Mercantile Bank
Holdings Limited
Member of CGD Group

Annual Report **2010**

your bank, your partner, our focus

Mercantile Bank Holdings Limited

Reg No: 1989/000164/06
Member of CGD Group

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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 business, 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 (Pty) 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
Banks Act	Banks Act, No. 94 of 1990, as amended
Bank Regulations	Regulations relating to banks issued under section 90 of the 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
CPA	Consumer Protection Act, No. 68 of 2008
CREDCOM	Credit Committee
DAC	Directors' Affairs Committee
EXCO	Executive Committee
FAIS	The Financial Advisory and Intermediary Services Act, No. 37 of 2002
FICA	The Financial Intelligence Centre Act, No. 38 of 2001
FSC	Financial Sector Charter
GAC	Group Audit Committee
HLAMDA	Home Loan and Mortgage Disclosure Act, Act No. 63 of 2000
IFRS	International Financial Reporting Standards and Interpretations
JSE	JSE Limited
King II	King Report on Corporate Governance for South Africa 2002
King III	King Report on Corporate Governance for South Africa 2009
Mercantile	Mercantile Bank Holdings Limited and its subsidiaries
NCA	The National Credit Act, No. 34 of 2005
OHSA	Occupational Health and Safety Act, No 85 of 1993
RMC	Risk and Capital Management Committee
ROA	Return on average assets
ROE	Return on average equity
SABRIC	South African Banking Risk Information Centre
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 2011

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 °	
K R Kumbier #	(appointed 1 June 2010)
J P M Lopes *#	
T H Njikizana ^°	

* Portuguese

^ Zimbabwean

\# Executive

° Independent non-executive

Administration

Group Secretary
A de Villiers
(appointed 1 January 2010)

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

Five year Group salient features

Years ended 31 December

	2010	2009	2008	2007	2006
	R'000	R'000	R'000	R'000	R'000
Statement of financial position					
Total assets	**6 254 311**	5 818 734	5 916 775	4 705 784	4 449 218
Loans and advances	**3 720 907**	3 629 574	3 403 789	2 814 743	2 066 432
Cash and cash equivalents	**1 759 897**	1 400 937	1 464 959	1 252 376	1 683 974
Shareholders' equity	**1 539 394**	1 437 671	1 269 030	839 914	667 418
Deposits	**4 563 988**	4 246 598	4 389 347	3 768 183	3 539 147
Statement of comprehensive income					
Profit before tax	**144 071**	217 069	257 798	165 302	100 643
Profit after tax	**101 026**	162 202	419 973	165 273	100 643
Headline earnings	**100 269**	160 851	410 107	159 684	100 643
Financial performance ratios (%)					
(No tax was raised in 2006 and 2007 as the Group deemed it appropriate to recognise deferred tax for the first time in 2008, mainly in respect of tax losses incurred in the financial years prior to 2005.)					
ROE	**6.8**	12.0	39.8	21.9	16.5
ROA	**1.7**	2.8	7.9	3.6	2.6
Cost to income	**65.5**	52.7	49.0	56.4	71.7
Share statistics (cents)					
Earnings per ordinary share	**2.6**	4.1	10.7	4.2	2.6
Headline earnings per ordinary share	**2.6**	4.1	10.5	4.1	2.6
Net asset value per share	**39.4**	36.8	32.4	21.4	17.0
Tangible net asset value per share	**33.6**	32.4	30.5	20.8	16.7

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 117th largest banking institution by assets in a current issue of "The Banker's Almanac". Its short- and long-term 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	A	March 2010	Negative
Moody's*	P-1	A1	July 2010	Stable
Standard & Poor's	A-2	A –	April 2010	Negative

* On 21 December 2010 Moody's placed CGD on ratings review for a possible downgrade.

Moody's confirmed the following RSA national scale issuer ratings of the Bank on 11 June 2010:

Short term	P-1.za
Long term	A2.za
Outlook	On ratings review for possible downgrade based on Moody's review of CGD's stand alone rating (see above*).

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, mobile and payment products.

Financial overview

Against the background of continued uncertainty in economic conditions both internationally and domestically, the Group experienced a tough trading environment in 2010 with headline earnings declining for the year under review by 37.7%, mainly due to:

- the negative endowment effect resulting from the lower interest rate environment in South Africa and the Group's high level of unleveraged capital. The Group's capital adequacy ratio as at 31 December 2010 was 23.5% (2009: 26.3%);
- the termination by Woolworths Financial Services (WFS) of its card processing agreement in October 2009 following the sale by WFS of a controlling interest in its financial services business;
- the increase in the Group's cost base following the implementation of the new core banking system in April 2010. The increased amortisation and depreciation charge year on year amounted to R14.5 million; and
- the general lower level of business activity experienced, in line with depressed national economic activity and broad industry trends.

Notwithstanding the difficult market conditions, the quality of the Group's lending portfolio remained sound with a net charge for credit losses as a percentage of gross loans and advances of 0.1% (2009:0.3%).

Cost to income increased from 52.7% for the year ended 31 December 2009 to 65.5% for the year ended 31 December 2010 whilst both ROE at 6.8% (December 2009: 12.0%) and ROA at 1.7% (December 2009: 2.8%) declined reflecting the weaker market conditions and lower earnings of the Group.

Directorate and Company Secretary

Mr K R Kumbier was appointed as Executive Director: Finance and Business with effect from 1 June 2010 and Ms S Rapeti, a non-executive director, resigned with effect from 29 July 2010.

Ms A de Villiers was appointed as Company Secretary with effect from 1 January 2010.

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 owned businesses and the diversity of the Group's Board. Whilst reasonable progress has been made in respect of employment equity targets, these remain challenging, particularly in the area of senior management, and the Group is behind in terms of achieving these targets, with various initiatives in place to rectify over time.

The SENS announcement dated 5 October 2010 advised that discussions with the short-listed candidates for the sale of 10% of the Group's equity were terminated based on the prevailing uncertain international market conditions. No further developments have taken place since then in this regard, but the Group remains committed to empowerment at shareholder level.

New Banking System

The Group's new core banking system was successfully implemented in April 2010 at a cost of R242 million. The new platform is expected to enhance the Group's competitiveness in the market and support achievement of the Group's strategic objectives, as it provides a more flexible and integrated environment enhancing risk management, controls, product capabilities and service offerings. No profits can be directly attributed to the systems replacement but the drivers outlined above are expected to provide a positive benefit to the Group over time.

Outlook

The policy stimulus measures implemented in international markets is supportive of an improved economic outlook for 2011 and the Group is confident of an improved performance going forward.

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, the JSE and our professional advisors for their sound guidance.

J A S de Andrade Campos
Chairman

24 February 2011

D J Brown
Chief Executive Officer

24 February 2011

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 fair presentation of 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 74, 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 2011

D J Brown
Chief Executive Officer

24 February 2011

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 2010 all such returns as are required of a public company in terms of the Companies Act, and that all such returns are true, correct and up to date.

A de Villiers
Company Secretary

24 February 2011

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 statement of financial position and the consolidated statement of financial position as at 31 December 2010, the statement of comprehensive income and the consolidated statement of comprehensive income, the statement of changes in equity and the consolidated statement of changes in equity and the statement of cash flows and the consolidated statement of cash flows for the year then ended, a summary of significant accounting policies and other explanatory notes as set out on pages 10 to 74.

Directors' responsibility for the financial statements

The Directors are responsible for the preparation and fair presentation of these financial statements in accordance with IFRS and in the manner required by the Companies Act of South Africa, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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 2010, and of their financial performance and their cash flows for the year then ended in accordance with IFRS, and in the manner required by the Companies Act of South Africa.

Deloitte & Touche
Registered Auditors

Per Riaan Eksteen
Partner

24 February 2011

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 Risk Advisory, NB Kader Tax & Legal Services, L Geeringh Consulting, L Bam Corporate Finance, JK Mazzocco Human Resources, CR Beukman Finance, TJ Brown Clients, NT Mtoba Chairman of the Board, MJ Comber Deputy Chairman of the Board

A full list of partners and directors is available on request

B-BBEE rating: Level 2 contributor/AAA (certified by Empowerdex)

Member of Deloitte Touche Tohmatsu Limited

Directors' report

for the year ended 31 December 2010

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 2010.

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 business, 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 74 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 (2009: 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 °
K R Kumbier # (appointed 1 June 2010)
J P M Lopes *#
T H Njikizana ^°
S Rapeti ° (resigned 29 July 2010)

* Portuguese, ^ Zimbabwean, # Executive,
° Independent non-executive

The Directors of the Company as at 24 February 2011 are shown on page 3.

The Company Secretary is A de Villiers and the registered addresses of the Company are:

Postal:	**Physical:**
PO Box 782699	1st Floor
Sandton	Mercantile Bank
2146	142 West Street
	Sandown
	2196

6. Dividends

No dividend was declared during the year under review (2009: nil).

7. Subsidiary companies and companies not consolidated

All subsidiary companies are incorporated in the Republic of 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 tax earned by subsidiaries amounted to R110.0 million (2009: R169.0 million) and aggregate losses amounted to R7.9 million (2009: R5.9 million).

Directors' report

for the year ended 31 December 2010 (continued)

7. Subsidiary companies and companies not consolidated (continued)

The principal consolidated subsidiary companies are as follows:

	Issued share capital R'000	Effective holding %	Nature of business^	Shares at cost 2010 R'000	Shares at cost 2009 R'000	Owing to subsidiaries 2010 R'000	Owing to subsidiaries 2009 R'000
Company name							
LSM (Troyeville) Properties (Pty) Limited	–	100	1	**140**	140	**–**	–
Mercantile Bank Limited	124 969	100	2	**1 485 448**	1 485 448	**12 757**	11 946
Mercantile Insurance Brokers (Pty) Limited	250	100	3	**294**	294	**–**	–
Portion 2 of Lot 2 Sandown (Pty) Limited	–	100	1	**8 832**	8 832	**–**	–

^ Nature of business

1 – Property holding 2 – Banking 3 – Insurance brokers

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

8. Going concern

The Directors in performing their assessment of the Group and Company's ability to continue as a going concern considered the approved operating budget for the next financial year as well as the cash flow forecast for the year ahead. The approved operating budget was reviewed and analysed based on the current developments in the market and operating model for the Group and the Company. The Directors believe the Group and the Company will have sufficient capital and cash resources to operate as a going concern in the year ahead.

9. Special resolutions

There were no special resolutions during the period under review.

10. Events after the reporting period

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 2010

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.

IFRSs which became effective in the current reporting period have had no impact on the Group.

2. Basis of consolidation

Subsidiaries are all 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 and 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 in the Group's statement of financial position 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 have 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 2010 (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 profit and loss.

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 in the statement of financial position. Derivative financial instruments are initially recorded at cost and are remeasured to fair value excluding transaction costs at each subsequent reporting date. Changes in the fair value of derivatives are recognised in profit and loss.

Derivatives in unlisted equity options where the underlying equity instruments do 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 less impairment.

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 profit and loss.

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 designated as financial assets 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, foreign banks and Money Market funds. 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 2010 (continued)

4. Financial instruments (continued)

4.2 Financial assets (continued)

Other investments

Investments consist of unlisted and listed equity investments. Other investments, which are an integral part of the Group's structured loan portfolio, are designated at fair value through profit and loss. All 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 other comprehensive income until the financial asset is sold, otherwise disposed of, or found to be impaired. At that time the cumulative gains or losses previously recognised in other comprehensive income are included in profit and loss.

Negotiable securities

Negotiable securities consist of government stock, treasury bills, debentures and promissory notes.

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 other comprehensive income until the financial asset is sold, otherwise disposed of, or found to be impaired. At that time the cumulative gains or losses previously recognised in other comprehensive income are included in 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 profit and loss. Variable rate loans and advances are designated as loans and receivables and are measured at amortised cost.

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

Other account receivables

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, tax 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 profit and loss.

4.4 Fair value estimation

The fair value of publicly traded derivatives, securities and investments is based on quoted market values at the reporting 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 reporting 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.

Accounting policies

for the year ended 31 December 2010 (continued)

4. Financial instruments (continued)

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 to maturity or the next market-based revaluation date to the current net carrying amount of the financial asset or financial liability.

4.6 Impairments

Specific impairments are made against identified financial assets. 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 assets. Both the specific and portfolio impairments raised during the year, less the recoveries of advances previously written off, are charged to profit and loss.

The recoverable amount is the sum of the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects the portfolio of advances' 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 through profit and loss 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 profit and loss.

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. All gains and losses on the sale of subsidiaries are recognised in profit and loss.

7. Associated companies

Associated companies are those companies in which the Group exercises significant influence, but have no 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's 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 statement of financial position at open-market fair value based on valuations by independent registered professional valuators at each reporting 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 profit and loss in the year in which they arise.

