table below:

	Balance at 1 January 2020	Purchases	Disposals	Movement in fair value	Balance at 31 December 2020
2020	\$'000	\$'000	\$'000	\$'000	\$'000
Financial Instruments					
Unlisted equities	4,000	-	-	5,666	9,666
Total	4,000	-	-	5,666	9,666

	Balance at 1 January 2019	Purchases	Disposals	Movement in fair value	Balance at 31 December 2019
2019	\$'000	\$'000	\$'000	\$'000	\$'000
Financial Instruments					
Unlisted equities	4,000	-	-	-	4,000
Total	4,000	-	-	-	4,000

Interest bearing liabilities were initially measured at fair value (net of transaction costs) but are subsequently measured at amortised cost. The Company considers the fair value of the interest-bearing liabilities to be approximate to that of the fair value.

Derivative financial instruments

Reporting date positions

The notional amount and fair value of derivative financial instruments at balance date is set out in the table below:

	2020			2019		
	Exposure	Fair value asset	Fair value liability	Exposure	Fair value asset	Fair value liability
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Forward foreign exchange contracts	673,100	17,471	14	578,679	10,033	-
	673,100	17,471	14	578,679	10,033	-

All derivative contracts are expected to be settled within 12 months.

Section 3 Results for the year

3.1 Gross written premium

Accounting policies

Gross written premium comprises amounts charged to policyholders (direct premium) or other insurers (inwards reinsurance premium) for insurance contracts. Premiums charged to policyholders, excludes stamp duties and goods and services tax (GST) collected on behalf of third parties.

	2020 \$'000	2019 \$'000
Direct premium	560,322	431,974
Inward reinsurance premium	1,408	1,274
	<u>561,730</u>	<u>433,248</u>

3.2 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.

Dividend/Distribution revenue

Dividends are recognised on the date the dividends/distributions are declared, which for listed equity securities is deemed to be the ex-dividend date. Dividend revenue is recognised net of franking credits, and gross of withholding tax.

Refer to note 2.2 (d) fair value measurement Accounting policies for further details.

	2020 \$'000	2019 \$'000
Dividend from subsidiary	542	749
Interest revenue	49,770	76,717
Dividend/Distribution revenue	1,210	3,583
Unrealised gains/(losses) including derivatives	(45,775)	26,656
Realised gains including derivatives	90,369	33,156
Other income gains/(losses)	(1,436)	1,489
Total investment income	<u>94,680</u>	<u>142,350</u>

Represented by:

Investment income on assets backing insurance liabilities	59,917	65,891
Investment income on equity holders' funds	34,763	76,459
	<u>94,680</u>	<u>142,350</u>

3.3 Other underwriting expenses

	2020	2019
	\$'000	\$'000
Depreciation and amortisation expense	4,859	5,172
Employee expenses:		
• Salaries and wages	25,250	26,595
• Superannuation contributions	1,592	1,769
• Employee benefits	291	(90)
Occupancy expenses	1,719	2,255
Marketing expenses	436	458
Administrative expenses	24,886	22,073
	<u>59,033</u>	<u>58,232</u>

3.4 Net cash provided by operating activities

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

	2020	2019
	\$'000	\$'000
(Loss)/profit after income tax	(107,698)	119,952
Less items classified as investing/financing activities:		
– (Gain) on sale of investments	(90,369)	(33,156)
– Unrealised loss/(gains) on investments including derivatives	45,775	(26,656)
– Dividend income	(542)	(749)
Add non-cash items:		
– Share-based payments	(457)	(1)
– Loss on disposal of plant and equipment	-	33
– Depreciation and amortisation	4,869	5,172
– Interest (income)/expense leases	(221)	674
Net cash (used in)/provided by operating activities before change in assets and liabilities	<u>(148,643)</u>	<u>65,269</u>
Change in assets and liabilities during the financial year:		
(Increase)/decrease in receivables	(7,644)	14,039
Increase in outstanding claims liability	179,421	22,096
(Decrease)/increase in payables and borrowings	(16,072)	10,472
Decrease/(increase) in deferred acquisition costs	142,614	(13,791)
(Increase) in deferred tax balances	(46,811)	(1,243)
Increase/(decrease) in provision for employee entitlements	549	(161)
Increase in unearned premiums	192,812	78,279
Net cash provided by operating activities	<u>296,226</u>	<u>174,960</u>

3.5 Income taxes

Accounting policies

Income tax on the profit and 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 substantially 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. The following temporary differences are not provided for: goodwill not deductible for tax purposes; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit; nor differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. 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.

The Company is a member of Genworth Mortgage Insurance Australia Limited tax consolidation group. Under the tax consolidation system, the head entity is liable for the current income tax liabilities of that group. Entities are jointly and severally liable for the current income tax liabilities of the tax consolidated group where the head entity defaults, subject to the terms of the valid tax sharing agreement between the entities in the group. Assets and liabilities arising in the Company under the tax funding arrangement are recognised as amounts receivable from or payable to other entities in the tax consolidated group.

	2020 \$'000	2019 \$'000
(a) Income tax (benefit)/ expense		
Current tax	(1,713)	50,714
Deferred tax	(45,063)	(1,250)
<i>(Over)/under provision in prior year:</i>		
Current tax	(700)	(439)
Deferred tax	(35)	7
	<u>(47,511)</u>	<u>49,032</u>

Reconciliation of income tax (benefit)/expense to prima facie tax payable

	2020 \$'000	2019 \$'000
Prima facie income tax (benefit)/expense calculated at 30% of profit	(46,563)	50,695
(Increase)/decrease in income tax (benefit)/expense due to:		
Foreign tax rate differential	21	(6)
Over provision in prior year	(735)	(433)
Franking tax credit	(396)	(868)
Non-deductible items	324	96
Other non-taxable items	(162)	(452)
Income tax expense	<u>(47,511)</u>	<u>49,032</u>

(b) Deferred tax assets

Deferred tax asset balance comprises temporary differences	2020	2019
attributable to:	\$'000	\$'000
Leases	557	624
Employee benefits	3,519	3,774
Share-based payments and accrued expenses	504	465
Provision for indirect claims handling costs	5,333	4,073
Deferred acquisition costs	44,038	-
Other	202	119
	<u>54,153</u>	<u>9,055</u>
Net deferred tax		
Balance at 1 January	9,055	7,846
Debited to retained earnings	-	(34)
Credited to the statement of comprehensive income	45,063	1,250
Over provision of prior year tax	35	(7)
Closing balance at 31 December	<u>54,153</u>	<u>9,055</u>

As at 31 December 2020 the Company had carried forward tax losses in New Zealand amounting to \$74,145,000 (2019: \$75,160,000). These tax losses will be available to be used against future taxable income generated by the Company's New Zealand operations. No deferred tax asset has been recognised in respect of these tax losses due to insufficient certainty of future profits to utilise those losses.

In 2020, due to a strengthening of outstanding claims liabilities as a response to the COVID-19 pandemic, the Company has incurred a tax loss in Australia. Management considers it is probable that future taxable profits will be available to utilise those tax losses.

3.6 Dividends

Accounting policy

A provision for dividends is made in respect of ordinary shares where the dividends are declared on or before the reporting date but have not yet been distributed at that date.

(a) Ordinary shares

The Company paid an ordinary franked dividend per share of \$0.0221 amounting to \$31,000,000 to its shareholder, GMA on 18 March 2020. In 2019, the Company paid an ordinary franked dividend per share of \$0.0949 and \$0.050 amounting to \$133,000,000 and \$70,000,000 to its shareholder, GMA on 21 February 2019 and 21 August 2019 respectively. In addition, the Company also paid a special unfranked dividend per share of \$0.0714 amounting to \$100,000,000 to its shareholder GMA on 27 November 2019.

(b) Dividend franking account

In accordance with the tax consolidation legislation Genworth Mortgage Insurance Australia Limited, as the head entity in the tax consolidated group, has assumed the benefit of available franking credits.

