Mercantile Bank
Holdings Limited
Member of CGD Group

Annual Report 2008

your bank, your partner, our focus

Mercantile Bank Holdings Limited

Member of CGD Group

Reg No. 1989/000164/06

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Mercantile Group

The Group and glossary of terms

Mercantile Bank Holdings Limited is a registered bank controlling and investment holding company and its holding company is CGD. Its two principal operating subsidiaries comprise:

Mercantile Bank Limited provides a full range of international and domestic banking services. It operates in selected retail, commercial, corporate and alliance banking niches in which it offers banking, financial and investment services. It is a wholly-owned subsidiary of Mercantile Bank Holdings Limited.

Mercantile Insurance Brokers (Proprietary) Limited offers life assurance and short-term broking services to the Group and external parties through third party agreements. Its products encompass the full range available in the market including short-term insurance, pension, health benefits and life assurance. It is a wholly-owned subsidiary of Mercantile Bank Holdings Limited.

Abbreviation:	Definition/Description:
AGM	Annual General Meeting
ALCO	Asset and Liability Committee
ALM	Asset and Liability Management
Bank Regulations	Regulations relating to Banks issued under Section 90 of the Banks Act, 1990, as amended
Banks Act	Banks Act, No.94 of 1990, as amended
BCM	Business Continuity Management
BEE	Black Economic Empowerment
CEO	Chief Executive Officer
CGD	Caixa Geral de Depósitos S.A., a company registered in Portugal
Companies Act	Companies Act, No. 61 of 1973, as amended
CREDCOM	Credit Committee
EXCO	Executive Committee
FAIS	The Financial Advisory and Intermediary Services Act
FICA	The Financial Intelligence Centre Act
FSC	Financial Sector Charter
GAC	Group Audit Committee
IFRS	International Financial Reporting Standards and Interpretations
JSE	JSE Limited
King II	King Report on Corporate Governance for South Africa 2002
Mercantile	Mercantile Bank Holdings Limited and its subsidiaries
NCA	The National Credit Act
RMC	Risk and Capital Management Committee
ROA	Return on average assets
ROE	Return on average equity
SARB	South African Reserve Bank
the Bank	Mercantile Bank Limited
the Board	Where applicable, the Board of Directors of Mercantile Bank Holdings Limited or collectively the Board of Directors of Mercantile Bank Holdings Limited and Mercantile Bank Limited
the Company	Mercantile Bank Holdings Limited
the Code	Code of Banking Practice
the Group	Mercantile Bank Holdings Limited and its subsidiaries

Board of Directors and administration

at 24 February 2009

Board of Directors

J A S de Andrade Campos *† (*Chairman*)
D J Brown # (*Chief Executive Officer*)
G P de Kock †
L Hyne †
A T Ikalafeng †
J P M Lopes *#
T H Njikizana ^†
S Rapeti †

Administration

Group Secretary

R van Rensburg

Transfer secretaries

Computershare Investor Services (Proprietary) Limited
70 Marshall Street
Johannesburg
2001 South Africa

Postal address

P O Box 61051
Marshalltown
2107 South Africa

Registered office

1st Floor
Mercantile Bank
142 West Street
Sandown
2196

Postal address

P O Box 782699
Sandton
2146

* Portuguese
^ Zimbabwean
\# Executive
† Independent Non-Executive

Five year Group salient features

Year ended 31 December

	2004 R'000	2005 R'000	2006 R'000	2007 R'000	2008 R'000
Balance sheet					
Total assets	2 721 068	3 406 382	4 449 218	4 705 784	**5 916 775**
Loans and advances	975 611	1 458 677	2 066 432	2 814 743	**3 403 789**
Cash and cash equivalents	1 148 861	1 408 972	1 683 974	1 252 376	**1 464 959**
Shareholders' equity	500 939	550 179	667 418	839 914	**1 269 030**
Deposits	2 112 569	2 636 547	3 539 147	3 768 183	**4 389 347**
Income statement					
Profit/(Loss) before taxation	(212 966)*	66 996	100 643	165 302	**257 798**
Profit/(Loss) after taxation	(213 016)*	66 996	100 643	165 273	**419 973**
Headline earnings/(loss)	(213 756)	68 025	100 643	159 684	**410 107**
Financial performance ratios (%) (Comparatives for 2004 are not shown due to losses incurred in that year)					
Return on average equity (before taxation)		12.7	16.5	21.9	**26.2**
Return on average equity (after taxation)		12.7	16.5	21.9	**39.8**
Return on average assets (before taxation)		2.2	2.6	3.6	**4.9**
Return on average assets (after taxation)		2.2	2.6	3.6	**7.9**
Cost to income		91.0	71.7	56.4	**49.0**
Share statistics (cents)					
Earnings/(Loss) per ordinary share (before taxation)	(11.6)	1.71	2.56	4.21	**6.57**
Earnings/(Loss) per ordinary share (after taxation)	(11.6)	1.71	2.56	4.21	**10.70**
Headline earnings/(loss) per ordinary share (before taxation)	(11.7)	1.73	2.56	4.07	**6.32**
Headline earnings/(loss) per ordinary share (after taxation)	(11.7)	1.73	2.56	4.07	**10.45**
Net asset value per share	12.7	14.0	17.0	21.4	**32.4**
Tangible net asset value per share	12.6	13.8	16.7	20.8	**30.5**

* In the reporting year December 2004 guarantees received from CGD in 2002, primarily to underwrite certain non-performing loans, were cancelled, as part of the recapitalisation of the Group resulting in the raising of credit impairments of R173 million. Excluding the transactions related to the CGD guarantees, the loss after taxation would have been R40 million.

Group review

CGD, which is wholly owned by the Portuguese state, remains the Group's holding company with a shareholding of 91.75%. CGD is ranked as the world's 109th largest banking institution by assets in a current issue of "The Banker's Almanac". Its short and long-term financial liability ratings were confirmed by the three leading international rating agencies – Fitch Ratings, Moody's and Standard & Poor's as follows:

	Short term	Long term	Date	Outlook
Fitch Ratings	F1+	AA-	October 2008	Stable
Moody's	P-1	Aa1	November 2008	Stable
Standard & Poor's	A-1	A+	January 2009	Stable

Moody's Investors Service confirmed the following RSA national scale issuer ratings to the Bank in September 2008:

Short term	P-1.za
Long term	A2.za
Outlook	Stable

Business focus

The Group's strategy remains unchanged, namely:

- to grow enterprise banking business by offering products and services to small and mid-sized businesses across the South African spectrum whilst retaining a key segment focus on Portuguese customers; and
- to grow existing and seek out new opportunities in the alliance banking arena, primarily in the areas of card and payment products.

Financial review

Before taxation performance

The Group has again recorded a strong growth in profit, which increased by 56.0% for the 2008 financial year compared to the 2007 financial year. HEPS increased by 55.3%. These increases are largely attributable to:

- an increase in net interest income (after credit losses) of 49.8% as a result of the positive endowment effect of higher interest rates, higher capital due to profit retention, growth in lending of 20.9% and growth in deposits of 16.5%;
- growth in gross recurring non-interest income of 47.9% (net of costs growth: 24.6%) from core business activities with a particularly strong contribution from treasury; and
- non-recurring gains of R9.8 million on the disposal of Visa shares as part of that entity's public listing.

Costs increased year on year by 16.7% of which 12.5% relates to increased employee costs. The higher employee costs are largely due to salary package adjustments, increased headcount to support business growth as well as higher performance bonus costs in line with the Group's results. Efficiency continues to improve with the overall cost to income ratio reducing from 56.4% in December 2007 to 49.0%. Expenses (e.g. interchange and broker fees) incurred directly in the generation of fee and commission income, previously included in operating expenditure, are now deducted from fee and commission income in determining the cost to income ratio and presented accordingly in the income statement.

In line with market conditions, loans and advances have reflected some stress resulting in non-performing loans and advances as a percentage of total lending increasing to 3.8% as at December 2008 from a level of 2.5% in December 2007.

ROE improved to 26.2% (December 2007: 21.9%) whilst ROA was at 4.9% (December 2007: 3.6%).

After taxation performance: recognition of deferred taxation

In accordance with IFRS the Group deemed it appropriate to recognise deferred taxation at the end of 2008 mainly in respect of taxation losses incurred in the financial years prior to 2005. The effect of this recognition resulted in a non-recurring taxation credit of R162.2 million for the year ended 31 December 2008. The impact of this credit on the key performance ratios of the Group was:

HEPS increased year on year by 156.8%, ROE of 39.8% and ROA of 7.9%.

Directorate

Tapiwa Njikizana was appointed as an independent non-executive director on 6 November 2008.

Julio Lopes, an executive director seconded to the Group by CGD has had his contract renewed for a further three years from 9 November 2008.

Dave Brown, the CEO, was reappointed with effect from 29 March 2009 for a further period of three years.

We thank the Board for their valuable contribution and support during the year.

Group review (continued)

Financial Sector Charter

The Group remains fully committed to achieving the targets (as applicable to the Group's strategy) set out in the charter and plans are in place to deliver on these targets. Good progress continues to be made in this respect in the key areas of procurement, financing of black businesses and the diversity of the Group's Board. Whilst good progress has been made in respect of employment equity targets, these remain challenging in the areas of middle/senior management and the Group is behind in terms of achieving these targets.

Discussions are underway with two short listed candidates for empowerment at shareholder level and it is anticipated that agreement could be achieved on a prospective transaction in this regard before the end of 2009.

New banking system

The implementation of the replacement of the core retail banking systems and enhancement/upgrade of current systems architecture is well underway with a go-live date planned for the first quarter of 2010. Expenditure capitalised on this project as at 31 December 2008 is as follows:

- Property and equipment: R21.2 million; and
- Intangible assets: R74.6 million.

Following on completion of the process mapping phase of the project in December 2008 and the design of the operational data store required as a platform for future management information, tactical and strategic reporting, the overall spend on the project is now expected to increase to an estimated R210 million. As previously communicated, the increase in the original estimated cost was mainly due to the expanded scope in terms of upgrading/enhancing the current systems architecture of the Bank.

Most cost estimates have now become firm by way of concluding rand based contracts. The project will be funded from cash resources over the period of the project against agreed deliverables.

The pro forma effect of the transaction on the tangible net asset value per share of the Group at 31 December 2008, based on the above revised cost estimates, is expected to be a decrease of approximately 2.6 cents. The pro forma effect of the transaction has not been reviewed or reported on by the Group's auditors.

The rationale for this project remains the creation of a new systems platform to support the growth of the Group in line with our strategic objectives. The project will result in a more flexible and integrated systems environment enhancing our risk management and controls whilst providing us with greater capacity to compete in the market in the areas of product and service. No profits can be directly attributed to this project but the project drivers outlined above are expected to provide a positive benefit to the Group over time. The project is expected to be completed by the first quarter of 2010 – the delay in expected implementation from the third quarter of 2009 is largely due to a revision to the implementation plan to accommodate a later version of software release.

Outlook

The current difficult global economic conditions are expected to have an increasingly negative impact on the South African economy. This, together with the high level of consumer indebtedness on the domestic front, will make 2009 an extremely challenging year. In addition, Woolworths Financial Services have advised Mercantile that its card processing agreement will be terminated in the second half of 2009, following the sale of a controlling stake in the business to a competitor bank, which will put pressure on the rate of growth in fee income during the coming year. Similarly, the lower interest rate environment expected to prevail in 2009 will impact negatively on the Group's net interest income (negative endowment) given the structure of the Group's funding sources.

We thank all our staff for their commitment and dedication during the year under review and to our clients and shareholders we convey our appreciation for your trust and support. We also thank the SARB and our professional advisors for their sound guidance.

J A S de Andrade Campos	D J Brown
Chairman	*Chief Executive Officer*
24 February 2009	24 February 2009

Annual financial statements

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Directors' responsibility

In terms of the Companies Act, the Directors are required to maintain adequate accounting records and to prepare annual financial statements that fairly present the financial position at year-end and the results and cash flows for the year of the Company and the Group.

To enable the Board to discharge its responsibilities, management has developed and continues to maintain a system of internal controls. The Board has ultimate responsibility for this system of internal controls and reviews the effectiveness of its operations, primarily through the GAC and other risk monitoring committees and functions.

The internal controls include risk-based systems of accounting and administrative controls designed to provide reasonable, but not absolute, assurance that assets are safeguarded and that transactions are executed and recorded in accordance with sound business practices and the Group's written policies and procedures. These controls are implemented by trained and skilled staff, with clearly defined lines of accountability and appropriate segregation of duties. The controls are monitored by management and include a budgeting and reporting system operating within strict deadlines and an appropriate control framework. As part of the system of internal controls the Group's internal audit function conducts inspections, financial and specific audits and co-ordinates audit coverage with the external auditors.

The external auditors are responsible for reporting on the Company and Group annual financial statements.

The Company and Group annual financial statements are prepared in accordance with IFRS and incorporate responsible disclosures in line with the accounting policies of the Group. The Company and Group annual financial statements are based on appropriate accounting policies consistently applied except as otherwise stated and are supported by reasonable and prudent judgements and estimates. The Board believes that the Group will be a going concern in the year ahead. For this reason they continue to adopt the going concern basis in preparing the annual financial statements.

These annual financial statements, set out on pages 10 to 71, have been approved by the Board of Mercantile Bank Holdings Limited and are signed on their behalf by:

J A S de Andrade Campos
Chairman

24 February 2009

D J Brown
Chief Executive Officer

24 February 2009

Certificate from the Company Secretary

In terms of section 268G(d) of the Companies Act, I certify that, to the best of my knowledge and belief, the Company has lodged with the Registrar of Companies for the financial year ended 31 December 2008 all such returns as are required of a public company in terms of the Act, and that all such returns are true, correct and up-to-date.

R van Rensburg
Company Secretary
24 February 2009

Independent auditor's report

to the members of Mercantile Bank Holdings Limited

Report on the financial statements

We have audited the Company and Group annual financial statements, which comprise the Directors' report, the balance sheet and the consolidated balance sheet as at 31 December 2008, the income statement and the consolidated income statement, the statement of changes in equity and the consolidated statement of changes in equity and the cash flow statement and the consolidated cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory notes as set out on pages 10 to 71.

Directors' responsibility for the financial statements

The Company's Directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and in the manner required by the Companies Act of South Africa. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall financial statement presentation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company and the Group as at 31 December 2008, and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards, and in the manner required by the Companies Act of South Africa.

Deloitte & Touche.

Per **Riaan Eksteen**
Partner

24 February 2009

Building 8, Deloitte Place, The Woodlands,
Woodmead Drive, Sandton, 2196

National Executive:

GG Gelink Chief Executive, AE Swiegers Chief Operating Officer, GM Pinnock Audit, DL Kennedy Tax, L Geeringh Consulting, L Bam Corporate Finance, CR Beukman Finance, TJ Brown Clients & Markets, NT Mtoba Chairman of the Board, J Rhynes Deputy Chairman of the Board

A full list of partners and directors is available on request

B-BBEE rating: Level 3 contributor/AA (certified by Empowerdex)

Directors' report
for the year ended 31 December 2008

The Directors have pleasure in presenting their report, which forms part of the audited annual financial statements of the Company and the Group for the year ended 31 December 2008.

1. Nature of business

The Company is a registered bank controlling and investment holding company incorporated in the Republic of South Africa. Through its subsidiaries, the Company is involved in the full spectrum of domestic and international banking and financial services to niche markets in retail, commercial, corporate and alliance banking.

2. Holding company

The majority shareholder of the Company is CGD (91.75%).

3. Financial results

An overview of the financial results is set out in the Group Review commencing on page 5 of the Annual Report. Details of the Company and Group financial results are set out on pages 12 to 71 and in the opinion of the Directors require no further comment.

4. Share capital

There were no changes to the authorised and issued share capital of the Company during the year (2007: nil).

The authorised and issued share capital of the Company and Group is detailed in note 15 to the annual financial statements.

5. Directors, Company Secretary and registered addresses

The Directors of the Company during the year were as follows:

J A S de Andrade Campos *† (*Chairman*)
D J Brown # (*Chief Executive Officer*)
G P de Kock †
L Hyne †
A T Ikalafeng †
J P M Lopes *#
T H Njikizana ^† (appointed 6 November 2008)
S Rapeti †

The Directors of the Company as at 24 February 2009 are shown on page 3.

The Company Secretary is R van Rensburg and the registered addresses of the Company are:

Postal:	Physical:
P O Box 782699	1st Floor
SANDTON	Mercantile Bank
2146	142 West Street
	SANDOWN
	2196

* Portuguese ^ Zimbabwean # Executive
† Independent Non-Executive

6. Dividends

No dividend was declared during the year under review (2007: nil).

7. Subsidiary companies and companies not consolidated

All subsidiary companies are incorporated in South Africa. A register containing details of all non-trading companies is available for inspection at the registered office of the Company.

Aggregate income after taxation earned by subsidiaries amounted to R421.5 million (2007: R169.3 million) and aggregate losses amounted to R0.5 million (2007: R3.2 million).

Directors' report
for the year ended 31 December 2008 (continued)

7. Subsidiary companies and companies not consolidated (continued)

The principal consolidated subsidiary companies are as follows:

Company name	Issued share capital R'000	Effective holding %	Nature of business ^	Shares at cost 2008 R'000	Shares at cost 2007 R'000	Owing to subsidiaries 2008 R'000	Owing to subsidiaries 2007 R'000
LSM (Troyeville) Properties (Pty) Limited	–	100	1	**140**	140	–	–
Mercantile Bank Limited	124 969	100	2	**1 485 448**	1 485 448	**10 793**	9 825
Mercantile Insurance Brokers (Pty) Limited	250	100	3	**294**	294	–	–
Mercantile Nominees (Pty) Limited	–	100	4	–	–	–	–
Mercantile Registrars Limited	100	100	5	–	–	–	–
Portion 2 of Lot 8 Sandown (Pty) Limited	–	100	1	**8 832**	8 832	–	–
						10 793	9 825

Notes:

^ Nature of business

1. Property holding
2. Banking
3. Insurance brokers
4. Nominee company
5. Investment company

Mercantile Matrix Finance (Pty) Limited and Mercantile E-Bureau (Pty) Limited have not been consolidated into the Group's results, the impact being immaterial.

8. Going concern

The Company and Group annual financial statements have been prepared on the going concern basis.

9. Special resolutions

There were no special resolutions during the year under review.

10. Post balance sheet events

No material events have occurred between the accounting date and the date of this report that require adjustment to or disclosure in the annual financial statements.

Accounting policies

for the year ended 31 December 2008

The principal accounting policies adopted in the preparation of these annual financial statements are set out below:

1. Basis of presentation

The Company and Group annual financial statements have been prepared in accordance with IFRS issued by the International Accounting Standards Board, using the historical cost convention as modified by the revaluation of certain financial assets, liabilities and properties.

In the current year, the Group has adopted IFRIC 11 – IFRS 2 Group and Treasury transactions, which is effective for annual reporting periods beginning on or after 1 March 2007. The impact of this adoption has been disclosed in note 32 of the annual financial statements.

2. Basis of consolidation

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

3. Recognition of assets and liabilities

3.1 Assets

The Group recognises assets when it obtains control of a resource as a result of past events and from which future economic benefits are expected to flow to the Group.

3.2 Liabilities

The Group recognises liabilities when it has a present obligation as a result of past events and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation.

3.3 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation, as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made.

3.4 Contingent liabilities

The Group discloses a contingent liability where it has a possible obligation as a result of past events, the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group, or it is possible that an outflow of resources will be required to settle the obligation, or the amount of the obligation cannot be measured with sufficient reliability.

4. Financial instruments

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group has become a party to the contractual provisions of that instrument. Regular way purchases or sales of financial assets are recognised using settlement date accounting. On initial recognition, financial instruments are recognised at their fair value and in the case of a financial instrument not at fair value through profit and loss, transaction costs that are directly attributable to the acquisition or issue of the financial instrument are included.

The Group derecognises a financial asset when:

- the contractual rights to the cash flows arising from the financial assets have expired or been forfeited by the Group; or
- it transfers the financial asset including substantially all the risks and rewards of ownership of the asset; or
- it transfers the financial asset, neither retaining nor transferring substantially all the risks and rewards of ownership of the asset, but no longer retains control of the asset.

A financial liability is derecognised when and only when the liability is extinguished, that is, when the obligation specified in the contract is discharged, cancelled or has expired.

Accounting policies

for the year ended 31 December 2008 (continued)

4. **Financial instruments** (continued)

The difference between the carrying amount of a financial liability (or part thereof) extinguished or transferred to another party and consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in income.

4.1 Derivative financial instruments

Derivative financial assets and liabilities are classified as held-for-trading.

The Group uses the following derivative financial instruments to reduce its underlying financial risks and/or to enhance yields:

- forward exchange contracts;
- foreign currency swaps;
- interest rate swaps; and
- unlisted equity options.

Derivative financial instruments ("derivatives") are not entered into for trading or speculative purposes. All derivatives are recognised on the balance sheet. Derivative financial instruments are initially recorded at cost and are remeasured to fair value at each subsequent reporting date. Changes in the fair value of derivatives are recognised in income.

Derivatives in unlisted equity options where the underlying asset does not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, are measured at cost.

Embedded derivatives are separated from the host contract and accounted for as a separate derivative when:

- the embedded derivative's economic characteristics and risks are not closely related to those of the host contract;
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and
- the combined instrument is not measured at fair value with changes in fair value reported in income.

A derivative's notional principal reflects the value of the Group's investment in derivative financial instruments and represents the amount to which a rate or price is applied to calculate the exchange of cash flows.

4.2 Financial assets

The Group's principal financial assets are cash and cash equivalents, bank term deposits, other investments, negotiable securities, loans and advances and other accounts receivable.

Financial assets at fair value through profit and loss

Loans and receivables with fixed interest rates and corporate bonds are classified at fair value through profit and loss. Financial assets are designated at fair value through profit and loss, primarily to eliminate or significantly reduce the accounting mismatch. The Group seeks to demonstrate that by applying the fair value option, it significantly reduces measurement inconsistency that would otherwise arise from measuring derivatives at fair value with gains and losses in profit and loss, and the loans and receivables and corporate bonds at amortised cost.

Available-for-sale

Available-for-sale financial assets are those non-derivatives that are designated as available-for-sale or are not classified as loans and receivables, held to maturity investments or financial assets at fair value through profit and loss.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, deposits held by the Group with the SARB, domestic banks and foreign banks as well as resale agreements. These financial assets have been designated as loans and receivables and are measured at amortised cost.

Bank term deposits

Bank term deposits comprise deposits held by the Group with domestic and foreign banks with a residual maturity of greater than three months. These financial assets have been designated as loans and receivables and are measured at amortised cost.

Accounting policies

for the year ended 31 December 2008 (continued)

4. Financial instruments (continued)

4.2 Financial assets (continued)

Other investments

Investments consist of unlisted equity investments. Other investments have been designated as available-for-sale. These assets are measured at fair value, at each reporting date, with the resultant gains or losses being recognised in equity until the financial asset is sold, or otherwise disposed of, or found to be impaired. At that time the cumulative gains or losses previously recognised in equity are included in income.

Negotiable securities

Negotiable securities consist of government stock, corporate bonds, Treasury bills and debentures.

Government stock has been designated as available-for-sale. These assets are measured at fair value, at each reporting date, with the resultant gains or losses being recognised in equity until the financial asset is sold, or otherwise disposed of, or found to be impaired. At that time the cumulative gains or losses previously recognised in equity are included in income.

Corporate bonds are designated at fair value through profit and loss.

All other negotiable securities are classified as loans and receivables and are carried at amortised cost subject to impairment.

Loans and advances

Loans and advances principally comprise amounts advanced to third parties in terms of certain products. Fixed rate loans and advances are designated at fair value through profit and loss with resultant gains and losses being included in income. Variable rate loans and advances are designated as loans and receivables and are measured at amortised cost.

Other accounts receivable

Other accounts receivable comprise items in transit, prepayments and deposits and other receivables. These assets have been designated as loans and receivables and are measured at amortised cost.

4.3 Financial liabilities

The Group's financial liabilities include deposits, taxation payable and other accounts payable consisting of accruals, product related credits and sundry creditors. All financial liabilities, other than liabilities designated at fair value through profit and loss and derivative instruments, are measured at amortised cost. For financial liabilities designated at fair value through profit and loss and derivative instruments which are measured at fair value through profit and loss, the resultant gains and losses are included in income.

4.4 Fair value estimation

The fair value of publicly traded derivatives, securities and investments is based on quoted market values at the balance sheet date. In the case of an asset held by the Group, the current bid price is used as a measure of fair value. In the case of a liability held, the current offer or asking price is used as a measure of fair value. Mid-market prices are used as a measure of fair value where there are matching asset and liability positions.

In assessing the fair value of non-traded derivatives and other financial instruments, the Group uses a variety of methods and assumptions that are based on market conditions and risks existing at each balance sheet date. Quoted market prices or dealer quotes for the same or similar instruments are used for the majority of securities, long-term investments and long-term debt. Other techniques, such as option pricing models, estimated discounted value of future cash flows, replacement cost, termination cost and net asset values of underlying investee entities are used to determine fair value for all remaining financial instruments.

4.5 Amortised cost

Amortised cost is determined using the effective interest rate method. The effective interest rate method is a way of calculating amortisation using the effective interest rate of a financial asset or financial liability. It is the rate that discounts the expected stream of future cash flows through maturity or the next market-based revaluation date to the current net carrying amount of the financial asset or financial liability.