Accounting policies

for the year ended 31 December 2010 (continued)

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 statement of financial position at open-market fair value on the basis of their existing use at the date of revaluation, less any subsequent accumulated depreciation 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 other comprehensive income, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense. The increase is credited to profit and loss to the extent that an expense was previously charged to profit and loss. A decrease in the 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 reporting 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 profit and loss 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 for impairment where there are indicators of impairment, and adjusted if appropriate, at each reporting 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 or its 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 profit and loss. 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 programmes and the acquisition of software licences are recognised as intangible assets if they are expected to generate future economic benefits that exceed related costs beyond one year.

Accounting policies

for the year ended 31 December 2010 (continued)

10. Intangible assets (continued)

Computer software (continued)

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 any indication of impairment and is written down when the carrying amount exceeds the recoverable amount.

The recoverable amount is the higher of fair value less costs to sell or its 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 profit and loss.

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

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 within twelve months, the asset is available for immediate sale in its present condition and management is committed to the sale.

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. Tax

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

12.1 Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are neither taxable nor deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting date.

12.2 Deferred tax

Deferred tax 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 tax liabilities are generally recognised for all taxable temporary differences and deferred tax 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 tax 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 tax 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 tax assets is reviewed at each reporting 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 tax 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 reporting date. The measurement of deferred tax 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.

Accounting policies

for the year ended 31 December 2010 (continued)

12. Tax (continued)

12.2 Deferred tax (continued)

Deferred tax 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 tax authority and the Group intends to settle its current tax assets and liabilities on a net basis.

12.3 Current and deferred tax for the year

Current and deferred tax are recognised as an expense or income in profit or loss, except when they relate to items credited or debited to other comprehensive income, in which case the tax is recognised in other comprehensive income.

13. Instalment sales and leases

13.1 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 profit and loss 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.

13.2 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.

14. Interest income and interest expense

Except where interest is suspended, interest income and expense are recognised in profit and loss 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.

15. 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 right to receive payment has been established.

16. 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 profit and loss as accrued.

17. 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 profit and loss 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.

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 profit and loss immediately.

18. 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.

Accounting policies

for the year ended 31 December 2010 (continued)

18. Equity compensation plans (continued)

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.

19. 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.

19.1 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 profit and loss, 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 for 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.

19.2 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. The 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 the reported fair value of financial instruments.

19.3 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 deterioration in the financial health of the investee, industry and sector performance, changes in technology, operational and financing cash flows.

19.4 Income taxes

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

20. Recent accounting developments

There are new and revised standards and interpretations in issue that are not yet effective and there are no plans to early adopt. 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 of the following standards has not been assessed as at the date of authorisation of the annual financial statements:

Accounting policies

for the year ended 31 December 2010 (continued)

20. Recent accounting developments (continued)

- IFRS 9 Financial Instruments: Classification and measurement, issued during November 2009 and subsequent amendments in 2010, is effective for annual periods beginning on or after 1 January 2013. The Group will comply with the applicable standard from the year ending 31 December 2013;
- IAS 12 Income Taxes: Limited scope amendment (recovery of underlying assets), issued during December 2010 is effective for annual periods beginning on or after 1 January 2012. The Group will comply with the applicable standard from the year ending 31 December 2012; and
- IAS 24 Related-party Disclosures: Revised definition of related parties, issued during November 2009 is effective for annual periods beginning on or after 1 January 2011. The Group will comply with the applicable standard from the year ending 31 December 2011.

The following revised standards and interpretations which have been issued but which are not yet effective, will have no effect on the Group:

- IFRS 1 First-time Adoption of IFRS: Limited exemption from comparative IFRS 7 disclosures for first-time adopters, issued during January 2010 and effective for annual periods beginning on or after 1 July 2010;
- IFRS 1 First-time Adoption of IFRS: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 January 2011;
- IFRS 1 First-time Adoption of IFRS: Replacement of 'fixed dates' for certain exceptions with 'the date of transition to IFRSs', issued during December 2010 and effective for annual periods beginning on or after 1 July 2011;
- IFRS 1 First-time Adoption of IFRS: Additional exemption for entities ceasing to suffer from severe hyperinflation, issued during December 2010 and effective for annual periods beginning on or after 1 July 2011;
- IFRS 3 Business Combinations: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 July 2010;
- IFRS 7 Financial Instruments: Disclosures: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 January 2011;
- IFRS 7 Financial Instruments: Disclosures: Amendments enhancing disclosures about transfers of financial assets, issued during October 2010 and effective for annual periods beginning on or after 1 July 2011;
- IAS 1 Presentation of Financial Statements: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 January 2011;
- IAS 21 The Effects of Changes in Foreign Exchange Rates: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 July 2010;
- IAS 27 Consolidated and Separate Financial Statements: Amendments resulting from May 2010 annual Improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 July 2010;
- IAS 28 Investments in Associates: Amendments resulting from May 2010 annual Improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 July 2010;

Accounting policies

for the year ended 31 December 2010 (continued)

20. Recent accounting developments (continued)

- IAS 31 Interest in Joint Ventures: Amendments resulting from May 2010 annual Improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 July 2010;
- IAS 32 Financial Instruments: Presentation: Amendments relating to classification of rights issues, issued during 2009 is effective for annual periods beginning on or after 1 February 2010;
- IAS 34 Interim Financial Reporting: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 January 2011;
- IFRIC 13 Customer Loyalty Programmes: Amendments resulting from May 2010 annual improvements to IFRSs, issued during May 2010 and effective for annual periods beginning on or after 1 January 2011;
- IFRIC 14 IAS 19: The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction: Amendments with respect to voluntary prepaid contributions, issued during November 2009 and effective for annual periods beginning on or after 1 July 2011; and
- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments, issued during January 2009 and effective for annual periods beginning on or after 1 July 2010.

Statements of financial position

at 31 December 2010

		Group		Company	
		2010	2009	**2010**	2009
	Note	**R'000**	R'000	**R'000**	R'000
ASSETS					
Intangible assets	2	**224 402**	170 325	**–**	–
Property and equipment	3	**126 887**	131 483	**–**	–
Tax	4	**101**	256	**–**	256
Other accounts receivable	5	**49 021**	29 539	**7**	4
Interest in subsidiaries	6	**–**	–	**1 555 647**	1 454 312
Other investments	7	**10 969**	23 590	**29**	29
Deferred tax assets	8	**62 382**	102 936	**–**	–
Non-current assets held for sale	9	**–**	5 510	**–**	–
Loans and advances	10	**3 720 907**	3 629 574	**–**	–
Derivative financial instruments	11	**34 717**	21 406	**–**	–
Negotiable securities	12	**265 028**	267 902	**–**	–
Bank term deposits	13	**–**	35 276	**–**	–
Cash and cash equivalents	14	**1 759 897**	1 400 937	**223**	224
Total assets		**6 254 311**	5 818 734	**1 555 906**	1 454 825
EQUITY AND LIABILITIES					
Shareholders' equity		**1 539 394**	1 437 671	**1 555 892**	1 454 811
Share capital and share premium	15	**1 202 760**	1 202 571	**1 210 143**	1 210 143
Capital redemption reserve fund		**3 788**	3 788	**3 788**	3 788
Share-based payments reserve		**3 190**	1 894	**–**	–
General reserve		**7 478**	7 478	**–**	–
Property revaluation reserve		**54 547**	52 708	**–**	–
Available-for-sale reserve		**10 502**	13 883	**991 239**	889 094
Retained earnings/(Accumulated loss)		**257 129**	155 349	**(649 278)**	(648 214)
Liabilities		**4 714 917**	4 381 063	**14**	14
Deferred tax liabilities	8	**21 038**	18 870	**–**	–
Deposits	16	**4 563 988**	4 246 598	**–**	–
Derivative financial instruments	11	**28 122**	16 230	**–**	–
Provisions and other liabilities	17	**29 920**	38 142	**–**	–
Other accounts payable	19	**71 849**	61 153	**14**	14
Tax	4	**–**	70	**–**	–
Total equity and liabilities		**6 254 311**	5 818 734	**1 555 906**	1 454 825

Statements of comprehensive income

for the year ended 31 December 2010

		Group		Company	
		2010	2009	**2010**	2009
	Note	**R'000**	R'000	**R'000**	R'000
Interest income	21	**450 918**	529 584	**–**	–
Interest expenditure	22	**(194 558)**	(261 315)	**–**	–
Net interest income		**256 360**	268 269	**–**	–
Net charge for credit losses	10.4	**(3 422)**	(9 323)	**–**	–
Net interest income after credit losses		**252 938**	258 946	**–**	–
Net gain on disposal of available-for-sale investments		**885**	1 583	**–**	–
Net non-interest income		**168 485**	200 059	**–**	–
Non-interest income	23	**271 587**	287 909	**–**	–
Fee and commission expenditure	24	**(103 102)**	(87 850)	**–**	–
Net interest and non-interest income		**422 308**	460 588	**–**	–
Operating expenditure	25	**(278 804)**	(247 578)	**(1 064)**	(1 134)
Operating profit		**143 504**	213 010	**(1 064)**	(1 134)
Share of income from associated company		**567**	4 059	**–**	–
Profit/(Loss) before tax		**144 071**	217 069	**(1 064)**	(1 134)
Tax	26	**(43 045)**	(54 867)	**–**	256
Profit/(Loss) after tax		**101 026**	162 202	**(1 064)**	(878)
Other comprehensive (loss)/income					
Revaluation of owner-occupied properties		**2 554**	8 812	**–**	–
(Losses)/Gains on remeasurement to fair value		**(3 331)**	2 576	**102 145**	168 858
Release to profit and loss on disposal of available-for-sale financial assets		**(885)**	(1 583)	**–**	–
Tax relating to other comprehensive income/loss		**120**	(2 614)	**–**	–
Other comprehensive (loss)/income net of tax		**(1 542)**	7 191	**102 145**	168 858
Total comprehensive income		**99 484**	169 393	**101 081**	167 980
Profit after tax attributable to:					
Equity holders of the Group		**101 026**	162 202	**(1 064)**	(878)
Total comprehensive income attributable to:					
Equity holders of the Group		**99 484**	169 393	**101 081**	167 980
Earnings per ordinary share (cents)	27.1	**2.6**	4.1		
Diluted earnings per ordinary share (cents)	27.2	**2.6**	4.1		

Statements of changes in equity

for the year ended 31 December 2010

	Share capital and share premium R'000	Capital redemption reserve fund R'000	Share-based payments reserve R'000	General reserve R'000	Property revaluation reserve R'000	Available-for-sale reserve R'000	Retained earnings/ Accumulated loss R'000	Total R'000
Group								
Shareholders' equity at 1 January 2009	1 202 571	3 788	4 650	7 478	46 364	13 036	(8 857)	1 269 030
Net movement for the year	–	–	(2 756)	–	6 344	847	164 206	168 641
Profit after tax	–	–	–	–	–	–	162 202	162 202
Other comprehensive income	–	–	–	–	8 812	993	–	9 805
Tax relating to other comprehensive income	–	–	–	–	(2 468)	(146)	–	(2 614)
Share-based payments expense/(write back)	–	–	(2 756)	–	–	–	2 004	(752)
Shareholders' equity at 31 December 2009	**1 202 571**	**3 788**	**1 894**	**7 478**	**52 708**	**13 883**	**155 349**	**1 437 671**
Net movement for the year	**189**	**–**	**1 296**	**–**	**1 839**	**(3 381)**	**101 780**	**101 723**
Profit after tax	**–**	**–**	**–**	**–**	**–**	**–**	**101 026**	**101 026**
Other comprehensive income/(loss)	**–**	**–**	**–**	**–**	**2 554**	**(4 216)**	**–**	**(1 662)**
Tax relating to other comprehensive income/loss	**–**	**–**	**–**	**–**	**(715)**	**835**	**–**	**120**
Decrease of treasury shares held within the Group	**189**	**–**	**–**	**–**	**–**	**–**	**–**	**189**
Vesting of shares in the conditional share plan	**–**	**–**	**(104)**	**–**	**–**	**–**	**–**	**(104)**
Share-based payments expense	**–**	**–**	**1 400**	**–**	**–**	**–**	**754**	**2 154**
Shareholders' equity at 31 December 2010	**1 202 760**	**3 788**	**3 190**	**7 478**	**54 547**	**10 502**	**257 129**	**1 539 394**

Statements of changes in equity

for the year ended 31 December 2010 (continued)

	Share capital and share premium R'000	Capital redemption reserve fund R'000	Available-for-sale reserve R'000	Accumulated loss R'000	Total R'000
Company					
Shareholders' equity at 1 January 2009	1 210 143	3 788	720 236	(647 336)	1 286 831
Net movement for the year	–	–	168 858	(878)	167 980
Loss after tax	–	–	–	(878)	(878)
Other comprehensive income	–	–	168 858	–	168 858
Shareholders' equity at 31 December 2009	**1 210 143**	**3 788**	**889 094**	**(648 214)**	**1 454 811**
Net movement for the year	**–**	**–**	**102 145**	**(1 064)**	**101 081**
Loss after tax	**–**	**–**	**–**	**(1 064)**	**(1 064)**
Other comprehensive income	**–**	**–**	**102 145**	**–**	**102 145**
Shareholders' equity at 31 December 2010	**1 210 143**	**3 788**	**991 239**	**(649 278)**	**1 555 892**