(c) Dividends not recognised at reporting date

On 12 February 2021, the Directors determined that no final dividend declaration would be made for the year ended 31 December 2020.

Section 4 Insurance Contracts

Accounting policy

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 risk other than financial risk.

4.1 Net claims incurred

	2020 \$'000	2019 \$'000
(a) Claims analysis		
Gross claims incurred	296,809	162,282
Reinsurance and other recoveries revenue	(6,988)	(11,155)
Net claims incurred	<u>289,821</u>	<u>151,127</u>

(b) Claims development

	2020			2019		
	Current Year \$'000	Prior Years \$'000	Total \$'000	Current Year \$'000	Prior Years \$'000	Total \$'000
Gross claims expense						
Direct	133,460	147,785	281,245	169,886	(11,749)	158,137
Inwards reinsurance	5,705	9,859	15,564	4,724	(579)	4,145
Gross claims incurred ¹	<u>139,165</u>	<u>157,644</u>	<u>296,809</u>	<u>174,610</u>	<u>(12,328)</u>	<u>162,282</u>
Reinsurance and other recoveries						
Reinsurance and other recoveries	(398)	(6,590)	(6,988)	(1,722)	(9,433)	(11,155)
Net claims incurred	<u>138,767</u>	<u>151,054</u>	<u>289,821</u>	<u>172,888</u>	<u>(21,761)</u>	<u>151,127</u>

¹ including reinsurance and other recoveries provision movement

4.2 Deferred acquisition costs

Accounting policies

Costs associated with obtaining and recording mortgage insurance contracts are referred to as acquisition costs and are capitalised when they relate to the acquisition of new business or the renewal of existing business. These are presented as deferred acquisition costs (DAC) and amortised under the same basis as the earning pattern of premium over the period of the related insurance contracts. The balance at the reporting date represents the capitalised acquisition costs relating to unearned premium and is stated at cost subject to the liability adequacy test (refer to note 4.6).

Refer to note 4.7 Accounting estimates and judgements for further detailed information.

	2020 \$'000	2019 \$'000
Opening balance as at 1 January	182,878	169,087
Acquisition costs incurred during the year	56,824	59,468
Amortisation charge	(199,438)	(45,677)
Balance as at 31 December	<u>40,264</u>	<u>182,878</u>
Comprising:		
Current	5,958	38,564
Non-current	<u>34,306</u>	<u>144,314</u>
	<u>40,264</u>	<u>182,878</u>

After conducting the liability adequacy test as at 31 March 2020, the Company had a liability deficiency of \$184.5 million which resulted in a DAC write-down of \$184.5 million (2019: nil). Refer to note 4.6 for further details.

4.3 Outstanding claims

Accounting policies

Claims expense and a liability for outstanding claims are recognised in respect of direct and inward reinsurance business. The liability covers claims reported and outstanding, incurred but not reported (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 and 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.

Refer to note 4.7 Accounting estimates and judgements and note 4.8 Actuarial assumptions and methods for further detailed information.

	2020 \$'000	2019 \$'000
Central estimate	462,514	318,920
Risk margin	<u>77,292</u>	<u>41,465</u>
Gross outstanding claims	<u>539,806</u>	<u>360,385</u>

	2020 \$'000	2019 \$'000
(a) Reconciliation of changes in outstanding claims		
Opening balance as at 1 January	360,385	338,289
Current year net claims incurred	289,821	151,127
Movement in non-reinsurance and borrower recoveries	10,514	1,567
Net claims paid	<u>(120,914)</u>	<u>(130,598)</u>
Balance as at 31 December	<u>539,806</u>	<u>360,385</u>
Comprising:		
Current	148,304	159,841
Non-current	<u>391,502</u>	<u>200,544</u>
	<u>539,806</u>	<u>360,385</u>

(b) Claims development

Underwriting years	Prior years	2011 \$'000	2012 \$'000	2013 \$'000	2014 \$'000	2015 \$'000	2016 \$'000	2017 \$'000	2018 \$'000	2019 \$'000	2020 \$'000	Total \$'000
At end of year of underwriting		992	1,079	1,021	777	1,424	860	1,162	1,019	632	2,231	
One year later		6,668	7,805	6,825	12,917	6,803	8,620	6,716	11,193	13,399		
Two years later		10,997	11,246	20,870	20,319	16,711	8,680	8,885	18,599			
Three years later		9,989	24,535	29,722	21,130	13,560	8,238	18,443				
Four years later		15,925	43,917	28,494	20,825	14,601	17,099					
Five years later		23,182	34,634	30,254	31,018	31,787						
Six years later		14,669	21,273	18,955	38,764							
Seven years later		14,053	13,540	31,205								
Eight years later		10,687	26,026									
Nine years later		15,274										
Net incurred to date		122,436	184,055	167,346	145,750	84,886	43,497	35,206	30,811	14,031	2,231	
Net paid to date		94,031	142,462	111,257	75,378	31,548	8,882	4,417	1,456	60	-	
Net outstanding claims provision at 31												
December 2020	145,794	28,405	41,593	56,089	70,372	53,338	34,615	30,789	29,355	13,971	2,231	506,552
Non-reinsurance recoveries on unpaid claims at 31												
December 2020												33,254
Gross outstanding claims provision at 31												
December 2020												539,806

For further details on the impact from COVID-19 refer to note 1.2(e).

4.4 Non reinsurance recoveries

Accounting policies

Reinsurance and 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 Company 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.

	2020 \$'000	2019 \$'000
Balance as at 1 January	22,740	21,173
Movement of non-reinsurance recoveries	10,514	1,567
Balance as at 31 December	<u>33,254</u>	<u>22,740</u>

There were no reinsurance recoveries at 31 December 2020 (2019: nil).

4.5 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 12 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 or receivable is recorded as unearned premium reserve.

Refer to note 4.7 Accounting estimates and judgements and note 4.8 Actuarial assumptions and methods for further detailed information.

	2020 \$'000	2019 \$'000
Balance as at 1 January	1,247,365	1,169,086
Premiums incepted during the year	561,730	433,248
Premiums earned during the year	(368,918)	(354,969)
Balance as at 31 December	<u>1,440,177</u>	<u>1,247,365</u>
Comprising:		
Current	303,749	274,083
Non-current	1,136,428	973,282
	<u>1,440,177</u>	<u>1,247,365</u>

4.6 Liability adequacy test

Accounting policies

The liability adequacy test (LAT) is an assessment of the carrying amount of the unearned premium liability and is conducted at each reporting date. It comprises current estimates of the present value of the expected cash flows relating to future claims plus an additional risk margin to reflect the inherent uncertainty in the central estimate. If the future claim costs exceed the unearned premium liability less related deferred reinsurance expense and deferred acquisition costs, then the unearned premium liability is deemed to be deficient. The test is performed at the portfolio level of contracts that are subject to broadly similar risks and that are managed together as a single portfolio. Any deficiency is recognised in the statement of comprehensive income, with a corresponding impact in the statement of financial position, recognised first through the write down of related deferred acquisition costs and any remaining balance being recognised as an unexpired risk liability.

The probability of adequacy (POA) adopted for liability adequacy test is set at 70% and differs from the 75% probability of adequacy adopted in determining the outstanding claims liabilities (refer to note 4.8(a)). The reason for this difference is that the former is in effect an impairment test used only to test the sufficiency of net premium liabilities whereas the latter is a measurement accounting policy used in determining the carrying value of the outstanding claims liabilities.

The process used to determine the risk margin is discussed in note 4.8(a).