Accounting policies

for the year ended 31 December 2008 (continued)

4. Financial instruments (continued)

4.6 Impairments

Specific impairments are made against identified doubtful advances. Portfolio impairments are maintained to cover potential losses, which although not specifically identified, may be present in the advances portfolio.

Advances which are deemed uncollectible are written off against the specific impairments. A direct reduction of an impaired financial asset occurs when the Group writes off an impaired account. The Group's policies set out the criteria for write-offs, which involves an assessment of the likelihood of commercially viable recovery of the carrying amount of impaired financial asset. Both the specific and portfolio impairments raised during the year less the recoveries of advances previously written off, are charged to income.

Interest for non-performing loans and advances is not recognised to income but is suspended. In certain instances, interest is also suspended where portfolio impairments are raised.

The recoverable amount is the sum of the estimated future cash flows, discounted to their present value using a pre-taxation discount rate that reflects the portfolio of advances' original effective interest rate.

If the recoverable amount of the advance is estimated to be less than the carrying amount, the carrying amount of the advance is reduced to its recoverable amount by raising a specific impairment, which is recognised as an expense.

Where the impairment loss subsequently reverses, the carrying amount of the advance is increased to the revised estimate of its recoverable amount, subject to the increased carrying amount not exceeding the carrying amount that would have been determined had no impairment loss been recognised for the advance in prior years. A reversal of an impairment loss is recognised as income immediately.

5. Foreign currency transactions

Transactions in foreign currencies are converted into the functional currency at prevailing exchange rates on the transaction date. Monetary assets, liabilities and commitments in foreign currencies are translated into the functional currency using the rates of exchange ruling at each reporting date. Gains and losses on foreign exchange are included in income.

6. Subsidiaries

Investments in subsidiaries in the Company's annual financial statements are designated as available-for-sale assets and are recognised at fair value. Fair value is estimated as the net asset value of the investee entities. All gains and losses on the sale of subsidiaries are recognised in income.

7. Associated companies

Associated companies are those companies in which the Group exercises significant influence, but not control or joint control, over their financial and operating policies and holds between 20% and 50% interest therein.

The carrying values of investments in associated companies represent the aggregate of the cost of the investments plus post-acquisition equity accounted income and reserves. These investments are accounted for using the equity method in the Group annual financial statements. This method is applied from the effective date on which the enterprise became an associated company, up to the date on which it ceases to be an associated company.

The results and assets and liabilities of associated companies are incorporated in the financial statements using the equity method of accounting, except when the investment is classified as held for sale, in which case it is accounted for in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

8. Investment properties

Investment properties are held to earn rentals and/or for capital appreciation. The Group carries investment properties in the balance sheet at open-market fair value based on valuations by independent registered professional valuators at each balance sheet date. The open-market fair value is based on capitalisation rates for open market net rentals for each property. Fair value movements are included in income in the year in which they arise.

9. Property and equipment

9.1 Owner-occupied properties

Owner-occupied properties are held for use in the supply of services or for administrative purposes and are stated in the balance sheet at open-market fair value on the basis of their existing use at the date of revaluation, less any subsequent accumulated depreciation

Accounting policies

for the year ended 31 December 2008 (continued)

9. Property and equipment (continued)

9.1 Owner-occupied properties (continued)

calculated using the straight-line method and subsequent accumulated impairment losses. The open-market fair value is based on capitalisation rates for open market net rentals for each property. Revaluations are performed annually by independent registered professional valuators.

Any revaluation increase, arising on the revaluation of owner-occupied properties, is credited to the non-distributable reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense. The increase is credited to income to the extent that an expense was previously charged to income. A decrease in carrying amount arising on the revaluation of owner-occupied properties is charged as an expense to the extent that it exceeds the balance, if any, held in the non-distributable reserve relating to a previous revaluation of that asset. On the subsequent sale or retirement of a revalued property, the revaluation surplus, relating to that property, in the non-distributable reserve is transferred to distributable reserves. The properties' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

9.2 Equipment

All equipment is stated at historical cost less accumulated depreciation and subsequent accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to income as they are incurred.

Depreciation on equipment is calculated using the straight-line method to allocate cost to residual values over estimated useful lives. Leasehold improvements are depreciated over the period of the lease or over such lesser period as is considered appropriate. Equipment residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Assets are reviewed annually for impairment and whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

The estimated useful lives of property and equipment are as follows:

Leasehold improvements	5 – 10 years
Computer equipment	3 – 5 years
Furniture and fittings	10 years
Office equipment	5 – 10 years
Motor vehicles	5 years
Owner-occupied properties	50 years
Land	Not depreciated

Gains and losses on disposal of property and equipment are determined by comparing proceeds with the carrying amount and are recognised in income. Depreciation of an asset begins when it is available for use and ceases at the earlier of the date that the asset is classified as held for sale or the date the asset is derecognised.

10. Intangible assets

Computer software

Direct costs associated with purchasing, developing and maintaining computer software programs and the acquisition of software licences are recognised as intangible assets if they are expected to generate future economic benefits that exceed costs beyond one year.

Computer software and licences that are recognised as intangible assets are amortised on the straight-line basis at rates appropriate to the expected useful lives of the assets, which is usually between three and five years, but where appropriate over a maximum of ten years and are carried at cost less any accumulated amortisation and any accumulated impairment losses. The carrying amount of capitalised computer software and licences is reviewed annually for indication of impairment and is written down when the carrying amount exceeds the recoverable amount.

Recoverable amount is the higher of fair value less costs to sell and value in use. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is immediately recognised in income.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually and whenever there is an indication that the asset may be impaired.

Accounting policies
for the year ended 31 December 2008 (continued)

11. Non-current assets held for sale

Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell.

12. Taxation

Income taxation expense represents the sum of the taxation currently payable and deferred taxation.

12.1 Current taxation

The taxation currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

12.2 Deferred taxation

Deferred taxation is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred taxation liabilities are generally recognised for all taxable temporary differences, and deferred taxation assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred taxation liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred taxation assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred taxation assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred taxation assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. The measurement of deferred taxation liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred taxation assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Accounting policies

for the year ended 31 December 2008 (continued)

12. Taxation (continued)

12.3 Current and deferred tax for the period

Current and deferred taxation are recognised as an expense or income in profit or loss, except when they relate to items credited or debited directly to equity, in which case the taxation is also recognised directly in equity.

13. Sale and repurchase agreements and lending of securities

Securities sold subject to linked repurchase agreements ("repos") are reflected in the annual financial statements as investments with the proceeds recognised in cash and cash equivalents and the counterparty liability is included in amounts due to other banks, deposits from banks, other deposits, or deposits due to customers, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective interest rate method.

Securities purchased under agreements to resell ("reverse repos") are recorded as cash and cash equivalents. Securities lent to counterparties are also retained in the annual financial statements.

Securities borrowed are not recognised in the annual financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded with the gain or loss being included in income. The obligation to return them is recorded at fair value in other accounts payable.

14. Instalment sales and leases

14.1 The Group as the lessee

The leases entered into by the Group are primarily operating leases. The total payments made under operating leases are charged to income on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

14.2 The Group as the lessor

Leases and instalment sale agreements are regarded as financing transactions with rentals and instalments receivable, less unearned finance charges, being included in advances. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

15. Interest income and interest expense

Except where interest is suspended, interest income and expense are recognised in income for all interest-bearing instruments measured at amortised cost using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and basis points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

16. Fee, commission and dividend income

Fees and commissions are recognised on an accrual basis unless included in the effective interest rate. Dividend income from investments is recognised when the shareholder's rights to receive payment have been established.

17. Retirement funds

The Group operates defined contribution funds, the assets of which are held in separate trustee-administered funds. The retirement funds are funded by payments from employees and by the relevant Group companies. The Group contributions to the retirement funds are based on a percentage of the payroll and are charged to income as accrued.

18. Post-retirement medical benefits

The Group provides for post-retirement medical benefits to certain retired employees. These benefits are only applicable to employees who were members of the Group's medical aid scheme prior to May 2000 and who elected to retain the benefits in 2005 and are based on these employees remaining in service up to retirement age. The Group provides for the present value of the obligations in excess of the fair value of the plan assets which are intended to offset the expected costs relating to the post-retirement medical benefits. The costs of the defined benefit plan are assessed using the projected unit credit method. Under this method, the cost of providing post-retirement medical benefits is charged to income so as to spread the regular cost over the service lives of employees in accordance with the advice of qualified actuaries, who value the plans annually.

Accounting policies

for the year ended 31 December 2008 (continued)

18. Post-retirement medical benefits (continued)

Actuarial gains and losses, the effect of settlements on the liability and plan assets and the curtailment gain due to the change in the post-retirement subsidy of in-service members are recognised in income immediately.

19. Equity compensation plans

Share options and/or conditional share awards in the Company are awarded to employees of the Bank at the discretion of the Remuneration Committee and approved by the Board of the Company. The Group has applied the requirements of IFRS 2 to share-based payments.

These share-based payments are equity-settled and measured at fair value at the grant date and expensed on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest.

Fair value of share options is measured by use of a Black-Scholes model. The fair value has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

A Share Incentive Trust is used for share option awards and its financial position and results are consolidated.

20. Segment information

A business segment is a distinguishable component of the Group that is engaged in providing specific products or services whilst a geographical segment provides products or services in a particular economic environment.

21. General credit-risk reserve

Banks Act circular 21/2004 required that a general credit-risk reserve be recognised within Shareholders' equity for any shortfall between total impairments raised in terms of IAS 39 and the provisions required in terms of Regulation 28 of the Regulations relating to Banks. Such reserve was maintained through an appropriation of distributable reserves to a general credit-risk reserve. The new Bank Regulations, which were effective 1 January 2008, no longer require general credit-risk reserves, which resulted in the balance of this reserve being transferred to distributable reserves.

22. Critical accounting estimates and judgements

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities. 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.

22.1 Impairment losses on loans and advances

The Group reviews its loan portfolios to assess impairment on a monthly basis. In determining whether an impairment loss should be recorded in income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

22.2 Fair value of financial instruments

The fair value of financial instruments that are not quoted in active markets are determined by using valuation techniques. Where valuation techniques are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are certified before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices. To the extent practical, models use only observable data. However areas such as credit risk, volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial instruments.

Accounting policies

for the year ended 31 December 2008 (continued)

22. Critical accounting estimates and judgements (continued)

22.3 Impairment of available-for-sale equity investments

The Group determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates among other factors, the normal volatility in share price. In addition impairment may be appropriate when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, operational and financing cash flows.

22.4 Income taxes

There are many transactions and calculations for which the ultimate taxation determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated taxation issues based on estimates of whether additional taxes will be due. Where the final taxation outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income taxation and deferred taxation provisions in the period in which such determination is made.

23. Recent accounting developments

There are standards and interpretations in issue that are not yet effective. These include the following standards and interpretations that could be applicable to the business of the Group and may have an impact on future financial statements. The impact of initial application has not been assessed as at the date of authorisation of the annual financial statements and will not be early adopted.

IFRS 2 (Share Based Payments) was issued during 2008 but is only effective for annual periods beginning on or after 1 January 2009. The Group will comply with the applicable standard from the year ending 31 December 2009.

IFRS 3 (Business Combinations) was issued during 2008 but is only effective for business combinations concluded on or after 1 July 2009. The Group will comply with the applicable standard from the year ending 31 December 2010.

IFRS 8 (Operating Segments) was issued during 2006 but is only effective for annual periods beginning on or after 1 January 2009. The Group will comply with the applicable standard from the year ending 31 December 2009.

IFRIC 13 (Customer loyalty programmes) was issued during 2007 but is only effective for annual periods beginning on or after 1 July 2008. The Group will apply IFRIC 13 from the year ending 31 December 2009.

IFRIC 15 (Agreements for the Construction of Real Estate) was issued during 2008 but is only effective for annual periods beginning on or after 1 January 2009. The Group will comply with the applicable standard from the year ending 31 December 2009.

IFRIC 17 (Distributions of Non-cash Assets to Owners) was issued during 2008 but is only effective for annual periods beginning on or after 1 July 2009. The Group will comply with the applicable standard from the year ending 31 December 2010.

IAS 1 (Presentation of Financial Statements) was issued during 2008 but is only effective for annual periods beginning on or after 1 January 2009. The Group will comply with the applicable standard from the year ending 31 December 2009.

IAS 23 (Borrowing costs) was issued during 2008 but is only effective for annual periods beginning on or after 1 January 2009. The Group will comply with the applicable standard from the year ending 31 December 2009.

IAS 27 (Consolidated and Separate Financial Statements) was issued during 2008 but is only effective for annual periods beginning on or after 1 July 2009. The Group will comply with the applicable standard from the year ending 31 December 2010.

IAS 28 (Investments in Associates) was issued during 2008 but is only effective for annual periods beginning on or after 1 July 2009. The Group will comply with the applicable standard from the year ending 31 December 2010.

IAS 31 (Interest in Joint Ventures) was issued during 2008 but is only effective for annual periods beginning on or after 1 July 2009. The Group will comply with the applicable standard from the year ending 31 December 2010.

IAS 39 (Financial Instruments: Recognition and measurement) was issued during 2008 but is only effective for annual periods beginning on or after 1 July 2009. The Group will comply with the applicable standard from the year ending 31 December 2010.

Accounting policies

for the year ended 31 December 2008 (continued)

23. Recent accounting developments (continued)

On 22 May 2008, the International Accounting Standards Board issued its latest standard, titled Improvements to International Financial Reporting Standards 2008. The Standard included 35 amendments to various current Standards. The following amendments have not been applied in the 2008 financial year as they are not yet effective.

Standard	Annual periods beginning on or after
IFRS 1 (AC 138) – First-time adoption of International Financial Reporting Standards	1 January 2009
IFRS 5 (AC 142) – Non-current Assets Held for Sale and Discontinued Operations	1 July 2009
IAS 1 (AC 101) – Presentation of Financial Statements	1 January 2009
IAS 16 (AC 123) – Property, Plant and Equipment	1 January 2009
IAS 19 (AC 116) – Employee Benefits	1 January 2009
IAS 20 (AC 134) – Accounting for Government Grants and Disclosure of Government Assistance	1 January 2009
IAS 27 (AC 132) – Consolidated and Separate Financial Statements	1 January 2009
IAS 28 (AC 110) – Investments in Associates	1 January 2009
IAS 29 (AC 124) – Financial Reporting in Hyperinflationary Economies	1 January 2009
IAS 31 (AC 119) – Interests in Joint Ventures	1 January 2009
IAS 32 (AC 125) – Financial Instruments: Presentation	1 January 2009
IAS 36 (AC 128) – Impairment of Assets	1 January 2009
IAS 38 (AC 129) – Intangible Assets	1 January 2009
IAS 39 (AC 133) – Financial Instruments: Recognition and Measurement	1 January 2009
IAS 40 (AC 135) – Investment Property	1 January 2009
IAS 41 (AC 137) – Agriculture	1 January 2009

Balance sheets

at 31 December 2008

		Group		Company	
		2008	2007	2008	2007
	Note	R'000	R'000	R'000	R'000
ASSETS					
Intangible assets	2	**76 894**	23 569	**–**	–
Property and equipment	3	**128 672**	96 969	**–**	–
Other accounts receivable	4	**39 273**	23 639	**4**	19
Interest in subsidiaries	5	**–**	–	**1 286 608**	844 168
Interest in associated company	6	**–**	4 251	**–**	–
Other investments	7	**12 315**	228	**29**	20
Deferred taxation assets	8	**157 275**	–	**–**	–
Non-current assets held for sale	9	**5 289**	–	**–**	–
Loans and advances	10	**3 403 789**	2 814 743	**–**	–
Derivative financial instruments	11	**56 873**	43 814	**–**	–
Negotiable securities	12	**247 141**	275 577	**–**	–
Bank term deposits	13	**324 295**	170 618	**–**	–
Cash and cash equivalents	14	**1 464 959**	1 252 376	**224**	197
Total assets		**5 916 775**	4 705 784	**1 286 865**	844 404
EQUITY AND LIABILITIES					
Shareholders' equity		**1 269 030**	839 914	**1 286 831**	844 371
Share capital and share premium	15	**1 202 571**	1 207 422	**1 210 143**	1 210 143
Capital redemption reserve fund		**3 788**	3 788	**3 788**	3 788
Share-based payments reserve		**4 650**	7 019	**–**	7 019
General reserve		**7 478**	7 478	**–**	–
Property revaluation reserve		**46 364**	53 705	**–**	–
Available-for-sale reserve		**13 036**	(48)	**720 236**	276 748
General credit-risk reserve		**–**	19 403	**–**	–
Accumulated loss		**(8 857)**	(458 853)	**(647 336)**	(653 327)
Non-current liabilities					
Deferred taxation liabilities	8	**15 259**	–	**–**	–
Liabilities		**4 632 486**	3 865 870	**34**	33
Deposits	16	**4 389 347**	3 768 183	**–**	–
Derivative financial instruments	11	**95 091**	15 356	**–**	–
Provisions	17	**48 596**	42 435	**–**	–
Other accounts payable	19	**98 958**	39 780	**34**	33
Taxation	20	**494**	116	**–**	–
Total equity and liabilities		**5 916 775**	4 705 784	**1 286 865**	844 404

Income statements

for the year ended 31 December 2008

		Group		Company	
		2008	2007	**2008**	2007
	Note	**R'000**	R'000	**R'000**	R'000
Interest income	22	**661 776**	467 247	**–**	–
Interest expenditure	23	**(337 813)**	(250 012)	**–**	–
Net interest income		**323 963**	217 235	**–**	–
Net charge for credit losses	10	**(6 618)**	(5 358)	**–**	–
Net interest income after credit losses		**317 345**	211 877	**–**	–
Net gain on disposal and revaluation of available-for-sale investments		**9 837**	5 602	**–**	–
Non-interest income	24	**260 003**	190 871	**–**	–
Recurring		**260 003**	175 796	**–**	–
Non-recurring		**–**	15 075	**–**	–
Fee and commission expenditure	25	**(76 968)**	(28 841)	**–**	–
Net interest and non-interest income		**510 217**	379 509	**–**	–
Operating expenditure	26	**(253 154)**	(216 978)	**(1 028)**	(846)
Operating profit		**257 063**	162 531	**(1 028)**	(846)
Share of income from associated company		**735**	2 771	**–**	–
Profit/(Loss) before taxation		**257 798**	165 302	**(1 028)**	(846)
Taxation	27	**162 175**	(29)	**–**	(29)
Profit/(Loss) after taxation		**419 973**	165 273	**(1 028)**	(875)
Earnings per ordinary share after taxation (cents)	28.1	**10.70**	4.21		
Earnings per ordinary share before taxation (cents)	28.1	**6.57**	4.21		
Diluted earnings per ordinary share after taxation (cents)	28.2	**10.70**	4.21		
Diluted earnings per ordinary share before taxation (cents)	28.2	**6.57**	4.21		
Dividends per share (cents)		**–**	–		

Statements of changes in equity

for the year ended 31 December 2008

	Share capital and share premium R'000	Capital redemption reserve fund R'000	Share-based payments reserve R'000	General reserve R'000	Property re-valuation reserve R'000	Available-for-sale reserve R'000	General credit-risk reserve R'000	Accu-mulated loss R'000	Total R'000
Group									
Shareholders' equity at 1 January 2007	1 207 046	3 788	3 025	7 478	45 588	5 216	13 954	(618 677)	667 418
Net movement for the year	376	–	3 994	–	8 117	(5 264)	5 449	159 824	172 496
Revaluation of owner-occupied property	–	–	–	–	8 117	–	–	–	8 117
Gains and losses on remeasurement to fair value	–	–	–	–	–	338	–	–	338
Release to income on disposal of available-for-sale financial assets	–	–	–	–	–	(5 602)	–	–	(5 602)
Increase in general credit-risk reserve	–	–	–	–	–	–	5 449	(5 449)	–
Reduction of treasury shares held within the Group	376	–	–	–	–	–	–	–	376
Share-based payments expense	–	–	3 994	–	–	–	–	–	3 994
Profit after taxation	–	–	–	–	–	–	–	165 273	165 273
Shareholders' equity at 31 December 2007	1 207 422	3 788	7 019	7 478	53 705	(48)	19 403	(458 853)	839 914
Net movement for the year	(4 851)	–	(2 369)	–	(7 341)	13 084	(19 403)	449 996	429 116
Revaluation of owner-occupied property	–	–	–	–	10 689	–	–	–	10 689
Gains and losses on remeasurement to fair value	–	–	–	–	–	25 121	–	–	25 121
Release to income on disposal of available-for-sale financial assets	–	–	–	–	–	(9 837)	–	–	(9 837)
Decrease in general credit-risk reserve	–	–	–	–	–	–	(19 403)	19 403	–
Transfer from share-based payments reserve to accumulated loss	–	–	(7 019)	–	–	–	–	7 019	–
Transfer to deferred taxation liability	–	–	–	–	(18 030)	(2 200)	–	–	(20 230)
Increase of treasury shares held within the Group	(4 851)	–	–	–	–	–	–	–	(4 851)
Share-based payments expense	–	–	4 650	–	–	–	–	3 601	8 251
Profit after taxation	–	–	–	–	–	–	–	419 973	419 973
Shareholders' equity at 31 December 2008	1 202 571	3 788	4 650	7 478	46 364	13 036	–	(8 857)	1 269 030

Statements of changes in equity

for the year ended 31 December 2008 (continued)

	Share capital and share premium R'000	Capital redemption reserve fund R'000	Share-based payments reserve R'000	Available-for-sale reserve R'000	Accu-mulated loss R'000	Total R'000
Company						
Shareholders' equity at 1 January 2007	1 210 143	3 788	3 025	106 011	(652 452)	670 515
Net movement for the year	–	–	3 994	170 737	(875)	173 856
Gains and losses on remeasurement to fair value	–	–	–	170 737	–	170 737
Share-based payments expense	–	–	3 994	–	–	3 994
Loss after taxation	–	–	–	–	(875)	(875)
Shareholders' equity at 31 December 2007	**1 210 143**	**3 788**	**7 019**	**276 748**	**(653 327)**	**844 371**
Net movement for the year	–	–	(7 019)	443 488	5 991	442 460
Gains and losses on remeasurement to fair value	–	–	–	443 488	–	443 488
Transfer to accumulated loss	–	–	(7 019)	–	7 019	–
Loss after taxation	–	–	–	–	(1 028)	(1 028)
Shareholders' equity at 31 December 2008	**1 210 143**	**3 788**	**–**	**720 236**	**(647 336)**	**1 286 831**

Cash flow statements

for the year ended 31 December 2008

		Group		Company	
		2008	2007	2008	2007
	Note	R'000	R'000	R'000	R'000
Operating activities					
Cash receipts from customers	29.1	993 977	626 780	–	–
Cash paid to suppliers and employees	29.2	(637 963)	(474 363)	(1 028)	(846)
Cash generated from operations	29.3	356 014	152 417	(1 028)	(846)
Dividends received		861	21	–	–
Taxation recovered	29.4	307	81	–	–
Net (increase) in income earning assets	29.5	(725 743)	(376 789)	–	–
Net increase in deposits and other accounts	29.6	659 857	216 409	984	905
Net cash inflow/(outflow) from operating activities		291 296	(7 861)	(44)	59
Investing activities					
Purchase of property, equipment and intangible assets		(89 963)	(20 000)	–	–
Acquisition of investments		(472)	–	–	–
Proceeds on sale of property, equipment and intangible assets		63	53	–	–
Proceeds on disposal of investments		9 907	7 319	71	–
Dividends received from associated company		1 752	2 146	–	–
Net cash (outflow)/inflow from investing activities		(78 713)	(10 482)	71	–
Net cash inflow/(outflow) for year		212 583	(18 343)	27	59
Cash and cash equivalents at beginning of year		1 252 376	1 270 719	197	138
Cash and cash equivalents at end of year	14	1 464 959	1 252 376	224	197

Notes to the annual financial statements

for the year ended 31 December 2008

	Group 2008 Fair value R'000	Group 2008 Carrying amount R'000	Group 2007 Fair value R'000	Group 2007 Carrying amount R'000
1. Categories and fair values of financial instruments				
Assets				
Available-for-sale	32 853	32 853	6 802	6 802
Other investments	12 315	12 315	228	228
Negotiable securities – Government stock	20 538	20 538	6 574	6 574
Loans and receivables	5 304 555	5 305 008	4 337 039	4 345 362
Current accounts	503 622	503 622	655 384	655 384
Credit card	14 920	14 920	15 184	15 184
Mortgage loans	1 560 921	1 560 921	1 196 303	1 196 303
Instalment sales and leases	349 480	349 480	276 720	276 720
Structured loans	254 795	254 795	83 878	83 878
Other advances	566 140	566 140	433 057	433 057
Negotiable securities – Treasury bills	226 150	226 603	203 880	204 010
Negotiable securities – Debentures	–	–	26 000	34 193
Bank term deposits	324 295	324 295	170 618	170 618
Cash and cash equivalents	1 464 959	1 464 959	1 252 376	1 252 376
Other accounts receivable	39 273	39 273	23 639	23 639
Loans and receivables designated at fair value through profit and loss	153 911	153 911	185 017	185 017
Mortgage loans	53 946	53 946	40 962	40 962
Instalment sales and leases	21 300	21 300	26 997	26 997
Other advances	78 665	78 665	86 258	86 258
Corporate bonds	–	–	30 800	30 800
Held-for-trading	56 873	56 873	43 814	43 814
Derivative financial instruments	56 873	56 873	43 814	43 814
	5 548 192	5 548 645	4 572 672	4 580 995
Liabilities				
Held-for-trading	95 091	95 091	15 356	15 356
Derivative financial instruments	95 091	95 091	15 356	15 356
Other financial liabilities	4 488 799	4 488 799	3 808 079	3 808 079
Deposits	4 389 347	4 389 347	3 768 183	3 768 183
Taxation	494	494	116	116
Other accounts payable	98 958	98 958	39 780	39 780
	4 583 890	4 583 890	3 823 435	3 823 435

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Company 2008 Fair value R'000	Company 2008 Carrying amount R'000	Company 2007 Fair value R'000	Company 2007 Carrying amount R'000
1. Categories and fair values of financial instruments (continued)				
Assets				
Available-for-sale	1 286 637	1 286 637	844 188	844 188
Other investments	29	29	20	20
Interest in subsidiaries	1 286 608	1 286 608	844 168	844 168
Loans and receivables	228	228	216	216
Cash and cash equivalents	224	224	197	197
Other accounts receivable	4	4	19	19
	1 286 865	1 286 865	844 404	844 404
Liabilities				
Other financial liabilities	34	34	33	33
Other accounts payable	34	34	33	33
	34	34	33	33

Cash and cash equivalents have short terms to maturity. For this reason, the carrying amounts at the reporting date approximate the fair values.