Statements of cash flows

for the year ended 31 December 2010

		Group		Company	
	Note	**2010 R'000**	2009 R'000	**2010 R'000**	2009 R'000
Cash flows from operating activities					
Cash receipts from customers	28.1	**716 255**	767 387	**–**	–
Cash paid to customers, suppliers and employees	28.2	**(551 098)**	(591 002)	**(1 064)**	(1 134)
Cash generated from/(utilised in) operations	28.3	**165 157**	176 385	**(1 064)**	(1 134)
Dividends received		**348**	381	**–**	–
Tax (paid)/recovered	28.4	**(118)**	(211)	**256**	–
Net (increase)/decrease in income earning assets	28.5	**(53 431)**	35 506	**–**	–
Net increase/(decrease) in deposits and other accounts	28.6	**308 793**	(170 820)	**807**	1 134
Net cash inflow/(outflow) from operating activities		**420 749**	41 241	**(1)**	–
Cash flows from investing activities					
Purchase of intangible assets	2	**(74 896)**	(100 861)	**–**	–
Purchase of property and equipment	3	**(3 569)**	(3 528)	**–**	–
Acquisition of investments		**–**	(7 000)	**–**	–
Proceeds on sale of property and equipment		**–**	12	**–**	–
Proceeds on disposal of investments		**12 875**	2 055	**–**	–
Dividends received and capital repayment from associated company		**3 801**	4 059	**–**	–
Net cash (outflow) from investing activities		**(61 789)**	(105 263)		
Net cash inflow/(outflow) for the year		**358 960**	(64 022)	**(1)**	–
Cash and cash equivalents at the beginning of the year		**1 400 937**	1 464 959	**224**	224
Cash and cash equivalents at the end of the year	14	**1 759 897**	1 400 937	**223**	224

Notes to the annual financial statements

for the year ended 31 December 2010

1. Categories and fair values of financial instruments

1.1 Category analysis of financial instruments

	Group 2010 Fair value R'000	Group 2010 Carrying amount R'000	Group 2009 Fair value R'000	Group 2009 Carrying amount R'000
Assets				
Available-for-sale	**30 201**	**30 201**	34 923	34 923
Other investments	**10 969**	**10 969**	15 908	15 908
Negotiable securities – Government stock	**19 232**	**19 232**	19 015	19 015
Loans and receivables	**5 698 203**	**5 699 526**	5 215 509	5 215 720
Loans and advances				
– Current accounts	**617 914**	**617 914**	593 688	593 688
– Credit card	**14 249**	**14 249**	15 193	15 193
– Mortgage loans	**1 813 965**	**1 813 965**	1 705 368	1 705 368
– Instalment sales and leases	**263 906**	**263 906**	317 612	317 612
– Structured loans	**211 045**	**211 045**	247 715	247 715
– Other advances	**723 632**	**723 632**	621 249	621 249
Negotiable securities				
– Treasury bills	**214 435**	**215 758**	197 367	197 578
– Land Bank promissory notes	**30 038**	**30 038**	51 309	51 309
Bank term deposits	**–**	**–**	35 276	35 276
Cash and cash equivalents	**1 759 897**	**1 759 897**	1 400 937	1 400 937
Tax	**101**	**101**	256	256
Other accounts receivable	**49 021**	**49 021**	29 539	29 539
Designated at fair value through profit and loss	**76 196**	**76 196**	136 431	136 431
Loans and advances				
– Mortgage loans	**38 641**	**38 641**	40 130	40 130
– Instalment sales and leases	**66**	**66**	24 182	24 182
– Other advances	**37 489**	**37 489**	64 437	64 437
Other investments	**–**	**–**	7 682	7 682
Held-for-trading				
Derivative financial instruments	**34 717**	**34 717**	21 406	21 406
	5 839 317	**5 840 640**	5 408 269	5 408 480

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

1. Categories and fair values of financial instruments (continued)

1.1 Category analysis of financial instruments (continued)

	Group 2010		Group 2009	
	Fair value R'000	**Carrying amount R'000**	Fair value R'000	Carrying amount R'000
Liabilities				
Held-for-trading				
Derivative financial instruments	**28 122**	**28 122**	16 230	16 230
Amortised cost	**4 635 837**	**4 635 837**	4 307 821	4 307 821
Deposits	**4 563 988**	**4 563 988**	4 246 598	4 246 598
Tax	**–**	**–**	70	70
Other accounts payable	**71 849**	**71 849**	61 153	61 153
	4 663 959	**4 663 959**	4 324 051	4 324 051

	Company 2010		Company 2009	
	Fair value R'000	**Carrying amount R'000**	Fair value R'000	Carrying amount R'000
Assets				
Available-for-sale	**1 555 676**	**1 555 676**	1 454 341	1 454 341
Other investments	**29**	**29**	29	29
Interest in subsidiaries	**1 555 647**	**1 555 647**	1 454 312	1 454 312
Loans and receivables	**230**	**230**	484	484
Tax	**–**	**–**	256	256
Cash and cash equivalents	**223**	**223**	224	224
Other accounts receivable	**7**	**7**	4	4
	1 555 906	**1 555 906**	1 454 825	1 454 825
Liabilities				
Amortised cost				
Other accounts payable	**14**	**14**	14	14
	14	**14**	14	14

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

1. Categories and fair values of financial instruments (continued)

1.2 Valuation techniques and assumptions applied for the purpose of measuring fair value

- Cash and cash equivalents have short terms to maturity. For this reason, the carrying amounts at the reporting date approximate the fair values.
- Treasury bills and Land Bank promissory notes have short terms to maturity and are carried at amortised cost. Fair value is based on quoted market values at the reporting 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 publicly traded derivatives, securities and investments is based on quoted market values at the reporting 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 unlisted investments which are an integral part of the Group's structured loan portfolio are valued in terms of the shareholders' agreement conditions. 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.

1.3 Fair value measurements recognised in the statement of financial position

Financial instruments that are measured subsequent to initial recognition at fair value are grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

1. Categories and fair values of financial instruments (continued)

1.3 Fair value measurements recognised in the statement of financial position (continued)

	Group			
	Level 1 R'000	Level 2 R'000	Level 3 R'000	Total R'000
2010				
Assets				
Available-for-sale				
Other investments	**10 724**	**245**	**–**	**10 969**
Negotiable securities – Government stock	**19 232**	**–**	**–**	**19 232**
Designated at fair value through profit and loss				
Loans and advances				
– Mortgage loans	**–**	**38 641**	**–**	**38 641**
– Instalment sales and leases	**–**	**66**	**–**	**66**
– Other advances	**–**	**37 489**	**–**	**37 489**
Held-for-trading				
Derivative financial instruments	**34 717**	**–**	**–**	**34 717**
	64 673	**76 441**	**–**	**141 114**
Liabilities				
Held-for-trading				
Derivative financial instruments	**28 122**	**–**	**–**	**28 122**
	28 122	**–**	**–**	**28 122**
2009				
Assets				
Available-for-sale				
Other investments	15 637	271	–	15 908
Negotiable securities – Government stock	19 015	–	–	19 015
Designated at fair value through profit and loss				
Loans and advances				
– Mortgage loans	–	40 130	–	40 130
– Instalment sales and leases	–	24 182	–	24 182
– Other advances	–	64 437	–	64 437
Other investments	–	–	7 682	7 682
Held-for-trading				
Derivative financial instruments	21 406	–	–	21 406
	56 058	129 020	7 682	192 760
Liabilities				
Held-for-trading				
Derivative financial instruments	16 230	–	–	16 230
	16 230	–	–	16 230

There were no transfers between Level 1 and 2 during the year.

A Level 3 investment was disposed of during the year.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

1. Categories and fair values of financial instruments (continued)

1.3 Fair value measurements recognised in the statement of financial position (continued)

	Company			
	Level 1	**Level 2**	**Level 3**	**Total**
	R'000	**R'000**	**R'000**	**R'000**
2010				
Assets				
Available-for-sale				
Other investments	–	**29**	–	**29**
2009				
Assets				
Available-for-sale				
Other investments	–	29	–	29

1.4 Reconciliation of Level 3 fair value measurements of financial assets

	Group	
	2010	2009
	R'000	R'000
Designated at fair value through profit and loss		
Other investments – unlisted equities		
Balance at the beginning of the year	**7 682**	–
Acquisitions	–	7 000
Gains on remeasurement to fair value in comprehensive income	**2 032**	682
Realisation	**(9 714)**	–
Balance at the end of the year	–	7 682

2. Intangible assets

Computer software		
Cost at the beginning of the year	**221 805**	120 987
Additions	**74 896**	100 861
Net transfer from/(to) property and equipment*	**227**	(5)
Write-off of obsolete software	–	(38)
Cost at the end of the year	**296 928**	221 805
Accumulated amortisation and impairment losses at the beginning of the year	**(51 480)**	(44 093)
Amortisation	**(20 819)**	(7 428)
Net transfer(from)/to property and equipment*	**(227)**	3
Write-off of obsolete software	–	38
Accumulated amortisation and impairment losses at the end of the year	**(72 526)**	(51 480)
Net carrying amount at the end of the year	**224 402**	170 325

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

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

3. Property and equipment

	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							
2010							
Open market value/cost at the beginning of year	96 464	19 591	91 915	9 967	30 631	492	249 060
Revaluations	700	–	–	–	–	–	700
Additions	–	72	2 417	3	1 077	–	3 569
Transfer*	–	–	(227)	–	–	–	(227)
Write-off of obsolete assets	–	–	(27)	–	(23)	–	(50)
Disposals	–	–	–	(3)	–	–	(3)
Open market value/cost at the end of the year	97 164	19 663	94 078	9 967	31 685	492	253 049
Accumulated depreciation and impairment losses at the beginning of the year	–	(15 410)	(70 358)	(9 227)	(22 192)	(390)	(117 577)
Depreciation	(1 854)	(744)	(5 530)	(179)	(2 358)	(48)	(10 713)
Revaluation	1 854	–	–	–	–	–	1 854
Transfer*	–	–	227	–	–	–	227
Write-off of obsolete assets	–	–	21	–	23	–	44
Disposals	–	–	–	3	–	–	3
Accumulated depreciation and impairment losses at the end of the year	–	(16 154)	(75 640)	(9 403)	(24 527)	(438)	(126 162)
Net carrying amount at the end of the year	97 164	3 509	18 438	564	7 158	54	126 887

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

Notes to the annual financial statements

for the year ended 31 December 2010 (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							
2009							
Open market value/cost at the beginning of the year	89 364	18 917	93 989	9 341	27 321	415	239 347
Revaluations	7 100	–	–	–	–	–	7 100
Additions	–	674	428	48	2 301	77	3 528
Transfer*	–	–	(1 854)	583	1 276	–	5
Write-off of obsolete assets	–	–	(648)	(4)	(248)	–	(900)
Disposals	–	–	–	(1)	(19)	–	(20)
Open market value/cost at the end of the year	96 464	19 591	91 915	9 967	30 631	492	249 060
Accumulated depreciation and impairment losses at the beginning of the year	–	(14 620)	(68 613)	(8 422)	(18 676)	(344)	(110 675)
Depreciation	(1 712)	(790)	(4 247)	(242)	(2 468)	(46)	(9 505)
Revaluation	1 712	–	–	–	–	–	1 712
Transfer*	–	–	1 854	(568)	(1 289)	–	(3)
Write-off of obsolete assets	–	–	648	4	238	–	890
Disposals	–	–	–	1	3	–	4
Accumulated depreciation and impairment losses at the end of the year	–	(15 410)	(70 358)	(9 227)	(22 192)	(390)	(117 577)
Net carrying amount at the end of the year	96 464	4 181	21 557	740	8 439	102	131 483

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

	Group	
	2010	2009
	R'000	R'000
Historical cost of properties that have been revalued	**36 910**	36 910

- 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 2010.
- A register containing details of owner-occupied properties and the revaluation thereof is available for inspection at the registered office of the Company.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group		Company	
	2010	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000
4. Tax				
South African Revenue Services				
Tax overpaid	**101**	256	–	256
Tax owing	–	70	–	–
5. Other accounts receivable				
Items in transit	**21 254**	12 941	–	–
Prepayments and deposits	**3 887**	6 597	**7**	4
Other receivables	**23 880**	10 001	–	–
	49 021	29 539	**7**	4