The table below provides the details of the net premium liabilities (net of reinsurance and adjusted for appropriate risk margin) used in the LAT as at 31 December 2020, 31 March 2020 and 31 December 2019:

	31 December 2020 \$'000	31 March 2020 \$'000	31 December 2019 \$'000
Unearned premium	1,440,177	1,272,130	1,247,365
Less: Deferred acquisition costs	(40,264)	(185,293) ¹	(182,878)
Less: Deferred reinsurance costs	-	(43,146)	-
Net unearned premium	1,399,913	1,043,691	1,064,487
Net central estimate of present value of expected cash flows associated with future claims	983,564	1,071,823	899,295
Risk margin of the present value of expected cash flows on future claims	137,124	156,349	121,454
Net premium liabilities	1,120,688	1,228,172	1,020,749
LAT surplus/(deficiency)	279,225	(184,481)	43,738
Risk margin percentage	17%	17%	17%
Probability of adequacy	70%	70%	70%

1. Prior to the write-down

Expected future claims are inherently uncertain, particularly in the current environment as the economic effects of COVID-19 continue to emerge. The Company has projected future claims from COVID-19 based on a range of possible economic scenarios and has adopted a central scenario estimate for the liability valuation incorporating a median view of economic forecasts.

At 31 March 2020, the Company had a LAT deficiency of \$184.5 million which resulted in a DAC write down of \$184.5 million. This related to older book years, as newer book years have benefitted from higher pricing and enhanced underwriting standards and are expected to remain profitable.

At 31 December 2020, under the Company's central scenario estimate, expected future claims (including an appropriate risk margin) exceeded the net insurance liabilities, creating a LAT surplus of \$279.2 million.

The \$184.5 million DAC write-down is included in the "Acquisition costs" line which totals \$198.8 million in the statement of comprehensive income for the year, and is the key driver of the reduction in "Deferred acquisition costs" in the statement of financial position from \$182.9 million at 31 December 2019 to \$40.3 million at 31 December 2020.

4.7 Accounting estimates and judgements

Critical accounting estimates and judgements

The Company 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 gross premium revenue / unearned premium / deferred acquisition costs (note 3.1, note 4.5 and note 4.2)

Premium is earned over periods of up to 12 years. The principle underlying the earning recognition is to derive a premium earnings curve which recognises the premium in accordance with the incidence of claims risk.

The review of the premium earnings curve 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 earnings curve. Changes to earnings curve assumptions, which in turn impact the timing of the recognition of unearned premium and DAC, are recognised 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.

Deferred acquisition costs are amortised under the same premium earnings curve as the related insurance contract.

Estimation of outstanding claims liabilities (note 4.3)

Provision is made for the estimated claim cost of reported delinquencies at the reporting date, including the cost of delinquencies incurred but not yet reported to the Company.

The estimated cost of claims includes expenses to be incurred in settling claims gross of expected third party recoveries. The Company 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.

A risk margin is added to the central estimate as an additional allowance for uncertainty in the ultimate cost of claims over and above the central estimate. The overall margin adopted by the Company is determined after considering the uncertainty in the portfolio, industry trends, the Company'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 Company, where more information about the claim event is generally available. IBNR claims may often not be apparent to the insured until sometime after the events giving rise to the claims have happened.

In calculating the estimated cost of unpaid claims, the Company uses a variety of estimation techniques, generally based upon statistical analysis of historical experience, 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 might create distortion in the underlying statistics or 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.

In establishing the COVID-19 specific element of the net outstanding claims liability, significant management judgement has been applied to derive a reasonable estimate of the probability-weighted view of potential future cash flows. Key areas of judgement relate to the exposure period, the estimation of potential economic loss, related key macroeconomic variables (including unemployment), reinsurance coverage and legal risk. Given the extent of the uncertainty, the range of potential financial outcomes in relation to these matters is unusually wide. All related uncertainties have been factored into the Company's probability weighting when estimating the provision. For further details on the impact from COVID-19 refer to note 1.2(e).

4.8 Actuarial assumptions and methods

(a) Outstanding claims

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

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

- Delinquent policies advised to the Company by lenders as being 90 days delinquent at the valuation date.
- IBNR, being the liability for future claims from policies which have missed at least 1 monthly repayment (or equivalent) and are not currently reported by lenders as being 3 months or more in delinquency. This includes policies that were reported delinquent in past periods and may re-report as delinquent in future periods.

For loans where the mortgagee is in possession (MIP) and a claim has been submitted, the claimed amount adjusted for amounts not eligible to be claimed is provided. For loans where there is a MIP but a claim has not yet been submitted, a case estimate based approach is used utilising the current outstanding loan balance including accumulated arrears adjusted for selling costs, the most recent property valuation, or an estimate thereof, and any amounts not eligible to be claimed.

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

Actuarial assumptions and process

Historical information relating to arrears and claims history for the Company is provided to the Appointed Actuary 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, mortgagor groups, property price appreciation since inception, 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, house price appreciation (HPA) band 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 according to the geographic location, loan balance, external dispute resolution (those borrowers accessing ombudsman services or seeking legal representation) and the lender, to adjust 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 for policies being 90 days delinquent at the valuation date:

- Average frequency factor is 31% (2019: 26%)
- Average severity factor is 27% (2019: 28%)

Incurred But Not Reported

The IBNR provision is estimated by analysing the historical pattern of reported delinquencies, separated into:

- Policies estimated as being between 30 and 90 days delinquent at the valuation date, or otherwise delinquent at that date but not reported by lenders, and
- Policies which were at least 30 days delinquent in prior periods and may re-report as delinquent in subsequent periods.
- In the context of the increased uncertainty created by the COVID-19 pandemic and the associated government stimulus and repayment deferrals, the Company has revised its estimate of the re-delinquency reserve in 2020. At 31 December 2019, the Company was holding a claims reserves within its IBNR for a period of 6 months after a delinquent loan had been cured to allow for the possibility that the loan could become re-delinquent. At 31 December 2020, the Company holds re-delinquency claims reserves for all policies that have at any point experienced delinquency up until the associated policy is cancelled or a case reserve is established. This change in assumption increased the outstanding claims liability by \$116.1 million and its non-reinsurance recoveries by \$7.0 million as at 31 December 2020.

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 Company is determined after considering the uncertainty in the portfolio, industry trends, the Company'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 Company 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 18% (2019: 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 (2019: nil).

The weighted average term to settlement is estimated to be 28 months (2019: 22 months).

Sensitivity Analysis

The valuation of outstanding claims incorporates a range of factors that involve interactions with economic indicators, statistical modelling and observed historical claims development. Certain variables are expected to impact outstanding claims liabilities more than others and consequently a greater degree of sensitivity to these variables is expected.

Future economic conditions and, in particular, house prices, interest rates and unemployment impact frequency and, to a lesser extent, severity.

The actuarial result is based on the central estimate of the net outstanding claims liabilities. The impact on the profit and loss before income tax to changes in key actuarial assumptions is set out in the table below.

Various scenarios regarding key economics including house price appreciation (HPA), unemployment and mortgage, as well as the upper and lower bounds of a 95% confidence interval of frequency outcomes are applied as sensitivity factors. The impact of applying the sensitivities is asymmetric around the central estimate due to the assumed asymmetry of the distribution of outcomes of the net outstanding claims liabilities.

Impact on outstanding claims liabilities to changes in key variables

Sensitivity Change	2020				2019			
	Net Outstanding Claims Liability		Net Premium Liability		Net Outstanding Claims Liability		Net Premium Liability	
	\$M	%	\$M	%	\$M	%	\$M	%
Base	429		984		297		899	
Ultimate Loss Ratio								
Upside Economics – 5% House Price Appreciation (HPA), 1% reduction in unemployment rate	(22)	(5)	(145)	(15)	(9)	(3)	(62)	(7)
Downside Economics - 5% House Price Depreciation (HPD), 1% increase in unemployment rate	22	5	156	16	9	3	102	11
Downside Economics - 10% HPD, 1% increase in unemployment rate	34	8	209	21	18	6	146	16
Downside Economics - 15% HPD	33	8	146	15	27	9	154	17
Discount Rate								
+ 0.5%	-	-	(27)	(2)	-	-	(19)	(2)
+ 1.0%	-	-	(50)	(5)	-	-	(39)	(4)

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 curve is revised when experience indicates such differences are ongoing.

