



# Managing Director's letter to shareholders

## Dear shareholder

I'm very pleased to announce another very strong result for your Company.

The period to 31 December 2006 has been an exciting one for Suncorp with our announcement in October of plans to merge with Promina – another important step in our journey to become the leading diversified financial services organisation in Australia.

While the merger activities have understandably taken the spotlight, you can be assured that the focus of management has been on ensuring continued strong business performance. I pay tribute to all our employees who continue to rise to the challenge of improving the way we deliver to all our stakeholders.

The results of their efforts can be seen in the strong financial performance of the Company in the period to December 2006.

## Financial performance summary

Net profit after tax for the six months to December 2006 increased by 16.1% to \$527 million. Underlying profit, which excludes investment returns and non-recurring items, and is the best indicator of overall business performance, increased by 19.7% to \$589 million.

This is a very pleasing result given the level of competition across Banking, General Insurance and Wealth Management and proves that the Suncorp business is in good shape to tackle the challenges ahead.

All three businesses have contributed to the overall result.

## Banking

The Banking business delivered a 13.3% increase in profit before tax to \$289 million for the half-year to December 2006. Total lending grew by 14.6%, ahead of industry growth rates, in an environment where overall credit formation slowed as a result of recent interest rate increases.

In the current highly competitive market, the Bank seeks to optimise total income by managing price and volume while at all times being conscious of the need to maintain the quality of its franchise.

Housing receivables reached \$22.4 billion, an increase of 14% compared with the prior December. A number of initiatives including fixed rate offers and improvements to approval times for priority brokers, which were introduced in prior periods, have had their full effect in this half. The Bank also continues to capture new business by capitalising on its extensive branch network through product initiatives and continued improvements in customer service. This is supported by the strategic use of broker introduced business, particularly outside of Queensland, where lending growth has also been strong.

In Business Banking, receivables grew by 15.2% to \$18.5 billion. The commercial portfolio, which targets lending to small and medium enterprises (SMEs) grew strongly by 22.1% while growth was also achieved in corporate lending (39.4%) and property investment (22.8%). Lending to agribusiness customers increased by 11.1% to \$3.1 billion, despite the drought, which continues to have a crippling effect on rural Australia.

Our century-long commitment to the agribusiness sector means we are well placed to work with our customers through seasonal variations, thereby preserving credit quality across the portfolio. The Development Finance portfolio, which comprises lending for residential apartment developments, and land subdivisions in suburban metropolitan areas, continues to be impacted by the slow down in the property cycle with lending decreasing by 2.3% over the prior half-year period.

Suncorp continues to achieve above industry growth rates in retail deposits which increased by 14.2% to \$15.5 billion. This continues to be driven by the success of the Every Day Options transaction account which has now attracted more than \$3.2 billion in deposits since it was introduced in March 2004.

## General Insurance

Pre-tax profit in the General Insurance business of \$383 million in the half was underpinned by further improvements in claims management as well as a generally favourable claims environment over the period. The business remains focused on driving profitable growth as price based competition increases across most portfolios.

The insurance trading result (ITR) which is the underwriting result plus investment income, increased by 25.4% to \$262 million, equating to a substantial insurance margin of 21% of net earned premium. This is well above our long term guidance range of 11% to 14%.

Gross written premium (GWP) of \$1.3 billion was down slightly on December 2005 reflecting continued pressure on premium rates, particularly in commercial and motor classes. In compulsory third party (CTP) and commercial liability classes, customers continue to benefit as the tort law reforms are passed on in the form of reduced premiums.

We continue to drive improvements in customer service at all points of customer interaction and have developed a number of unique segmented customer offerings to address customer needs and drive profitable growth.

Suncorp continues to be very conservative in the way it provides for future claims, particularly in long tail classes. In effect we are ensuring that we are well placed to cover any volatility which may occur in the claims settlement process. While this creates a strain on current year profits it does allow us to return these provisions to profit as claims are settled. In this half we have been able to release \$120 million of profits set aside in prior periods.

## Wealth Management

The Wealth Management business continues to be a strong contributor to overall Group profit, delivering a pre-tax profit of \$54 million, an increase of 28.6% on the prior December half-year period.

Solid investment earnings and good net inflows resulted in strong growth in both funds under management (up 11.3% to \$13.7 billion) and funds under administration (up 19.5% to \$6.8 billion).

The value of new business increased by 25.2% and was boosted by increased volumes and improved retention rates on most products.

Strong investment management was again a highlight, with the Suncorp Superannuation Balanced Fund achieving 1<sup>st</sup> quartile returns over 1, 3, 5 and 7 years as measured by Intech's Growth Fund Survey.

### Delivering to our stakeholders

As I have previously mentioned Suncorp's strategy and business model is based on the continued strong performance of our three lines of business. However, we measure our performance against a number of criteria in addition to our financial results. It's important that we provide benefits to each of our four key stakeholders – our customers, employees, the community and, you, our shareholders.

**Customer** focus has and will always be a key priority for Suncorp. In an increasingly competitive market, the ability to differentiate through customer service will be a key competitive advantage. The business has continued to embed customer-led design principles across the organisation which means we put the customer at the centre of everything we do. The Suncorp business model allows us to gain a high level of insight into customer needs across the spectrum of financial services solutions and underpins our industry leading 2.96 products per customer.

Our **employees** remain the heart and soul of the Company. In the six months to December 2006 the Company has introduced a number of policies designed to attract, retain and develop its employees. For example, a talent management framework has been rolled out across the Group to help employees identify appropriate career opportunities within Suncorp. The success of our people strategies has resulted in the Gallup employee engagement measure placing Suncorp in the top 30% of companies participating in the Gallup survey worldwide.