Treasury and debentures have short terms to maturity and are carried at amortised cost. Fair value is based on quoted market values at balance sheet date.

The fair values of loans and advances that are carried at amortised cost approximate the fair values reported as they bear variable rates of interest. In addition, fair value is approximated through the credit impairment models.

Deposits generally have short terms to maturity, thus the values reported approximate the fair value.

The fair value of public traded derivatives, securities and investments is based on quoted market values at balance sheet date.

The fair value of other financial assets and financial liabilities, excluding derivatives, is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and adjusted by relevant market pricing.

The fair value of other investments and interest in subsidiaries which are unlisted, is determined by reference to the net asset value of the entity.

The fair value of loans and advances designated at fair value through profit and loss is calculated using the credit spread observed at origination. The fair values are adjusted for deterioration of credit quality through the application of the credit impairment models.

	Group/Company 2008 R'000	Group/Company 2007 R'000
Loans and receivables designated at fair value through profit and loss		
Cumulative changes in fair value attributable to credit risk	–	–
Changes in fair value attributable to changes in credit risk recognised during the period	–	–

At reporting date there are no significant concentrations of credit risk.

To confirm the amount of the fair value attributable to changes in credit risk, a review of those loans or receivables designated at fair value through profit and loss was conducted. The Group has no credit derivatives over loans and receivables designated at fair value through profit and loss.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	Group 2007 R'000
2. Intangible assets		
Computer software		
Cost at beginning of year	61 294	51 674
Additions	59 411	15 850
Net transfer from property and equipment	282	424
Write-off of obsolete software	–	(6 654)
Cost at end of year	120 987	61 294
Accumulated amortisation and impairment losses at beginning of year	(37 725)	(40 123)
Amortisation	(6 086)	(3 716)
Net transfer from property and equipment	(282)	(424)
Write-off of obsolete software	–	6 538
Accumulated amortisation and impairment losses at end of year	(44 093)	(37 725)
Net carrying amount at end of year	76 894	23 569

3. Property and equipment

	Owner-occupied properties R'000	Leasehold improve-ments R'000	Computer equipment R'000	Furniture and fittings R'000	Office equipment R'000	Motor vehicles R'000	Total R'000
Group							
2008							
Open market value/cost at beginning of year	80 064	18 325	70 593	8 567	23 666	415	201 630
Revaluations	9 300	–	–	–	–	–	9 300
Additions	–	699	24 917	439	4 497	–	30 552
Transfer*	–	–	(203)	348	(427)	–	(282)
Write-off of obsolete assets	–	–	(29)	(13)	(12)	–	(54)
Disposals	–	(107)	(1 289)	–	(403)	–	(1 799)
Open market value/cost at end of year	89 364	18 917	93 989	9 341	27 321	415	239 347
Accumulated depreciation and impairment losses at beginning of year	–	(13 908)	(64 896)	(7 791)	(17 750)	(316)	(104 661)
Depreciation	(1 389)	(819)	(5 216)	(330)	(1 722)	(28)	(9 504)
Revaluation	1 389	–	–	–	–	–	1 389
Transfer*	–	–	203	(314)	393	–	282
Write-off of obsolete assets	–	–	28	13	11	–	52
Disposals	–	107	1 268	–	392	–	1 767
Accumulated depreciation and impairment losses at end of year	–	(14 620)	(68 613)	(8 422)	(18 676)	(344)	(110 675)
Net carrying amount at end of year	89 364	4 297	25 376	919	8 645	71	128 672

* Transfer between various categories of property and equipment and intangible assets.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

3. Property and equipment

(continued)

	Owner-occupied properties R'000	Leasehold improvements R'000	Computer equipment R'000	Furniture and fittings R'000	Office equipment R'000	Motor vehicles R'000	Total R'000
Group							
2007							
Open market value/cost at beginning of year	73 164	18 129	68 568	8 436	22 464	339	191 100
Revaluations	6 900	–	–	–	–	–	6 900
Additions	–	213	2 918	14	893	112	4 150
Transfer*	–	(17)	(893)	117	369	–	(424)
Disposals	–	–	–	–	(60)	(36)	(96)
Open market value/cost at end of year	80 064	18 325	70 593	8 567	23 666	415	201 630
Accumulated depreciation and impairment losses at beginning of year	–	(12 825)	(60 209)	(7 191)	(15 632)	(287)	(96 144)
Depreciation	(1 272)	(1 092)	(5 621)	(485)	(1 769)	(65)	(10 304)
Revaluation	1 272	–	–	–	–	–	1 272
Transfer*	–	9	934	(115)	(404)	–	424
Disposals	–	–	–	–	55	36	91
Accumulated depreciation and impairment losses at end of year	–	(13 908)	(64 896)	(7 791)	(17 750)	(316)	(104 661)
Net carrying amount at end of year	80 064	4 417	5 697	776	5 916	99	96 969

* Transfer between various categories of property and equipment and intangible assets.

	Group 2008 R'000	Group 2007 R'000
Historical cost of properties that have been revalued	**36 910**	36 910

Notes:

1. G J van Zyl, a valuator with Van Zyl Valuers and a Member of The Institute of Valuers of South Africa, independently valued the properties at 31 December 2008.
2. A register containing details of owner-occupied properties and the revaluation thereof is available for inspection at the registered office of the Company.

4. Other accounts receivable

	Group 2008 R'000	Group 2007 R'000	Company 2008 R'000	Company 2007 R'000
Items in transit	**2 626**	3 913	–	—
Prepayments and deposits	**6 206**	4 948	**4**	19
Other receivables	**30 441**	14 778	–	–
	39 273	23 639	**4**	19

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Company 2008 R'000	Company 2007 R'000
5. Interest in subsidiaries		
Unlisted		
Shares at fair value	1 297 401	853 993
Mercantile Bank Limited	1 296 760	853 380
Mercantile Insurance Brokers (Pty) Limited	641	613
Loan – amount owing to Mercantile Bank Limited	(10 793)	(9 825)
	1 286 608	844 168

A list of principal subsidiary companies is contained in note 7 of the Directors' report. The loan is interest free and has no fixed terms of maturity.

	Group 2008 R'000	Group 2007 R'000
6. Interest in associated company		
Statman Investments (Pty) Limited *		
Shares at cost	675	675
Accumulated share of post-acquisition profits	7 852	7 117
Dividends received	(5 293)	(3 541)
	3 234	4 251
Reclassification of investment as a non-current asset held for sale (see note 9)	(3 234)	–
	–	4 251
Directors' valuation of the unlisted associated company	3 234	4 251

* The percentage shareholding of the Group in this company is 21.4%. The financial year-end is February.

Summarised financial information of the associated company is disclosed in note 30.4.

	Group 2008 R'000	Group 2007 R'000	Company 2008 R'000	Company 2007 R'000
7. Other investments				
Available-for-sale				
Unlisted equities	312	228	29	20
Listed equities	12 003	–	–	–
African Bank Investment Limited	648	–	–	–
Kap International Limited	11	–	–	–
Visa Inc.	11 344	–	–	–
Total	12 315	228	29	20
Directors' estimate of fair value	12 315	228	29	20

A register containing details of investments is available for inspection at the registered office of the Company.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	2007 R'000
8. Deferred taxation		
Reconciliation		
Balance at the beginning of the year	–	–
Current year charge		
– per the income statement	162 246	–
– per the statement of changes in equity	(20 230)	–
Balance at the end of the year	142 016	–
Comprising		
Deferred taxation assets	157 275	–
Deferred taxation liabilities	(15 259)	–
	142 016	–
Deferred taxation is attributable to the following temporary differences		
Assets		
Property and equipment	(9 621)	–
Intangibles	3	–
Short and long-term provisions	2 576	–
Calculated taxation losses	160 885	–
Other	3 432	–
	157 275	–
Liabilities		
Revaluations	20 230	–
Other	(4 971)	–
	15 259	–

Deferred taxation assets have been recognised for the carry forward amount of unused tax losses relating to the Group's operations where, *inter alia*, taxation losses can be carried forward and there is evidence that it is probable that sufficient taxable profits will be available in the future to utilise all tax losses carried forward.

	Group 2008 R'000	2007 R'000
9. Non-current assets held for sale		
Unlisted investment – Bond Exchange of South Africa Limited	2 055	–
Interest in associated company	3 234	–
	5 289	–

Unlisted investment

The Group intends to dispose of the investment in the Bond Exchange of South Africa Limited and anticipates that the disposal will be concluded by June 2009.

The investment has been valued at the offer price less costs to sell in terms of the scheme arrangement proposed by the purchaser.

No impairment loss was recognised on reclassification of the investment as a non-current asset held for sale at 31 December 2008.

Interest in associated company

The Group intends to dispose of Statman Investments (Pty) Limited and anticipates that the disposal will be concluded by June 2009.

The investment has been valued at the carrying amount as the offer price by the purchaser has not yet been concluded.

No impairment loss was recognised on reclassification of the interest in associated company as a non-current asset held for sale at 31 December 2008.

Summarised financial information of the associated company is disclosed in note 30.4.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	Group 2007 R'000
10. Loans and advances		
Category analysis		
Amortised cost	3 329 515	2 755 878
Current accounts	506 103	657 886
Credit card	22 420	21 555
Mortgage loans	1 568 744	1 200 419
Instalment sales and leases	352 406	277 562
Structured loans	285 225	131 191
Other advances	594 617	467 265
Fair value through profit and loss	154 106	154 528
Mortgage loans	53 960	40 980
Instalment sales and leases	21 338	27 026
Other advances	78 808	86 522
	3 483 621	2 910 406
Less: Impairments for credit losses	(58 849)	(57 187)
Less: Interest in suspense	(20 983)	(38 476)
	3 403 789	2 814 743

All loans and advances are denominated in South African Rand.

	Group 2008 R'000	Group 2007 R'000
Maturity analysis		
Repayable on demand	757 379	900 360
Maturing within six months	11 319	136 671
Maturing after six months but within 12 months	36 288	158 547
Maturing after 12 months	2 678 635	1 714 828
	3 483 621	2 910 406

The maturity analysis is based on the remaining period to contractual maturity at year-end.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

10. Loans and advances (continued)

	Gross amount R'000	Interest in suspense R'000	Total impairments R'000	Net balance R'000
Detailed category analysis of loans and advances				
Group				
2008				
Current accounts	**506 103**	**409**	**2 072**	**503 622**
Credit card	**22 420**	**2 254**	**5 246**	**14 920**
Mortgage loans	**1 622 704**	**3 694**	**4 143**	**1 614 867**
Instalment sales and leases	**373 744**	**654**	**2 310**	**370 780**
Structured loans	**285 225**	**–**	**30 430**	**254 795**
Other advances	**673 425**	**13 972**	**14 648**	**644 805**
	3 483 621	**20 983**	**58 849**	**3 403 789**
2007				
Current accounts	657 886	210	2 292	655 384
Credit card	21 555	1 568	4 803	15 184
Mortgage loans	1 241 399	1 768	2 366	1 237 265
Instalment sales and leases	304 588	256	615	303 717
Structured loans	131 191	19 918	27 395	83 878
Other advances	553 787	14 756	19 716	519 315
	2 910 406	38 476	57 187	2 814 743

	Total R'000	Current accounts R'000	Credit card R'000	Mortgage loans R'000	Instalment sales and leases R'000	Structured loans R'000	Other advances R'000
Impairments for credit losses							
Group							
2008							
Balance at the beginning of the year	**57 187**	**2 292**	**4 803**	**2 366**	**615**	**27 395**	**19 716**
Movements for the year:							
Credit losses written-off	**(5 858)**	**(1 288)**	**(666)**	**–**	**(640)**	**–**	**(3 264)**
Net impairments raised/(released)	**7 520**	**1 068**	**1 109**	**1 777**	**2 335**	**3 035**	**(1 804)**
	58 849	**2 072**	**5 246**	**4 143**	**2 310**	**30 430**	**14 648**
2007							
Balance at the beginning of the year	64 394	7 672	8 641	1 447	5 904	25 395	15 335
Movements for the year:							
Credit losses written-off	(14 414)	(240)	(3 483)	(683)	(5 646)	–	(4 362)
Net impairments raised/(released)	7 207	(5 140)	(355)	1 602	357	2 000	8 743
	57 187	2 292	4 803	2 366	615	27 395	19 716

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

10. Loans and advances (continued)

	Group 2008 R'000	Group 2007 R'000
Impairments for credit losses consist of:		
Portfolio impairments	19 768	32 663
Specific impairments	39 081	24 524
Balance at end of the year	58 849	57 187
Net charge for credit losses		
Net impairments raised	(7 520)	(7 207)
Recoveries in respect of amounts previously written off	902	1 849
	(6 618)	(5 358)

	Gross amount R'000	Interest in suspense R'000	Portfolio impairment R'000	Net balance R'000
Category analysis of performing loans and advances				
Group				
2008				
Current accounts	502 086	–	966	501 120
Credit card	15 988	–	1 068	14 920
Mortgage loans	1 591 909	–	415	1 591 494
Instalment sales and leases	367 848	–	671	367 177
Structured loans	232 213	–	15 430	216 783
Other advances	640 457	–	1 218	639 239
	3 350 501	–	19 768	3 330 733
2007				
Current accounts	656 479	–	1 867	654 612
Credit cards	15 317	–	826	14 491
Mortgage loans	1 220 604	–	554	1 220 050
Instalment sales and leases	301 319	–	332	300 987
Structured loans	131 191	19 918	27 395	83 878
Other advances	513 104	–	1 689	511 415
	2 838 014	19 918	32 663	2 785 433

	Group 2008 R'000	Group 2007 R'000
Category analysis of performing loans and advances excluding loans and advances with renegotiated terms		
Current accounts	502 086	656 479
Credit card	15 988	15 317
Mortgage loans	1 591 067	1 220 604
Instalment sales and leases	367 848	301 319
Structured loans	232 213	131 191
Other advances	637 500	512 349
	3 346 702	2 837 259

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

10. Loans and advances (continued)

	Group 2008 R'000	Group 2007 R'000
Category analysis of loans and advances with renegotiated terms that would otherwise be past due or impaired		
Current accounts	–	–
Credit card	–	–
Mortgage loans	842	–
Instalment sales and leases	–	–
Structured loans	–	–
Other advances	2 957	755
	3 799	755

	Past due for: 0 – 30 days R'000	31 – 60 days R'000	61 –90 days R'000	Total gross amount R'000	Fair value of collateral and other credit enhancements R'000
Category age analysis of loans that are past due but not individually impaired					
Group					
2008					
Current accounts	703	–	–	703	–
Credit card	336	254	342	932	–
Mortgage loans	17 740	7 198	–	24 938	20 142
Instalment sales and leases	731	559	–	1 290	971
Structured loans	–	–	–	–	–
Other advances	268	1 133	–	1 401	1 199
	19 778	9 144	342	29 264	22 312
2007					
Current accounts	–	–	–	–	–
Credit cards	119	201	215	535	–
Mortgage loans	2 413	6 689	–	9 102	7 203
Instalment sales and leases	191	283	–	474	474
Structured loans	–	–	–	–	–
Other advances	1 284	245	–	1 529	1 279
	4 007	7 418	215	11 640	8 956

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

10. Loans and advances (continued)

	Gross amount R'000	Interest in suspense R'000	Specific impairment R'000	Net balance R'000	Fair value of collateral and other credit enhancements R'000
Category analysis of loans and advances that are individually impaired					
Group					
2008					
Current accounts	**4 017**	**409**	**1 106**	**2 502**	**2 173**
Credit card	**6 432**	**2 254**	**4 178**	**–**	**–**
Mortgage loans	**30 795**	**3 694**	**3 728**	**23 373**	**26 127**
Instalment sales and leases	**5 896**	**654**	**1 639**	**3 603**	**3 706**
Structured loans	**53 012**	**–**	**15 000**	**38 012**	**28 462**
Other advances	**32 968**	**13 972**	**13 430**	**5 566**	**6 510**
	133 120	**20 983**	**39 081**	**73 056**	**66 978**
2007					
Current accounts	1 407	210	425	772	219
Credit cards	6 238	1 568	3 977	693	–
Mortgage loans	20 795	1 768	1 812	17 215	18 338
Instalment sales and leases	3 269	256	283	2 730	2 705
Structured loans	–	–	–	–	–
Other advances	40 683	14 756	18 027	7 900	9 016
	72 392	18 558	24 524	29 310	30 278

Collateral held as security and other credit enhancements

Fair value of collateral and other credit enhancements is determined with reference to the realisable value of security under forced-sale conditions.

All customers of the Bank are accorded a client risk grading. The risk grading of a client reflects, in broad terms, the client's creditworthiness and standing with the Bank. Specific criteria are applicable to the different risk grades. The risk grading of clients calls for judgement and continuing critical appraisal of the client's financial standing and forms an integral part of the Bank's assessment of the risk concerned. Changes in the risk grades are automated based on arrears on an instalment debt account.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

10. Loans and advances (continued)

Description of collateral held as security and other credit enhancements	Method of valuation
Cession of debtors	15% – 60% of debtors repayable under 90 days and depending on debtor credit quality
Pledge of shares	variable depending on liquidity and credit quality of the shares pledged
Limited pledge and cession	variable depending on asset type and value
Cession of life and endowment policies	100% of surrender value
Pledge of call and savings accounts, fixed and notice deposits	90% – 100%
Vacant land	50% of professional valuation
Residential properties	75% of professional valuation
Commercial and industrial properties	70% of professional valuation
Catering, industrial and office equipment	variable depending on asset type and depreciated value
Trucks	variable depending on asset type and depreciated value
Earth moving equipment	variable depending on asset type and depreciated value
Motor vehicles	variable depending on asset type and depreciated value
General notarial bond	variable depending on asset type and depreciated value
Special notarial bond	variable depending on asset type and depreciated value

All collateral held by the Bank in respect of an advance will be realised in accordance with the terms of the agreement or facility conditions applicable thereto. Cash collateral and pledged assets that can be allocated in accordance with the terms of the pledge and cession or suretyship are applied in reduction of related exposures. Pledged assets, other than cash or cash equivalent collateral, and tangible security articles are appropriated and disposed of, where necessary, after legal action, in compliance with the applicable Court rules and directives.

A customer in default will be advised of the default and afforded an opportunity to regularise the arrears. Failing normalisation of the account legal action and repossession procedures will be followed and all attached assets disposed of in accordance with the applicable legislation. In the case of insolvent and deceased estates, the duly appointed liquidator/trustee disposes of all assets.

11. Derivative financial instruments

	Notional principal of assets R'000	Fair value of assets R'000	Notional principal of liabilities R'000	Fair value of liabilities R'000
Group				
2008				
Held-for-trading				
Foreign exchange contracts	**1 015 487**	**56 689**	**1 067 003**	**86 094**
Interest rate swaps	**16 816**	**184**	**130 639**	**8 997**
	1 032 303	**56 873**	**1 197 642**	**95 091**
2007				
Held-for-trading				
Foreign exchange contracts	924 445	39 566	486 032	7 481
Interest rate swaps	31 500	4 248	152 658	7 875
	955 945	43 814	638 690	15 356

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	Group 2007 R'000
12. Negotiable securities		
Loans and receivables		
Treasury bills	**226 603**	204 010
Debentures	**–**	34 193
Available-for-sale		
Government stock	**20 538**	6 574
Held at fair value through profit and loss		
Corporate bonds	**–**	30 800
	247 141	275 577
Maturity analysis		
Repayable within one month	**24 823**	102 752
Maturing within six months	**178 258**	145 769
Maturing after six months but within 12 months	**23 522**	20 482
Maturing after 12 months but within five years	**–**	–
Maturing after five years	**20 538**	6 574
	247 141	275 577

The maturity analysis is based on the remaining period to contractual maturity at year-end.

	Group 2008 R'000	Group 2007 R'000
13. Bank term deposits		
Foreign bank balances	**324 295**	170 618
	324 295	170 618
Maturity analysis		
Maturing within three to six months	**211 379**	170 618
Maturing after six months but within 12 months	**112 916**	–
	324 295	170 618

	Group 2008 R'000	Group 2007 R'000	Company 2008 R'000	Company 2007 R'000
14. Cash and cash equivalents				
Cash and bank notes	**26 764**	35 910	**–**	–
Central Bank balances	**79 388**	60 889	**–**	–
Domestic bank balances	**257 251**	315 080	**224**	197
Foreign bank balances	**1 101 556**	840 497	**–**	–
	1 464 959	1 252 376	**224**	197

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

15. Share capital and share premium

15.1 Issued – Group

	Number of issued ordinary shares	Share capital R'000	Share premium R'000	Total R'000
Total shares in issue	3 925 208 024	36 292	1 170 754	1 207 046
Reduction of treasury shares held within the Group	1 330 000	376	–	376
At 31 December 2007	**3 926 538 024**	**36 668**	**1 170 754**	**1 207 422**
Increase of treasury shares held within the Group	(15 423 900)	(4 851)	–	(4 851)
At 31 December 2008	**3 911 114 124**	**31 817**	**1 170 754**	**1 202 571**

15.2 Issued – Company

	Number of issued ordinary shares	Share capital R'000	Share premium R'000	Total R'000
At 31 December 2007 and 31 December 2008	**3 938 918 524**	**39 389**	**1 170 754**	**1 210 143**

15.3 Authorised

The total authorised number of ordinary shares is 4 465 955 440 shares (2007: 4 465 955 440 shares) with a par value of 1 cent each. The total authorised number of preference shares is 15 150 486 shares (2007: 15 150 486 shares) with a par value of 25 cent each.

15.4 Unissued

The unissued ordinary and preference shares are under the control of the directors until the next AGM.

15.5 Share incentive schemes

The number of shares which could be utilised for the purposes of the share incentive schemes is 393 891 852 (2007: 393 891 852), which is 10% (2007: 10%) of the issued share capital of the Company at year-end. At 31 December 2008, 73 410 400 share options and Conditional Share Plan awards were outstanding under these schemes. The balance available to be utilised under these schemes is 320 481 452. The number of scheme shares that may be issued to a single participant is 59 083 778 or 1.5% of the total number of issued shares.

The Group recognised total expenses of R8.3 million (2007: R4.0 million) related to equity-settled share-based payment transactions.

Share option scheme

Effective 18 July 2007, options can be exercised in respect of 33% of the option shares after the expiration of three years from the offer date, in respect of a further 33% after the expiration of four years from the offer date and the remaining option shares after the expiration of five years from the offer date. Options granted prior to this date, may be exercised in respect of 33% of the option shares after the expiration of two years from the offer date, in respect of a further 33% after the expiration of three years from the offer date and the remaining option shares after the expiration of four years from the offer date. Such percentages are to be carried forward on a cumulative basis. Prior to 2008, should the options not be exercised by the fifth anniversary date of the offer, the option holder was obliged to exercise the option in respect of at least 20% of the options in question by the sixth anniversary date of the offer or else the said 20% of the options would lapse. The same rule applied for the seventh, eighth, ninth and tenth anniversary of the offer date until the options in question either lapsed or were exercised.

The scheme was modified in 2008 whereby the expiry condition from the sixth anniversary date was removed and all unexpired options now lapse after ten years from the date of issue. This modification had no material impact on the expense recognised in terms of share-based payments.

Refer to the shareholder's spread on page 84 for information relating to the shares held by the Bank. The Mercantile Share Incentive Trust acts as agent on behalf of the Bank in respect of this scheme.

Notes to the annual financial statements
for the year ended 31 December 2008 (continued)

15. Share capital and share premium (continued)

15.5 Share incentive schemes (continued)

Conditional Share Plan ("CSP")

On 27 May 2008 the shareholders approved the CSP incentive scheme which is in line with global best practice and emerging South African practice. The purpose of the scheme is to recognise contributions made by selected employees and to provide for an incentive for their continuing relationship with the Group, by providing them with the opportunity of receiving shares in the company, thereby providing participants with an incentive to advance the Group's interest and to ensure that the Group attracts and retains the core competencies required for formulating and implementing the Group's business strategies.