The Company completed the annual review of its premium earnings pattern in the fourth quarter of 2020. The review resulted in no changes to the earnings curve pattern adopted in the fourth quarter of 2017.

The impact of shortening (or lengthening) the earnings curve by six months would increase (or decrease) the current unearned premium by less than \$10 million, with an equal and opposite impact in non-current unearned premium, as at 31 December 2020 and 31 December 2019.

4.9 Capital adequacy

APRA's Prudential Standard GPS 110 Capital Adequacy requires additional disclosure in the annual financial statements to improve policyholder and market understanding of the capital adequacy of the Company.

	2020 \$'000	2019 \$'000
Tier 1 capital		
Paid-up ordinary shares	1,401,559	1,401,559
Other reserves	(603,087)	(602,630)
Retained earnings	578,744	717,442
Less: Deductions	(77,054)	(36,956)
Net surplus/(deficit) relating to insurance liabilities	110,764	(44,398)
Common equity Tier 1 capital	1,410,926	1,435,017
Tier 2 capital	190,000	200,000
Total capital base	1,600,926	1,635,017
Insurance risk charge	331,959	284,375
Insurance concentration risk charge	506,871	469,360
Asset risk charge	165,527	125,109
Operational risk charge	43,416	36,192
Aggregation benefit	(71,681)	(55,395)
Total PCA	976,092	859,641
PCA coverage	1.64x	1.90x

Section 5 Capital management and financing

5.1 Capital management

The capital management strategy plays a central role in managing risk to create shareholder value whilst meeting the crucial and equally important objective of providing an appropriate level of capital to protect both policyholders' interests and satisfy regulators. Capital finances growth, capital expenditure and business plans and also provides support in the face of adverse outcomes from insurance and other activities and investment performance.

The determination of the capital amount and mix is built around three core considerations. The Company aims to hold capital to meet the highest requirements derived from the following three considerations:

(a) Regulatory capital

The Company is subject to APRA's prudential standards, which set out the basis for calculating the Prescribed Capital Requirement (PCR), which is the minimum level of capital that the regulator deems must be held to meet policyholder obligations. The capital base is expected to be adequate for the size, business mix, complexity and risk profile of the business and so the PCR utilises a risk based approach to capital adequacy. The PCR is the sum of the capital charges for insurance, investments and other assets, investment concentration, operational and catastrophe concentration risk plus any supervisory adjustment imposed by APRA.

It is the Company's policy to hold regulatory capital levels in excess of the PCR required by APRA. The Company maintains sufficient capital to support the PCR, which is APRA's derivation of the required capital to meet a 1 in 200 year risk of absolute ruin, and has at all times during the current and prior financial year complied with the externally imposed capital requirements to which it is subject.

Capital calculations for regulatory purposes are based on a premium liabilities model, which is different from the deferral and matching model which underpins the measurement of assets and liabilities in the financial statements. The premium liabilities model estimates future expected claim payments arising from future events insured under existing policies. This differs from the measurement of the outstanding claims liabilities on the statement of financial position, which considers claims relating to events that occur only up to and including the reporting date.

(b) Ratings capital

The Company sets its target capital strength by reference to a target financial strength rating from an independent ratings agency. The ratings help to reflect the financial strength of the Company and demonstrate to the stakeholders the ability to pay claims.

Following an assessment of the impact of the COVID-19 pandemic, in May 2020, ratings agencies revised the insurer financial strength (IFS) rating of the Company. The Company's rating was affirmed by Standard & Poor's at 'A', with the outlook changed from 'stable' to 'negative'. Fitch revised its rating from 'A+' (Strong) to 'A' (Strong); with the outlook maintained as 'negative'. Both agencies acknowledged the capital strength and strong competitive position of the Company.

(c) Economic capital

The Company uses an economic capital model (ECM) to assess the level of capital required for the underwriting, claims estimation, credit, market, liquidity, operational and Company risk to which it is exposed. Economic capital is determined as the level of capital the Company needs to ensure that it can satisfy its ultimate policyholder obligations in relation to all insurance contracts issued on or before the end of the business plan year. The ECM is used by management to help in the determination of strategic capital allocation, business planning, underwriting performance, pricing and reinsurance arrangements. The Company reviews its capital structure on an ongoing basis to optimise the allocation of capital whilst minimising the cost of capital. Active management of the business and its capital has enabled the Company to maintain its insurer financial strength and credit rating.

Internal capital adequacy assessment process (ICAAP) management

The Company has implemented an ICAAP as part of its compliance with the LAGIC standards. The purpose of ICAAP is to assist the Company in making a proactive internal assessment of its capital requirements considering the current strategy, business plan and associated risks inherent in that business plan. In addition to the internal capital requirement, the ICAAP recognises the capital required for regulatory and ratings agency purposes and identifies planned and potential sources of capital required to meet these objectives. The ICAAP is also designed to further augment the current corporate governance practices undertaken by the Board of Directors in respect of the ongoing assessment of the Company's risk profile, risk appetite, strategic plan and capital adequacy.

The ICAAP summary statement is designed to summarise the major components of the ICAAP, which are:

- i. Risk Management Framework
- ii. Risk Management Strategy
- iii. Capital Management and Planning
 - The identification of the amount of capital required to be held against the risks of the business;
 - The strategy for ensuring adequate capital is maintained over time, including the identification of specific capital targets; and
 - The plans for how target levels of capital are to be met and the means available for sourcing additional capital if and when required;
- iv. Capital Monitoring
 - The actions and procedures for monitoring the Company's compliance with its regulatory capital requirements and capital targets including the triggers to alert management to, and specified actions to avert and rectify, potential breaches of these requirements; and
 - The processes for reporting on the ICAAP and its outcomes to the Board and senior management.
- v. Stress Testing and scenario analysis relating to potential risk exposures and available capital resources.
- vi. ICAAP integration - ensuring that the ICAAP is taken into account in making business decisions.

5.2 Interest bearing liabilities

Accounting policies

Interest bearing liabilities are initially recognised at fair value less transaction costs that are directly attributable to the transaction. After initial recognition the liabilities are carried at amortised cost using the effective interest rate method.

Finance related costs include interest, which is accrued at the contracted rate and included in payables; amortisation of transaction costs which are capitalised, presented together with borrowings, and amortised over the life of the borrowings. This cost also includes the write off capitalised transaction costs and premium paid on the early redemption of the borrowings.

	2020 \$'000	2019 \$'000
Subordinated notes		
\$200 million subordinated notes (A)	-	200,000
\$190 million subordinated notes (B)	190,000	-
Less: capitalised transaction costs	(2,219)	(631)
	<u>187,781</u>	<u>199,369</u>

(A) On 3 July 2015, the Company issued \$200,000,000 of 10-year, non-call five-year subordinated notes. The notes qualified as Tier 2 Capital under the APRA's capital adequacy framework. On 3 July 2020, the Company exchanged \$146,575,000 of the outstanding \$200,000,000 due in July 2025 (existing 2015 notes) for \$146,575,000 of a new 10-year, non-call five-year floating rate subordinated notes due on 3 July 2030 (new 2020 notes). \$5,000,000 of the existing 2015 notes were redeemed on 25 August 2020 with the remainder \$48,425,000 of existing 2015 notes redeemed by the Company on 6 October 2020.

Key terms and conditions are:

- Interest is payable quarterly in arrears, with the rate each calendar quarter being the average of the 90-day bank bill swap rate at the end of the prior quarter plus a margin equivalent to 3.5% per annum.
- The notes mature on 3 July 2025 (non-callable for the first five years) with the issuer having the option to redeem at par from 3 July 2020. Redemption at maturity, or any earlier date provided for in the terms and conditions of issue, is subject to prior approval by APRA.