Suncorp continues to play an active part in the **communities** we are part of. Our Queensland Skin Cancer initiative continues to raise awareness about the risk and prevention of this disease. In conjunction with the Queensland Institute of Medical Research we have raised more than \$850,000 which has assisted in treatment and research into a cure for skin cancer.

Suncorp has supported the Hear & Say Centre since 1994. Since July 2006 we have raised \$190,000 for this charity which teaches deaf or hearing impaired children and infants to listen, speak and integrate into the hearing community. We also recently entered into a three year sponsorship partnership with Youngcare, which is a charity set up to provide support to young Australians with high care needs.

We also continue our close association with Rugby Union through sponsorship of the Wallabies and Queensland Reds with the primary focus being on taking the game to local communities at a grass roots level, with coaching clinics for boys and girls in rural and regional areas.

Suncorp's employees are consistently generous in donating time and money to our sponsorships. We have in place a day's paid volunteer leave for every staff member to give something back to the communities we are part of. Participation in this program has grown substantially in the year to December 2006 and is highly valued among our employees.

While we continue to provide benefits to all our stakeholders in the six months to December 2006 our **shareholders** have again benefited from the strong financial performance of the business. The declaration of an interim ordinary dividend of 52 cents per share is consistent with our aim of achieving ordinary dividend growth of at least 10% for the year. And in the event of the Promina merger proceeding, we intend to pursue a consistent dividend policy for the merged group centred on providing sustainable growth in annual dividends.

### Cyclone Larry rebuilding

In my last report I outlined the significant work undertaken by our employees in supporting our customers and the communities affected by the devastation of Cyclone Larry. It's hard to believe that 20 March 2007 marks a year since the cyclone left a trail of destruction and a huge rebuilding challenge. Suncorp is proud to have played a part in the recovery effort, with 75% of the 8,000 Cyclone Larry claims received now completed. Suncorp has also been an active participant in the State Government Task Force and I was personally honoured to join Peter Cosgrove as a member of the Operation Recovery Task Force.

### Promina merger

As you are no doubt aware, in October 2006 we advised the market of our intention to merge with Promina to create the second largest domestic insurer in both Australia and New Zealand. Promina's strong suite of brands (including AAMI, APIA, Shannons, Just Car Insurance, Vero and AA insurance) complement the Suncorp and GIO brands and, together, give us an unrivalled portfolio to target well defined customer segments.

The combination of Suncorp and Promina's life insurance businesses will create Australia's seventh largest life insurance business while the merged group's funds management business will have approximately \$24 billion of funds under management (on a pro-forma basis).

Suncorp's banking operations will also benefit by accessing the merged groups significant customer base to offer retail banking products as part of an appropriate financial solutions package.

The proposal to merge with Promina is entirely consistent with Suncorp's strategic journey and now has us well on our way to achieving our vision of being the most desirable financial services company in Australia. Today, our three lines of business compete strongly in their respective markets and we have made huge strides in optimising the inherent advantages of having all three businesses under the one roof.

The formal announcement of our offer on 13 October 2006 was the culmination of many months of careful planning and signalled the start of an approval process which, if all goes according to plan, will conclude on 20 March 2007. The hard work and planning in the lead-up has served us well as we have progressively ticked off the major milestones and approvals. These include:

- The signing of a Merger Implementation Agreement (MIA) 10 days following the public announcement of the offer;
- Supporting Promina in the preparation of a comprehensive Scheme Booklet, which provides Promina shareholders with information to consider before voting on whether the merger should proceed;
- The report of the Independent Expert, Grant Samuel who concluded that the Scheme was in the best interests of Promina shareholders;
- A decision not to oppose the merger by the ACCC following comprehensive submissions by Suncorp and Promina;
- Approval by the Federal Treasurer under the *Financial Sector (Shareholdings) Act 1998*;
- Agreement by the Queensland Government to propose amendments to the relevant State Legislation to allow four members of the Promina Board to join an expanded Suncorp Board.

The presentation of our half-year result and Promina's full-year result represent another important step in the process. On 5 March, Promina shareholders will have an opportunity to vote on the Scheme. In the event this is successful, the Federal Court will convene on 12 March to hear an application for approval of the Scheme.

### Entitlement offer

In the event Promina shareholder and Federal Court approvals are received, Suncorp intends to undertake an entitlement offer to fund part of the cash consideration payable to Promina shareholders. The size of the entitlement offer is expected to be approximately \$1.15 billion.

The Chairman, in his letter, has provided more detail about what you can expect to receive in relation to the offer, should it proceed.

### Outlook

We expect that competition will continue to be strong across all our businesses and geographies and that recent interest rate rises will have a continuing impact on credit formation, particularly in the home loan market.

On a stand alone basis, we believe we are on track to deliver to the full-year outlook we outlined at our full-year results presentation in September 2006. This means that for the year to June 2007 we would expect to increase profit before tax and bad debts in the Bank by approximately 10%, achieve an ITR in the General Insurer in the 16% – 19% range (assuming no major weather events), grow profit on an underlying basis in Wealth Management by approximately 10% and, at the Group level, achieve ordinary dividend growth of at least 10%.

Obviously, in the event the Promina merger proceeds we would anticipate keeping our shareholders up to date as information comes to hand.

### Conclusion

I'd like to conclude by once again thanking you for your support and loyalty. While the year ahead will no doubt be challenging, I believe we are well placed to deliver enhanced value to our shareholders over the medium to long term.



**John Mulcahy**  
Managing Director and CEO