The tables below set out the movement in the options and conditional awards:

Share option scheme

	Exercise price (cents)	Options at beginning of year	Granted during year	Forfeited during year	Exercised during year	Options at end of year	Exercisable options at end of year	Relating to directors[1]
Grant date								
2008								
20 November 2001	32	954 400	–	(160 000)	–	794 400	794 400	–
11 February 2002	32	200 000	–	(40 000)	–	160 000	160 000	–
5 October 2004	18	5 000 000	–	–	–	5 000 000	5 000 000	5 000 000
7 October 2004	17	1 000 000	–	(85 000)	(165 000)	750 000	750 000	–
3 January 2005	15	700 000	–	(170 000)	(530 000)	–	–	–
11 February 2005	20	500 000	–	–	–	500 000	330 000	–
1 April 2005	39	–	–	–	–	–	–	–
27 July 2005	32	750 000	–	–	–	750 000	495 000	–
2 December 2005	31	350 000	–	(350 000)	–	–	–	–
9 February 2006	41	750 000	–	–	–	750 000	247 500	–
3 March 2006	38	500 000	–	–	–	500 000	165 000	–
22 March 2006	40	12 500 000	–	(1 900 000)	–	10 600 000	3 498 000	7 000 000
26 February 2007	34	21 250 000	–	(3 150 000)	–	18 100 000	–	8 000 000
1 June 2007	36	500 000	–	–	–	500 000	–	–
1 December 2007	36	1 000 000	–	–	–	1 000 000	–	–
		45 954 400	–	(5 855 000)	(695 000)	39 404 400	11 439 900	20 000 000

(1) Refer to note 30.3

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

15. Share capital and share premium (continued)

15.5 Share incentive schemes (continued)

	Exercise price (cents)	Options at beginning of year	Granted during year	Forfeited during year	Exercised during year	Options at end of year	Exercisable options at end of year	Relating to directors[1]
2007								
20 November 2001	32	3 943 000	–	(1 988 600)	(1 000 000)	954 400	954 400	–
11 February 2002	32	200 000	–	–	–	200 000	200 000	–
5 October 2004	18	5 000 000	–	–	–	5 000 000	3 300 000	5 000 000
7 October 2004	17	2 000 000	–	–	(1 000 000)	1 000 000	660 000	–
3 January 2005	15	700 000	–	–	–	700 000	231 000	–
11 February 2005	20	500 000	–	–	–	500 000	165 000	–
1 April 2005	39	1 000 000	–	(1 000 000)	–	–	–	–
27 July 2005	32	750 000	–	–	–	750 000	247 500	–
2 December 2005	31	350 000	–	–	–	350 000	115 500	–
9 February 2006	41	750 000	–	–	–	750 000	–	–
3 March 2006	38	500 000	–	–	–	500 000	–	–
22 March 2006	40	14 800 000	–	(2 300 000)	–	12 500 000	–	7 000 000
26 February 2007	34	–	24 000 000	(2 750 000)	–	21 250 000	–	8 000 000
1 June 2007	36	–	500 000	–	–	500 000	–	–
1 December 2007	36	–	1 000 000	–	–	1 000 000	–	–
		30 493 000	**25 500 000**	**(8 038 600)**	**(2 000 000)**	**45 954 400**	**5 873 400**	**20 000 000**

[1] Refer to note 30.3

The Group has not granted any share options in 2008 in terms of the share option scheme. Inputs into the Black-Scholes model in determining the charge for share-based payments for options granted during 2007 are as follows:

	2007
Weighted average fair value share price at grant date	34 cents
Weighted average exercise price	34 cents
Expected volatility	82.10%
Option life	10 years
Risk free rate	7.58%
Expected dividends	Nil

Expected volatility was determined by calculating the historical volatility of the Mercantile Bank Holdings Limited share price from September 2004 to the grant date of each option. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

15. Share capital and share premium (continued)

15.5 Share incentive schemes (continued)

Conditional Share Plan

	Market price at date of grant (cents)	Conditional awards at beginning of year	Granted during year	Forfeited during year	Vested during year	Conditional awards at end of year	Relating to directors[1]
Grant date							
2008							
22 February 2008	32	–	28 445 000	(2 314 000)	–	26 131 000	7 600 000
26 March 2008	31	–	4 000 000	–	–	4 000 000	–
7 May 2008	30	–	1 400 000	(1 400 000)	–	–	–
24 July 2008	26	–	375 000	–	–	375 000	–
1 October 2008	32	–	500 000	–	–	500 000	–
1 November 2008	28	–	2 200 000	–	–	2 200 000	–
1 December 2008	29	–	800 000	–	–	800 000	–
		–	37 720 000	(3 714 000)	–	34 006 000	7 600 000

[1] Refer to note 30.3

	Group 2008 R'000	Group 2007 R'000
16. Deposits		
Call deposits and current accounts	1 707 699	1 386 951
Savings accounts	166 422	174 714
Term and notice deposits	2 326 438	2 066 671
Negotiable certificates of deposit	32 361	39 695
Foreign deposits	156 427	100 152
	4 389 347	3 768 183
Maturity analysis		
Repayable on demand and within one month	2 815 837	2 069 725
Maturing after one month but within six months	1 060 031	1 267 181
Maturing after six months but within 12 months	505 318	284 187
Maturing after 12 months	8 161	147 090
	4 389 347	3 768 183

The maturity analysis is based on the remaining period to contractual maturity at year-end.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

17. Provisions

	Staff incentives R'000	Audit fees R'000	Post-retirement medical benefits R'000	Leave pay R'000	Other risks R'000	Total R'000
Group						
At 31 December 2006	10 382	2 100	12 853	8 329	5 330	38 994
Additional provision raised	14 976	4 880	1 490	3 073	2 100	26 519
Charged to provision	(12 356)	(3 790)	–	(2 738)	(4 194)	(23 078)
At 31 December 2007	**13 002**	**3 190**	**14 343**	**8 664**	**3 236**	**42 435**
Additional provision raised	**20 788**	**5 810**	**188**	**3 383**	**308**	**30 477**
Charged to provision	**(13 181)**	**(5 370)**	**–**	**(2 931)**	**(2 834)**	**(24 316)**
At 31 December 2008	**20 609**	**3 630**	**14 531**	**9 116**	**710**	**48 596**

Post-retirement medical benefits

Refer to note 18 for detailed disclosure of this provision.

Leave pay

In terms of Group policy, employees are entitled to accumulate leave not taken during the year, within certain limits.

Other risks

Consists of provisions for legal claims and other risks. At any time, there are legal or potential claims made against the Group, the outcome of which cannot at present be foreseen. These claims are not regarded as material either on an individual basis or in aggregate. Provisions are raised for all liabilities that are expected to materialise.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

18. Post-retirement medical benefits

The Bank operates a partly funded post-retirement medical scheme. The assets of the funded plans are held independently of the Group's assets in a separate trustee-administered fund. Independent actuaries value this scheme at least every three years. The last actuarial valuations were carried out at 31 December 2008. The actuary's opinion is that the plan is in a sound financial position.

	Group			
	2008	2007	2006	2005
	R'000	R'000	R'000	R'000
The amounts recognised in the balance sheet are as follows (refer to note 17):				
Present value of total service liabilities	**19 664**	20 223	18 989	16 651
Fair value of plan assets	**(5 133)**	(5 880)	(6 136)	(6 237)
– Provident fund	**(922)**	(838)	(1 457)	(1 624)
– Endowment bond	**(3 118)**	(3 446)	(3 729)	(4 104)
– Annuities	**(1 093)**	(1 596)	(950)	(509)
Liability in the balance sheet	**14 531**	14 343	12 853	10 414
The amounts recognised in the income statement are as follows (refer to note 26):				
Current service cost	**89**	116	115	414
Interest costs	**1 568**	1 539	1 365	1 659
Expected return on plan assets	**(529)**	(549)	(396)	(575)
Actuarial loss	**368**	936	1 957	1 736
Employer benefit payments	**(1 308)**	(1 202)	(1 168)	(1 085)
Payments from plan assets	**–**	650	846	540
Effect on curtailment	**–**	–	(280)	(455)
Total included in staff costs	**188**	1 490	2 439	2 234
Reconciliation of the movement in the present value of total service liabilities:				
At the beginning of year	**20 223**	18 989	16 651	22 277
Current service cost	**89**	116	115	414
Interest costs	**1 568**	1 539	1 365	1 659
Actuarial loss	**(908)**	781	2 306	1 610
Employer benefit payments	**(1 308)**	(1 202)	(1 168)	(1 085)
Net effect of settlements	**–**	–	–	(7 769)
Effect of curtailment	**–**	–	(280)	(455)
At the end of the year	**19 664**	20 223	18 989	16 651
Reconciliation of the movement in the fair value of plan assets:				
At the beginning of year	**5 880**	6 136	6 237	6 328
Expected return on plan assets	**529**	549	396	575
Actuarial (loss)/gain	**(1 276)**	(155)	349	(126)
Payments from plan assets	**–**	(650)	(846)	(540)
At the end of the year	**5 133**	5 880	6 136	6 237

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

18. Post-retirement medical benefits (continued)

The principal actuarial assumptions used were as follows:

Discount rate	9.25% (2007: 8.00%) compounded annually
Investment return	10.25% (2007: 9.00%) compounded annually
Rate of medical inflation	8.50% (2007: 7.25%) compounded annually
Salary inflation	8.00% (2007: 6.75%) compounded annually

The effect of a 1% increase/decrease on the assumed rate of medical inflation would be an increase in the liability in an amount of R1.8 million and a decrease of R1.5 million, respectively.

	Group		Company	
	2008	2007	**2008**	2007
	R'000	R'000	**R'000**	R'000
19. Other accounts payable				
Accruals	**22 830**	13 438	**11**	9
Product-related credits	**21 068**	12 090	**14**	16
Sundry creditors	**55 060**	14 252	**9**	8
	98 958	39 780	**34**	33

	Group	
	2008	2007
	R'000	R'000
20. Taxation		
South African Revenue Services		
Taxation owing by the Group	**494**	116

21. Contingent liabilities and commitments

21.1 Guarantees, letters of credit and committed undrawn facilities

	Group 2008 R'000	Group 2007 R'000
Guarantees	**331 494**	391 335
Lending related	**16 022**	16 760
Mortgage	**74 051**	105 724
Performance	**241 421**	268 851
Letters of credit	**6 886**	19 937
Committed undrawn facilities	**331 720**	223 589
	670 100	634 861

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	Group 2007 R'000
21. Contingent liabilities and commitments (continued)		
21.2 Commitments under operating leases		
The total minimum future lease payments under operating leases are as follows:		
Property rentals:		
Due within one year	4 478	3 304
Due between one and five years	7 824	4 289
	12 302	7 593
After tax effect on operating leases	8 857	5 467

A register containing details of the existence and terms of renewal and escalation clauses is available for inspection at the registered office of the Company.

	Group 2008 R'000	Group 2007 R'000
21.3 Capital commitments		
Contracted for	79 383	–
Authorised but not yet contracted for	13 635	–
	93 018	–
22. Interest income		
Interest on:		
Loans and receivables	631 982	435 241
Cash and cash equivalents and bank term deposits	154 375	142 501
Negotiable securities	23 166	18 776
Structured loans	56 185	356
Loans and advances	398 256	273 608
Loans and receivables at fair value through profit and loss	26 680	30 549
Mortgage loans	5 384	4 187
Instalment sales and leases	3 695	3 246
Other advances	16 159	13 410
Corporate bonds	1 442	9 706
Held-for-trading		
Interest rate swaps	3 114	1 457
	661 776	467 247
23. Interest expenditure		
Interest on:		
Deposits	335 839	244 013
Repurchase agreements	–	2 095
Held-for-trading		
Interest rate swaps	1 974	3 904
	337 813	250 012

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group	
	2008 R'000	2007 R'000
24. Non-interest income		
Fee and commission income	177 554	138 716
Loans and receivables at fair value through profit and loss	273	161
Loans and receivables	175 464	136 558
Other	1 817	1 997
Trading income	81 441	51 861
Held-for-trading	75 960	57 609
Foreign currency	71 138	42 516
Foreign currency commissions	10 007	8 540
Derivative assets	(4 063)	(583)
Derivative liabilities	(1 122)	7 136
Loans and receivables at fair value through profit and loss	5 481	(6 653)
Loans and advances	5 030	(5 824)
Corporate bonds	451	(829)
Loans and receivables		
Profit on settlement	–	905
Investment income	1 008	294
Dividends	861	21
Rental income	147	273
	260 003	190 871
25. Fee and commission expenditure		
Foreign currency commissions	24 214	17 490
Commissions and transaction expenses	52 754	11 351
	76 968	28 841

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group		Company	
	2008	2007	2008	2007
	R'000	R'000	R'000	R'000
26. Operating expenditure				
Auditors' remuneration				
Audit fees – current year	6 030	5 825	–	–
– prior year	(240)	273	–	–
Fees for other services – Taxation advisory fees	102	427	–	–
– Review of Regulatory returns	575	80		
– Other	20	–	–	–
	6 487	6 605	–	–
Professional fees				
Collections	88	297	–	–
Consulting	2 203	2 058	14	54
Legal	1 049	853	–	–
Computer consulting and services	27 015	21 407	–	–
	30 355	24 615	14	54
Depreciation and amortisation (refer to notes 2 and 3)	15 590	14 020	–	–
Directors' emoluments (refer to note 30.3)				
Executive directors	8 738	7 737	–	–
Non-executive directors' fees	3 134	3 071	–	–
	11 872	10 808	–	–
Lease charges				
Motor vehicles	–	9	–	–
Equipment	14	104	–	–
	14	113	–	–
Staff costs				
Salaries, wages and allowances	109 163	88 803	–	–
Post-retirement medical benefits (refer to note 18)	188	1 490	–	–
Contributions to retirement funds	7 073	6 473	–	–
Share-based payments including directors	8 253	4 041	–	–
Other	8 985	5 750	–	–
	133 662	106 557	–	–
(Profit)/Loss on sale of property and equipment	(29)	13	–	–
Operating leases – premises	7 082	6 637	–	–
Marketing and communication	7 661	7 886	578	440
Indirect taxation				
Non-claimable Value-Added Tax	8 067	5 052	–	–
Skills development levy	565	931	–	–
	8 632	5 983	–	–
Other operating costs	31 828	33 741	436	352
Total operating expenditure	253 154	216 978	1 028	846
Number of persons employed by the Group at year-end	445	422		

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	Group 2007 R'000	Company 2008 R'000	Company 2007 R'000
27. Taxation				
S.A. normal taxation	**(71)**	(29)	**–**	(29)
– Current year	**(6)**	–	**–**	–
– Prior year	**(65)**	(29)	**–**	(29)
Deferred tax	**162 246**	–	**–**	–
– Current year	**(72 055)**	–	**–**	–
– Prior year	**234 301**	–	**–**	–
	162 175	(29)	**–**	(29)
Direct taxation				
South African normal taxation	**71**	29	**–**	29
South African tax rate reconciliation				
South African standard tax rate (%)	**28.00**	29.00	**28.00**	29.00
Exempt income (%)	**(0.17)**	(0.40)	**0.00**	0.00
Expenses not deductible for tax purposes (%)	**0.55**	0.70	**0.00**	0.00
Capital gain – 50% portion not taxed for 2008	**(0.53)**	0.00	**0.00**	0.00
Underprovision prior year (%)	**0.01**	0.00	**0.00**	3.40
Other timing differences recognised for the first time (%)	**(6.05)**	0.00	**0.00**	0.00
Deferred taxation not raised (%)	**0.00**	4.20	**0.00**	0.00
Tax losses recognised for the first time (%)	**(84.70)**	0.00	**0.00**	0.00
Tax losses (utilised) (%)	**0.00**	(33.50)	**(28.00)**	(29.00)
Effective tax rate (%)	**(62.89)**	0.00	**0.00**	3.40
Estimated tax losses available for set-off against future taxable income	**581 743**	748 480	**7 156**	5 558

	Group 2008 R'000	Group 2007 R'000
28. Earnings, diluted earnings, headline earnings and diluted headline earnings per ordinary share		
28.1 Earnings per ordinary share		
Profit after taxation	**419 973**	165 273
Profit before taxation	**257 798**	165 302
Weighted number of ordinary shares in issue ('000)	**3 924 414**	3 925 485
Earnings per ordinary share after taxation (cents)	**10.70**	4.21
Earnings per ordinary share before taxation (cents)	**6.57**	4.21
28.2 Diluted earnings per ordinary share		
Profit after taxation	**419 973**	165 273
Profit before taxation	**257 798**	165 302
Weighted diluted number of ordinary shares in issue ('000)	**3 924 414**	3 925 485
Earnings per ordinary share after taxation (cents)	**10.70**	4.21
Earnings per ordinary share before taxation (cents)	**6.57**	4.21

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

	Group 2008 R'000	Group 2007 R'000
28. Earnings, diluted earnings, headline earnings and diluted headline earnings per ordinary share (continued)		
28.3 Headline and diluted headline earnings per ordinary share		
Profit before taxation	**257 798**	165 302
Adjustment for:		
Realisation of available-for-sale reserve on disposal of investments	**(9 837)**	(5 602)
(Profit)/Loss on disposal of property and equipment	**(29)**	13
Headline earnings before taxation	**247 932**	159 713
Taxation	**162 175**	(29)
Headline earnings after taxation	**410 107**	159 684
Headline earnings per ordinary share after taxation (cents)	**10.45**	4.07
Headline earnings per ordinary share before taxation (cents)	**6.32**	4.07
Diluted headline earnings per ordinary share after taxation (cents)	**10.45**	4.07
Diluted headline earnings per ordinary share before taxation (cents)	**6.32**	4.07

	Group 2008 R'000	Group 2007 R'000	Company 2008 R'000	Company 2007 R'000
29. Cash flow notes				
29.1 Cash receipts from customers				
Interest income	**661 776**	467 247	**–**	–
Non-interest income and gain on disposal and revaluation of available-for-sale sale investments	**269 840**	196 473	**–**	–
Adjusted for: Dividends received	**(861)**	(21)	**–**	–
Net (gain) on disposal and revaluation of available-for-sale investments	**(9 837)**	(5 602)	**–**	–
Revaluation of fair value financial instruments	**72 157**	(33 166)	**–**	–
Recoveries in respect of amounts previously written off	**902**	1 849	**–**	–
Total cash receipts from customers	**993 977**	626 780	**–**	–
29.2 Cash paid to suppliers and employees				
Interest expenditure	**(337 813)**	(250 012)	**–**	–
Operating expenditure and fee and commission expenditure	**(330 122)**	(245 819)	**(1 028)**	(846)
Adjusted for: Depreciation and amortisation	**15 590**	14 020	**–**	–
(Profit)/Loss on sale of property and equipment	**(29)**	13	**–**	–
Share-based payments	**8 250**	3 994	**–**	–
Increase in provisions	**6 161**	3 441	**–**	–
Total cash paid to suppliers and employees	**(637 963)**	(474 363)	**(1 028)**	(846)

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

29. Cash flow notes (continued)

	Group		Company	
	2008	2007	**2008**	2007
	R'000	R'000	**R'000**	R'000
29.3 Reconciliation of profit before taxation to cash generated from operations				
Profit/(Loss) before taxation	**257 798**	165 302	**(1 028)**	(846)
Profit before taxation adjusted for:				
Dividends received	**(861)**	(21)	**–**	–
Net (gain) on disposal and revaluation of available-for-sale investments	**(9 837)**	(5 602)	**–**	–
Revaluation of fair value financial instruments	**72 157**	(33 166)	**–**	–
Net impairments raised	**7 520**	7 207	**–**	–
Depreciation and amortisation	**15 590**	14 020	**–**	–
(Profit)/Loss on sale of property and equipment	**(29)**	13	**–**	–
Share-based payments	**8 250**	3 994	**–**	–
Increase in provisions	**6 161**	3 441	**–**	–
Reversal of income from associated company	**(735)**	(2 771)	**–**	–
Cash generated from operations	**356 014**	152 417	**(1 028)**	(846)
29.4 Taxation recovered				
Amounts (unpaid)/prepaid at beginning of year	**(116)**	(6)	**–**	29
Income statement charge	**(71)**	(29)	**–**	(29)
Less: Amounts unpaid at end of year	**494**	116	**–**	–
Total taxation recovered	**307**	81	**–**	–
29.5 Net increase in income earning assets				
Decrease in negotiable securities	**30 432**	128 610	**–**	–
(Increase) in loans and advances	**(602 498)**	(748 036)	**–**	–
(Increase)/Decrease in bank term deposits	**(153 677)**	242 637	**–**	–
Net (increase) in income earning assets	**(725 743)**	(376 789)	**–**	–
29.6 Net increase in deposits and other accounts				
Increase in deposits	**621 164**	229 036	**–**	–
(Increase)/Decrease of treasury shares held within the Group	**(4 851)**	376	**–**	–
Increase/(Decrease) in other accounts	**43 544**	(13 003)	**984**	905
Net increase in deposits and other accounts	**659 857**	216 409	**984**	905

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

30. Related-party information

30.1 Identity of related parties with whom transactions have occurred

The holding Company and material subsidiaries of the Group are identified on page 11 in the Directors' report and the associated Company is disclosed in notes 6 and 9 to the annual financial statements. All of these entities and the directors are related parties. There are no other related parties with whom transactions have taken place, other than as listed below.

30.2 Related-party balances and transactions

The Company, its subsidiaries and associated company, in the ordinary course of business, enter into various financial services transactions with the ultimate holding company and its subsidiaries, other entities within the Group and the associated company. These transactions are governed by terms no less favourable than those arranged with third parties.

	2008 R'000	2007 R'000
Balances between the ultimate holding company (CGD) and Mercantile Bank Limited:		
CGD – Lisbon (Branch of CGD)	**1 348 916**	897 628
Nostro accounts	**4 316**	1 763
Vostro accounts	**(2 142)**	(2 994)
Deposit accounts	**1 346 742**	898 859
CGD – Paris (Branch of CGD)	**(3 191)**	152
Nostro accounts	**84**	174
Vostro accounts	**(3 275)**	(22)
CGD – London (Branch of CGD)		
Vostro accounts	**(18)**	(18)
CGD	**1 345 707**	897 762
Banco Comercial e de Investimentos – Mozambique (BCI) (Subsidiary of CGD)	**(63 781)**	(37 928)
Vostro accounts	**(4 032)**	(142)
Fixed deposits	**(59 730)**	(37 327)
Call and notice deposits	**(19)**	(459)
	1 281 926	859 834

Interest was paid to BCI amounting to R3.4 million (2007: R7.9 million).

Interest received from CGD in respect of the above balances during the year amounted to R41.1 million (2007: R73.1 million).

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

30. Related-party information (continued)

30.2 Related-party balances and transactions (continued)

		2008 R'000	2007 R'000
Balances with the Company, its subsidiaries and associated company:			
Loan to:	**Loan from:**		
Mercantile Bank Holdings Limited	Mercantile Bank Limited	**10 793**	9 825
Portion 2 of Lot 8 Sandown (Pty) Limited	Mercantile Bank Limited	**44 832**	43 987
LSM (Troyeville) Properties (Pty) Limited	Mercantile Bank Limited	**6 265**	5 931
Mercantile Insurance Brokers (Pty) Limited	Mercantile Bank Limited	**467**	162
Mercantile Registrars Limited	Mercantile Bank Limited	**3 042**	3 042
Mercantile Bank Limited	Mercantile Nominees (Pty) Limited	**–**	31
Statman Investments (Pty) Limited	Mercantile Bank Limited	**468**	695
Deposit with:	**Deposit by:**		
Mercantile Bank Limited	Mercantile Insurance Brokers (Pty) Limited	**1 973**	1 621
Mercantile Bank Limited	Mercantile Nominees (Pty) Limited	**–**	799
Mercantile Bank Limited	Mercantile Bank Holdings Limited	**224**	197
Transactions with the Company, its subsidiaries and associated company:			
Interest received by:	**Interest paid by:**		
Mercantile Bank Limited	Portion 2 of Lot 8 Sandown (Pty) Limited	**6 527**	5 862
Mercantile Bank Limited	LSM (Troyeville) Properties (Pty) Limited	**918**	765
Mercantile Insurance Brokers (Pty) Limited	Mercantile Bank Limited	**100**	81
Mercantile Bank Limited	Statman Investments (Pty) Limited	**81**	40
Non-interest income earned by:	**Operating expenditure paid by:**		
Portion 2 of Lot 8 Sandown (Pty) Limited	Mercantile Bank Limited	**10 680**	9 251
LSM (Troyeville) Properties (Pty) Limited	Mercantile Bank Limited	**1 018**	1 011
Mercantile Bank Limited	Mercantile Insurance Brokers (Pty) Limited	**164**	68
Portion 2 of Lot 8 Sandown (Pty) Limited	Mercantile Insurance Brokers (Pty) Limited	**142**	112
Dividends earned by:	**Dividends paid by:**		
Mercantile Bank Limited	Statman Investments (Pty) Limited	**1 752**	2 146

Other

Post-retirement medical plan

Details of the post-retirement medical plan are disclosed in note 18.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

30. Related-party information (continued)

30.3 Director and director-related activities

No loans were made to directors during the year under review. There were no material transactions with directors, other than the following:

	Directors' fees R'000	Salary R'000	Fringe benefits R'000	Retirement funds and medical aid contributions R'000	Performance bonus R'000	Total R'000
Director						
2008						
J A S de Andrade Campos	**1 199**	**–**	**–**	**–**	**–**	**1 199**
D J Brown	**–**	**2 368**	**–**	**251**	**3 500**	**6 119**
G P de Kock	**519**	**–**	**–**	**–**	**–**	**519**
L Hyne	**480**	**–**	**–**	**–**	**–**	**480**
A T Ikalafeng	**420**	**–**	**–**	**–**	**–**	**420**
J P M Lopes	**–**	**1 541**	**479**	**49**	**550**	**2 619**
T H Njikizana						
(appointed 6 November 2008)	**50**	**–**	**–**	**–**	**–**	**50**
S Rapeti	**466**	**–**	**–**	**–**	**–**	**466**
	3 134	**3 909**	**479**	**300**	**4 050**	**11 872**
2007						
J A S de Andrade Campos	1 100	–	–	–	–	1 100
D J Brown	–	2 146	–	236	2 681	5 063
G P de Kock	498	–	–	–	–	498
M J M Figueira						
(resigned 28 February 2007)	–	259	59	–	–	318
L Hyne	452	–	–	–	–	452
A T Ikalafeng	347	–	–	–	–	347
J P M Lopes	–	1 429	383	44	500	2 356
A M Osman						
(resigned 21 November 2007)	226	–	–	–	–	226
S Rapeti	448	–	–	–	–	448
	3 071	3 834	442	280	3 181	10 808

	2008 R'000	2007 R'000
Share-based payments expense relating to Directors:		
D J Brown	**2 273**	1 458
Amounts paid by CGD to:		
M J M Figueira (resigned 28 February 2007)	**–**	124
J P M Lopes	**666**	560
	666	684

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

30. Related-party information (continued)

30.3 Director and director-related activities (continued)

Service agreements

D J Brown, Chief Executive Officer

Mr Brown's employment as Chief Executive Officer commenced on 31 March 2004. The Board at a Board meeting held on 31 October 2008 approved the renewal of Mr Brown's service contract for a further three years, upon expiry in March 2009. The re-appointment of Mr Brown as an executive director with effect from 29 March 2009 upon expiry in terms of the Articles of Association of the Company, will be confirmed at the AGM to be held on 28 May 2009.