(B) On 3 July 2020, the Company exchanged \$146,575,000 of the outstanding \$200,000,000 due in July 2025 (existing 2015 notes) for \$146,575,000 of new 10-year, non-call five-year floating rate subordinated notes due on 3 July 2030 (new 2020 notes). The Company also issued \$43,425,000 additional new 2020 notes. The new 2020 notes qualify as Tier 2 Capital under the APRA's capital adequacy framework. As at 31 December 2020 the Company has \$190,000,000 of new 2020 notes on issue.

Key terms and conditions are:

- Interest is payable quarterly in arrears, with the rate each calendar quarter being the average of the 90-day bank bill swap rate at the end of the prior quarter plus a margin equivalent to 5.0% per annum.
- The notes mature on 3 July 2030 (non-callable for the first five years) with the issuer having the option to redeem at par from 3 July 2025. Redemption at maturity, or any earlier date provided for in the terms and conditions of issue, is subject to prior approval by APRA.

5.3 Equity

(a) Share capital

	2020 \$'000	2019 \$'000
Issued fully paid capital		
1,401,559,000 ordinary shares (2019: 1,401,559,000)	<u>1,401,559</u>	<u>1,401,559</u>

The Company does not have par value in respect of its issued shares. All Ordinary shares are fully paid. Ordinary shares have the right to receive dividends as declared and, in the event of winding up the Company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of and amounts paid up on shares held.

Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the Company.

(b) Share-based payment reserve

	2020 \$'000	2019 \$'000
Balance as at 1 January	638	639
Share-based compensation	(422)	36
Share-based payment settled	<u>(35)</u>	<u>(37)</u>
Balance as at 31 December	<u>181</u>	<u>638</u>

Refer to note 7.5 Share-based payments for further detailed information.

5.4 Capital commitments and contingencies

Capital commitments

There were no capital commitments as at 31 December 2020 (31 December 2019: nil).

Contingencies

Contingent liabilities are not recognised on the balance sheet but are disclosed where the possibility of settlement is less than probable but more than remote. Provisions are not required with respect to these matters as it is not probable that a future sacrifice of economic benefits will be required, or the amount is not reliably measurable. If settlement becomes probable, a provision is recognised. The best estimate of the settlement amount is used in measuring a contingent liability for disclosure.

There were no contingent liabilities as at 31 December 2020 (31 December 2019: nil).

5.5 Other reserves

	2020	2019
	\$'000	\$'000
Other reserves	<u>(603,268)</u>	<u>(603,268)</u>

The balance in the other reserves comprises goodwill which has not been recognised as an asset due to the acquisition of the lenders mortgage insurance business from GE Mortgage Insurance Pty Ltd and GE Capital Mortgage Insurance Corporation (Australia) Pty Ltd, being between entities under common control with the Company at that time. Consequently, goodwill has not been recognised as an asset in the financial statements of the acquirer.

Section 6 Operating assets and liabilities

6.1 Cash and cash equivalents

Accounting policies

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 acquisitions of three months or less that are readily convertible to known amounts of cash, that are subject to an insignificant risk of changes in value and which are used to meet short-term cash commitments. Cash and cash equivalents are measured at fair value, being the principal amount.

Cash at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the statement of financial position as follows:

	2020	2019
	\$'000	\$'000
Cash assets	<u>82,831</u>	<u>65,999</u>

6.2 Trade and other receivables

Accounting policies

The collectability of receivables is assessed at balance date and an impairment loss is made for any doubtful accounts. The amounts are discounted where the time value of money effect is material.

	2020	2019
	\$'000	\$'000
Premium receivable from external parties	416	682
Premium receivable from related entities	11,231	16,712
Other related entities receivables	33,834	5,499
Other receivables	<u>8,836</u>	<u>5,219</u>
	<u>54,317</u>	<u>28,112</u>
Comprising:		
Current	45,347	13,931
Non-current	<u>8,970</u>	<u>14,181</u>
	<u>54,317</u>	<u>28,112</u>

Under the tax consolidation system, current tax liabilities recognised for the year by the Company are assumed by GMA, the head entity in the tax consolidated group. The current tax liabilities arising for the Company under the tax funding agreement are recognised as an intercompany receivable to the head entity in the tax consolidated group. Included in the related party receivables are the balances related to taxes

receivables from the parent entity of \$30,100,000 (2019: \$4,518,000) and other related entities of \$3,734,000 (2019: \$981,000).

Carrying amounts of receivables reasonably approximate fair value at statement of financial position date. None of the receivables are impaired or past due at 31 December 2020 and 31 December 2019.

6.3 Leases

The Company leases properties for its office space. These leases have varying terms (from three to five years), escalation clauses and renewal rights. On renewal, the terms of the leases are usually renegotiated. At the time of adopting AASB 16, the Company determined that it was not reasonably certain to exercise renewal options. The optional term is usually the same length as the initial term.

The Company also leased equipment for its offices. These leases have varying terms, from one year to three years. The equipment asset leased are of low value.

Accounting policies

The Company recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset, less any lease incentives received.

The right-of-use-asset is subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of property, plant and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurement of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate. Generally, the Company uses its incremental borrowing rate as the discount rate.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate or if the Company changes its assessment of whether it will exercise extension or termination option. When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset or is recorded in profit and loss if the carrying amount of the right-of-use asset has been reduced to zero.

The Company has elected not to recognise right-of-use assets and lease liabilities for leases of low value assets, including office equipment. The Company recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

As an intermediate lessor

The Company classifies a sub-lease as finance or an operating lease by reference to the right-of-use asset arising from the head lease, rather than by reference to the underlying asset (i.e. the item of property being leased).

The Company accounts for its interests in the head lease and the sub-lease separately. At the commencement date of a sub-lease, the Company assesses whether the sub-lease transfers substantially all the risks and rewards incidental to ownership of the right-of-use asset arising from the head lease. If this is the case, then the sub-lease is a finance lease; if not, then it is an operating lease.

At inception of a finance sub-lease, the Company derecognises the right-of-use asset that arises from the head lease and recognises its net investment in the sub-lease as a receivable, measured as the present value of the future payments to be received from the tenant, using the same discount rate used for the head lease.

The Company subsequently measures the net investment in a sub-lease using the effective interest rate method.

Lease assets (right-of-use assets)

	2020	2019
	\$'000	\$'000
Balance as at 1 January	11,166	14,346
Additions	300	-
Disposal	(8)	-
Decrease from recognition of sub-lease asset	(2,739)	-
Depreciation charge for the year	(2,671)	(3,245)
Modification of leases	(93)	65
Balance as at 31 December	<u>5,955</u>	<u>11,166</u>

Lease liabilities

	2020	2019
	\$'000	\$'000
Balance as at 1 January	16,430	19,108
Payments made	(4,935)	(3,551)
Additions	300	-
Disposal	(17)	-
Interest expense	639	808
Modification of leases	(93)	65
Balance as at 31 December	<u>12,324</u>	<u>16,430</u>

Comprising:

Current	4,978	4,790
Non-current	7,346	11,640
	<u>12,324</u>	<u>16,430</u>

Maturity analysis – contractual undiscounted cash flows

Future payments to be made arising from lease contracts:		
Within one year	5,097	4,909
One year or later and no later than five years	7,942	12,879
Total undiscounted lease liabilities as at 31 December	<u>13,039</u>	<u>17,788</u>

Amounts recognised in profit and loss

Depreciation charge for the period	(2,671)	(3,245)
Interest expense on lease liabilities	(639)	(808)
Income from subleasing right-of-use assets	<u>221</u>	<u>158</u>

The interest expense on lease liabilities and the income from subleasing the right-of-use assets are presented as financing costs in the statement of comprehensive income.

6.4 Intangibles

The intangibles balance represents software development expenditure.