	Company	
	2010	2009
	R'000	R'000
6. Interest in subsidiaries		
Unlisted		
Shares at fair value based on net asset value	**1 568 404**	1 466 259
Mercantile Bank Limited	**1 566 781**	1 465 233
Mercantile Insurance Brokers (Pty) Limited	**1 623**	1 026
Loan – amount owing to Mercantile Bank Limited	**(12 757)**	(11 947)
	1 555 647	1 454 312

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		Company	
	2010	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000
7. Other investments				
Available-for-sale				
Unlisted equities	**245**	271	**29**	29
Listed equities	**10 724**	15 637	–	–
African Bank Investments Limited	–	751	–	–
Capitec Bank Holdings Limited	–	13	–	–
Kap International Limited	–	16	–	–
Visa Inc.	**10 724**	14 857	–	–
Designated at fair value through profit and loss				
Unlisted equities	–	7 682	–	–
Total	**10 969**	23 590	**29**	29

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 2010 (continued)

	Group 2010 R'000	Group 2009 R'000
8. Deferred tax		
Balance at the beginning of the year	**84 066**	142 016
Current year charge		
Per the statement of comprehensive income	**(42 842)**	(55 336)
Per the statement of changes in equity/other comprehensive income	**120**	(2 614)
	41 344	84 066
Comprising		
Deferred tax assets	**62 382**	102 936
Deferred tax liabilities	**(21 038)**	(18 870)
	41 344	84 066
Deferred tax is attributable to the following temporary differences		
Assets		
Property plant and equipment	**(29 104)**	(15 100)
Intangible assets	**3**	3
Provisions and other liabilities	**(10 661)**	(4 078)
Calculated tax losses	**83 087**	106 477
Other	**19 057**	(3 236)
	62 382	84 066
Liabilities		
Revaluations	**27 060**	22 844
Other	**(6 022)**	(3 974)
	21 038	18 870

Deferred tax assets have been recognised for the carry forward amount of unused tax losses relating to the Group's operations where, *inter alia,* tax 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 2010 R'000	Group 2009 R'000
9. Non-current assets held for sale		
Interest in associated company	–	3 234
Properties in possession	–	2 276
	–	5 510

Interest in associated company

This investment was classified as a non-current asset held for sale in 2008 and although the main underlying investments of this company were disposed of in 2009, Statman Investments (Pty) Limited was liquidated during 2010.

Properties in possession

The property was valued at the sale price less costs to sell and realised during the first quarter of 2010.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group 2010 R'000	Group 2009 R'000
10. Loans and advances		
10.1 Category analysis		
Amortised cost	**3 712 206**	3 565 474
Current accounts	**633 290**	598 961
Credit card	**18 968**	19 950
Mortgage loans	**1 824 348**	1 709 032
Instalment sales and leases	**268 408**	321 022
Structured loans	**230 036**	266 589
Other advances	**737 156**	649 920
Designated at fair value through profit and loss	**76 285**	128 928
Mortgage loans	**38 665**	40 150
Instalment sales and leases	**66**	24 241
Other advances	**37 554**	64 537
Gross loans and advances	**3 788 491**	3 694 402
Less: Portfolio impairments for credit losses	**(5 513)**	(20 750)
Specific impairments for credit losses	**(62 071)**	(44 078)
	3 720 907	3 629 574

In 2010, gross loans and advances are reported net of suspended interest as this is the true reflection of the gross loans and advances balance prior to any impairment and as such the 2009 comparatives have been reclassified.

Loans and advances in foreign currencies are converted into South African rand at prevailing exchange rates at the reporting date.

	Group 2010 R'000	Group 2009 R'000
10.2 Maturity analysis		
Repayable on demand and maturing within one month	**703 519**	684 638
Maturing after one month but within six months	**151 228**	5 533
Maturing after six months but within 12 months	**38 919**	53 090
Maturing after 12 months	**2 894 825**	2 951 141
	3 788 491	3 694 402

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 2010 (continued)

10. Loans and advances (continued)

10.3 Detailed category analysis of loans and advances

	Gross amount R'000	Portfolio impairments R'000	Specific impairments R'000	Net balance R'000
Group				
2010				
Current accounts	**633 290**	**1 633**	**13 743**	**617 914**
Credit card	**18 968**	**658**	**4 061**	**14 249**
Mortgage loans	**1 863 013**	**1 145**	**9 262**	**1 852 606**
Instalment sales and leases	**268 474**	**650**	**3 852**	**263 972**
Structured loans	**230 036**	**88**	**18 903**	**211 045**
Other advances	**774 710**	**1 339**	**12 250**	**761 121**
	3 788 491	**5 513**	**62 071**	**3 720 907**
2009				
Current accounts	598 961	1 918	3 355	593 688
Credit card	19 950	917	3 840	15 193
Mortgage loans	1 749 182	870	2 814	1 745 498
Instalment sales and leases	345 263	841	2 628	341 794
Structured loans	266 589	15 088	3 786	247 715
Other advances	714 457	1 116	27 655	685 686
	3 694 402	20 750	44 078	3 629 574

10.4 Impairments for credit losses

	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
Group							
2010							
Balance at the beginning of the year	**64 828**	**5 273**	**4 757**	**3 684**	**3 469**	**18 874**	**28 771**
Movements for the year:							
Credit losses written-off	**(2 542)**	**(4)**	**(694)**	**(230)**	**(442)**	**–**	**(1 172)**
Net impairments raised/(released)	**5 298**	**10 107**	**656**	**6 953**	**1 475**	**117**	**(14 010)**
	67 584	**15 376**	**4 719**	**10 407**	**4 502**	**18 991**	**13 589**

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

10. Loans and advances (continued)

10.4 Impairments for credit losses (continued)

	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
2009							
Balance at the beginning of the year	58 849	2 072	5 246	4 143	2 310	30 430	14 648
Movements for the year:							
Credit losses written-off	(4 255)	(1 786)	(597)	(381)	(159)	–	(1 332)
Net impairments raised/ (released)	10 234	4 987	108	(78)	1 318	(11 556)	15 455
	64 828	5 273	4 757	3 684	3 469	18 874	28 771

	Group	
	2010 R'000	2009 R'000
Net charge for credit losses in the statement of comprehensive income		
Net impairments raised	**(5 298)**	(10 234)
Recoveries in respect of amounts previously written off	**1 876**	911
	(3 422)	(9 323)

10.5 Category analysis of performing loans and advances

	Gross amount R'000	**Portfolio impairment R'000**	**Net balance R'000**
Group			
2010			
Current accounts	**608 089**	**1 633**	**606 456**
Credit card	**14 884**	**658**	**14 226**
Mortgage loans	**1 761 523**	**1 145**	**1 760 378**
Instalment sales and leases	**257 594**	**650**	**256 944**
Structured loans	**181 207**	**88**	**181 119**
Other advances	**736 184**	**1 339**	**734 845**
	3 559 481	**5 513**	**3 553 968**
2009			
Current accounts	585 251	1 918	583 333
Credit cards	16 110	917	15 193
Mortgage loans	1 699 485	870	1 698 615
Instalment sales and leases	332 687	841	331 846
Structured loans	213 228	15 088	198 140
Other advances	668 707	1 116	667 591
	3 515 468	20 750	3 494 718

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

10. Loans and advances (continued)

10.6 Category analysis of performing loans and advances excluding loans and advances with renegotiated terms

	Group	
	2010	2009
	R'000	R'000
Current accounts	**608 089**	585 251
Credit card	**14 884**	16 110
Mortgage loans	**1 749 528**	1 661 970
Instalment sales and leases	**256 885**	331 231
Structured loans	**181 207**	213 228
Other advances	**726 588**	662 137
	3 537 181	3 469 927

10.7 Category analysis of loans and advances with renegotiated terms, that would otherwise be past due or impaired

	2010	2009
Current accounts	**–**	–
Credit card	**–**	–
Mortgage loans	**11 995**	37 515
Instalment sales and leases	**709**	1 456
Structured loans	**–**	–
Other advances	**9 596**	6 570
	22 300	45 541

10.8 Category age analysis of loans and advances that are past due but not individually impaired

	Past due for 1 – 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
Group					
2010					
Current accounts	**–**	**–**	**–**	**–**	**–**
Credit card	**–**	**–**	**–**	**–**	**–**
Mortgage loans	**10 214**	**6 295**	**16 490**	**32 999**	**31 241**
Instalment sales and leases	**299**	**–**	**–**	**299**	**203**
Structured loans	**–**	**–**	**20 446**	**20 446**	**13 195**
Other advances	**1 536**	**4 346**	**3 562**	**9 444**	**6 032**
	12 049	**10 641**	**40 498**	**63 188**	**50 671**
2009					
Current accounts	–	–	–	–	–
Credit cards	–	–	–	–	–
Mortgage loans	18 718	20 346	1 901	40 965	37 905
Instalment sales and leases	933	608	159	1 700	1 136
Structured loans	–	–	–	–	–
Other advances	3 353	1 340	2 962	7 655	2 963
	23 004	22 294	5 022	50 320	42 004

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

10. Loans and advances (continued)

10.9 Category analysis of loans and advances that are individually impaired

	Gross amount R'000	Specific impairment R'000	Net balance R'000	Fair value of collateral and other credit enhancements R'000
Group				
2010				
Current accounts	**25 201**	**13 743**	**11 458**	**8 076**
Credit card	**4 084**	**4 061**	**23**	**–**
Mortgage loans	**101 490**	**9 262**	**92 228**	**97 716**
Instalment sales and leases	**10 880**	**3 852**	**7 028**	**7 128**
Structured loans	**48 829**	**18 903**	**29 926**	**36 233**
Other advances	**38 526**	**12 250**	**26 276**	**28 749**
	229 010	**62 071**	**166 939**	**177 902**
2009				
Current accounts	13 710	3 355	10 355	5 279
Credit cards	3 840	3 840	–	–
Mortgage loans	49 697	2 814	46 883	46 120
Instalment sales and leases	12 576	2 628	9 948	8 947
Structured loans	53 361	3 786	49 575	27 233
Other advances	45 750	27 655	18 095	30 405
	178 934	44 078	134 856	117 984

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

10. Loans and advances (continued)

10.10 Collateral held as security and other credit enhancements

Fair value of collateral and other credit enhancements are determined with reference to the realisable value of security.

All customers of the Bank are accorded a client risk grading. The risk grading of a client is dependent upon the client's creditworthiness and standing with the Bank and is subjected to ongoing assessment of the client's financial standing and the acceptability of their dealings with the Bank including adherence to repayment terms and compliance with other Bank set conditions.

Description of collateral held as security and other credit enhancements	Method of valuation
Cession of debtors	15% – 75% of debtors due and payable 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 a loan and advance can be realised in accordance with the terms of the agreement or the facility conditions applicable thereto. Cash collateral and pledged assets that can be realised 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 will dispose of all assets.

10.11 Structured loans

The Group has unlisted equity options attached to certain loans in this category, which have been recognised at cost in accordance with accounting policy 4.1 on page 13.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

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				
2010				
Held-for-trading				
Foreign exchange contracts	**1 319 956**	**34 658**	**363 419**	**23 525**
Interest rate swaps	**7 000**	**59**	**67 159**	**4 597**
	1 326 956	**34 717**	**430 578**	**28 122**
2009				
Held-for-trading				
Foreign exchange contracts	744 076	21 353	269 289	8 652
Interest rate swaps	7 000	53	116 210	7 578
	751 076	21 406	385 499	16 230

	Group 2010 R'000	Group 2009 R'000
12. Negotiable securities		
Loans and receivables		
Treasury bills	**215 758**	197 578
Promissory notes – Land Bank	**30 038**	51 309
Available-for-sale		
Government stock	**19 232**	19 015
	265 028	267 902
Maturity analysis		
Maturing within one month	**49 782**	19 894
Maturing after one month but within six months	**191 188**	228 993
Maturing after six months but within 12 months	**4 826**	–
Maturing after one year but within five years	**19 232**	–
Maturing after five years	**–**	19 015
	265 028	267 902

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 2010 (continued)

	Group 2010 R'000	Group 2009 R'000
13. Bank term deposits		
Domestic bank balances	–	35 276
	–	35 276
Maturity analysis		
Maturing after six months but within 12 months	–	35 276
	–	35 276

	Group 2010 R'000	Group 2009 R'000	Company 2010 R'000	Company 2009 R'000
14. Cash and cash equivalents				
Cash on hand	**20 504**	24 003	–	–
Central Bank balances	**103 248**	86 249	–	–
Money Market funds	**305 787**	493 136	–	–
Domestic bank balances	**185 378**	91 506	**223**	224
Foreign bank balances*	**1 144 980**	706 043	–	–
	1 759 897	1 400 937	**223**	224

*Refer to note 29.2 for balances with CGD included in this amount.