In consideration for the rendering of his services under the Service Agreement, Mr Brown is also entitled to payment of an annual incentive bonus calculated in accordance with a performance plan as agreed with the Board from time to time.

J P M Lopes, Executive Director

Mr Lopes has been seconded to Mercantile by CGD.

Mr Lopes's employment in Mercantile commenced on 9 November 2005, and his contract was renewed by the Board upon expiry on 9 November 2008 for three years. In terms of the Service Agreement Mr Lopes agreed to perform such duties, functions and services as are assigned to him from time to time by the Board of Directors and which are consistent and commensurate with his position as Executive Director.

Mr Lopes will in accordance with the Company's Articles of Association stand for re-election at the AGM on 28 May 2009.

Share options and conditional share awards

In terms of the share option scheme the following share options in the Company have been granted to Mr Brown (refer to note 15.5):

- on 5 October 2004, 5 000 000 at an exercise price of 18 cents each;
- on 22 March 2006, 7 000 000 at an exercise price of 40 cents each; and
- on 26 February 2007, 8 000 000 at an exercise price of 34 cents each.

In terms of the Conditional Share Plan, 7 600 000 conditional share awards were granted to Mr Brown on 27 May 2008 with a market value on the date of grant of 32 cents each (refer to note 15.5).

Directors' interests

No directors held beneficial and/or non-beneficial interests, directly or indirectly, in shares issued by the Company (2007: nil).

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

30. Related-party information (continued)

30.4 Summarised financial information of the associated company

	Statman Investments (Pty) Limited 2008 R'000	Statman Investments (Pty) Limited 2007 R'000
Income statement		
Profit after taxation	**5 201**	7 242
Balance sheet		
Non-current assets	**12 919**	12 623
Current assets	**15 654**	19 573
Current liabilities	**(8 493)**	(7 271)
Non-current liabilities	**(557)**	(701)
Equity	**15 110**	19 864
Minority interest	**4 413**	4 360
Percentage held	**21.4**	21.4
Nature of business	Investment holding	
Place of incorporation	South Africa	

The Group's share of profit and losses is determined by reference to the management accounts of the associated company at 30 November 2008, which is the date at which the most recent management accounts are available.

31. Segment information

The primary business segments of the Group are as follows:

Business segment	Scope of products and services
Retail banking and Commercial banking*	Banking, investment and other financial services offered to banking customers.
Treasury*	Managing internal liquidity, foreign exchange services as well as serving retail and alliance banking customers.
Alliance banking and MBL credit card*	Card processing services and electronic banking offered to banking customers.
Support and other services	Support services for the above segments, insurance brokers, surplus capital, associate income, inter-group eliminations and taxation.

* Excludes the allocation of attributable support costs.

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

31. Segment information (continued)

The primary segments are as follows:

	Retail and Commercial banking 2008 R'000	Retail and Commercial banking 2007 R'000	Treasury 2008 R'000	Treasury 2007 R'000	Alliance banking, MBL credit card, and electronic banking 2008 R'000	Alliance banking, MBL credit card, and electronic banking 2007 R'000	Support and other services 2008 R'000	Support and other services 2007 R'000	Total 2008 R'000	Total 2007 R'000
Segment results										
Segment revenue[1]	347 155	241 602	59 612	40 046	53 799	53 316	56 269	49 903	516 835	384 867
Segment expenditure	(69 766)	(55 256)	(17 974)	(16 360)	(24 483)	(25 461)	(140 931)	(119 901)	(253 154)	(216 978)
Contribution/(Loss) before allocated costs	268 249	183 740	41 638	23 686	30 801	19 231	79 285	(61 384)	419 973	165 273
Other information										
Net capital expenditure	82 432	980	100	325	458	13 744	5 120	(1 799)	88 110	13 250
Depreciation and amortisation	(4 804)	(2 467)	(201)	(247)	(5 626)	(5 582)	(4 959)	(5 724)	(15 590)	(14 020)
Other non-cash operating expenditure	–	–	–	–	–	–	14 382	7 448	14 382	7 448
Share of income from associated companies	–	–	–	–	–	–	735	2 771	735	2 771
Segment position										
Segment assets	3 514 732	2 826 280	2 068 762	1 703 613	32 658	52 434	300 623	123 457	5 916 775	4 705 784
Segment liabilities	3 733 064	3 311 084	680 888	325 143	160 396	178 739	73 398	50 904	4 647 745	3 865 870
Carrying amounts of segment assets include:										
Investments in associated company	–	–	–	–	–	–	3 234	4 251	3 234	4 251

The secondary segments are as follows:

	Gauteng 2008 R'000	Gauteng 2007 R'000	Other provinces 2008 R'000	Other provinces 2007 R'000	Total 2008 R'000	Total 2007 R'000
Segment revenue[1]	413 801	350 390	103 034	34 477	516 835	384 867
Net capital expenditure	87 630	13 141	480	109	88 110	13 250
Segment assets	5 255 010	4 244 890	661 765	460 894	5 916 775	4 705 784

[1] Segment revenue consists of net interest income, net profit/(loss) on disposal and revaluation of assets and non-interest income net of fee and commission expenditure

Notes to the annual financial statements

for the year ended 31 December 2008 (continued)

32. Presentation adjustments and explanatory notes

Balance sheet and cash flow statement

- Structured loans previously included under other categories of loans and advances are reported separately in 2008. Comparatives for the year ended 31 December 2007 have been reclassified accordingly for all affected disclosures.
- Bank term deposits with a residual maturity greater than three months from the reporting date previously presented with cash and cash equivalents are now presented separately in the balance sheet and the cash flow statement. Comparatives for the year ended 31 December 2007 have been reclassified accordingly for all affected disclosures.
- With the adoption of IFRIC 11 – IFRS 2 Group and Treasury transactions, a share-based payment reserve in respect of the Mercantile Share Option scheme is not required. This reserve has therefore been transferred to accumulated loss and share-based payments expense for this scheme are processed to accumulated loss with effect from 1 January 2008.

  In the case of the Mercantile Conditional Share Plan introduced in 2008, a share-based payments reserve has been created to separate the effects of this plan from other classes of reserves for management purposes.
- The new Bank Regulations, effective 1 January 2008, no longer require general credit-risk reserves. The balance of this reserve as at 31 December 2007 was transferred to accumulated loss in 2008.

Income statement

- Interest income relating to structured loans previously included under other categories of loans and advances is reported separately in 2008. Comparatives for the year ended 31 December 2007 have been reclassified accordingly for all affected disclosures.
- Expenditure directly attributable to fee and commission income, previously included under operating expenditure is now presented separately in the income statement. Comparatives for the year ended 31 December 2007 have been reclassified accordingly for all affected disclosures.

Segment report

- Certain term loans previously included with Alliance Banking, MBL credit card and electronic banking are now presented as part of Retail and Commercial banking. Comparatives for the year ended 31 December 2007 have been reclassified accordingly.

Risk management and control

Group risk management philosophy

The Group recognises that the business of banking and financial services is conducted within an environment of complex inter-related risks. The Group operates in a dynamic environment where the past is not necessarily an acceptable guide to the future which has emerged even more clearly with the advent of the current global financial crisis. Risk management is a key focus of the Group and addresses a wide spectrum of risks that are continually evaluated and policies and procedures reviewed and stress tested to adapt to changing circumstances. In any economy there are sectors that are more vulnerable to cyclical downturn than others. Economic variances are monitored to assist in managing exposure to such sectors. The concentration of risk in our target market sectors is managed to achieve a balanced portfolio however we acknowledge the propensity to concentration risk in being a small bank and this is carefully monitored. Our business development efforts are focused on the stronger companies and individuals, establishing policy criteria, which eliminate weaker credit or investments from the portfolio. A passive role in the face of potential or actual adverse conditions is not accepted.

The Group remains well positioned to effectively manage identified threats in such a way that will minimise risks to the Group. An independent review of the risk management and control is planned to take place in 2009.

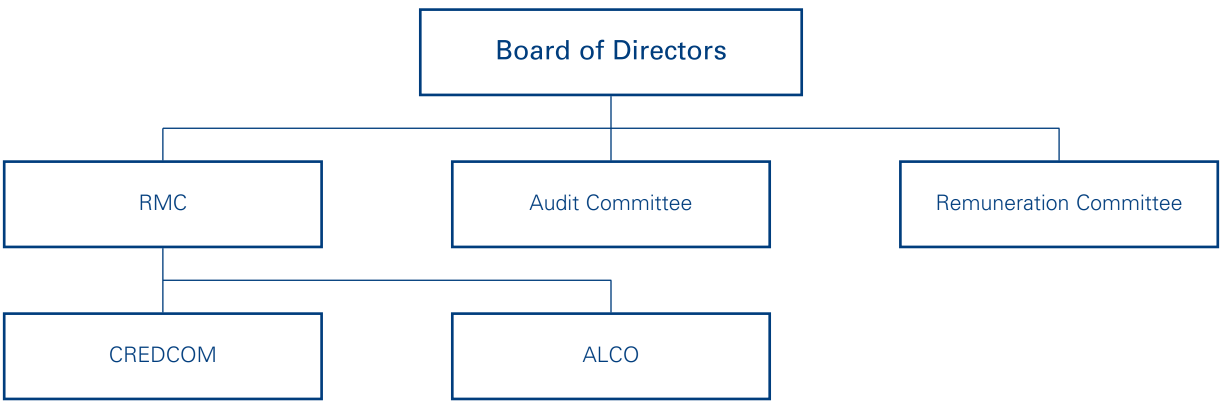
A philosophy of enterprise-wide risk management within a Risk Management Monitoring and Control Framework has been established to ensure that all business and operational risks are managed effectively within acceptable risk profiles, policies and parameters. The management of risk is an independent process from that of taking on/creating risk within the Group. Risk management policies are essentially conservative, with proper regard to the mix of risk and reward. The Group will take all necessary steps to safeguard its depositors' funds, its own asset base and shareholders' funds.

Enterprise-wide risk management

An Enterprise-wide Risk Management Framework is adopted to ensure appropriate and focused management of all risks. Risk assessment is a dynamic process and is reviewed regularly. Risk dimensions will vary in importance based on the business activities of an organisation. The overall objective of enterprise-wide risk management is to ensure an integrated and effective risk management framework, where all risks are identified, quantified and managed in order to achieve an optimal risk reward profile. The presence of accurate measures of risk makes risk adjusted performance possible, creates the potential to generate increased shareholder returns and allows the risk taking behaviour to be more closely aligned with our strategic objectives.

Risk management is performed on a Group wide basis involving the Board, credit management, senior management, independent risk management, business line management, finance and control, legal/compliance, treasury and operations, with significant support from internal audit and information technology.

Committee Structure



Risk management and control (continued)

Risk management life cycle/process

All of the Group's policies and procedures manuals are subject to ongoing review and are signed off by the relevant divisional heads. These standards are an integral part of the Group's governance infrastructure and risk management profile, reflecting the expectations and requirements of the Board in respect of key areas of control. The standards ensure alignment and consistency in the way that prevalent risk types are managed and form part of the four phases of the risk management life cycle, defined as:

Risk identification (and comprehension)

Risk identification focuses on recognising and understanding existing risks or risks that may arise from positions taken and future business activity as a continuing practice.

Risk measurement (and evaluation using a range of analytical tools)

Once risks have been identified, they need to be measured. Certain risks will obviously lend themselves more easily to determination and measurability than others, but it is necessary to ascertain the magnitude of each risk.

Risk management (as an independent function)

The Group's principal business focuses on the management of liabilities and assets in the balance sheet. Major risks are managed and reviewed by an independent risk function. The ALCO and RMC meet on a regular basis to collaborate on risk control, establish how much risk is acceptable and decide on how the Group will stay within targets and laid down thresholds.

Risk monitoring (and compliance with documented policies)

Open, two-way communication between the Group and the SARB is fundamental to the entire risk monitoring and supervisory process. To achieve this, responsible line heads are required to document conclusions and communicate findings to the ALCO and RMC in the first instance and to the SARB via the Finance Division through BA returns and periodic meetings.

Risk control (stress testing)

The Group follows a policy of ongoing stress testing. Critical variables are sensitive to market changes both domestic and international. These are identified and stress modelled to determine the possible impact of any deterioration of such identified variables on the Group's results. Both internal and external events are considered in formulating appropriate modelling criteria.

Management of risk

Principal risk categories have been identified, defined and categorised into direct and indirect risks. This set of risk definitions forms the basis of management and control relative to each division within the Group and also forms a consistent common language for outside examiners and/or regulators to follow.

Direct risks are found in most banking transactions. They are quantifiable and can be clearly defined. These risks are evaluated through examination of our databases, statistics and other records.

Indirect risks are considered to ensure that a complete risk assessment is carried out. They are present in almost every decision made by management and the Board and thus impact on the Group's image and success. These decisions are usually intended to enhance the Group's long-term viability or success and therefore are difficult to quantify at a given point in time.

Board Committees monitor various aspects of the different identified risks, which include:

Direct Risks	Indirect Risks
Credit Risk	Strategic Risk
Counterparty Risk	Reputation Risk
Currency Risk	Legal Risk
Liquidity Risk	Fraud Risk
Interest Rate Risk	International Risk
Market (Position) Risk	Political Risk
Solvency Risk	Competitive Risk
Operational Risk	Pricing Risk
Technology Risk	Sensitivity Risk
Compliance Risk	

Risk management and control (continued)

Management of risk (continued)

The responsibility for understanding the risks incurred by the Group and ensuring that they are appropriately managed lies with the Board. The Board approves risk management strategies and delegates the power to take decisions on risks and to implement strategies on risk management and control to the RMC. Discretionary limits and authorities are in turn delegated to line heads and line managers within laid down parameters to enable them to execute the Group's strategic objectives within predefined risk management policies. Major risks are managed, controlled and reviewed by an independent risk function.

The Board fully recognises that they are accountable for the process of risk management and the system of internal control. Management reports regularly to the Board on the effectiveness of internal control systems and significant control weaknesses identified.

A process is in place whereby the Top 10 risks faced by the Group are identified. These risks are assessed and evaluated in terms of a risk score attached to inherent risk and residual risk. Action plans are put in place to reduce the identified inherent risks to within acceptable residual risk parameters. The Top 10 risks are re-evaluated quarterly.

The Group subscribes to the 10 Principles of Sound Practices for the Effective Management and Supervision of Operational Risk as defined by the Basel Committee or Banking Supervision.

Continued focus remains on BCM. BCM ensures the availability of key staff and processes required to support essential activities in the event of an interruption to, or disruption of, business. BCM is an important aspect of risk management and its value has been proven in creating a more resilient operational platform, through activities such as business impact assessments, business continuity planning and implementation, testing of business continuity and implementing corrective actions. Comprehensive simulations are conducted on an ongoing basis, with identified gaps addressed and/or plans put in place to resolve the identified issues.

The Capital Management Committee under the auspices of the RMC proactively evaluates and manages the Capital requirements of the Group as determined by Basel II requirements. A comprehensive evaluation of the capital requirements under the Internal Capital Adequacy Assessment Process was undertaken during the year with consideration given to all risks impacting on the need for capital reserves within the Group. The basis of the assessment resulted in the Group identifying two risks – implementation of a new core system for the Group and the inherent concentration of the book given the nature of the Group's customers relative to its size which resulted in the prudent decision to hold a capital buffer in addition to the regulatory requirements.

Under the Enterprise-wide Risk Management Framework we have categorised the direct risks of the Group and report on those deemed to be of the most significance:

Credit risk

Credit parameters and tolerance levels are clearly defined and reflected in governing procedures and policies. The Group offers a spread of banking products common within the banking industry with a specific focus on small and medium sized businesses across a wide variety of industries. Whilst personal market products are also offered, no specific targeting of the broader personal retail based market is undertaken. The primary risks encountered are associated with the lending of money and the issuing of contingent financial or performance guarantees to third parties on behalf of customers.

Dependent upon the risk profile of the customer, the risk inherent in the product offering and the track record/payment history of the client, varying types and levels of security are taken to mitigate credit related risks. Clean or unsecured lending will only be considered for financially strong borrowers.

Counterparties to derivatives expose the Group to credit-related losses in the event of non-performance. The counterparties to these contracts are financial institutions. The Group continually monitors its positions and the credit ratings of its counterparties and limits the amount of contracts it enters into with any one party.

At year-end, the Group did not consider there to be any significant concentration of risk which had not been adequately provided for. There were no material exposures in advances made to foreign entities at year-end, except for the deposits placed with CGD as disclosed in note 30.2.

A portfolio analysis report is prepared and presented to the RMC analysing the performance and makeup of the book including customer and segment concentration analyses.

Risk management and control (continued)

Management of risk (continued)

Credit risk (continued)

The Group has adopted a conservative approach to credit granting within a specifically defined and structured approval process. The granting of credit is managed via a mandated approval process whereby levels of credit approval are determined by the experience of the mandated individual with dual or multiple sign-off on all material values. An ongoing weekly review is also undertaken by the CREDCOM of all new and renewal proposals for lending in excess of R2 million. In addition an early warning system is applied to actively manage all accounts within the risk structure. The system identifies a number of characteristics relating to the performance of the accounts and based on various predefined algorithms, flags issues of concern. Monitoring is done by the Early Warning Department and any concerns are raised with the Credit Department and Retail or Commercial banking units. The Group is in the process of further enhancing a Decision Support tool to assist credit decision makers through the provision of indicative performance criteria and other information necessary to assist in making increasingly informed decisions. Such indicative performance data will be measured against predefined acceptance bands and result in the allocation of an overall acceptability rating.

There have been no material changes in the credit approval structure or overall make-up of the book from the prior reporting period.

The table below summarises the Group's maximum exposure to credit risk at balance sheet date:

	Loans and advances R'000	Committed undrawn facilities R'000	Other R'000	Total R'000
2008				
Current accounts	**506 103**	**–**	**–**	**506 103**
Credit card	**22 420**	**19 364**	**–**	**41 784**
Mortgage loans	**1 622 704**	**312 357**	**–**	**1 935 061**
Instalment sales and leases	**373 744**	**–**	**–**	**373 744**
Structured loans	**285 225**	**–**	**–**	**285 225**
Other advances	**673 425**	**–**	**–**	**673 425**
Negotiable securities	**–**	**–**	**247 141**	**247 141**
Bank term deposits	**–**	**–**	**324 295**	**324 295**
Cash and cash equivalents	**–**	**–**	**1 464 959**	**1 464 959**
Guarantees	**–**	**–**	**331 494**	**331 494**
Letters of credit	**–**	**–**	**6 886**	**6 886**
	3 483 621	**331 721**	**2 374 775**	**6 190 117**
2007				
Current accounts	657 886	–	–	657 886
Credit card	21 555	32 679	–	54 234
Mortgage loans	1 241 399	190 910	–	1 432 309
Instalment sales and leases	304 588	–	–	304 588
Structured loans	131 191	–	–	131 191
Other advances	553 787	–	–	553 787
Negotiable securities	–	–	275 577	275 577
Bank term deposits	–	–	170 618	170 618
Cash and cash equivalents	–	–	1 252 376	1 252 376
Guarantees	–	–	391 335	391 335
Letters of credit	–	–	19 937	19 937
	2 910 406	223 589	2 109 843	3 545 267

Risk management and control (continued)

Management of risk (continued)

Operational risk

The Group subscribes to the 10 Principles of Sound Practices for the Effective Management and Supervision of Operational Risk.

Operational risks faced by the Group are extensive and *inter alia* include risks associated with reputation, robbery, fraud, theft of data, legal challenges, statutory and legislative compliance, operational processes, employment policies, documentation risk and business continuity. Strategies, procedures and action plans to monitor, manage and limit the risks associated with operational processes, systems and external events include:

- documented operational policies, processes and procedures with segregation of duties;
- training and upskilling staff on operational procedures and legislative compliance;
- an operational event logger wherein all losses associated with operational issues including theft and robbery are recorded and evaluated to facilitate corrective action;
- ongoing improvements to the Disaster Recovery and Business Continuity plans including conducting a variety of simulation exercises in the branches and critical operations environments; and
- conducting a variety of internal audits and reviews by both the Compliance and Internal Audit Departments in line with annual plans approved by the Board.

There have been no material losses during the reporting period that require specific identification.

Market risk

Market risk is the risk of revaluation of any financial instrument as a consequence of changes in market prices or rates and can be quantified as the potential change in the value of the banking book as a result of changes in the financial environment between now and a future point in time. The Board determines market risk limits. These limits are reviewed at least annually dependent on market events.

The Group does not currently have any proprietary trading positions and therefore has minimal exposure to market risk. Before the Group enters into a proprietary trading position, the Trading Committee will evaluate and approve such positions. This Committee will ensure that the Group is prudently positioned, taking into account agreed limits, policies, prevailing markets, available liquidity and the relationship between risk and reward primarily to the financial risks of changes in foreign currency exchange rates and interest rates. The Group enters into derivative financial instruments to manage its exposure to interest rate and foreign currency risk, including:

- forward exchange contracts; and
- interest rate and foreign currency swaps.

Detailed market risk reports are produced on a daily basis, which allows for monitoring against prescribed limits. In the unlikely event of an unauthorised limit violation, the ALM records such violation, which is immediately corrected and reported to the ALCO, which is a subcommittee of the RMC.

The Group does not perform a detailed sensitivity analysis on the potential impact of a change in exchange rates due to the fact that the Group does not currently have any proprietary trading positions. The impact of changes in open foreign currency client positions is modelled to take cognisance of credit risks associated with volatility in foreign currency exchange rates with the purpose of covering adverse positions through calling for variation margins. A detailed sensitivity analysis is performed for liquidity and interest rate risk as described below.

There has been no significant change to the Group's exposure to market risks or the manner in which it manages and measures the risk.

Foreign currency risk

The Group, in terms of approved limits, manages short-term foreign currency exposures relating to trade imports, exports and interest flows on foreign liabilities.

The Group has conservative limits in terms of net open foreign currency positions that are well below the limits allowed by the SARB. For the year under review the highest net open position recorded for any single day was R6.2 million (2007: R5.1 million).

Risk management and control (continued)

Management of risk (continued)

Foreign currency risk (continued)

The transaction exposures and foreign exchange contracts at balance sheet date are summarised as follows:

	US Dollar R'000	Euro R'000	Pound Sterling R'000	Other R'000	Total R'000
2008					
Total foreign exchange assets	1 361 063	35 327	26 585	12 277	1 435 252
Total foreign exchange liabilities	(129 695)	(13 782)	(12 828)	(130)	(156 435)
Commitments to purchase foreign currency	301 762	76 282	8 299	14 086	400 429
Commitments to sell foreign currency	(1 532 755)	(100 155)	(22 371)	(26 754)	(1 682 035)
Year-end effective net open foreign currency positions	**375**	**(2 328)**	**(315)**	**(521)**	**(2 789)**
2007					
Total foreign exchange assets	913 287	65 356	30 444	8 116	1 017 203
Total foreign exchange liabilities	(60 493)	(18 578)	(20 794)	(89)	(99 954)
Commitments to purchase foreign currency	245 343	67 736	20 242	8 320	341 641
Commitments to sell foreign currency	(1 097 925)	(114 958)	(30 513)	(16 640)	(1 260 036)
Year-end effective net open foreign currency positions	212	(444)	(621)	(293)	(1 146)

Interest rate risk

Interest rate risk is the impact on net interest earnings and the sensitivity to economic value as a result of increases or decreases in interest rates arising from the execution of the core business strategies and the delivery of products and services to customers. Interest margins may increase as a result of such changes, but may reduce or create losses in the event that unexpected adverse movements arise. The ALM forum monitors interest rate repricing on a daily basis and reports back to the ALCO and RMC.

The Group is exposed to interest rate risk as it takes deposits from clients at both fixed and floating interest rates. The Group manages the risk by maintaining an appropriate mix between fixed and floating rate funds and by the use of interest rate swap contracts.