Accounting policies

Acquired software

Acquired intangible assets are initially recorded at their cost at the date of acquisition, being the fair value of the consideration provided and, for assets acquired separately, incidental costs directly attributable to the acquisition. All intangible assets acquired have a finite useful life and are amortised on a straight line basis over the estimated useful life of the assets being the period in which the related benefits are expected to be realised (shorter of legal benefit and expected economic life).

Internally developed capitalised software

Software development expenditure that meets the criteria for recognition as an intangible asset is capitalised in the statement of financial position and amortised over its expected useful life, subject to impairment testing. Costs incurred in researching and evaluating a project up to the point of formal commitment to a project is expensed as incurred. Only software development projects with total budgeted expenditure of more than \$250,000 are considered for capitalisation. Smaller projects and other costs are treated as maintenance costs, being an ongoing part of maintaining effective technology, and are expensed as incurred.

All capitalised costs are deemed to have an expected useful life of five years unless it can be clearly demonstrated for a specific project that the majority of the net benefits are to be generated over a longer or shorter period. The capitalised costs are amortised on a straight line basis over the period following completion of a project or implementation of part of a project.

Impairment assessment

The recoverability of the carrying amount of the asset is reviewed at each reporting date by determining whether there is an indication that the carrying value may be impaired. If such indication exists, the item is tested for impairment by comparing the recoverable amount, or value in use, of the asset to the carrying value. An impairment charge is recognised in the statement of comprehensive income when the carrying value exceeds the calculated recoverable amount. The impairment charges can be reversed if there has been a change in the estimate used to determine the recoverable amount.

There was no impairment charge recognised during the year. (2019: nil).

For further details on the impact from COVID-19 refer to note 1.2(e).

Reconciliations

Reconciliations of the carrying amounts for intangibles are set out below:

	2020 \$'000	2019 \$'000
Cost		
Balance as at 1 January	32,454	30,618
Additions	407	2,226
Disposals	-	(390)
Balance as at 31 December	<u>32,861</u>	<u>32,454</u>

	2020 \$'000	2019 \$'000
Accumulated amortisation and impairment losses		
Balance as at 1 January	(25,114)	(24,423)
Amortisation	(1,257)	(1,049)
Disposals	-	358
Balance as at 31 December	<u>(26,371)</u>	<u>(25,114)</u>
Total net intangibles	<u><u>6,490</u></u>	<u><u>7,340</u></u>

6.5 Goodwill

Accounting policies

Business combinations are accounted for by applying the purchase method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill has an indefinite useful life and is therefore not subject to amortisation, but is tested for impairment annually, or more often if there is an indication of impairment. Goodwill is stated at deemed cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill is allocated to cash-generating units (CGU). At 31 December 2020, the Company comprises of a single CGU (Mortgage Insurance Australia), which reflects the level at which goodwill is monitored for impairment by management.

The impairment test involves the use of accounting estimates and assumptions. The recoverable amount of the CGU is determined on the basis of value in use calculation which is performed on a pre-tax basis. The present value of future cash flow projections is based on the most recent management approved budgets.

For further details on the impact from COVID-19 refer to note 1.2(e).

	2020 \$'000	2019 \$'000
Goodwill - at deemed cost	<u><u>7,490</u></u>	<u><u>7,490</u></u>

The following describes the key assumptions on which management based its cash flow projections when conducting the impairment testing:

- Cash flow forecast is based on the latest five-year business plan approved by management. This business plan is based on a combination of historical performance and management's expectations of future performance based on prevailing and anticipated market factors.
- Terminal value is calculated using a perpetuity growth formula applied to the cash flows projected for the last year of the forecast period. The terminal growth rate used by management for its impairment assessment as at 31 December 2020 is 1.6% (2019: 1.7%).
- Discount rate reflects a beta and equity risk premium associated to the Company. The pre-tax discount rate used at 31 December 2020 is 12.9% (2019: 13.6%).

Management believes that any reasonably possible change in the key assumptions on which the value in use of the Company's CGU is based would not cause the goodwill to be impaired. This is demonstrated in the sensitivity analysis below:

Sensitivity analysis

Under each of the stressed assumption scenarios used below (all other assumptions remaining constant), The Company's goodwill is not impaired:

- Reduction of the projected cash flows by 15%.
- Terminal growth rate of 0%.
- Increase of the discount rate by 200 basis points.

6.6 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.

	2020	2019
	\$'000	\$'000
Accrued expenses	15,252	15,841
Trade creditors and other payables	33,424	22,517
Related party payables	2	98
Derivative financial instrument	14	-
	<u>48,692</u>	<u>38,456</u>
Comprising:		
Current	47,750	37,370
Non-current	942	1,086
	<u>48,692</u>	<u>38,456</u>

6.7 Employee benefits provision

Accounting policies

The carrying amount of provisions for employee entitlements approximates fair value.

Wages, salaries and annual leave

The accruals for employee entitlements to wages, salaries and annual leave represent present obligations resulting from employees' services provided up to the statement of financial position date, calculated at undiscounted amounts based on wage and salary rates that the entity expects to pay as at reporting date including related on-costs.

Long service leave

The Company's net obligation in respect of long-term benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods. A liability for long service leave is recognised as the present value of estimated future cash outflows to be made in respect of services provided by employees up to the reporting date. The estimated future cash outflows are discounted using corporate bond yields which have terms to maturity that match, as closely as possible, the estimated future cash outflows. Factors which affect the estimated future cash outflows such as expected future salary increases including related on-costs and expected settlement dates are incorporated in the measurement.

Superannuation commitments

The Company has a defined contribution superannuation plan. Employees are entitled to varying levels of benefits on retirement based on accumulated employer contributions and investment earnings thereon as well as benefits in the event of disability or death. Contributions by the Company are, as a minimum, in accordance with the Superannuation Guarantee Levy.

	2020 \$'000	2019 \$'000
Annual leave	2,943	2,583
Long service leave	4,702	4,513
	<u>7,645</u>	<u>7,096</u>
Comprising:		
Current	5,842	5,313
Non-current	1,803	1,783
	<u>7,645</u>	<u>7,096</u>

As at the balance date there were 181 employees (2019: 195).

Section 7 Other disclosures

7.1 Remuneration of auditors

	2020 \$	2019 \$
Audit and review of financial statements	351,868	351,868
Regulatory audit services	64,026	64,026
Audit related services	53,330	12,780
	<u>469,224</u>	<u>428,674</u>

7.2 Key management personnel disclosures

The following were key management personnel of the Company at any time during the reporting period and unless otherwise indicated, were key management personnel for the entire period.

Directors of the Company

Pauline Blight-Johnston (appointed on 2 March 2020)

David Foster

Ian MacDonald

Gai McGrath

Graham Mirabito (appointed on 10 August 2020)

Rajinder Singh (appointed on 9 September 2020)

Stuart Take

Andrea Waters (appointed on 16 March 2020)

Duncan West

Former Directors

Christine Patton (resigned on 9 August 2020)

Gayle Tollifson (resigned on 15 March 2020)

Jerome Upton (resigned on 8 September 2020)

Executive KMP

Michael Bencsik

Andrew Cormack

Steven Degetto

The key management personnel compensation is:

	2020	2019
	\$'000	\$'000
Short-term employee benefits	3,342	4,857
Post-employment benefits	265	725
Equity compensation benefits	104	1,541
	<u>3,711</u>	<u>7,123</u>

7.3 Related party disclosures

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

(a) Other related party transactions

The following transactions occurred with related parties:

Type of transactions	Class of related party	2020	2019
		\$'000	\$'000
Share based payment	Parent entity	578	(553)
Service and management fees	Other related entities	1,250	1,250
income			
Service and management fees	Ultimate parent entity	(4,561)	(4,581)
expense			
Dividends paid	Parent entity	(31,000)	(303,000)
Dividends received	Other related entities	542	749
Tax receipt	Parent entity	-	10,520

(b) Outstanding balances

The following balances are outstanding at the reporting date in relation to transactions with related parties:

Type	Class of related party	2020	2019
		\$'000	\$'000
Premium receivable	Other related entities	11,231	16,712
Expense	Other related entity	51	15
reimbursement			
Tax receivable	Parent entity	30,100	4,518
Expense	Parent entity	3,706	1,606
reimbursement			
Share-based payment	Other related entities	(23)	(657)
Service and management fees	Ultimate parent	(2)	(98)

Parent entity

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.