15. Share capital and share premium

	Number of issued ordinary shares	Share capital R'000	Share premium R'000	Total R'000
15.1 Issued – Group				
Shares in issue net of treasury shares at 1 January 2009	3 911 114 124	31 817	1 170 754	1 202 571
At 31 December 2009	3 911 114 124	31 817	1 170 754	1 202 571
Decrease of treasury shares held within the Group	844 501	189	–	189
At 31 December 2010	**3 911 958 625**	**32 006**	**1 170 754**	**1 202 760**

26 959 899 (December 2009: 27 804 400) Treasury shares have been eliminated from share capital and premium.

	Number of issued ordinary shares	Share capital R'000	Share premium R'000	Total R'000
15.2 Issued – Company				
At 31 December 2009 and 31 December 2010	**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 (2009: 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 (2009: 15 150 486 shares) with a par value of 25 cents each.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

15. Share capital and share premium (continued)

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 (2009: 393 891 852) which is 10% (2009: 10%) of the issued share capital of the Company at year-end. At the reporting date, 107 694 400 (2009: 83 128 400) share options and Conditional Share Plan awards were outstanding under these schemes. The balance available to be utilised under these schemes is 286 197 452 (2009: 310 763 452). The number of scheme shares that may be issued to a single participant is 59 083 778 (2009: 59 083 778) or 1.5% (2009: 1.5%) of the total number of issued shares.

The Group recognised expenses of R2.154 million (2009: R0.752 million write back of expenses) relating to equity-settled share-based payment transactions (refer to note 25).

Share option scheme

In terms of the Trust Deed, as amended in 2007, options can be exercised in respect of 33% of the option shares after the expiration of three years from the offer date, 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. Prior to 2008, should the options not have been 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 to remove the expiry condition from the sixth anniversary date 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. The scheme was replaced by the Conditional Share Plan and no further options were granted after implementation of the Conditional Share Plan.

The Mercantile Share Incentive Trust acts as agent on behalf of the Bank in respect of this scheme.

Conditional Share Plan

The Conditional Share Plan incentive scheme, implemented in 2008, aims to attract, retain and reward selected employees who are able to contribute to the growth of the Group and provide for an incentive to encourage their continued employment relationship with the Group. By providing them the opportunity to receive shares in the Company, participants are incentivised 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 awards, other than a guaranteed 25% of all awards, are subject to performance conditions measured over a period of three years.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

15. Share capital and share premium (continued)

15.5 Share incentive schemes (continued)

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

	Exercise price (cents)	Options at the beginning of the year	Forfeited during the year	Exercised during the year	Options at the end of the year	Exercisable options at the end of the year	Relating to directors*
Share option scheme							
Grant date							
2010							
20 November 2001	**32**	**394 400**	–	–	**394 400**	**394 400**	–
11 February 2002	**32**	**160 000**	–	–	**160 000**	**160 000**	–
5 October 2004	**18**	**5 000 000**	–	–	**5 000 000**	**5 000 000**	**5 000 000**
7 October 2004	**17**	**750 000**	–	**(500 000)**	**250 000**	**250 000**	–
11 February 2005	**20**	**500 000**	–	–	**500 000**	**500 000**	–
27 July 2005	**32**	**750 000**	–	–	**750 000**	**750 000**	–
9 February 2006	**41**	**750 000**	–	–	**750 000**	**750 000**	–
22 March 2006	**40**	**10 600 000**	**(800 000)**	–	**9 800 000**	**9 800 000**	**7 000 000**
26 February 2007	**34**	**17 600 000**	**(1 450 000)**	–	**16 150 000**	**10 659 000**	**8 000 000**
1 June 2007	**36**	**500 000**	–	–	**500 000**	**330 000**	–
		37 004 400	**(2 250 000)**	**(500 000)**	**34 254 400**	**28 593 400**	**20 000 000**
2009							
20 November 2001	32	794 400	(400 000)	–	394 400	394 400	–
11 February 2002	32	160 000	–	–	160 000	160 000	–
5 October 2004	18	5 000 000	–	–	5 000 000	5 000 000	5 000 000
7 October 2004	17	750 000	–	–	750 000	750 000	–
11 February 2005	20	500 000	–	–	500 000	500 000	–
27 July 2005	32	750 000	–	–	750 000	750 000	–
9 February 2006	41	750 000	–	–	750 000	495 000	–
3 March 2006	38	500 000	(500 000)	–	–	–	–
22 March 2006	40	10 600 000	–	–	10 600 000	6 996 000	7 000 000
26 February 2007	34	18 100 000	(500 000)	–	17 600 000	5 808 000	8 000 000
1 June 2007	36	500 000	–	–	500 000	165 000	–
1 December 2007	36	1 000 000	(1 000 000)	–	–	–	–
		39 404 400	(2 400 000)	–	37 004 400	21 018 400	20 000 000

The Group has not granted employees any further share options since 2007.

* Refer to note 29.3

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

15. Share capital and share premium (continued)

15.5 Share incentive schemes (continued)

	Market price at date of grant (cents)	Conditional awards at the beginning of the year	Granted during the year	Forfeited during the year	Exercised during the year	Conditional awards at the end of the year	Relating to directors*
Conditional Share Plan							
Grant date							
2010							
22 February 2008	**32**	**22 749 000**	–	**(974 522)**	**(259 478)**	**21 515 000**	**7 600 000**
26 March 2008	**31**	**4 000 000**	–	–	–	**4 000 000**	–
24 July 2008	**26**	**375 000**	–	–	–	**375 000**	–
1 November 2008	**28**	**2 200 000**	–	**(200 000)**	–	**2 000 000**	–
18 March 2009	**26**	**15 800 000**	–	**(1 214 977)**	**(85 023)**	**14 500 000**	**5 000 000**
1 July 2009	**25**	**1 000 000**	–	–	–	**1 000 000**	–
25 February 2010	**20**	–	**20 050 000**	–	–	**20 050 000**	**5 000 000**
1 June 2010	**24**	–	**10 000 000**	–	–	**10 000 000**	**10 000 000**
1 December 2010	**20**	–	**1 500 000**	–	–	**1 500 000**	–
		46 124 000	**31 550 000**	**(2 389 499)**	**(344 501)**	**74 940 000**	**27 600 000**
2009							
22 February 2008	32	26 131 000	–	(3 382 000)	–	22 749 000	7 600 000
26 March 2008	31	4 000 000	–	–	–	4 000 000	–
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)	–	–	–
18 March 2009	26	–	16 660 000	(860 000)	–	15 800 000	5 000 000
1 July 2009	25	–	1 000 000	–	–	1 000 000	–
		34 006 000	17 660 000	(5 542 000)	–	46 124 000	12 600 000

* Refer to note 29.3

16. Deposits

	Group 2010 R'000	Group 2009 R'000
Call deposits and current accounts	**2 364 767**	2 216 193
Savings accounts	**175 595**	181 826
Term and notice deposits	**1 719 410**	1 610 863
Negotiable certificates of deposit	**103 867**	27 576
Foreign deposits	**200 349**	210 140
	4 563 988	4 246 598

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

16. Deposits (continued)

Maturity analysis

	Group	
	2010	2009
	R'000	R'000
Repayable on demand and maturing within one month	**3 051 177**	3 281 792
Maturing after one month but within six months	**817 335**	562 306
Maturing after six months but within 12 months	**622 906**	396 940
Maturing after 12 months	**72 570**	5 560
	4 563 988	4 246 598

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

17. Provisions and other liabilities

	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 1 January 2009	20 609	3 630	14 531	9 116	710	48 596
Additional provision raised	8 615	6 200	–	3 017	508	18 340
Charged to provision	(19 035)	(6 130)	(668)	(2 611)	(350)	(28 794)
At 31 December 2009	**10 189**	**3 700**	**13 863**	**9 522**	**868**	**38 142**
Additional provision raised	–	**7 520**	**1 286**	**2 087**	**778**	**11 671**
Reversal of provision	**(1 270)**	–	–	–	–	**(1 270)**
Charged to provision	**(8 919)**	**(6 610)**	–	**(2 168)**	**(926)**	**(18 623)**
At 31 December 2010	–	**4 610**	**15 149**	**9 441**	**720**	**29 920**

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 against the Group, the outcome of which cannot at present be foreseen. Such 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 2010 (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 annually and the last valuation was carried out at 31 December 2010. The actuary's opinion is that the plan is in a sound financial position.

	Group				
	2010	2009	2008	2007	2006
	R'000	R'000	R'000	R'000	R'000
The amounts recognised in the statement of financial position are as follows (refer to note 17):					
Present value of total service liabilities	**20 648**	19 370	19 664	20 223	18 989
Fair value of plan assets	**(5 499)**	(5 507)	(5 133)	(5 880)	(6 136)
Provident fund	**(1 832)**	(1 674)	(922)	(838)	(1 457)
Endowment bond	**(2 530)**	(2 718)	(3 118)	(3 446)	(3 729)
Annuities	**(1 137)**	(1 115)	(1 093)	(1 596)	(950)
Liability in the statement of financial position	**15 149**	13 863	14 531	14 343	12 853
The amounts recognised in the statement of comprehensive income are as follows (refer to note 25):					
Current service cost	**50**	92	89	116	115
Interest costs	**1 767**	1 785	1 568	1 539	1 365
Expected return on plan assets	**(578)**	(526)	(529)	(549)	(396)
Actuarial gain/(loss)	**1 488**	(660)	368	936	1 957
Employer benefit payments	**(1 441)**	(1 359)	(1 308)	(1 202)	(1 168)
Payments from plan assets	**–**	–	–	650	846
Effect on curtailment	**–**	–	–	–	(280)
Total included in staff costs	**1 286**	(668)	188	1 490	2 439
Reconciliation of the movement in the present value of total service liabilities:					
At the beginning of the year	**19 370**	19 664	20 223	18 989	16 651
Current service cost	**50**	92	89	116	115
Interest costs	**1 767**	1 785	1 568	1 539	1 365
Actuarial gain/(loss)	**902**	(812)	(908)	781	2 306
Employer benefit payments	**(1 441)**	(1 359)	(1 308)	(1 202)	(1 168)
Effect of curtailment	**–**	–	–	–	(280)
At the end of the year	**20 648**	19 370	19 664	20 223	18 989
Reconciliation of the movement in the fair value of plan assets:					
At the beginning of the year	**5 507**	5 133	5 880	6 136	6 237
Expected return on plan assets	**578**	526	529	549	396
Actuarial (loss)/gain	**(586)**	(152)	(1 276)	(155)	349
Payments from plan assets	**–**	–	–	(650)	(846)
At the end of the year	**5 499**	5 507	5 133	5 880	6 136

The principal actuarial assumptions used were as follows:

Discount rate	**8.25%**	(2009: 9.50%) compounded annually
Investment return	**9.25%**	(2009: 10.50%) compounded annually
Rate of medical inflation	**7.00%**	(2009: 8.00%) compounded annually
Salary inflation	**6.50%**	(2009: 7.50%) 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 R1.973 million (2009: R2.047 million) and a decrease of R1.680 million (2009: R1.730 million), respectively.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group 2010 R'000	Group 2009 R'000	Company 2010 R'000	Company 2009 R'000
19. Other accounts payable				
Accruals	**20 058**	16 702	**14**	14
Product-related credits	**31 190**	18 613	**–**	–
Sundry creditors	**20 601**	25 838	**–**	–
	71 849	61 153	**14**	14

	Group 2010 R'000	Group 2009 R'000
20. Contingent liabilities and commitments		
20.1 Guarantees, letters of credit and committed undrawn facilities		
Guarantees	**305 669**	303 514
Lending related	**8 850**	15 983
Airways releases	**–**	1 813
Mortgage	**65 113**	27 925
Performance	**231 706**	257 793
Letters of credit	**10 260**	12 330
Committed undrawn facilities	**129 903**	190 834
	445 832	506 678

20.2 Commitments under operating leases

The total minimum future lease payments under operating leases are as follows:

Property rentals:

	Group 2010 R'000	Group 2009 R'000
Due within one year	**5 264**	4 254
Due between one and five years	**11 352**	7 011
	16 616	11 265
After tax effect on operating leases	**11 964**	8 111

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.

The 2009 comparative amounts have been adjusted due to an error in disclosure. The restatement only affected the 2009 figures and did not affect any other year's comparative disclosure.

20.3 Capital commitments

	Group 2010 R'000	Group 2009 R'000
Contracted for consulting services for the core banking system	**5 360**	51 628
	5 360	51 628

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group	
	2010	2009
	R'000	R'000
21. Interest income		
Loans and receivables	**438 991**	511 271
Cash and cash equivalents and bank term deposits	**64 515**	84 747
Negotiable securities	**18 791**	24 212
Loans and advances	**355 685**	402 312
Loans and receivables designated at fair value through profit and loss		
Loans and advances	**11 867**	17 689
Held-for-trading		
Interest rate swaps	**60**	624
	450 918	529 584
22. Interest expenditure		
Deposits	**190 768**	257 332
Held-for-trading		
Interest rate swaps	**3 790**	3 983
	194 558	261 315
23. Non-interest income		
Fee and commission income	**208 396**	224 957
Loans and receivables*	**206 725**	222 888
Other	**1 671**	2 069
Trading income	**62 836**	62 501
Held-for-trading	**61 622**	62 463
Foreign currency	**60 261**	61 991
Derivative assets	**2**	(48)
Derivative liabilities	**1 359**	520
Designated at fair value through profit and loss	**1 214**	38
Loans and advances	**(818)**	(644)
Other investments	**2 032**	682
Investment income	**355**	451
Dividends	**348**	381
Rental income	**7**	70
	271 587	287 909

* In 2010, foreign currency commission is included in fee and commission income and therefore the 2009 comparatives have been adjusted accordingly.