Under interest rate swap contracts, the Group agrees to exchange the difference between fixed and floating rate interest amounts calculated on agreed notional principal amounts. Such contracts enable the Group to mitigate the risk of changing interest rates on the fair value of issued fixed rate debt and the cash flow exposures on the issued variable rate debt. The interest rate swaps reprice on a quarterly basis. The floating rate on the interest rate swaps is based on the three-month JIBAR and/or prime rate. The Group will settle the difference between the fixed and floating interest rate on a net basis.

Sources of interest rate risk include volatility and changes in interest rate levels, yield curves and spreads. These affect the interest rate margin realised between lending income and borrowing costs when applied to our rate sensitive assets and liabilities. The Group is also exposed to basis risk, which is the difference in repricing characteristics of two floating-rate indices such as the South African prime rate and three-month JIBAR.

To measure such risk, the Group aggregates interest rate sensitive assets and liabilities into fixed time bands in accordance with the respective interest repricing dates. The Group uses both dynamic maturity gap and duration analysis, which measures the mismatch level between the average time over which the cash inflows are generated and cash outflows are required. Various reports are prepared taking alternative strategies and interest rate forecasts into consideration. These reports are presented to the ALCO and RMC on a regular basis.

To monitor the effect of the gaps on net interest income, a regular forecast of interest rate sensitive asset and liability scenarios is produced. It includes relevant banking activity performance and trends, different forecasts of market rates and expectations reflected in the yield curve.

Risk management and control (continued)

Management of risk (continued)

Interest rate risk (continued)

For regulatory purposes, the assessment and measurement of interest rate risk is based on the accumulated impact of interest rate sensitive instruments resulting from a parallel movement of plus or minus 200 basis points on the yield curve.

In addition, the impact on equity and profit and loss resulting from a change in interest rates is calculated monthly based on management's forecast of the most likely change in interest rates.

At reporting date, a 50 basis point change was applied as a sensitivity analysis to determine exposure to interest rates. If interest rates increased/decreased by 50 basis points and all other variables remained constant, the Group's net profit and equity at year-end would increase/decrease by R8.6 million (2007: increase/decrease by R13.6 million). This is mainly attributable to the Group's exposure to interest rates on its lending and borrowings in the banking book.

The table below summarises the Group's exposure to interest rate risk. Assets and liabilities are included at carrying amounts, categorised by the earlier of contractual re-pricing or maturity dates and also indicate their effective interest rates at year-end:

	Up to 1 month R'000	1 – 3 months R'000	3 – 12 months R'000	1 – 5 years R'000	Over 5 years R'000	Non-interest bearing R'000	Total R'000	Effective interest rate %
2008								
Assets								
Intangible assets	–	–	–	–	–	76 894	76 894	–
Property and equipment	–	–	–	–	–	128 672	128 672	–
Other accounts receivable	–	–	–	–	–	39 273	39 273	–
Other investments	–	–	–	–	–	12 315	12 315	–
Deferred taxation assets	–	–	–	–	–	157 275	157 275	–
Non-current assets held for sale	–	–	–	–	–	5 289	5 289	–
Loans and advances	3 329 515	–	–	109 470	44 636	(79 832)	3 403 789	15.32
Derivative financial instruments	–	184	–	–	–	56 689	56 873	–
Negotiable securities	24 823	87 275	114 505	–	20 538	–	247 141	11.84
Bank term deposits	–	–	324 295	–	–	–	324 295	9.42
Cash and cash equivalents	947 999	410 808	–	–	–	106 152	1 464 959	9.42
Total assets	4 302 337	498 267	438 800	109 470	65 174	502 727	5 916 775	
Equity and liabilities								
Shareholders' equity	–	–	–	–	–	1 269 030	1 269 030	–
Deferred taxation liabilities	–	–	–	–	–	15 259	15 259	–
Deposits	2 813 096	550 288	1 012 189	8 161	–	5 613	4 389 347	8.30
Derivative financial instruments	7 091	1 906	–	–	–	86 094	95 091	–
Provisions	–	–	–	–	–	48 596	48 596	–
Other accounts payable	–	–	–	–	–	98 958	98 958	–
Taxation	–	–	–	–	–	494	494	–
Total equity and liabilities	2 820 187	552 194	1 012 189	8 161	–	1 524 044	5 916 775	
On balance sheet interest sensitivity gap	1 482 150	(53 927)	(573 389)	101 309	65 174	–	1 021 317	
Derivative financial instruments	27 559	119 758	–	(106 331)	(40 986)	–	–	
Total net interest sensitivity gap	1 509 709	65 831	(573 389)	(5 022)	24 188	–	1 021 317	

Risk management and control (continued)

Management of risk (continued)

Interest rate risk (continued)

	Up to 1 month R'000	1 – 3 months R'000	3 – 12 months R'000	1 – 5 years R'000	Over 5 years R'000	Non-interest bearing R'000	Total R'000	Effective interest rate %
2007								
Assets								
Intangible assets	–	–	–	–	–	23 569	23 569	–
Property and equipment	–	–	–	–	–	96 969	96 969	–
Other accounts receivable	–	–	–	–	–	23 639	23 639	–
Interest in associated company	–	–	–	–	–	4 251	4 251	–
Other investments	–	–	–	–	–	228	228	–
Loans and advances	2 755 877	–	–	111 091	43 438	(95 663)	2 814 743	13.48
Derivative financial instruments	4 248	–	–	–	–	39 566	43 814	–
Negotiable securities	102 752	145 769	20 482	–	6 574	–	275 577	11.13
Bank term deposits	–	–	170 618	–	–	–	170 618	9.01
Cash and cash equivalents	784 050	371 528	–	–	–	96 798	1 252 376	9.01
Total assets	3 646 927	517 297	191 100	111 091	50 012	189 357	4 705 784	
Equity and liabilities								
Shareholders' equity	–	–	–	–	–	839 914	839 914	–
Deposits	2 122 749	590 292	802 812	146 742	348	105 240	3 768 183	7.06
Derivative financial instruments	7 875	–	–	–	–	7 481	15 356	–
Provisions	–	–	–	–	–	42 435	42 435	–
Other accounts payable	–	–	–	–	–	39 780	39 780	–
Taxation	–	–	–	–	–	116	116	–
Total equity and liabilities	2 130 624	590 292	802 812	146 742	348	1 034 966	4 705 784	
On balance sheet interest sensitivity gap	1 516 303	(72 995)	(611 712)	(35 651)	49 664	–	845 609	
Derivative financial instruments	80 950	93 209	(21 500)	(110 101)	(42 558)	–	–	
Total net interest sensitivity gap	1 597 253	20 214	(633 212)	(145 752)	7 106	–	845 609	

Liquidity risk

Liquidity risk is the risk of being unable to meet current and future cash flow and collateral requirements when they become due, without negatively affecting the normal course of business. The Group is exposed to daily cash needs from overnight deposits, current accounts, maturing deposits, loan drawdowns and guarantees.

To measure liquidity risk, the Group aggregates assets and liabilities into fixed time bands in accordance with the respective maturity dates, which measures the mismatch level between the average time over which the cash inflows are generated and cash outflows are required.

The ALM forum monitors liquidity risk on a daily basis and reports back to the ALCO and RMC. Ultimate responsibility for liquidity risk management rests with the Board. An appropriate liquidity risk management framework has been developed for the management of the Group's short, medium and long-term funding and liquidity requirements.

Through active liquidity management, the Group seeks to preserve stable, reliable and cost effective sources of funding. To accomplish this, management uses a variety of liquidity risk measures that consider market conditions, prevailing interest rates, liquidity needs and the desired maturity profile of liabilities.

Risk management and control (continued)

Management of risk (continued)

Liquidity risk (continued)

To manage this risk, the Group performs, amongst others, the following:

- maintenance of stock of readily available, high quality liquid assets in excess of the statutory requirements as well as strong balance sheet liquidity ratios;
- assumptions based sensitivity analysis to assess potential cash flows at risk;
- management of concentration risk, being undue reliance on any single counterparty or counterparty group, sector, market, product, instrument, currency and tenor;
- maintenance of sources of funding for contingency funding needs;
- monitoring of daily cash flow movements/cash flow requirements, including daily settlements and collateral management processes;
- creation and monitoring of prudential liquidity risk limits; and
- maintenance of an appropriate term mix of funding.

There were no significant changes in the Group's liquidity position during the current financial year or the manner in which it manages and measures the risk. The Group is adequately funded and able to meet all its current and future obligations.

The table below summarises assets and liabilities of the Group into relevant maturity groupings, based on the remaining period to the contractual maturity at balance sheet date:

	Assets R'000	Liabilities R'000	Total mismatch R'000
2008			
Maturing up to one month	**1 894 158**	**3 008 043**	**(1 113 885)**
Maturing between one and three months	**518 300**	**591 013**	**(72 713)**
Maturing between three and six months	**322 211**	**509 066**	**(186 855)**
Maturing between six months and one year	**181 561**	**505 792**	**(324 231)**
Maturing after one year	**2 699 350**	**17 152**	**2 682 198**
Non-contractual	**301 195**	**16 679**	**284 516**
	5 916 775	**4 647 745**	**1 269 030**
2007			
Maturing up to one month	1 924 770	2 162 753	(237 983)
Maturing between one and three months	592 643	751 773	(159 130)
Maturing between three and six months	258 494	519 894	(261 400)
Maturing between six months and one year	179 121	284 360	(105 239)
Maturing after one year	1 721 402	147 090	1 574 312
Non-contractual	29 354	–	29 354
	4 705 784	3 865 870	839 914

Risk management and control (continued)

Management of risk (continued)

Liquidity risk (continued)

The remaining period to contractual maturity of financial liabilities of the Group as at balance sheet date which includes the interest obligation on unmatured deposits and derivatives calculated up to maturity date is summarised in the table below:

	Up to 1 month R'000	1 – 3 months R'000	3 – 6 months R'000	6 – 12 months R'000	Over 1 year R'000
2008					
Deposits	**2 822 081**	**565 940**	**529 882**	**551 597**	**9 669**
Derivative financial instruments	**45 937**	**37 929**	**2 774**	**2 306**	**6 202**
Other accounts payable	**98 958**	–	–	–	–
Taxation	**494**	–	–	–	–
Guarantees, letters of credit and committed undrawn facilities	**670 100**	–	–	–	–
Operating lease commitments	**397**	**794**	**1 207**	**2 080**	**7 824**
Capital commitments	**24 738**	**11 415**	**17 980**	**30 497**	**8 388**
	3 662 705	**616 078**	**551 843**	**586 480**	**32 083**
2007					
Deposits	2 060 662	768 400	537 375	306 368	175 918
Derivative financial instruments	3 444	3 344	1 850	1 322	7 018
Other accounts payable	39 780	–	–	–	–
Taxation	116	–	–	–	–
Guarantees, letters of credit and committed undrawn facilities	634 861	–	–	–	–
Operating lease commitments	366	698	890	1 350	4 289
	2 739 229	772 442	540 115	309 040	187 225

Basel II – influencing risk management developments at the Bank

The Basel Committee released the revised international Basel II Capital Accord in June 2004. The Accord is designed to differentiate minimum regulatory capital requirements in a risk sensitive manner and encourage and acknowledge sound risk management, internal control and governance practices.

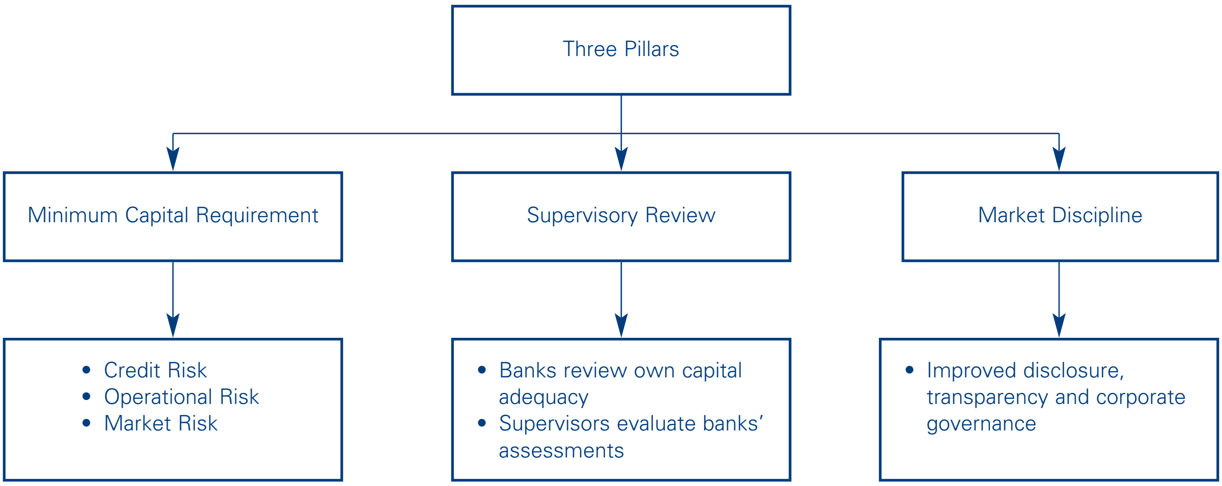
In today's complex environment, combining effective bank-level management with market discipline and regulatory supervision, best attains systemic safety and soundness. Building on these principles, the new Accord has far reaching implications for banks in terms of minimum capital standards linked to risks, risk measurement systems and methods, risk management practices and public disclosure of risk profile information. It focuses mainly on improving the management of credit and operational risks, enhancements to the supervisory review process and more extensive risk disclosure.

The overall objective of the new Accord is to improve the safety and soundness of the financial system. This will ensure a more resilient, more stable and a better source for credit, risk intermediation and growth. The principles of Basel II were built around three pillars. These pillars can briefly be summarised by the following diagram:

Risk management and control (continued)

Management of risk (continued)

Basel II (continued)



The new Accord provides a range of approaches that vary in levels of sophistication for the measurement of credit, operational and market risk to determine capital levels. It provides a flexible structure in which banks, subject to supervisory review, will adopt approaches that best fit their level of sophistication and their risk profile. The Bank evaluated the various options available and decided that the most appropriate approaches to follow for the calculation of the minimum capital requirement in terms of the Banks Act would be the Standardised Approach for Credit, Operational and Market risk.

The Accord has been implemented with effect 1 January 2008. The Bank forms part of various Basel II committees in association with the SARB, The Banking Association and other financial institutions.

The Group recognises the significance of Basel II in aligning regulatory capital to risk and further entrenching risk reward principles and practices in bank management and decision making.

Capital management

The Group and its principal subsidiary, the Bank, are subject to minimum capital requirements as defined in the Banks Act and Regulations. The management of the Group's capital takes place under the auspices of the RMC, through the ALCO. The RMC considers the various risks faced by the Group and analyses the need to hold capital against these risks whilst taking account of the regulatory requirements. In addition, the level of capital required to support the Group's targeted business growth is taken into consideration.

Risk weighted capital is allocated to the different business units in line with their targeted growth requirements.

The objective of the Group's capital management approach is to ensure the maintenance of sound capital ratios, taking all the above requirements into account, whilst producing appropriate returns to shareholders. Capital to support the Group's needs is currently generated by retained earnings.

In terms of regulation, the Group is able to consider different tiers of capital. The capital of the Bank consists almost entirely of tier 1 capital. Following the recapitalisation of the Group in 2004, it has remained capitalised well beyond regulatory and internal requirements.

The approach to capital management has been enhanced over the past year in line with Basel II.

Risk management and control (continued)

Management of risk (continued)

Capital management (continued)

The level of capital for the Bank is as follows:

	Risk-weighted exposures 31 December 2008 R'000	Risk-weighted assets 31 December 2007 R'000
Banking book		
Cash, off-balance sheet activities and central government transactions		–
Letters of credit and other bank advances		76 844
Residential mortgage loans, performance-related guarantees and committed undrawn facilities		582 554
Other assets including counterparty risk exposure		2 462 631
Credit risk	3 338 517	
Operational risk	564 151	
Market risk	3 910	
Equity	22 162	
Other assets	375 074	
	4 303 814	3 122 029

	2008 R'000	2007 R'000
Primary capital	1 157 213	798 377
Share capital and share premium	1 483 299	1 483 299
Reserves	6 734	12 231
Less: Deductions/Impairments	(332 820)	(697 153)
Secondary capital	18 418	39 025
General debt provisions	18 384	39 025
Fifty per cent of a revaluation surplus	34	–
Net qualifying capital and reserves	1 175 631	837 402

	2008	2007
Capital adequacy ratio (%)	27.3	26.8
Primary capital (%)	26.9	25.6
Secondary capital (%)	0.4	1.2

2008 is presented in line with the amended Banks Act and Bank Regulations effective 1 January 2008, whereas 2007 is presented in line with the preceding Banks Act and Bank Regulations.

Corporate governance

The Boards of Directors of Mercantile Bank Holdings Limited and the Bank (collectively referred to as "the Board") hold joint Board meetings. The Board subscribes to and is committed to ensuring that the Group complies with the principles and standards set out in the code of corporate practices and conduct expressed in King II and is satisfied that the Group complied in all material respects with these principles throughout the year under review.

The following is a summary of the corporate governance processes of the Group for the year ended 31 December 2008:

1. Board of Directors

The Board exercises effective control over the Group and gives strategic direction to the Bank's management.

Key responsibilities of the Board assisted by its Board Committees are to:

- approve the Group's strategy, vision and objectives and monitor/review the implementation thereof;
- approve and annually review the Group's limits of authorities;
- annually review corporate governance processes and assess the achievement of these against objectives set;
- annually review its charter and approve changes to the charters of the Board Committees;
- annually approve the non-executive Directors' remuneration and submit such for approval and ratification by shareholders at the AGM;
- annually approve executive Directors' remuneration and/or increases thereto;
- annually approve the Group's budget (includes capital expenditure);
- be accountable for financial, operational and internal systems of control and overall risk management;
- approve changes to the Group's financial and accounting policies;
- approve the audited financial statements and interim results;
- be responsible for ensuring that the Group complies with all relevant laws, regulations and codes of business practice and codes of ethics;
- appoint appropriate Board Committees and determine the composition thereof; and
- annually approve the Board and Board Committees' self-evaluations conducted on their effectiveness.

The Board comprises non-executive and executive Directors with different skills, professional knowledge and experience, with independent non-executive Directors comprising the majority on the Board. For detail on the composition of the Board and changes to such during the financial year ended 31 December 2008, the frequency of meetings and attendance thereof, refer to Annexure A to this document. The roles of the Chairman of the Board and CEO, who are appointed by the Board, are separated, thereby ensuring a clear division of responsibilities at the head of the Group. The Chairman of the Board is an independent non-executive Director.

Non-executive Directors offer independent judgement and, apart from their fees, there are no extraneous factors that could materially affect their judgement. If there is an actual or potential conflict of interest, the Director (executive or non-executive) concerned, after declaring his/her interest in terms of the Companies Act, is excluded from the related decision-making process.

The process of identification of suitable candidates to fill vacancies on the Board and to re-appoint Directors on termination of their term of office is conducted by the Directors' Affairs Committee. This Committee's nominations are submitted to the Board for approval, subject to the SARB having no objections to the nominations of new appointments. Any person appointed to fill a casual vacancy or as an addition to the Board, will retain office only until the next AGM unless the appointment is confirmed at that meeting.

All Directors except the CEO, who has a five year service contract, retire on a three-year rotational basis. The service contract of the CEO has been renewed for three years on expiry of his contract in March 2009. The re-appointment of the CEO as an executive Director with effect from 29 March 2009 upon expiry in terms of the articles of association of the Company will be confirmed at the AGM. The Service contract of Mr Lopes, an executive Director, seconded by the major shareholder has been renewed for three years upon expiry of his contract on 8 November 2008. If eligible for re-election, Mr Lopes and the other non-executive Directors standing for re-election, can be re-elected at the AGM. Directors are required to retire from the Board at age 70. The Board can however decide that a Director continues in office beyond this age. Such Director is still subject to retirement by rotation provisions as explained above.

To comply with the JSE Listings Requirements, the Board has commenced its search for a Financial Director whose portfolio will include broader aspects than finance and the Board is confident that a Financial Director will be appointed by 30 June 2009, the date by when the Company has to comply with the changed Listings Requirement.

The Board operates in terms of a charter, which defines its duties, responsibilities and powers. The charter is reviewed annually. The evaluation of the performance of the Board as a whole is conducted annually by means of a self-evaluation

Corporate governance (continued)

1. Board of Directors (continued)

process. An evaluation of the Chairman is conducted by the other Directors. The evaluation of individual non-executive Directors' performance is conducted on a bilateral basis between the Chairman and each Director.

At 31 December 2008, the Board, which has a unitary board structure, comprised eight Directors, of which two were executives. Mr Njikizana was appointed as an independent non-executive Director on 6 November 2008.

All the non-executive Directors are classified as independent, one of whom is a woman. Three of the Directors are classified as black in terms of the relevant legislation. The Board is satisfied that its composition currently reflects an appropriate balance in this respect.

The Board has unrestricted access to all company information, records, documents and property.

2. Group Secretary

The appointment and removal of the Group Secretary is a matter for consideration by the Board as a whole. The Group Secretary ensures that statutory and regulatory procedures are complied with. The Group Secretary attends all Board and Board Committee meetings. The Group Secretary provides a central source of advice and guidance on business ethics and compliance with good corporate governance, assisting the Board as a whole and its members individually with guidance as to how their duties, responsibilities and powers should be adequately discharged and exercised in the best interests of the Group. If necessary, Directors are entitled to obtain independent professional advice at the Group's expense.

The Group Secretary also maintains, and regularly updates, a corporate governance manual, copies of which are distributed to all Directors, and organises and conducts a Board approved induction programme to familiarise new Directors with the Group's operations, their fiduciary duties, and the Group's corporate governance processes. The Group Secretary assists the Board in developing a training framework annually to assist the non-executive Directors with continuous development as Directors and in particular in a banking environment.

3. Board Committees

To assist the Board in carrying out its duties and responsibilities, a number of Board Committees exist. This does not relieve the Board of any of its responsibilities. These Committees all operate in terms of approved charters, which define their roles. All Board Committees' charters are reviewed annually.

Changes to the charters are subject to Board approval. The performance of Board Committees, based on the duties and responsibilities as set out in the respective charters, are evaluated annually by means of a self-evaluation process, which results are discussed at the Board Committee concerned and then reviewed and approved by the Board.

For detail on the composition of the Board Committees, frequency of meetings and attendance thereof, refer to Annexure A.

All Directors who are not members of the Board Committees may attend Committee meetings.

All Directors who are not Committee members receive copies of the documentation sent to the Board Committees from time to time.

Further details on the Board Committees are provided below.

3.1 GAC

The GAC comprises three independent non-executive Directors, one of whom acts as Chairman, who is not the Chairman of the Board. Mr Ikalafeng resigned as a GAC member on 6 November 2008 and Mr Njikizana was appointed as a GAC member effective 6 November 2008. The CEO who stepped down as a GAC member effective 1 January 2008 attends GAC meetings as a permanent invitee.

GAC meetings are held at least four times per annum. The meetings of the Committee are attended by the head of Internal Audit, the External Auditors, the head of Risk, the Compliance Officer, the head of Finance, the head of Alliance Banking and Support Services and the head of Treasury. The head of Internal Audit, head of Risk, the Compliance Officer, the head of Alliance Banking and Support Services and head of Treasury do not attend the meeting held in April annually as the main purpose of the said meeting is to approve the statutory annual financial statements of subsidiary companies. If a special meeting is called the attendance of non-members is at the discretion of the Chairman of the GAC. The head of Internal Audit, the Compliance Officer, the head of Finance, the head of Risk, the CEO and the External Auditors have unrestricted access to the Chairman of the Committee. As defined in its charter, the primary objective of the Committee is to assist the Board to fulfil its responsibilities relative to:

- financial control and reporting;
- compliance with statutory and regulatory legislation which includes but is not limited to the Banks Act, Companies Act, the Listings Requirements of the JSE, Common law, IFRS and tax legislation;
- Corporate Governance;
- Risk Management; and
- shareholder reporting.

Corporate governance (continued)

3. Board Committees (continued)

3.1 GAC (continued)

Inter alia, the Committee reviews accounting policies, the audited annual financial statements, interim results, internal and external auditors' reports, regulatory public disclosures required in terms of the Bank Regulations, the adequacy and efficiency of internal control systems, the effectiveness of management information systems, the internal audit process and the Bank's continuing viability as a going concern and its complaints handling duties in terms of the Companies Act. The Compliance Officer also gives feedback to the Committee on compliance issues and updates on changes to legislation, which could have an impact on the Group.

The External Auditors' appointment is recommended by the Committee and approved at the AGM. The Committee reviews the External Auditors' terms of engagement and fees and also pre-approves an engagement letter on the principles of what non-audit services the External Auditors' could provide.

The GAC carried out its function, as detailed in its charter, during the year by considering all information provided by management for discussion, decision and/or recommendation to the Board for approval, at its meetings (refer to Annexure A). The GAC believes it has fulfilled its responsibilities in terms of its charter during the year under review.

The GAC has satisfied itself as to the independence of the External Auditors.

The GAC considers the annual financial statements of the Group to be a fair presentation of its financial position, and the results of operations and cash flows for the year ended 31 December 2008, in terms of IFRS, the Companies Act, the Banks Act and JSE Listings Requirements.

3.2 RMC

This Committee comprises five members, three of whom are independent non-executive Directors, the CEO and an Executive Director. The Chairman of the Board chairs this Committee.

RMC meetings are held at least four times per annum. The RMC meetings are attended by the head of Risk, the head of Risk Standards and Special Projects and Asset and Liability Management, the head of Finance, the head of Credit, the head of Alliance Banking and Support Services, the Compliance Officer, the head of Treasury and the head of Internal Audit.