7.4 Controlled entity

Accounting policies

Subsidiaries are entities controlled by the Company. Control exists when the Company is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entities. In assessing control, the Company considers the purpose and design of each entity in order to identify the relevant activities, how decisions about the relevant activities are made, who has the current ability to direct those activities and who receives the returns from those activities.

Investment in the controlled entity is carried at the cost of acquisition less accumulated impairment in the Company's financial statements.

Name of entity	Country of incorporation	Class of shares	Equity holding (%)	
			2020	2019
Genworth Financial Mortgage Indemnity Limited	Australia	Ordinary	100	100

7.5 Share-based payments

Accounting policies

Share-based remuneration is provided in various forms to eligible employees and executive directors of the Company in compensation for services provided to the Company.

The fair value at the grant date, being the date, both the employee and the employer agree to the arrangement, is determined using a valuation model based on the share price at grant date and the vesting conditions. The fair value does not change over the life of the instrument. At each reporting period during the vesting period and upon final vesting or expiry of the equity instruments, the total accumulated expense is revised based on the fair value at grant date and the latest estimate of the number of equity instruments that are expected to vest based on the vesting conditions and taking into account the expired portion of the vesting period. The movement in the total of accumulated expenses from the previous reporting date is recognised in the profit and loss with a corresponding movement in the share-based payment reserve.

To satisfy obligations under the various share-based remuneration plans, shares are generally expected to be equity settled.

Share Rights Plan

Between 7 May 2015 and 1 March 2017, the Company granted restricted share rights to a number of key employees. The aggregate amount of these share rights was \$1,501,907. One quarter of the share rights granted during the year vest on each of the first, second, third and fourth anniversaries of the grant date. If at any time an employee ceases continuous service with the Company, any unvested share rights are immediately cancelled, except in cases of retirement, redundancy, total and permanent disability or death.

From 1 January 2018, it was decided that no grants would be made under the share rights plan. All outstanding grants (prior to 2018) made under the share rights plan will continue to vest per the original terms and conditions of the plan.

Share rights plan grant date	Available to	Vesting period	Total (\$)
6 May 2016	Nominated employees	Four equal tranches vested on first anniversary of grant date	\$499,030
1 March 2017	Nominated employees	Four equal tranches vested on first anniversary of grant date	\$492,910

The fair value of the share rights is calculated as at the grant date using a Black Scholes valuation. The factors and assumptions used for the valuation are summarised in the below table:

	2017	2016
Grant date	1 March 2017	6 May 2016
Share price on grant date (\$)	\$2.81	\$3.00
Dividend yield	8.60%	11.36%
Risk free rate (%)	Tranche 1: 1.83% Tranche 2: 2.00% Tranche 3: 2.15% Tranche 4: 2.29%	Tranche 1: 1.57% Tranche 2: 1.57% Tranche 3: 1.57% Tranche 4: 1.80%
Vesting dates	Tranche 1: 1 March 2018 Tranche 2: 1 March 2019 Tranche 3: 1 March 2020 Tranche 4: 1 March 2021	Tranche 1: 1 March 2017 Tranche 2: 1 March 2018 Tranche 3: 1 March 2019 Tranche 4: 1 March 2020

The final tranche of the 2016 Equity Plan grant vested on 1 March 2020.

Key terms and conditions:

- The rights are granted for nil consideration.
- Holders do not receive dividends and do not have voting rights until the rights are exercised.

Deferred short term incentive

Plan	Eligibility	Nature of award	Vesting conditions
Short Term Incentive (STI) Deferral Plan	Executives and any employee with an annual STI award >\$50,000	<ul style="list-style-type: none"> • One-third of the dollar value of the annual short term incentive is converted to a grant of deferred share rights for executives. • For any annual STI payment greater than \$50,000 one-third of the amount greater than \$50,000 is converted to a grant of deferred share rights, provided the amount is \$10,000 or more (applies to any non-executive incentive > \$50,000). • Notional dividend equivalents accrue during the vesting period and are delivered through an adjustment to the number of vested share rights at the end of the deferral period. 	<ul style="list-style-type: none"> • Continuous active employment for 12 months from grant date. • Board and Committee satisfaction that adverse outcomes have not arisen that were not apparent when performance was assessed, and satisfaction that there was not excessive risk taking in achievement of results.

Details of the number of employee share rights granted, exercised and forfeited or cancelled during the year were as follows:

2020						
Grant date	Balance at 1 January 2020	Granted in the year	Exercised in the year	Cancelled/forfeited in the year	Balance at 31 December 2020	Vested and exercisable at end of the year
	Number	Number	Number	Number	Number	Number
6 May 2016	34,302	-	(34,302)	-	-	-
1 March 2017	85,393	-	(42,674)	(2,542)	40,177	-
1 March 2019	215,087	35,321	(244,532)	(5,876)	-	-
1 March 2020	-	117,533 ¹	-	-	117,533	-
Total	334,782	152,854	(321,508)	(8,418)	157,710	-

¹ The number of share rights granted in the period representing the deferred short term incentive component under the 2019 remuneration program.

2019						
Grant date	Balance at 1 January 2019	Granted in the year	Exercised in the year	Cancelled/forfeited in the year	Balance at 31 December 2019	Vested and exercisable at end of the year
	Number	Number	Number	Number	Number	Number
7 May 2015	21,292	-	(21,292)	-	-	-
22 June 2015	1,935	-	(1,935)	-	-	-
6 May 2016	74,970	-	(36,737)	(3,931)	34,302	-
1 March 2017	161,700	-	(51,298)	(25,009)	85,393	-
1 March 2018	166,920	16,464	(183,384)	-	-	-
4 February 2019	-	53,702	(53,702)	-	-	-
1 March 2019	-	215,087 ¹	-	-	215,087	-
Total	426,817	285,253	(348,348)	(28,940)	334,782	-

¹ The number of share rights granted in the year representing the deferred short term incentive component under the 2018 remuneration program.

Long term incentive plan

The Company implemented a long term incentive (LTI) plan for executive KMP which is performance oriented and reflects local market practice.

The vesting conditions for each of the LTI plan granted include:

- Continuous active employment for four years from grant date.
- Subject to performance conditions.

LTI grant date	Nature of award	Total
6 May 2016	share rights	\$1,729,230
1 March 2017	share rights	\$1,873,986
1 March 2018	share rights	\$1,886,491
1 March 2019	share rights	\$1,688,601
1 March 2020	Share rights	\$1,771,188

Key terms and conditions for the 2020 LTI:

- The rights are granted for nil consideration.
- Holders are entitled to receive notional dividend equivalents during the vesting period but do not have voting rights.
- Each allocation is split into two portions which are subject to different performance hurdles with a twelve-month deferral period after the performance period ends. The first vesting condition is not market related and requires continuous active employment for four years from grant date. The second set of vesting conditions are as follows:
 - 25% is subject to Underlying return on equity (ROE) performance condition. The Company's three-year average Underlying ROE measured against regulatory capital (based on the upper end of the Board's target range above the prescribed capital amount) is tested against target Underlying ROEs over a three-year period.
 - 75% is subject to relative total shareholder return (TSR) performance condition. The Company's TSR is tested against comparator group, the ASX 200 financial services excluding Real Estate Investment Trust (REITs) over a three-year period.
- The number of share rights offered is determined by dividing the grant value of the 2020 long term incentive plan by \$3.7341, being the 10-day volume weighted average price (VWAP) of the Company share price as at 31 December 2019 results, rounded down to the nearest whole share right. Each share right is a right granted to acquire a fully paid ordinary share of the Company.
- The fair value of the share rights is the share price as at the grant date.