24. Fee and commission expenditure		
Foreign currency	**22 089**	20 618
Commissions and transactions	**81 013**	67 232
	103 102	87 850

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group 2010 R'000	Group 2009 R'000	Company 2010 R'000	Company 2009 R'000
25. Operating expenditure				
Amortisation (refer to note 2)	**20 819**	7 428	–	–
Auditors' remuneration				
Audit fees – Current year	**7 500**	6 200	–	–
– Prior year	**–**	20	–	–
Fees for other services				
– Tax advisory fees	**160**	–	–	–
– Secondment of staff	**51**	403	–	–
Administrative and IT staff	**309**	403	–	–
Less: Amounts capitalised to intangible assets	**(258)**	–	–	–
– Quality assessment review of internal audit	**–**	203	–	–
– Other	**23**	–	–	–
	7 734	6 826	–	–
Depreciation (refer to note 3)	**10 713**	9 505	–	–
Directors' emoluments (refer to note 29.3)				
Executive directors	**7 904**	7 365	–	–
Non-executive directors' fees	**3 848**	3 758	–	–
	11 752	11 123	–	–
Indirect tax				
Non-claimable Value-Added Tax	**8 705**	4 600	–	–
Skills development levy	**1 086**	718	–	–
	9 791	5 318	–	–
Lease charges – equipment	**56**	3	–	–
Loss on sale of property and equipment	**6**	14	–	–
Marketing and communication	**7 193**	7 251	**579**	665
Operating leases – premises	**10 626**	7 733	–	–
Other operating costs	**29 135**	28 502	**485**	469
Professional fees				
Consulting	**3 101**	3 932	–	–
Legal	**252**	325	–	–
Computer consulting and services	**37 586**	34 405	–	–
	40 939	38 662	–	–

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group		Company	
	2010	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000
25. Operating expenditure (continued)				
Staff costs				
Salaries, wages and incentives	**115 045**	114 883	**–**	–
Post-retirement medical benefits (refer to note 18)	**1 286**	(668)	**–**	–
Contributions to retirement funds	**8 174**	7 989	**–**	–
Share-based payments expense/(write back) including directors	**2 154**	(752)	**–**	–
Other	**3 381**	3 761	**–**	–
	130 040	125 213	**–**	–
Total operating expenditure	**278 804**	247 578	**1 064**	1 134
Number of persons employed by the Group at year-end	**439**	435		

	Group		Company	
	2010	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000
26. Tax				
South African normal tax	**(203)**	469	**–**	256
Current year	**(203)**	(129)	**–**	–
Prior year	**–**	598	**–**	256
Deferred tax	**(42 842)**	(55 336)	**–**	–
Current year	**(38 924)**	(60 080)	**–**	–
Prior year	**(3 918)**	4 744	**–**	–
	(43 045)	(54 867)	**–**	256
Direct tax				
South African normal tax	**203**	(469)	**–**	(256)
South African tax rate reconciliation				
South African standard tax rate (%)	**28.00**	28.00	**28.00**	28.00
Exempt income (%)	**(0.66)**	(0.55)	**0.00**	0.00
Expenses not deductible for tax purposes (%)	**0.41**	0.54	**0.00**	0.00
Additional allowances for tax purposes (%)	**(0.14)**	(0.15)	**0.00**	0.00
Capital gain – 50% portion not taxable (%)	**(0.09)**	(0.10)	**0.00**	0.00
Under/(Over) provision prior years (%)	**2.57**	(2.46)	**0.00**	(22.57)
Tax losses (utilised) (%)	**(0.21)**	0.00	**(28.00)**	(28.00)
Effective tax rate (%)	**29.88**	25.28	**0.00**	(22.57)
Estimated tax losses available for set-off against future taxable income	**301 867**	384 462	**5 128**	4 062

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group 2010 R'000	Group 2009 R'000
27. Earnings, diluted earnings, headline earnings and diluted headline earnings per ordinary share		
27.1 Earnings per ordinary share		
Profit after tax	**101 026**	162 202
Weighted number of ordinary shares in issue ('000)	**3 911 255**	3 911 114
Earnings per ordinary share (cents)	**2.6**	4.1
27.2 Diluted earnings per ordinary share		
Profit after tax	**101 026**	162 202
Weighted diluted number of ordinary shares in issue ('000)	**3 935 365**	3 928 895
Diluted earnings per ordinary share (cents)	**2.6**	4.1
27.3 Headline and diluted headline earnings per ordinary share		
Profit after tax	**101 026**	162 202
Adjustment for non-headline items:		
Realisation of available-for-sale reserve on disposal of investments	**(885)**	(1 583)
Loss on disposal of property and equipment	**6**	14
Tax on non-headline items	**122**	218
Headline earnings	**100 269**	160 851
Headline earnings per ordinary share (cents)	**2.6**	4.1
Diluted headline earnings per ordinary share (cents)	**2.5**	4.1

	Group 2010 R'000	Group 2009 R'000	Company 2010 R'000	Company 2009 R'000
28. Notes to statements of cash flows				
28.1 Cash receipts from customers				
Interest income	**450 918**	529 584	**–**	–
Non-interest income and gain on disposal and revaluation of available-for-sale investments	**272 472**	289 492	**–**	–
Adjusted for:				
Dividends received	**(348)**	(381)	**–**	–
Net (gain) on disposal of available-for-sale investments	**(885)**	(1 583)	**–**	–
Revaluation of fair value financial instruments	**(7 778)**	(50 636)	**–**	–
Recoveries in respect of amounts previously written off	**1 876**	911	**–**	–
	716 255	767 387	**–**	–

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group		Company	
	2010	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000
28. Notes to statements of cash flows (continued)				
28.2 Cash paid to customers, suppliers and employees				
Interest expenditure	**(194 558)**	(261 315)	**–**	–
Operating expenditure and fee and commission expenditure	**(381 906)**	(335 428)	**(1 064)**	(1 134)
Adjusted for:				
Amortisation	**20 819**	7 428	**–**	–
Depreciation	**10 713**	9 505	**–**	–
Loss on sale of property and equipment	**6**	14	**–**	–
Vesting of shares in the conditional share plan	**(104)**	–	**–**	–
Share-based payments expense/(write back)	**2 154**	(752)	**–**	–
(Decrease) in provisions	**(8 222)**	(10 454)	**–**	–
	(551 098)	(591 002)	**(1 064)**	(1 134)
28.3 Reconciliation of profit before tax to cash generated from operations				
Profit/(Loss) before tax	**144 071**	217 069	**(1 064)**	(1 134)
Profit before tax adjusted for:				
Dividends received	**(348)**	(381)	**–**	–
Net (gain) on disposal of available-for-sale investments	**(885)**	(1 583)	**–**	–
Revaluation of fair value financial instruments	**(7 778)**	(50 636)	**–**	–
Net impairments raised	**5 298**	10 234	**–**	–
Amortisation	**20 819**	7 428	**–**	–
Depreciation	**10 713**	9 505	**–**	–
Loss on sale of property and equipment	**6**	14	**–**	–
Share-based payments expense/(write back)	**2 154**	(752)	**–**	–
Vesting of shares in the conditional share plan	**(104)**	–	**–**	–
(Decrease) in provisions	**(8 222)**	(10 454)	**–**	–
Share of income from associated company	**(567)**	(4 059)	**–**	–
Cash generated from operations	**165 157**	176 385	**(1 064)**	(1 134)
28.4 Tax				
Amounts paid/(unpaid) at the beginning of the year	**186**	(494)	**256**	–
Statement of comprehensive income (charge)/ recovery	**(203)**	469	**–**	256
Less: Amounts (overpaid) at the end of the year	**(101)**	(186)	**–**	(256)
Total tax (paid)/recovered	**(118)**	(211)	**256**	–

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	Group		Company	
	2010	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000
28. Notes to statements of cash flows (continued)				
28.5 Net movement in income earning assets				
Decrease/(Increase) in negotiable securities	**3 597**	(21 778)	**–**	–
(Increase) in loans and advances	**(92 304)**	(231 735)	**–**	–
Decrease in bank term deposits	**35 276**	289 019	**–**	–
Net (increase)/decrease in income earning assets	**(53 431)**	35 506	**–**	–
28.6 Net movement in deposits and other accounts				
Increase/(Decrease) in deposits	**317 390**	(142 749)	**–**	–
Decrease of treasury shares held within the Group	**189**	–	**–**	–
Increase in loan from subsidiary	**–**	–	**810**	1 154
(Increase)/Decrease in other accounts receivable	**(19 482)**	9 734	**(3)**	–
Increase/(Decrease) in other accounts payable	**10 696**	(37 805)	**–**	(20)
Net increase/(decrease) in deposits and other accounts	**308 793**	(170 820)	**807**	1 134

29. Related-party information

29.1 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 note 9 (liquidated during 2010) 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.

29.2 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. Except for the interest free loan from the Bank to the Company, transactions are governed by terms no less favourable than those arranged with third parties.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

	2010 R'000	2009 R'000
29. Related-party information (continued)		
29.2 Related-party balances and transactions (continued)		
Balances between the ultimate holding company (CGD) and the Bank:		
CGD – Lisbon (Branch of CGD)	**1 084 225**	614 171
Nostro accounts*	**2 530**	3 698
Vostro accounts	**(1 912)**	(1 568)
Deposit accounts*	**1 083 607**	612 041
CGD – Paris (Branch of CGD)	**225**	68
Nostro accounts*	**261**	92
Vostro accounts	**(36)**	(24)
CGD – London (Branch of CGD)		
Vostro accounts	**(16)**	(17)
CGD	**1 084 434**	614 222
Banco Comercial e de Investimentos – Mozambique (BCI) (Subsidiary of CGD)	**(107 659)**	(37 215)
Vostro accounts	**(3 326)**	(4)
Fixed deposits	**(103 800)**	(37 100)
Call and notice deposits	**(533)**	(111)
Total CGD	**976 775**	577 007

*These balances are included as part of note 14, cash and cash equivalents – foreign bank balances.

	2010 R'000	2009 R'000
Transaction between the ultimate holding company (CGD) and the Bank:		
Interest paid by CGD to the Bank	**1 353**	10 518
Interest paid by BCI to the Bank	**–**	268
Interest paid by the Bank to BCI	**2 294**	3 084

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

		2010 R'000	2009 R'000
29 Related-party information (continued)			
29.2 Related-party balances and transactions (continued)			
Balances with the Company, its subsidiaries and associated company:			
Loan to:	**Loan from:**		
Mercantile Bank Holdings Limited	Mercantile Bank Limited	**12 757**	11 947
Portion 2 of Lot 8 Sandown (Pty) Limited	Mercantile Bank Limited	**34 126**	40 390
LSM (Troyeville) Properties (Pty) Limited	Mercantile Bank Limited	**6 784**	6 494
Mercantile Insurance Brokers (Pty) Limited	Mercantile Bank Limited	**828**	290
Deposit with:	**Deposit by:**		
Mercantile Bank Limited	Mercantile Insurance Brokers (Pty) Limited	**2 794**	1 912
Mercantile Bank Limited	Mercantile Bank Holdings Limited	**223**	224
Mercantile Bank Limited	Statman Investments (Pty) Limited	**–**	3 636
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	**4 409**	5 121
Mercantile Bank Limited	LSM (Troyeville) Properties (Pty) Limited	**787**	759
Mercantile Insurance Brokers (Pty) Limited	Mercantile Bank Limited	**86**	96
Mercantile Bank Limited	Statman Investments (Pty) Limited	**–**	25
Statman Investments (Pty) Limited	Mercantile Bank Limited	**707**	86
Non-interest income earned by:	**Operating expenditure paid by:**		
Portion 2 of Lot 8 Sandown (Pty) Limited	Mercantile Bank Limited	**13 921**	11 813
LSM (Troyeville) Properties (Pty) Limited	Mercantile Bank Limited	**1 052**	1 072
Mercantile Bank Limited	Mercantile Insurance Brokers (Pty) Limited	**158**	190
Portion 2 of Lot 8 Sandown (Pty) Limited	Mercantile Insurance Brokers (Pty) Limited	**73**	153
Dividends earned by:	**Dividends paid by:**		
Mercantile Bank Limited	Statman Investments (Pty) Limited	**3 126**	4 059

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 2010 (continued)

29. Related-party information (continued)

29.3 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
Group						
2010						
Non-executive directors						
J A S de Andrade Campos	**1 413**	–	–	–	–	**1 413**
G P de Kock	**602**	–	–	–	–	**602**
L Hyne	**567**	–	–	–	–	**567**
A T Ikalafeng	**480**	–	–	–	–	**480**
T H Njikizana	**475**	–	–	–	–	**475**
S Rapeti (resigned 29 July 2010)	**311**	–	–	–	–	**311**
Executive directors						
D J Brown	–	**2 837**	–	**301**	–	**3 138**
J P M Lopes	–	**1 771**	**568**	**44**	–	**2 383**
K R Kumbier (appointed 1 June 2010)*	–	**2 227**	–	**156**	–	**2 383**
	3 848	**6 835**	**568**	**501**	–	**11 752**
2009						
Non-executive directors						
J A S de Andrade Campos	1 343	–	–	–	–	1 343
G P de Kock	560	–	–	–	–	560
L Hyne	525	–	–	–	–	525
A T Ikalafeng	445	–	–	–	–	445
T H Njikizana	382	–	–	–	–	382
S Rapeti	503	–	–	–	–	503
Executive directors						
D J Brown	–	2 609	–	273	2 000	4 882
J P M Lopes	–	1 662	516	55	250	2 483
	3 758	4 271	516	328	2 250	11 123

* A sign on bonus of R0.925 million, included under 'salary' was awarded to Mr Kumbier as part of his appointment in June 2010.