As defined in its charter, the RMC's objectives are to:

- assist the Board to fulfil its risk management and control responsibilities, in the discharge of its duties relating to risk and control management, assurance, monitoring and reporting of all risks identified and managed through the Enterprise Wide Risk Management Framework;
- provide monitoring and oversight of the risk management process;
- facilitate communication between the Board, GAC, Internal Auditors, Compliance and other parties engaged in the risk management activities;
- ensure the quality, integrity and reliability of the Group's risk management and control;
- review the Group's process and allocation of capital and the capital management policy; and
- provide an independent and objective oversight and review of the information presented by management on risk management generally and specifically taking into account reports by management and the GAC to the Board on financial, operational and strategic risks.

The RMC has fulfilled its responsibilities in terms of its charter during the year under review.

For more detailed information relating to the Risk Management of the Group refer to pages 60 to 71.

3.3 Directors' Affairs Committee

This Committee comprises all the non-executive Directors on the Board. Mr Njikizana was appointed a member of this Committee on 6 November 2008. The Chairman of the Board chairs this Committee. Meetings are held at least four times per annum.

As defined in its charter, the primary objectives of this Committee are to:

- assist the Board in its determination, evaluation and monitoring of the appropriateness and effectiveness of the corporate governance structures, processes, practices and instruments of the Group;
- assist the Board in ensuring that the Group is compliant in all material aspects with King II and other corporate governance practices;
- establish and maintain a continuity plan for the Board;
- be responsible for the process of Board nominations and appointments for recommendation to the Board and in doing so, review the skills, experience and other qualities required for the effectiveness of the Board;
- ensure that a management succession plan is in place; and
- assist the Board in determining whether the employment/appointment of any Directors should be terminated (excludes resignations).

Corporate governance (continued)

3. Board Committees (continued)

3.4 Remuneration Committee

This Committee comprises all the independent non-executive Directors of the Board excluding the Chairman of the Board. An independent non-executive Director chairs this Committee. The CEO attends this Committee's meetings by invitation. The Committee must meet at least twice per annum.

As defined in its charter, the Committee's primary objectives are to:

- assist the Board in determining the broad policy for executive and senior management remuneration and the Bank's remuneration philosophy (refer to item 5 below for further detail);
- assist the Board in reviewing the remuneration of the executive Directors and Company Secretary; and
- assist the Board in reviewing the non-executive Directors' fees.

3.5 Transformation Committee

This Committee comprises three independent non-executive Directors and the CEO. The Chairman of the Board chaired this Committee until 31 October 2008. On 31 October 2008 Mr Ikalafeng was appointed the Chairman of this Committee and the Chairman of the Board continued to serve as a member of this Committee. This Committee must meet at least four times per annum.

As defined in its charter, this Committee's primary objectives are to:

- assist the Board in determining the targets to be achieved and the monitoring of the progress towards achieving these targets in respect of the following key BEE initiatives as laid down in the Broad-Based BEE Act and the FSC:
  - employment equity targets for the various levels of management and other employees;
  - skills development programmes to promote black skills;
  - procurement from BEE accredited companies;
  - corporate social investment;
  - the amount of black SME loan approval;
  - the composition of the Board of Directors in relation to gender and black people; and
- assist the Board in determining which black individuals/entities should be considered for direct ownership in the Group.

3.6 Technology Committee

This Committee, which is a Committee of the Bank, comprises two independent non-executive Directors and two executive Directors. An independent non-executive Director chairs this Committee. This Committee was formed in 2006 to monitor and manage a special project of the Bank relating to the replacement of its core banking system. The Technology Committee fulfilled its charter for the 2008 year and will continue to fulfil its oversight role pending implementation of the new banking system.

4. Management Committees

A number of Management Committees have been formed to assist executive management and the Board in carrying out its duties and responsibilities. These are:

- ALCO
- CREDCOM
- Employment Equity Committee
- Retail/Commercial EXCO
- Treasury EXCO
- Alliance Banking EXCO
- Human Resources Committee
- IT Steering Committee; and
- Procurement Committee

All these Committees operate in terms of their charters, which define their duties and responsibilities.

Non-executive Directors may attend any Management Committee meetings.

5. Remuneration philosophy

The main purpose of the remuneration philosophy adopted in the Group is to promote performance-based and equitable remuneration practices.

In order to attract, motivate and retain staff the Group ensures that remuneration practices are fair, equitable and competitive. The three main elements of remuneration are described below.

The *total guaranteed package* concept gives all employees a certain degree of flexibility as they can structure their packages to include a 13th cheque, select the appropriate level of travel allowance (in accordance with SARS' regulations) and choose the appropriate medical aid plan. External equity is ensured by comparing packages to market levels through salary surveys. This is done at least once a year prior to annual salary review processes. Increases and movements in individual pay levels are based on performance, levels of competence and current position/pay level against market. The market median pay level for the comparative position is used as a guideline.

Corporate governance (continued)

5. Remuneration philosophy (continued)

Short-term incentives are important to support the pay for performance philosophy and form an important component of variable pay. The current incentive bonus scheme was introduced in 2004. The scheme is reviewed on an annual basis.

The third element of the remuneration mix is *long-term incentives.* The purpose of this element is to attract and reward key staff members whose contribution within the next three to five years is viewed as critical and whose retention is regarded as a priority. A new long-term incentive scheme – Conditional Share Plan, was introduced during the year under review to replace the previous share option scheme. If at a future date the Board wishes to use the share option scheme it would be able to do so.

The policy on the remuneration of executive Directors is consistent with that of senior management. Non-executive Directors receive fees for their services as Directors of the Group and for services rendered as members of the various Board Committees. Foreign exchange impact is taken into account for Directors who are non-resident.

6. Internal Audit function

The Internal Audit function forms part of the overall risk management and governance process within Mercantile. The head of Internal Audit, who reports functionally to the GAC and administratively to the CEO, performs a function independent from any other function in the Group. She has direct and unrestricted access to the Chairman of the GAC, the CEO, the Chairman of the RMC and the Chairman of the Board.

The GAC must concur with any decision to appoint or dismiss the head of Internal Audit.

The Board reviewed the Internal Audit Charter, which governs internal audit's activity in the Group, during the year. The charter defines the role, objectives, authority and responsibility of the Internal Audit function.

All significant operations, business activities and support functions are subject to Internal Audit review. The audit plan is risk based and is drawn up annually and approved by the GAC.

Internal Audit is responsible for reviewing the adequacy and effectiveness of control and governance processes throughout the Group. Any significant or material control weaknesses are reported to management, the GAC and/or the RMC for consideration and the necessary remedial action.

To complement the Group Internal Audit function:

- the Bank has entered into a co-sourcing arrangement with KPMG, to provide specialist internal audit skills in the IT and other specialists environments; and
- CGD's Internal Audit Department carries out assignments in accordance with CGD's requirements.

An independent review of the Internal Audit function is due to be conducted during the course of 2009.

7. External Auditor's services: Outsourcing policy

The Group will not contract its External Auditors on an outsourcing basis where such an engagement compromises their independence and, in particular, the following areas are specifically excluded from the services that are procured from the External Auditors:

- bookkeeping or other services related to accounting records or annual financial statements;
- financial information systems design and implementation;
- appraisal or valuation services, fairness opinions or contribution-in-kind reports for financial reporting purposes;
- actuarial services;
- internal audit outsourcing and or co-sourcing;
- performance of management functions;
- as staff-recruitment agent;
- broker-dealer, investment advisor or investment banking services; and
- legal services.

The following is a summary of the policy adopted by the GAC to ensure proper governance and approval of the use of External Auditors to provide non-audit services:

The GAC approved a "Blanket" engagement letter for non-audit services on the basis that the External Auditors confirm in writing prior to providing a service contained in the engagement letter approved by the GAC that such does not impair their independence and that they may provide such service. The GAC has approved that for non-audit services which the External Auditors may provide in terms of the engagement letter with a value of R250 000 or less, may be provided subject to the CEO's supporting such. A report on these services provided is submitted to the GAC meetings for notification.

The GAC requires that all non-audit services which the External Auditors may provide in terms of the engagement letter with a value of more than R250 000 must before the External Auditors provide the service be submitted to the GAC for approval.

Corporate governance (continued)

8. Compliance function

The role of the independent Compliance function is to identify, assess and monitor the statutory and regulatory risks faced by the Group and advise and report to senior management and the Board on these risks. The Compliance function is mandated to make the Board aware of any procedural concerns that may lead to non-compliance and alert members to incidents of non-compliance whilst taking remedial action to avert such incidents.

To ensure the independence of the Compliance function from the business activities of the Group, the Board authorised the Compliance function to:

– carry out its responsibilities on its own initiative in all areas of the Group in which regulatory risk may or may not exist;
– ensure it is provided with sufficient resources to enable it to carry out its responsibilities effectively;
– not have direct business line responsibilities; and
– report directly to the Board or a Committee of the Board, whenever necessary.

The Board approved a charter for the Compliance function. At least once a year, the Board will review the charter and its ongoing implementation to assess the extent to which the Group is managing its regulatory risks effectively.

The GAC annually reviews and approves a compliance plan. The GAC monitors the progress against the compliance plan, which sets out training, monitoring and review of compliance with the regulatory requirements in the Group.

The Compliance function keeps senior management and the Board informed about significant regulatory issues and any trends exhibited, and identifies where urgent intervention is needed.

Reporting to the Board is in the form of a Level of Compliance Report to both the RMC and the GAC (the same report is also submitted to the SARB, once discussed by the GAC).

The challenge of the increasing pace and organisational impact of regulatory change continued in 2008. Notable regulatory interventions during 2008 included an increased focus on consumer protection legislation, the implementation of the amendments to the Companies Act (the Corporate Laws Amendment Act, 2006) and the implementation of Basel II at the beginning of 2008. The latter necessitated the implementation of significant amendments to the Banks Act and amended Bank Regulations.

NCA, FICA and FAIS and the Occupational Health & Safety Act were the key areas that the Compliance Department focused on during the year under review.

The NCA has had a significant impact on credit providers throughout South Africa. The NCA imposes strict requirements on credit providers including affordability assessments, disclosure to consumers, advertising and marketing practices, complaints, pricing and reporting to the National Credit Regulator. Business processes and credit granting procedures have been reformulated to ensure compliance with this local legislation. Compliance as well as external service providers carried out extensive training throughout the year.

As required by FICA, the Compliance Department manages the ongoing monitoring and compliance with anti-money laundering and combating of terrorist financing legislation. In response to international best practice the Bank has developed and implemented a centralised electronic anti-money laundering system that is constantly enhanced. The system is primarily focused on transaction monitoring and detection of potential money laundering activity. Training of staff on anti-money laundering and related topics remains a key focus area and the training material is constantly updated to provide for any changes in legislation, internal best practice and industry trends.

The ongoing implementation of FAIS was the other major imperative for the business and the Compliance function during the year, with the majority of our Retail Banking Staff undergoing further training in the rendering of financial advice and related services, to meet the Fit and Proper requirements of the legislation. In-house training is also provided to all relevant staff on a regular basis. Reports on compliance with the requirements of FAIS were also completed and submitted to the Financial Services Board during the year.

Compliance risk is managed through internal policies and processes, which include legal, regulatory and business specific requirements. A compliance tool was developed to assist management in reporting compliance breaches electronically and thereby supporting Compliance in fulfilling its obligations. Regular training and advice is provided to ensure that all employees are familiar with their compliance obligations. Business units are independently monitored to ensure adherence to policies and procedures and business specific requirements.

No material incidents of non-compliance were reported during the year under review. The Compliance function was independently reviewed during the year.

Corporate governance (continued)

9. Dealing in securities of the Group

The Group's dealings in securities policy ("the policy") regarding dealings in the Group's securities by Directors and the Group Secretary, complies with the JSE Listings Requirements. Should any Director and the Group Secretary or their associates wish to trade in the Group's securities, held either directly or indirectly, beneficially or non-beneficially, written clearance must be obtained in advance from the Chairman of the Board or the designated Director for this purpose. The policy also restricts trading by certain individuals employed by the Bank, which includes but is not limited to the senior managers and the Mercantile Bank Holdings Limited long-term incentive schemes participants.

All individuals bound by the policy may not trade during the following periods:

– when the Company is trading under cautionary announcement;
– the period between the end of either the financial year or half-year and release of results pertaining to that period; and
– any period when there exists any matter, which constitutes unpublished price sensitive information.

The policy also emphasises that each individual (whether a Director or employee) is obliged to comply with the provisions of the Securities Services Act No 36 of 2004, which deals with insider trading rules.

The policy is implemented by the Group Secretary who is required to keep a written record of all written clearances given and, as soon as the trade has been executed, to ensure that disclosure is made on SENS in terms of the JSE Listings Requirements.

10. The Code

The Group subscribes to the Code that provides valuable safeguards for its clients. The Group attempts to conduct its business with uncompromising integrity and fairness, so as to promote complete trust and confidence. In meeting this fundamental objective, the Group conducts its relationships with the regulatory authorities, clients, competitors, employees, shareholders, suppliers and the community at large, by striving for high service levels with integrity, and encourages its employees to acquaint themselves with the Code and honour its precepts.

11. Integrated sustainability reporting (additional reporting not covered elsewhere in the Annual Report)

11.1 Ethical standards

The Group is committed to high moral, ethical and legal standards and expects all representatives of the Group to act in accordance with the highest standards of personal and professional integrity in all aspects of their activities and to comply with all applicable laws, regulations and the Group's policies.

The Group's commitment is clearly stated in the Group's Code of Ethics which contains a set of standards which the Group believes could contribute to its commercial success, as adherence thereto is a strategic business imperative.

The Board believes that the Group has adhered to the ethical standards during the year under review.

11.2 Talent management

Three major initiatives were implemented in 2008.

In order to increase the number of staff in the talent pools, a graduate trainee programme (Mercantile Trainee Programme/MTP) was launched and six graduates were employed on a two-year training programme. They receive structured on-the-job training in all areas of the Bank as well as attend formal training courses.

Establishing Mercantile as an employer of choice was identified as an important strategic objective.
A comprehensive process comprising interviews with recruitment agencies, previous employees and workshops and consultation with current staff was started to identify our employment brand and Employee Value Proposition ("EVP"). The outcome of this process will result in more successful and targeted talent recruitment, motivation and retention strategies.

The identification and nurturing of leadership potential is done through the creation of various talent pools i.e. middle management/professional level talent pool comprises staff who have been identified as potential successors to senior management positions. The leadership development of talent pool staff as well as current senior managers was regarded as an important strategic priority.

The senior management team attended a leadership alignment and effectiveness workshop which forms the foundation for further development of this group as well as all other managers.

11.3 Employee satisfaction and commitment

The levels of employee satisfaction and commitment were measured in an employee survey. The results indicated a number of areas that need attention in order to increase satisfaction and commitment. Following the communication of the results to all staff and workshops in which suggested actions were generated, action plans are being put in place to address issues.

The attrition rate is monitored on a quarterly basis. The annual 2008 attrition rate is down by approximately 4.0% compared to 2007.

Corporate governance (continued)

11. Integrated sustainability reporting (additional reporting not covered elsewhere in the Annual Report) (continued)

11.4 Brand values and culture transformation

The values underpin and drive the culture transformation process and the customer experience and satisfaction.

The EVP and Employee Survey process referred to are used to shape the culture and measure progress.

Customer satisfaction is a key strategic initiative and a survey is conducted annually to gauge the levels of satisfaction. The Customer Satisfaction Index has been tracked for the past five years and new targets and action plans are implemented every year.

11.5 Employee wellness

The overall well being of our employees is regarded as very important and we offer a comprehensive Employee Assistance Programme, provided by an external company, to all our staff. The 24-hour telephone counselling service is supplemented by face-to-face counselling (if required). Issues raised by employees are monitored by the service provider and quarterly reports are provided indicating trends and frequency of usage.

In addition to the above, a "wellness day" was held on the Mercantile premises and staff were able to obtain information and undergo health-screening tests on various aspects of physical and emotional wellbeing.

HIV/Aids is a stark reality in South Africa and initiatives are in place to ensure that this gets the required attention. Some of the initiatives are: HIV/Aids policy; awareness training to all staff; and training for managers.

11.6 Safety, health and environmental principles

The Group is, on an ongoing basis, striving to improve its facilities to ensure the safety and wellbeing of its employees during the execution of their duties and of persons who may enter any of its premises. Regular inspections of the workplace are carried out to identify potential hazards and the Group does not hesitate to take and enforce such measures that may be reasonably practicable, to eliminate or mitigate any hazard or potential hazard to the safety of its employees or other persons.

The Group acknowledges that the sound management of natural resources is a cornerstone of sustainable development. As a financial institution Mercantile recognises that its direct environmental impacts are associated primarily with the operation of the Bank's office infrastructure. Systems aimed at reducing resource consumption over time are in place. We continuously explore ways in which to reduce paper, energy and water usage. However, our business, through our lending practices, also impacts indirectly on the environment.

Assessment and management of environmental risks associated with a particular client or credit application is integral to the credit decision-making process. In order to apply those environmental standards Mercantile is adhering to its Environmental Risk Management Policy.

Mercantile is therefore committed to complying with relevant environmental legislation and regulations applicable to all its operations, as well as incorporating best practice where appropriate.

11.7 Fraud

Credit card fraud:

The Bank is an issuer of Visa Credit Cards and has, in line with the card association regulations, adopted pro-active measures to prevent fraudulent use of this product.

Monitoring Fraud reports are based on a set of parameters and perused on a daily basis with the aim to identify fraudulent transactional behaviour. If fraudulent activity is evident further action is taken to prevent future use of the card/card number.

Confirmed fraudulent transactions are reported to the card association, which determines common trends and alerts the industry accordingly.

Fraud awareness training presentations are conducted throughout the Group. These presentations are conducted at least once a year. In addition to the presentations, monthly newsletters are compiled and disseminated to all staff. The newsletters address a wide range of topics and are not limited to credit card fraud only.

Credit Card Fraud staff attend workshops presented by the card associations, meetings of industry role players and utilise internet based sources to stay abreast of the fraud trends and the prevention thereof. The Bank also works closely with the South African Banking Risk Information Centre ("SABRIC").

Fraud other than credit card fraud:

Mercantile has adopted a zero tolerance towards all types of fraud and theft.

Internal Audit investigates all incidents other than Credit Card Fraud, which is done by the Credit Card Fraud Department.

The Group has established a good working relationship with SABRIC and the Commercial Crime Units of the South African Police Services ("SAPS") throughout South Africa.

An incident when reported is investigated and all related evidence and statements taken. If the incident was perpetrated externally, criminal charges are laid. If the incident was perpetrated internally, disciplinary action is instituted in addition to criminal charges being laid. All incidents are reported to SABRIC and the SAPS.

Corporate governance (continued)

11. Integrated sustainability reporting (additional reporting not covered elsewhere in the Annual Report) (continued)

11.7 Fraud (continued)

The Group continuously arranges or participates in the training of relevant staff members to keep abreast of developments of the fraud trends and the prevention thereof.

11.8 Whistle blowing

The Group has a comprehensive Protected Disclosures Policy based on the Act bearing the same name. The policy addresses the reporting of corruption and corrupt activities in particular, as well as any impropriety conduct in general under the Whistle Blowing section of the policy. All employees are encouraged to make disclosures in good faith and on reasonable grounds.

All branch employees and selected head office employees received training on what to report on and how to do the reporting. Training will continue in 2009. The Policy caters for anonymous reporting, should the employee wish not to disclose his/her name.

An enhanced anonymous reporting system has been developed and will be rolled out to employees in 2009. This will allow all employees to report directly to Compliance and Internal Audit through electronic means. This system is deemed to simplify the anonymous reporting procedure and encourage employees to make use of the process in an efficient manner.

12. Transformation

The Group is fully committed to social and economic transformation and regards it as a key business imperative. Initiatives are driven and directed by the Board and integrated into the Group's strategic business plans. The Transformation Committee monitors the progress of transformation in the Group. The Committee's charter stipulates how transformation will be implemented, monitored and integrated across the Group.

The key elements of the charter, which are based on the FSC Scorecard requirements and aligned to the strategy of the Group, are as follows:

Employment Equity

Transformation in the workplace is an important aspect of employment equity, and the Group strives to provide an environment that values and fosters diversity and equality. This includes developing a culture that supports mutual trust, respect and dignity.

Adherence to the Employment Equity Act and associated Skills Development legislation is regarded as essential. The desired results of the implementation of the employment equity plan are to improve the representation of black people, women and people with disabilities towards reflecting the demographic profile of the country and prioritising the development and career advancement of the designated groups.

As employment equity is regarded as a key business imperative, it is included in each of the divisions' key result areas. Targets were set for 2004 to 2008 (subsequently also for 2009 to 2012) and progress monitored on a quarterly basis. Good progress has been made in the employment of black people in the skilled/junior management and semi-skilled categories and the overall level of representivity of black people has increased from 35.0% in 2004 to 54.2% in 2008. The challenge remains the attraction, employment and retention of suitably experienced and skilled employment equity candidates for middle management, professional, specialist banking positions and senior management level positions.

Corporate governance (continued)

12. Transformation (continued)

Employment Equity (continued)

The table below illustrates the number of staff per race category (as defined by the Department of Labour) as at 31 December 2008.

Occupation levels	Male			Female				Male	Foreign national		Total
*	A	C	I	A	C	I	W	W	Male	Female	
Top management	0	0	0	0	0	0	0	1	1	0	2
Senior management	0	0	0	0	0	0	7	9	0	0	16
Professional qualified and experienced specialists and mid-management	7	3	5	2	1	5	44	34	0	0	101
Skilled technical and academically qualified workers,junior management, supervisors, foremen and superintendents	7	5	7	18	16	5	52	12	0	0	122
Semi-skilled and discretionary decision making	27	14	2	48	38	7	22	2	0	0	160
Unskilled and defined decision making	6	0	0	0	0	0	0	0	0	0	6
TOTAL PERMANENT	47	22	14	68	55	17	125	58	1	0	407
Non-permanent employees	4	3	2	6	3	0	12	8	0	0	38
GRAND TOTAL	51	25	16	74	58	17	137	66	1	0	445

* A = African, C = Coloured, I = Indian, W = White

The identification of potential leaders and development of leadership and management skills is another strategic initiative that was identified and in addition to the existing management training, the executives and senior managers attended leadership workshops. This will be followed up by more interventions for the senior managers as well as other managers in 2009.

Skills Development

Various training components were presented in house over the last year as reflected in the schedule below:

Training programme attendance

Intervention	Number of staff attended
1. Management training	
• Performance management for managers modules 1 – 3	60
• HIV/Aids for managers	46
• Corrective Counselling and Positive Discipline	10
• Presentation Skills training	9
• Mentorship training	5
• Leadership training for senior managers	16
2. Customer Service and Culture	
• Telephone Etiquette and Skills	214
• Living the Brand workshops	31
3. Functional/Technical	
• Securities for Individuals and non Individuals	41
• Negotiation Skills	32
• National Credit Act (NCA)	48
• Deposits 1A	15
• Forex markets	20

Corporate governance (continued)

12. Transformation (continued)

Skills Development (continued)

Training programme attendance (continued)

Intervention	Number of staff attended
4. Systems	
• Microsoft Office	54
• User Application	34
5. Other	
• Financial Fitness	103
• Induction	51
• Substance Awareness	21
• First Aid/Health and Safety	60
• Change Management for MBL IT & Keystone	21
• Disciplinary Enquiries – Initiator and Chairperson training	11
• Teambuilding for Mentors and Mercantile Trainee Programme trainees	11
6. Various external training attended	96

Participation in the BANKSETA Learnership programme commenced in 2004 and another two groups of learners – graduates and matriculants were employed on a one year employment contract. The employment and retention of learners from previous programmes has been very successful.

The total spend on training for 2008 is ± R2.6 million. This represents 2.3% of payroll. A total amount of R0.7 million was spent on the training of black staff.

Corporate Social Investment

The Group is committed to the upliftment and transformation of communities and has developed a comprehensive framework for its Corporate Social Investment policy and plan. The implementation of this plan will commence as part of the conclusion of a BEE ownership transaction.

Procurement

A targeted procurement strategy to enhance BEE has been adopted. The objective is to actively promote the effective and efficient development and support of suppliers and contractors from historically disadvantaged South African enterprises. The principles are detailed in the Group's Procurement Policy.

Loan approval to black SMEs

Targets are in place aimed at identifying opportunities for loans to black SMEs.

Ownership and control

Discussions and negotiations with two short listed partners, regarding pricing and structure, for a proposed 10% BEE equity stake commenced during the year and are ongoing. Detailed information will be published as and when available.

13. Annual financial statements

Accounting policies and the basis of accounting on which annual financial statements are prepared, are set out on pages 12 to 21 of this report.

14. Regulation

The SARB, the Financial Services Board and the JSE regulate the various activities of the Group.

15. Communication with stakeholders

The Board communicates with its shareholders in accordance with the Companies Act and JSE Listings Requirements. Appropriate communication is also sent to the employees of the Bank from time to time. The Board has delegated authority to the CEO to speak to investment analysts from time to time. Communication with the SARB, the Registrar of Companies and the JSE is done in compliance with the respective laws/guidelines.