If an employee ceases employment with the Company before the performance conditions are tested, their unvested rights will generally lapse.

The fair value of the share rights for LTI linked to relative TSR performance huddles is calculated as at the grant date using Monte Carlo simulation. The factors and assumptions used for the valuation are summarised in the below table.

	2020	2019	2018	2017
Grant date	1 March 2020	1 March 2019	1 March 2018	1 March 2017
Share price on grant date (\$)	\$3.22	\$2.53	\$2.37	\$2.81
Dividend yield (%)	0% ¹	0% ¹	0% ¹	8.60%
Volatility (%)	31.94%	31.02%	34.1%	35.00%
Correlation	A correlation matrix for the ASX 200 financial services (excluding REITs) has been used	A correlation matrix for the ASX 200 financial services (excluding REITs) has been used	A correlation matrix for the ASX 200 financial services (excluding REITs) has been used	A correlation matrix for the ASX 200 (excluding resource companies) has been used
Risk free rate (%)	0.54%	2.24%	2.1%	2.0%
Vesting date	31 December 2023	31 December 2022	31 December 2021	31 December 2020

¹ Consistent with the requirements set out in AASB 2, given participants in the LTI plan are entitled to dividend equivalents on the underlying shares, the input for expected dividend yield has been set to zero. For the purposes of relative TSR fair value calculations, the expected dividend yield of the comparator group has also been set to zero.

Details of the number of employee share rights granted, exercised and forfeited or cancelled during the year were as follows:

2020						
Grant date	Balance at 1 January 2020	Granted in the year	Exercised in the year	Cancelled/forfeited in the year	Balance at 31 December 2020	Vested and exercisable at end of the year
	Number	Number	Number	Number	Number	Number
6 May 2016 ¹	-	60,393	(60,393)	-	-	-
1 March 2017	453,430	-	(80,112)	(373,318)	-	-
17 July 2017	75,025	-	(37,512)	(37,513)	-	-
1 March 2018	583,215	-	-	(336,233)	246,982	-
1 March 2019	777,190	-	-	(305,783)	471,407	-
1 March 2020	-	474,328	-	(23,620)	450,708	-
Total	1,888,860	534,721	(178,017)	(1,076,467)	1,169,097	-

¹ Represents notional dividends awarded as share rights associated with 2016 LTI plan share rights that had previously vested/been exercised on 31 December 2019.

2019						
Grant date	Balance at 1 January 2019	Granted in the year	Exercised in the year	Cancelled/forfeited in the year	Balance at 31 December 2019	Vested and exercisable at end of the year
	Number	Number	Number	Number	Number	Number
7 May 2015 ¹	-	23,789	(23,789)	-	-	-
6 May 2016	552,604	-	(139,291)	(413,313)	-	-
1 March 2017	531,042	-	-	(77,612)	453,430	-
17 July 2017	75,025	-	-	-	75,025	-
1 March 2018	667,766	-	-	(84,551)	583,215	-
1 March 2019	-	777,190	-	-	777,190	-
Total	1,826,437	800,979	(163,080)	(575,476)	1,888,860	-

¹ Represents notional dividends awarded as share rights associated with 2015 LTI plan share rights that had previously vested/been exercised on 31 December 2018.

Omnibus Incentive Plan

GFI and the Company entered into a Cost Agreement on 15 July 2005 (as varied from time to time) pursuant to which GFI agreed to offer its 2004 Omnibus Incentive Plan and its 2012 Omnibus Incentive Plan (Omnibus Incentive Plans) to certain employees of the Company.

Under the Omnibus Incentive Plans, GFI issues stock options, stock appreciation rights, restricted stock, restricted stock units (RSU), other stock-based awards and dividend equivalent awards with respect to its common stock to employees of its affiliates throughout the world. GFI has reserved for such costs and the amount of the reserve is marked to market to reflect the Company's exposure to those costs having regard to the price of GFI shares.

Details of the number of employee options granted, exercised and forfeited or cancelled during the year were as follows:

2020\								
Grant date	Expiry date	Exercise price (\$)	Balance at 1 January 2020	Granted in the year	Exercised in the year	Cancelled/ forfeited in the year	Balance at 31 December 2020	Vested and exercisable at end of the year
			Number	Number	Number	Number	Number	Number
10/02/2010	10/02/2020	18.41	27,000	-	-	(27,000)	-	-
09/02/2011	09/02/2021	16.55	26,500	-	-	(18,000)	8,500	8,500
14/02/2012	14/02/2022	11.53	32,100	-	-	(20,400)	11,700	11,700
15/02/2013	15/02/2023	11.76	31,500	-	-	(18,000)	13,500	13,500
20/02/2014	20/02/2024	19.77	14,000	-	-	-	14,000	14,000
Total			131,100	-	-	(83,400)	47,700	47,700
Weighted average exercise price (\$)			14.90	-	-	14.89	14.91	14.91

2019								
Grant date	Expiry date	Exercise price (\$)	Balance at 1 January 2019	Granted in the year	Exercised in the year	Cancelled/ forfeited in the year	Balance at 31 December 2019	Vested and exercisable at end of the year
			Number	Number	Number	Number	Number	Number
10/02/2010	10/02/2020	20.20	27,000	-	-	-	27,000	27,000
09/02/2011	09/02/2021	18.16	26,500	-	-	-	26,500	26,500
14/02/2012	14/02/2022	12.65	32,100	-	-	-	32,100	32,100
15/02/2013	15/02/2023	12.91	31,500	-	-	-	31,500	31,500
20/02/2014	20/02/2024	21.70	14,000	-	-	-	14,000	14,000
Total			131,100	-	-	-	131,100	131,100
Weighted average exercise price (\$)			16.35	-	-	-	16.35	16.35

7.6 Events subsequent to reporting date

On 12 February 2021, the Directors determined that no dividend declaration would be made for the year ended 31 December 2020.

There are no other events that have arisen since 31 December 2020 to the date of this report that, in the opinion of the Directors, have significantly affected or may significantly affect the operations of the Company or the state of affairs of the Company in future years.

Directors' declaration

In the opinion of the directors of Genworth Financial Mortgage Insurance Pty Limited (the Company):

(a) the financial statements and notes set out on pages 6 to 55 are in accordance with the Corporations Act 2001, including:

- (i) giving a true and fair view of the financial position of the Company as at 31 December 2020 and of its performance, as represented by the results of its operations and its cash flows for the year ended on that date; and
- (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001 and other mandatory professional reporting requirements; and

(b) the financial statements and notes comply with International Financial Reporting Standards; and

(c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in accordance with a resolution of the directors:



Ian MacDonald
Chairman

Dated at Sydney, 26 February 2021.



Independent Auditor's Report

To the shareholders of Genworth Financial Mortgage Insurance Pty Limited

Opinion

We have audited the **Financial Report** of Genworth Financial Mortgage Insurance Pty Limited (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the Company's financial position as at 31 December 2020 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The **Financial Report** comprises:

- Statement of financial position as at 31 December 2020;
- Statement of comprehensive income, Statement of changes in equity, and Statement of cash flows for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' Declaration.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Company in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Other Information

Other Information is financial and non-financial information in Genworth Financial Mortgage Insurance Pty Limited's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. This includes the Directors' report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.



We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*;
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Company's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an 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 *Australian Auditing Standards* 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 the Financial Report.

A further description of our responsibilities for the audit of the Financial Report is located at the *Auditing and Assurance Standards Board* website at:

http://www.auasb.gov.au/auditors_responsibilities/ar4.pdf. This description forms part of our Auditor's Report.

KPMG

David Kells

Partner

Sydney

26 February 2021