	2010 R'000	2009 R'000
Share-based payments expense relating to executive directors		
D J Brown	**656**	94
K R Kumbier (appointed 1 June 2010)	**135**	–
Amounts paid by CGD to executive directors		
J P M Lopes	**552**	585

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

29. Related-party information (continued)

29.3 Director and director-related activities (continued)

Service agreements

D J Brown, CEO
Mr Brown's employment contract as CEO was extended by the Board to March 2014.

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 contract was extended by the Board to July 2014. In terms of his 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.

K R Kumbier, Executive Director
Mr Kumbier was employed by Mercantile as Director: Finance and Business on 1 June 2010. His appointment will be affirmed at the AGM, to be held on 1 June 2011.

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, the following conditional share awards were granted to Mr Brown (refer to note 15.5):

- on 22 February 2008, 7 600 000 with a market value on the date of grant of 32 cents each;
- on 18 May 2009, 5 000 000 with a market value on the date of grant of 26 cents each; and
- on 25 February 2010, 5 000 000 with a market value on the date of grant of 20 cents each.

In terms of the Conditional Share Plan, the following conditional share awards were granted to Mr Kumbier (refer to note 15.5):

- on 1 June 2010, 10 000 000 with a market value on the date of grant of 24 cents each.

Directors' interests
Except for Mr Kumbier (appointed 1 June 2010) who holds 2 016 851 shares directly, no other directors held beneficial and/or non-beneficial interests, directly or indirectly, in shares issued by the Company (2009: nil).

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

30. Segment information

The reportable segments of the Group are as follows:

Segment	**Scope of products and services**
Business and Commercial Banking*	Banking, investment and other financial services offered to banking customers.
Treasury*	Managing internal liquidity, foreign exchange services as well as serving wholesale 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 and inter-group eliminations.

* Excludes the allocation of attributable support costs and tax. This is the measure reported to the chief operating decision maker for the purposes of resource allocation and assessment of segment performance.

All operations are located in South Africa.

Notes to the annual financial statements

for the year ended 31 December 2010 (continued)

30. Segment information (continued)

	Business and Commercial Banking		Treasury		Alliance banking, MBL credit card and electronic banking		Support and other services		Total	
	2010	2009	**2010**	2009	**2010**	2009	**2010**	2009	**2010**	2009
	R'000	R'000	**R'000**	R'000	**R'000**	R'000	**R'000**	R'000	**R'000**	R'000
Segment revenue^	**277 440**	291 779	**60 340**	45 224	**35 650**	63 055	**52 300**	69 853	**425 730**	469 911
Operating profit	**173 676**	197 583	**34 545**	25 888	**9 893**	39 583	**(74 610)**	(50 044)	**143 504**	213 010
Share of income from associated company									**567**	4 059
Profit before tax									**144 071**	217 069
Tax									**(43 045)**	(54 867)
Profit after tax									**101 026**	162 202
Statement of comprehensive income:										
Interest income	**356 931**	420 263	**38 024**	31 700	**5 710**	15 223	**50 253**	62 398	**450 918**	529 584
Interest expenditure	**(161 600)**	(217 271)	**(30 050)**	(34 725)	**(2 492)**	(8 143)	**(416)**	(1 176)	**(194 558)**	(261 315)
Net interest income/ (expenditure)	**195 331**	202 992	**7 974**	(3 025)	**3 218**	7 080	**49 837**	61 222	**256 360**	268 269
Depreciation	**5 600**	4 171	**147**	161	**516**	814	**4 450**	4 359	**10 713**	9 505
Amortisation	**13 260**	3 145	**6 188**	1 688	**852**	2 336	**519**	259	**20 819**	7 428
Net (charge for)/recovery of credit losses	**(5 068)**	(12 831)	**(36)**	–	**(315)**	(140)	**1 997**	3 648	**(3 422)**	(9 323)
Fair value profit/(loss)	**2 603**	382	**(28)**	128	**–**	–	**–**	–	**2 575**	510
Statement of financial position:										
Segment assets	**4 228 023**	3 986 816	**904 306**	746 313	**118 334**	127 165	**1 003 648**	958 440	**6 254 311**	5 818 734
Segment liabilities	**3 696 113**	3 486 095	**860 328**	712 768	**87 257**	73 780	**92 257**	127 290	**4 735 955**	4 399 933
Additions to non-current assets*	**1 173**	62 782	**839**	32 675	**11 142**	6 928	**65 311**	9 004	**78 465**	111 389
Interest in associated company									**–**	3 234

^Segment revenue consists of net interest income, net gain on disposal of available-for-sale investments and net non-interest income.

Revenue is earned from external customers.

Except for interest earned from CGD which is disclosed in note 29.2, there are no other large clients of the Group that individually contribute significantly to revenue.

* In 2009, non-current assets relating to the Bank's new core banking system were allocated solely to the Business and Commercial Banking segment. Post the implementation of this system in 2010, the allocation of such non-current assets to the various segments was assessed and allocated accordingly resulting in the comparatives for 2009 being adjusted.

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 that have become all too evident during the ongoing global financial crisis. The Group operates in a dynamic environment where the past is not necessarily an acceptable guide to the future. 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 variables 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 potential of concentration risk in being a small bank and this is carefully monitored and where appropriate corrective action is taken. Our business development efforts are focused on the stronger companies and individuals within established policy criteria, which policy serves to eliminate weaker credit from the portfolio. The Group remains well positioned to effectively manage identified threats in such a way that minimises risks to the Group. An independent review of risk management and controls was deferred and will take place during 2011.

A philosophy of enterprise-wide risk management within a Risk Management Monitoring and Control Framework has been implemented to ensure that all business and operational risks are managed effectively within acceptable risk profiles, policies and parameters. Risk management policies are conservative, with proper regard to the mix of risk and reward. The Group takes all necessary steps to safeguard its depositors' funds, its own asset base and shareholders' funds.

A number of risk initiatives were implemented during the year. These included:

- full implementation of a Risk Control Self Assessment process across all key areas of the Bank;
- a Treasury Middle Office has been implemented and all functions identified to improve on segregation and effective management have been migrated for both the treasury front and back offices;
- further enhancements to the Asset Liability Management monitoring and reporting were implemented;
- full implementation and further expansion of a prudential management schedule wherein all risk related ratios are monitored and reported to the ALCO and Board on a monthly basis; and
- a Risk Tolerance Strategy was documented and presented to the Board.

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 vary in importance dependent upon the business activities of an organisation and the related risks. 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 measurement 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 and its various committees, credit management, senior management, risk management, business line management, finance and control, legal/compliance, treasury and operations, with significant support from internal audit and information technology.

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 business unit 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. We have implemented a system of Risk Control Self Assessment across the Bank. The challenge is to ensure effective utilisation and evaluation against the deliverables identified and ongoing training is being scheduled. The standards and implementation of Risk Control Self Assessment ensure alignment and consistency in the way that prevalent risk types are identified, 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, whether quantifiable or not and whether direct or indirect.

Risk management and control

(continued)

Risk management life cycle/process (continued)

Risk management (as an independent function)

The Group's principal business focuses on the management of liabilities and assets in the statement of financial position. Major risks are managed and reviewed by an independent risk function. The ALCO, RMC and CREDCOM meet on a regular basis to collaborate on risk control, process review and establish how much risk is acceptable and to decide how the Group will stay within targets laid down in risk tolerance 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, RMC and CREDCOM and to the SARB via the Finance Division through BA returns and periodic meetings.

Risk control (stress and back 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 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. A policy of back testing for identified key variables has been approved by the Board and will be implemented during the first quarter 2011.

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 identified risks within the Enterprise-wide Risk Management Framework, 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	
Compliance Risk	

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 and tolerance levels. 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 on any 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 and any changes approved by the RMC.

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 on Banking Supervision.

Risk management and control
(continued)

Management of risk (continued)
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 requirements. A comprehensive re-evaluation of the capital requirements under the Internal Capital Adequacy Assessment Process is regularly undertaken with consideration being given to all risks impacting on the need for capital reserves within the Group. The outcome of these assessments resulted in the Group identifying different levels of risk related to specific characteristics of its business where it was deemed prudent to hold a capital buffer in addition to the regulatory capital 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 value of contracts it enters into with any one party to within pre-approved transactional limits.

At year-end, the Group did not have 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 29.2.

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.

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 Portfolio Management Department and any concerns are raised with the Credit Department and Business or Commercial banking units. The Group is implementing an enhanced Decision Support tool to assist credit decision makers through the provision of indicative performance criteria and other information by industry necessary to assist in making more informed decisions. Such indicative performance data will be measured against predefined acceptance bands and result in the allocation of an overall acceptability rating. The model is currently being tested. Once testing is complete, it will be submitted to the RMC for approval.

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

Risk management and control

(continued)

Management of risk (continued)

Credit risk (continued)

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

	Loans and advances R'000	Committed undrawn facilities R'000	Other R'000	Total R'000
2010				
Current accounts	**633 290**	**–**	**–**	**633 290**
Credit card	**18 968**	**14 848**	**–**	**33 816**
Mortgage loans	**1 863 013**	**115 055**	**–**	**1 978 068**
Instalment sales and leases	**268 474**	**–**	**–**	**268 474**
Structured loans	**230 036**	**–**	**–**	**230 036**
Other advances	**774 710**	**–**		**774 710**
Negotiable securities		**–**	**265 028**	**265 028**
Cash and cash equivalents	**–**	**–**	**1 759 897**	**1 759 897**
Guarantees	**–**	**–**	**305 669**	**305 669**
Letters of credit	**–**	**–**	**10 260**	**10 260**
	3 788 491	**129 903**	**2 340 854**	**6 259 248**
2009				
Current accounts	593 688	–	–	593 688
Credit card	15 193	15 285	–	30 478
Mortgage loans	1 745 498	175 549	–	1 921 047
Instalment sales and leases	341 794	–	–	341 794
Structured loans	247 715	–	–	247 715
Other advances	685 686	–	–	685 686
Negotiable securities	–	–	267 902	267 902
Bank term deposits	–	–	35 276	35 276
Cash and cash equivalents	–	–	1 400 937	1 400 937
Guarantees	–	–	303 514	303 514
Letters of credit	–	–	12 330	12 330
	3 629 574	190 834	2 019 959	5 840 367

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 include risks associated with reputation, robbery, fraud, theft of data, systems access and controls, 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;
- ongoing training and up skilling of 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 critical operations environments;
- 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;
- comprehensive data security and protection; ongoing review of the bank-wide Risk Control Self Assessment Process rolled out to job functional level in high-risk operational processing areas during 2010; and
- limiting access to systems and enforcing strong password controls.

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

Risk management and control

(continued)

Management of risk (continued)

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 prudential and regulatory limits. In the unlikely event of an unauthorised limit violation, the ALM Forum 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 on a daily basis 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 initial and variation margins. A detailed sensitivity analysis is performed for liquidity and interest rate risk (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. Various additional conservative prudential risk limits were introduced during 2009 and expanded in 2010. The results of the prudential risk limits and various sensitivities are reported to the ALCO, RMC and Board on a regular basis.

Basel III proposes various changes to the management and supervision of liquidity risk. The Group is monitoring these developments and will ensure that it is well positioned to meet the added requirements of Basel III prior to the implementation by the SARB.

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 R4.75 million (2009: R10.02 million). An adverse movement in the exchange rate of 10% would reduce the Group's income by R0.5 million (2009: R1.0 million).