Corporate governance (continued)

Annexure A

Attendance of meetings by Directors

	Date appointed to Board	Board (joint meetings)	Board Committees: Group Audit	Risk and Capital Manage-ment	Directors' Affairs	Remune-ration	Trans-formation	Technology (constituted Feb 2006)^
Number of meetings held during the year under review		5§	4	4	4	4	4	7
Directors								
J A S de Andrade Campos	26.07.2002	#5/5	†	#4/4	#4/4	†	#**4/4	†
D J Brown	29.03.2004	5/5	†	4/4	†	†	4/4	7/7
G P de Kock	23.11.2000	5/5	4/4	4/4	4/4	#4/4	†	7/7
L Hyne	01.06.2003	5/5	#4/4	4/4	4/4	4/4	†	†
A T Ikalafeng	16.11.2004	5/5	*2/3	†	4/4	4/4	#**4/4	†
J P M Lopes	09.11.2005	5/5	†	4/4	†	†	†	7/7
T H Njikizana‡	06.11.2008	n/a	1/1	n/a	n/a	n/a	n/a	n/a
S Rapeti	29.07.2005	5/5	†	†	4/4	4/4	4/4	#7/7

† non-member of Committee/permanent invitee. The ad hoc attendance by a Director of a meeting he/she is not a member or permanent invitee of, is not disclosed

* Resigned from GAC effective 6 November 2008

** J A S de Andrade Campos resigned as Chairman of the Transformation Committee effective 31 October 2008 and A T Ikalafeng was appointed Chairman of the Transformation Committee in his stead

‡ Was appointed to the Board, the GAC and Directors' Affairs Committee effective 6 November 2008. T H Njikizana attended the last Board meeting of the year as an invitee

\# chairman of meeting

§ one of which was a two day Strategy Board meeting

^ Board Committee of the Bank. All other Board Committees of the Company were also fulfilling the role of such for the Bank

Bank Regulations public disclosure

The December 2008 bi-annual disclosure required in terms of Regulation 43 of the Bank Regulations is published on the Group's website.

Analysis of shareholders

at 31 December 2008

SHAREHOLDERS' SPREAD

	2008	2007
Number of public shareholders	**6 402**	6 962

Percentage of shares held by:

	2008 Number	2008 %	2007 Number	2007 %
Public	**296 985 329**	**7.54**	311 342 829	7.91
Non-public	**3 641 933 195**	**92.46**	3 627 575 695	92.09
Directors	**–**	**–**	–	–
Employees	**110 600**	**0.003**	1 177 000	0.03
Trustees of share incentive scheme	**27 804 400**	**0.71**	12 380 500	0.31
Holders of 10% or more of shares	**3 614 018 195**	**91.75**	3 614 018 195	91.75
	3 938 918 524	**100.0**	3 938 918 524	100.0

MAJOR SHAREHOLDERS HOLDING IN EXCESS OF 5% OF THE COMPANY'S SHARE CAPITAL

	Number of shares	%
2008		
Caixa Geral de Depósitos SA	**3 614 018 195**	**91.75**
2007		
Caixa Geral de Depósitos SA	3 614 018 195	91.75

PERFORMANCE ON THE JSE DURING THE YEAR

	2008	2007
Number of shares issued	**3 938 918 524**	3 938 918 524
Share price (cents)		
Year-end	**28**	35
Highest	**38**	38
Lowest	**21**	25
Number of shares traded	**106 408 606**	255 239 004
Value of shares traded (R'000)	**31 946**	84 753
Average price (cents)	**30**	33
Market capitalisation (R'000)	**1 095 112**	1 374 288

Group addresses

Mercantile Bank Group

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142 West Street, Sandown, 2196
PO Box 782699, Sandton, 2146
Tel: +27 11 302 0300
Fax: +27 11 883 7765

Mercantile Insurance Brokers

Head Office

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Tel: +27 11 302 0556/7/8
Fax: +27 11 302 0752

Mercantile Bank Branches

Boksburg Branch

North Atlas Centre, cnr Atlas and
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Tel: +27 11 918 5276
Fax: +27 11 918 4159

Bruma Branch

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Tel: +27 11 622 0916
Fax: +27 11 622 8833

Cape Town City Branch

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Tel: +27 21 419 9402
Fax: +27 21 419 5929

Cape Town Tygerberg Branch

Ground Floor, Tygerpoort Building
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PO Box 5436, Tygervalley, 7536
Tel: +27 21 910 0161
Fax: +27 21 910 0163

Comaro Crossing Branch

Shop FF9, Comaro Crossing
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PO Box 31558, Braamfontein, 2017
Tel: +27 11 435 0640
Fax: + 27 11 435 1586

Durban Branch

Cowey Shopping Centre
123 Cowey Road
Berea, Durban, 4001
PO Box 519, Durban 4000
Tel: +27 31 209 9048
Fax: +27 31 209 9446

Germiston Branch

The Lake Shopping Centre
cnr William Hill and Lake Street
Germiston, 1401
PO Box 31558, Braamfontein, 2017
Tel: +27 11 824 5813
Fax: +27 11 824 5823

Horizon Branch

153 Ontdekkers Road, Horizon, 1730
PO Box 31558, Braamfontein, 2017
Tel: +27 11 763 6000
Fax: +27 11 763 8742

Pretoria Hatfield Branch

Pro-Equity Court, cnr Pretorius and
Gordon Street, Hatfield, Pretoria, 0083
PO Box 31558, Braamfontein, 2017
Tel: +27 12 342 1151
Fax: +27 12 342 1191

Pretoria West Branch

477 Mitchell Street
Pretoria West, 0183
PO Box 31558, Braamfontein, 2017
Tel: +27 12 327 4671
Fax: +27 12 327 4645

Sandton Branch

Ground Floor, 142 West Street
Sandown, 2196
PO Box 31558, Braamfontein, 2017
Tel: +27 11 302 0763
Fax: +27 11 884 1821

Strijdompark Branch

Shop 2, Homeworld Centre
cnr Malibongwe Drive and CR Swart
Road, Strijdom Park, Randburg, 2194
PO Box 31558, Braamfontein, 2017
Tel: +27 11 791 0854
Fax: +27 11 791 2387

Troyeville Branch

77 Bezuidenhout Street
Bertrams, 2094
PO Box 31558, Braamfontein, 2017
Tel: +27 11 624 1450
Fax: +27 11 614 9611

Vanderbijlpark Branch

Shops 1 and 2, Russell's Building
54 President Kruger Street
Vanderbijlpark, 1911
PO Box 31558, Braamfontein, 2017
Tel: +27 16 981 4132
Fax: +27 16 981 0767

Welkom Branch

Tulbagh House, 11 Tulbagh Street
Welkom, 9459
PO Box 2207, Welkom, 9460
Tel: +27 57 357 3142
Fax: +27 57 352 7879

Notice of Annual General Meeting

Mercantile Bank
Holdings Limited
Member of CGD Group

(Registration number 1989/000164/06)
(Incorporated in the Republic of South Africa)
Share code: MTL ISIN: ZAE000064721
("Mercantile" or "the Company")

Notice is hereby given that an Annual General Meeting ("the meeting") of the shareholders of the Company will be held at 12:30 on Thursday, 28 May 2009 in the Boardroom, First Floor, Mercantile Bank, 142 West Street, Sandown, Sandton for the following purposes:

ORDINARY RESOLUTIONS

1. ADOPTION OF ANNUAL FINANCIAL STATEMENTS

To receive and adopt the annual financial statements of the Company and of the Mercantile Group for the year ended 31 December 2008.

Explanatory note:

At the Annual General Meeting the Directors must present the audited annual financial statements for the year ended 31 December 2008 to shareholders together with the reports of the Directors and auditors as contained in the 2008 Annual Report.

2. NON-EXECUTIVE DIRECTORS' REMUNERATION

To approve and ratify the proposed fees payable on a monthly basis to the non-executive Directors of the Mercantile Group from time to time for the period 1 April 2009 to 31 March 2010 for serving as a Director on the Board and Board Committees.

2.1 Chairman of the Mercantile Board: R1 380 000 per annum

2.2 Director of the Mercantile Board: R189 000 per annum

2.3 Director of Mercantile Bank Limited ("the Bank"), the major subsidiary of the Company: R41 000 per annum

2.4 Chairman of the Group Audit Committee: R75 000 per annum

2.5 Member of the Group Audit Committee: R58 000 per annum

2.6 Chairman of the Remuneration Committee: R50 000 per annum

2.7 Member of the Remuneration Committee: R58 000 per annum

2.8 Member of the Risk and Capital Management Committee: R58 000 per annum

2.9 Chairman of the Transformation Committee: R50 000 per annum

2.10 Member of the Transformation Committee: R58 000 per annum

2.11 Member of the Directors' Affairs Committee: R58 000 per annum

2.12 Chairman of the Technology Committee (Committee of the Bank): R50 000 per annum

2.13 Member of the Technology Committee (Committee of the Bank): R58 000 per annum

Notice of Annual General Meeting (continued)

2.14 Chairmen of the Risk and Capital Management Committee and Directors' Affairs Committee if the Chairman of the Board is not the Chairman of these Committees: R50 000 per annum for each chairmanship.

Explanatory note:

Shareholders are requested to approve the remuneration payable to non-executive Directors for serving on the Boards and Board Committees of the Company and the Bank. The Chairman of the Mercantile Board's fee includes remuneration for the Chairman's participation on other Boards and Board Committees. The Board members' total fees are dependent on their participation on Board Committees. Refer to Annexure A on page 83 for the Board and Board Composition as at 31 December 2008.

3. RE-ELECTION OF DIRECTORS RETIRING BY ROTATION

To re-elect by way of separate resolutions Directors in the place of those retiring in accordance with the Company's articles of association. The Directors retiring are:

A T Ikalafeng (appointed 16 November 2004)

T H Njikizana (appointed 6 November 2008)

J P M Lopes (appointed 9 November 2008 on a three year contract which expired and which the Board renewed for a further three years)

and being eligible offer themselves for re-election.

An abbreviated curriculum vitae of each Director offering themselves for re-election is contained on page 91 of the Annual Report.

Explanatory note:

In accordance with the articles of association of the Company one-third of the Directors is required to retire at each meeting and may offer themselves for re-election. In terms of the articles of association of the Company the Managing Director, during the period of his service contract, is not taken into account when determining which Directors are to retire by rotation.

4. RE-APPOINTMENT OF CEO ON EXPIRY OF SERVICE CONTRACT

To confirm, approve and ratify the re-appointment of the executive director, D J Brown as the Chief Executive Officer of the Mercantile Group with effect from 29 March 2009.

Explanatory note:

In terms of the articles of association of the Company the Managing Director, during the period of his service contract, is not taken into account when determining which Directors are to retire by rotation. The Managing Director of Mercantile Group had a five year service agreement which expired on 30 March 2009 and the Board of Mercantile at its meeting held on 31 October 2008 approved the renewal of the Managing Director's service contract upon expiry for a further three years. As communicated to shareholders on SENS on 31 October 2008 shareholders are being asked to confirm and approve the re-appointment of the Managing Director.

5. AUDITORS

To recommend the re-appointment of Deloitte & Touche as independent auditors of the Company.

Explanatory note:

Deloitte & Touche has indicated their willingness to continue as the Company's auditors until the next Annual General Meeting. The Group Audit Committee has satisfied itself as to the independence of Deloitte & Touche. The Group Audit Committee has the power in terms of the SA Corporate Laws Amendment Act, 2006 to approve the remuneration of the external auditors. The remuneration and non-audit fees paid to the auditors during the year ended 31 December 2008 are contained on page 49.

As special business and requiring shareholder approval, shareholders are requested to consider and if deemed fit, pass with or without modification the following resolutions numbers 6, 7, 8, 9 and 10.

Notice of Annual General Meeting (continued)

6. AMENDMENT TO ARTICLES OF ASSOCIATION – SPECIAL RESOLUTION

"RESOLVED as a special resolution that the articles of association of the Company be and are hereby amended, with or without modification:

1. the deletion of existing article 46 and the insertion in its stead of the following new article 46:

   "Until otherwise determined by the meeting of members, the number of directors shall not be less than 5 (five) nor more than 20 (twenty) but not more than 49 (forty nine per centum), rounded off to the next lower integral number of the directors shall be employees of the Company or any of its subsidiaries, or of the Company's controlling company or of any of such controlling company's subsidiaries."

2. the deletion of "at no time be more than one-third of the number of directors in office" in article 65 thereof and the insertion in its stead of "always comply with article 46.""

The reason for that part of the special resolution contained in parts 1 and 2 thereof is to align the provisions of the articles to that of the Banks Act 94 of 1990 as amended.

The effect of the special resolution is to amend the Company's articles of association so as to provide for these matters.

7. CONTROL OF AUTHORISED BUT UNISSUED SHARES

"RESOLVED as an ordinary resolution that all the unissued shares in the authorised share capital of the Company be and are hereby placed under the control of the Directors of the Company, who are authorised to allot and issue the same to such persons and on such terms and conditions as they may determine in their sole and absolute discretion, subject to the provisions of the Companies Act, No. 61 of 1973 (as amended), the provisions of the Banks Act, No. 94 of 1990 (as amended) and the Listings Requirements of JSE Limited."

The approval is given in the form of a general authority and accordingly:

– is only valid until the next Annual General Meeting of the Company; and

– may be varied or revoked by any General Meeting of the Company prior to such Annual General Meeting.

8. GENERAL AUTHORITY TO ISSUE SHARES FOR CASH

"RESOLVED that the Directors be given the general authority to issue unissued shares of a class already in issue held under their control, for cash, when the Directors consider it appropriate in the circumstances, subject to the provisions of the Companies Act, No. 61 of 1973 (as amended), the provisions of the Banks Act, No. 94 of 1990 (as amended), the Listings Requirements of JSE Limited and to the following limitations, that:

- the authority shall be valid until the next Annual General Meeting of the Company (provided it shall not extend beyond 15 months from the date of this resolution);
- a paid press announcement giving full details, including the impact on net asset value, net tangible asset value, earnings and headline earnings per share, will be published at the time of any issue representing, on a cumulative basis within one financial year, 5% or more of the number of shares in issue prior to such issue;

– issues for cash in any one financial year may not exceed 15% of the Company's issued share capital;

– the issues must be made to public shareholders as defined by the Listings Requirements of JSE Limited; and

– in determining the price at which an issue of shares may be made in terms of this authority, the maximum discount permitted will be 10% of the volume weighted average traded price as determined over the 30 business days prior to the date that the price of the issue is determined or agreed by the Directors of the Company."

The approval of a 75% majority of the votes cast by shareholders present or represented by proxy at this meeting is required for this resolution to become effective.

9. LONG TERM INCENTIVE SCHEME: CONDITIONAL SHARE PLAN – AMENDMENTS TO RULES

"RESOLVED as an ordinary resolution that the amendments to the Mercantile Bank Holdings Limited Conditional Share Plan, substantially in the form tabled at the meeting at which this resolution will be proposed and considered and initialled by the Chairman of the meeting for the purposes of identification, be hereby approved and adopted by the Company with immediate effect."

Notice of Annual General Meeting (continued)

The approval of a 75% majority of the votes cast by shareholders present or represented by proxy at this meeting is required for this resolution to become effective.

Explanatory note:

The amendments to the rules of the Mercantile Bank Holdings Limited Conditional Share Plan are available for inspection at the registered office of the Company. The detail of the address is on page 3. Shareholders can contact the Company Secretary to make an arrangement to do so.

The salient features of the amendments to the Mercantile Bank Holdings Limited Conditional Share Plan follows:

To comply with the recent amendments to the JSE Limited Listings Requirements ("JSE") certain changes to the Conditional Share Plan rules are being proposed. These mainly relate to the scheme limit where the JSE requires that the scheme must provide, in the event of a sub-division or consolidation of securities for an adjustment to the number of equity securities that may be utilised for purposes of the scheme and ensuring that rolling over (meaning allowing equity securities which have already vested and been issued in terms of the scheme usually reverts back to the scheme) is prohibited.

10. LONG TERM INCENTIVE SCHEME: TRUST DEED CONSTITUTING THE MERCANTILE SHARE INCENTIVE SCHEME – AMENDMENTS

"RESOLVED as an ordinary resolution that the amendments of the Trust Deed constituting the Mercantile Share Incentive Scheme in the manner set out in the agreement between the trustees and the Company substantially in the form tabled at the meeting, and initialled by the Chairman for purposes of identification, be and is hereby approved."

The approval of a 75% majority of the votes cast by shareholders present or represented by proxy at this meeting is required for this resolution to become effective.

Explanatory note:

The proposed amendments to the Trust Deed are available for inspection at the registered office of the Company. The detail of the address is on page 3. Shareholders can contact the Company Secretary to make an arrangement to do so.

To comply with the amendments to the JSE certain changes to the Trust Deed constituting the Mercantile Share Incentive Scheme are being proposed. These changes mainly relate to ensuring that the Trust Deed contains rules for the treatment of securities (vested or unvested) in instances of mergers or takeovers.

There were no grants made under this scheme during the 2008 financial year and it is not the Board's intention to make any grants under this scheme in the next few years. However, the Board has discretion to make grants under this scheme.

11. SIGNATURE OF DOCUMENTS

"RESOLVED that any one Director or the Company Secretary of the Company be and is hereby authorised to do all such things and sign all documents and take all such action as they consider necessary to implement the resolutions set out in the notice convening this Annual General Meeting at which this ordinary resolution will be considered."

VOTING AND PROXIES

A member entitled to attend, speak and vote at this meeting is entitled to appoint a proxy (who need not be a member of the Company) to attend, vote and speak in his/her stead.

Members which are companies or other body corporates, may, in terms of section 188 (1) of the Companies Act, No. 61 of 1973 (as amended), by resolution of their Directors or other governing body, authorise any person to act as its representative at the meeting.

Certificated shareholders and own-name dematerialised shareholders, who are unable to attend this meeting but wish to be represented thereat, must complete and return the attached form of proxy in accordance with the instructions contained therein. A form of proxy is attached for this purpose and must be lodged at the Company's transfer secretaries or the Company's registered address by no later than 12:30 on Tuesday, 26 May 2009. The detail of these addresses are on page 3.

Notice of Annual General Meeting (continued)

Dematerialised shareholders, excluding own-name dematerialised shareholders, who wish to attend this meeting, must request their Central Securities Depository Participant ("CSDP") or broker to provide them with a Letter of Representation or must instruct their CSDP or broker to vote by proxy on their behalf in terms of the agreement entered into between the shareholder and their CSDP or broker.

By order of the Board

Ms R van Rensburg
Company Secretary

Sandton
6 March 2009

Registered office

First Floor
Mercantile Bank
142 West Street
Sandown, 2196
(P O Box 782699, Sandton, 2146)

Transfer Secretaries

Computershare Investor Services (Proprietary) Limited
Ground Floor
70 Marshall Street
Johannesburg 2001
(P O Box 61051, Marshalltown, 2107)

Brief *curriculum vitae* of each Director standing for re-election or re-appointment

A T Ikalafeng, age 42, holds a BSc degree and MBA degree from Marquette University in the USA, Certificate in Finance from Wits, and a CM(SA). He has held various marketing positions in the USA and Africa. He is founder and managing director of the multi-disciplinary branding consultancy called "The Brand Leadership Group." He is non-executive director at Foodcorp (Pty) Limited and a member of the Vega School of Brand Communications and Durban University of Technology advisory councils.

T H Njikizana, age 33, has over 14 years experience in public practice as a qualified CA (SA) and Registered Auditor. He trained with Coopers & Lybrand and after qualifying as a Chartered Accountant also had experience with Ernst & Young and Andersen internationally. Tapiwa's professional career includes experience in Africa (Zimbabwe, Botswana and South Africa) and international experience in the United Kingdom and the Republic of Ireland. Until 2007 T H Njikizana was the Technical Partner at South Africa's largest black owned audit and professional services firm. He is co-principal of W.Consulting which offers training and consulting services across Africa, the United Kingdom and Australia.
T H Njikizana is involved in many aspects affecting the accounting profession and is a member of the Association for the Advancement of Black Accountants in Southern Africa, as well as sitting on various SAICA committees including the Accounting Practices Committee since 2007. In 2007 T H Njikizana served as a member of the GAAP Monitoring Panel of the Johannesburg Securities Exchange ("JSE").

J P M Lopes, age 43, holds a Degree in Law from the Lusiada University of Lisbon and a Certificate in Corporate Finance from the London School of Business. He has been employed by CGD since 1991 and spent a number of years in London where he successfully managed the Derivative Products and Structured Products. His most recent appointment was Managing Director of Banco Interatlântico, which is an affiliated bank of CGD operating in the Republic of Cape Verde, focusing on Corporate Banking, Trade Financing and Private Banking.

D J Brown, age 54, holds a BComm Degree from the University of South Africa and an MBA from the University of Cape Town. In addition, he attended the Management Development Programme at the School of Business Leadership and the Advanced Management Program at Harvard Business School in the USA. DJ Brown spent 30 years with the Standard Bank Group where he held various senior positions including Managing Director of Stanbic Bank Botswana, Managing Director of Stanbic Bank Zambia, Managing Director of Stannic Asset Finance and Managing Director of Standard Bank Commercial Banking Division. Since 2004 D J Brown has been employed as CEO of Mercantile Bank.

Notes

Designed by motiv
Printed by ince

Form of proxy

Mercantile Bank Holdings Limited
Member of CGD Group
(Registration number 1989/000164/06)
(Incorporated in the Republic of South Africa)
Share code: MTL ISIN: ZAE000064721
("the Company")

for use by certificated and own-name dematerialised ordinary shareholders at the Annual General Meeting of the Company to be held at 12:30 on Thursday, 28 May 2009 ("the meeting") in the Boardroom, First Floor, Mercantile Bank, 142 West Street, Sandown, Sandton.

I/We (please print) full name/(s) ____________________

of (please print) address ____________________

being (a) member(s) of the Company, holding ________ ordinary shares in the Company, hereby appoint:

1. ____________________ or failing him/her

2. ____________________ or failing him/her

3. the Chairman of the meeting

as my/our proxy to attend, speak and vote on my/our behalf at the Annual General Meeting to be held at the registered office of the Company, in Sandton, on Thursday, 28 May 2009 at 12:30 and at any adjournment thereof, and to vote or abstain from voting on the ordinary resolutions to be proposed at the meeting, as follows:

Resolutions	For	Against	Abstain
1. Ordinary resolution number 1: Adoption of annual financial statements			
2. Ordinary resolution number 2: Non-executive Directors' remuneration			
3. Re-election of Directors			
3.1 Ordinary resolution number 3: A T Ikalafeng			
3.2 Ordinary resolution number 4: T H Njikizana			
3.3 Ordinary resolution number 5: J P M Lopes			
4. Ordinary resolution number 6: D J Brown			
5. Ordinary resolution number 7: Re-appointment of auditors			
6. Special resolution number 1: Amendments to articles of association.			
7. Ordinary resolution number 8: Control of authorised but unissued shares			
8. Ordinary resolution number 9: General authority to issue shares for cash			
9. Ordinary resolution number 10: Long term incentive scheme: Conditional Share Plan – amendments to rules			
10. Ordinary resolution number 11: Mercantile Share Incentive Trust Deed amendments			
11. Ordinary resolution number 12: Signature of documents			

Signed this ________ day of ________ 2009

Signature of member(s) ____________________

Assisted by me (where applicable) ____________________

Please read the notes and instructions on the reverse hereof.

Form of proxy (continued)

Notes:

1. A member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend, speak and vote in his/her stead. A proxy need not be a member of the Company.
2. Every person present and entitled to vote at the meeting as a member or as a proxy or as a representative of a body corporate shall, on a show of hands, have one vote only, irrespective of the number of shares such person holds or represents, but in the event of a poll, a member shall be entitled to that proportion of the total votes in the Company which the aggregate amount of the nominal value of the shares held by him/her/it bears to the aggregate amount of the nominal value of all the shares issued by the Company. It is the intention of the Company to request for a vote on a poll.
3. Please insert the relevant number of shares/votes in the appropriate spaces on the face hereof and how you wish your votes to be cast. If you return this form of proxy duly signed without any specific directions, the proxy will vote or abstain from voting at his/her/its discretion.

Instructions on signing and lodging this form of proxy:

1. A deletion of any printed matter and the completion of any blank spaces need not be signed or initialled. Any alteration or correction must be initialled by the authorised signatory/ies.
2. The Chairman shall be entitled to decline or accept the authority of a person signing this form of proxy:

   (a) under a power of attorney; or

   (b) on behalf of a company,

   unless that person's power of attorney or authority is deposited at the registered office of the Company not later than 12:30 on Tuesday, 26 May 2009.
3. You may insert the name of any person(s) whom you wish to appoint as your proxy in the blank space(s) provided for that purpose.
4. When there are joint holders of shares, all joint shareholders must sign this form of proxy.
5. The completion and lodging of this form of proxy will not preclude the member who grants this proxy from attending the meeting and speaking and voting in person thereat to the exclusion of any proxy appointed in terms hereof should such member wish to do so.
6. Documentary evidence establishing the authority of a person signing this form of proxy in a representative capacity must be attached to this form of proxy, unless previously recorded by the transfer secretaries of the Company or waived by the Chairman of the meeting. The Chairman of the meeting may reject any form of proxy not completed and/or received in accordance with these notes and/or instructions, or with the Articles of Association of the Company.
7. Completed forms of proxy should be returned to the registered office, First Floor, Mercantile Bank, 142 West Street, Sandown, 2196 (PO Box 782699, Sandton, 2146) or faxed to the Company Secretary (fax number +27 11 883-7765) or faxed to the transfer secretaries (fax number +27 11 688 5238) by no later than 12:30 on Tuesday, 26 May 2009.

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Mercantile Bank
Holdings Limited
Member of CGD Group

142 West Street, Sandown, 2196, South Africa
Tel +27 (0)11 302 0300, Fax +27 (0)11 302 0729