Risk management and control

(continued)

Management of risk (continued)

Foreign currency risk (continued)

The transaction exposures and foreign exchange contracts at the reporting date are summarised as follows:

	US Dollar R'000	Euro R'000	Pound Sterling R'000	Other R'000	Total R'000
2010					
Total foreign exchange assets	**1 104 488**	**25 697**	**6 856**	**8 145**	**1 145 186**
Total foreign exchange liabilities	**(172 412)**	**(19 874)**	**(7 910)**	**(337)**	**(200 533)**
Commitments to purchase foreign currency	**179 019**	**121 800**	**26 828**	**10 156**	**337 803**
Commitments to sell foreign currency	**(1 110 368)**	**(128 435)**	**(25 831)**	**(16 800)**	**(1 281 434)**
Year-end effective net open foreign currency positions	**727**	**(812)**	**(57)**	**1 164**	**1 022**
2009					
Total foreign exchange assets	615 326	48 369	32 490	9 877	706 062
Total foreign exchange liabilities	(182 815)	(16 896)	(7 253)	(3 176)	(210 140)
Commitments to purchase foreign currency	127 566	100 434	3 003	15 579	246 582
Commitments to sell foreign currency	(559 551)	(131 475)	(27 953)	(21 859)	(740 838)
Year-end effective net open foreign currency positions	526	432	287	421	1 666

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, RMC and Board.

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, by the use of interest rate swap contracts and by matching the maturities of deposits and assets as appropriate.

The objective with the management of interest rate risk is to ensure a higher degree of interest rate margin stability and lower interest rate risk over an interest rate cycle. This is achieved by hedging material exposures and by not allowing any proprietary interest rate positions. 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 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)

The yield on assets declined further during 2010, which can mainly be attributed to the steep decline in the prevailing prime and repo rates in South Africa during this period. South Africa was not immune to the global credit and liquidity crisis and this, together with market uncertainty in respect of the longer-term interest rate trends, resulted in the cost of funding contributing to the decline in margin. In addition, margins were further squeezed by the impact of lower interest rates on non-interest bearing deposits. Pressure on margins is likely to continue during 2011. Net interest income was also adversely impacted by the negative endowment effect due to the current high levels of excess capital of the Group.

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.

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. In addition to the above, the impact of a static bank specific favourable and unfavourable interest rate movement of 50 and 200 basis points respectively is calculated and monitored daily by the ALM forum. Various prudential limits that were approved and implemented during the 2009 financial year were refined and expanded during 2010.

At the reporting date, a 50 basis point change in prevailing interest rates was applied as a sensitivity analysis to determine the impact on earnings as a result of a change in 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 R10.6 million (2009: increase/decrease by R9.8 million). This is mainly attributable to the Group's exposure to interest rates on its surplus capital and lending and borrowings in the banking book.

Risk management and control

(continued)

Management of risk (continued)

Interest rate risk (continued)

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. The repricing profile indicates that the Group remains asset-sensitive as interest-earning assets reprice sooner than interest-paying liabilities, before and after derivative hedging activities. Thus, future net interest income remains vulnerable to a decrease in market interest rates.

	Up to 1 month R'000	1 – 3 months R'000	3 – 12 months R'000	1 – 5 years R'000	Over five years R'000	Non-interest sensitive R'000	Total R'000	Effective interest rate %
2010								
Assets								
Intangible assets	–	–	–	–	–	224 402	224 402	–
Property and equipment	–	–	–	–	–	126 887	126 887	–
Tax	–	–	–	–	–	101	101	–
Other accounts receivable	–	–	–	–	–	49 021	49 021	–
Other investments	–	–	–	–	–	10 969	10 969	–
Deferred tax assets	–	–	–	–	–	62 382	62 382	–
Loans and advances	3 749 310	–	–	45 499	30 786	(104 688)	3 720 907	8.62
Derivative financial instruments	59	–	–	–	–	34 658	34 717	–
Negotiable securities	49 782	63 161	132 853	19 232	–	–	265 028	6.72
Cash and cash equivalents	1 574 773	–	–	–	–	185 124	1 759 897	5.26
Total assets	5 373 924	63 161	132 853	64 731	30 786	588 856	6 254 311	
Equity and liabilities								
Shareholders' equity	–	–	–	–	–	1 539 394	1 539 394	–
Deferred tax liabilities	–	–	–	–	–	21 038	21 038	–
Deposits	2 845 361	340 102	679 748	30 643	–	668 134	4 563 988	4.17
Derivative financial instruments	2 860	1 736	–	–	–	23 526	28 122	–
Provisions and other liabilities	–	–	–	–	–	29 920	29 920	–
Other accounts payable	–	–	–	–	–	71 849	71 849	–
Total equity and liabilities	2 848 221	341 838	679 748	30 643	–	2 353 861	6 254 311	
Financial position interest sensitivity gap	2 525 703	(278 677)	(546 895)	34 088	30 786	–	1 764 005	
Derivative financial instruments	17 630	35 604	7 000	(33 975)	(26 259)	–	–	
Total net interest sensitivity gap	2 543 333	(243 073)	(553 895)	113	4 527	–	1 764 005	

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 five years R'000	Non-interest sensitive R'000	Total R'000	Effective interest rate %
2009								
Assets								
Intangible assets	–	–	–	–	–	170 325	170 325	–
Property and equipment	–	–	–	–	–	131 483	131 483	–
Tax	–	–	–	–	–	256	256	–
Other accounts receivable	–	–	–	–	–	29 539	29 539	–
Other investments	–	–	–	–	–	23 590	23 590	–
Deferred tax assets	–	–	–	–	–	102 936	102 936	–
Non-current assets held for sale	–	–	–	–	–	5 510	5 510	–
Loans and advances	3 652 205	–	–	62 420	–	(85 051)	3 629 574	12.57
Derivative financial instruments	–	53	–	–	–	21 353	21 406	–
Negotiable securities	19 895	114 007	114 985	–	19 015	–	267 902	9.34
Bank term deposits	–	–	35 276	–	–	–	35 276	7.22
Cash and cash equivalents	1 290 685	–	–	–	–	110 252	1 400 937	7.22
Total assets	4 962 785	114 060	150 261	62 420	19 015	510 193	5 818 734	
Equity and liabilities								
Shareholders' equity	–	–	–	–	–	1 437 671	1 437 671	–
Deferred tax liabilities	–	–	–	–	–	18 870	18 870	–
Deposits	2 676 096	292 106	666 650	5 560	–	606 186	4 246 598	6.73
Derivative financial instruments	6 140	1 438	–	–	–	8 652	16 230	–
Provisions and other liabilities	–	–	–	–	–	38 142	38 142	–
Other accounts payable	–	–	–	–	–	61 153	61 153	–
Tax	–	–	–	–	–	70	70	–
Total equity and liabilities	2 682 236	293 544	666 650	5 560	–	2 170 744	5 818 734	
Financial position interest sensitivity gap	2 280 549	(179 484)	(516 389)	56 860	19 015	–	1 660 551	
Derivative financial instruments	49 684	59 526	–	(70 501)	(38 709)	–	–	
Total net interest sensitivity gap	2 330 233	(119 958)	(516 389)	(13 641)	(19 694)	–	1 660 551	

Risk management and control

(continued)

Management of risk (continued)

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.

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

- the maintenance of a stock of readily available, high-quality liquid assets in excess of the statutory requirements as well as strong statement of financial position 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.

While international financial markets experienced significant stress in 2009, the South African domestic money market liquidity remained largely unaffected. Overall the Group's key liquidity risk metrics, which have been formulated to achieve a prudent liquidity profile, were maintained at acceptable levels. Through increased stress testing, scenario analysis and contingency planning, the Group continues to actively manage its stress funding sources and liquidity buffers to ensure that it exceeds the estimated stress funding requirements which could emanate from moderate to high-stressed liquidity events. Overall the Group's liquidity position remains strong.

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.

Risk management and control

(continued)

Management of risk (continued)

Liquidity risk (continued)

The remaining period to contractual maturity of financial liabilities of the Group at the reporting 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
2010					
Deposits	**3 051 846**	**574 149**	**253 830**	**658 218**	**80 601**
Derivative financial instruments	**1 316**	**19 985**	**2 077**	**147**	**4 597**
Other accounts payable	**71 849**				
Guarantees, letters of credit and		–	–	–	–
committed undrawn facilities	**445 832**	–	–	–	–
Operating lease commitments	**434**	**869**	**1 323**	**2 638**	**11 352**
Capital commitments	**4 106**	**1 254**	–	–	–
	3 575 383	**596 257**	**257 230**	**661 003**	**96 550**
2009					
Deposits					
Derivative financial instruments	3 283 724	295 726	276 889	418 630	6 066
Other accounts payable	1 720	5 742	1 190	–	7 578
Tax	61 153	–	–	–	–
Guarantees, letters of credit and	70	–	–	–	–
committed undrawn facilities	506 678	–	–	–	–
Operating lease commitments	396	793	1 179	1 886	7 011
Capital commitments	17 209	25 814	8 605	–	–
	3 870 950	328 075	287 863	420 516	20 655

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

	Assets R'000	Liabilities R'000	Total mismatch R'000
2010			
Maturing up to one month	**2 579 700**	**3 154 262**	**(574 562)**
Maturing between one and three months	**83 572**	**589 407**	**(505 835)**
Maturing between three and six months	**281 223**	**249 990**	**31 233**
Maturing between six months and one year	**47 455**	**623 053**	**(575 598)**
Maturing after one year	**2 942 409**	**77 167**	**2 865 242**
Non-contractual	**319 951**	**21 038**	**298 913**
	6 254 310	**4 714 917**	**1 539 393**
2009			
Maturing up to one month	2 182 345	3 382 879	(1 200 534)
Maturing between one and three months	122 559	298 338	(175 779)
Maturing between three and six months	122 685	270 899	(148 214)
Maturing between six months and one year	53 927	396 940	(343 013)
Maturing after one year	2 990 431	13 137	2 977 294
Non-contractual	346 787	18 870	327 917
	5 818 734	4 381 063	1 437 671

Risk management and control

(continued)

Basel III – influencing risk management developments at the Bank

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 implementation of Basel III is expected to have far reaching implications for banks in terms of minimum capital standards and liquidity requirements. In addition to this it is anticipated that the reforms will be accompanied by enhancements in supervision, risk management and governance requirements including added transparency and disclosure requirements. The Bank is monitoring developments and will ensure that it is well positioned to meet the added requirements of Basel III as approved for implementation by SARB.

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

Capital management

The Company 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 capital management strategy is focused on maximising shareholder value over time by optimising the level and mix of capital resources whilst ensuring sufficient capital is available to support the growth objectives of the Group. Decisions on the allocation of capital resources, conducted as part of the strategic planning and budget review, are based on a number of factors including growth objectives, return on economic and regulatory capital and the residual risk inherent to specific business lines. This is conducted as part of the Internal Capital Adequacy Assessment Process and strategic planning review on a regular basis. 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.

Capital adequacy and the use of regulatory capital are monitored by employing techniques based on the guidelines documented in the Regulations to the Banks Act and implemented by the SARB for supervisory purposes. The SARB uses the capital adequacy ratio of banks as a key supervisory tool. 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.

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

Capital to support the Group's needs is currently generated by retained earnings.

The approach to capital management has been further enhanced over the past year in line with Basel II and will remain a focus area for the future.

Risk management and control

(continued)

Capital management (continued)

The level of capital for the Bank is as follows:

	2010 R'000	2009 R'000
Risk weighted assets – Banking book		
Credit risk	**4 335 032**	3 917 762
Operational risk	**808 095**	775 636
Market risk	**2 350**	1 914
Equity	**10 940**	23 561
Other assets	**234 963**	169 447
	5 391 380	4 888 320
Net qualifying capital and reserves		
Primary capital	**1 276 395**	1 225 749
Share capital and share premium	**1 483 299**	1 483 299
Retained earnings	**10 659**	–
General reserves	**12 231**	12 231
Less: Deductions	**(229 794)**	(269 781)
Secondary capital	**5 161**	19 331
General allowance for credit impairment	**5 127**	19 297
Surplus resulting from a revaluation of specified assets	**34**	34
	1 281 556	1 245 080
Capital adequacy ratio (%)	**23.8**	25.5
Primary capital (%)	**23.7**	25.1
Secondary capital (%)	**0.1**	0.4

Corporate governance

The Boards of Directors of the Company and the Bank (collectively referred to as "the Board") hold joint Board meetings. The Board aims to entrench the collective behaviours and practices in the Group that will ensure delivery on our obligation to sound governance. The Board subscribes to and is committed to ensuring that the Group complies with the corporate governance principles of fairness, accountability, responsibility and transparency as set out in the third Report on Corporate Governance ("King III").

Although compliance with King III only becomes compulsory in the next reporting period (in accordance with the JSE Listings Requirements) the Group has made good progress in complying with the King III principles and statements in this regard are included in this report. Subsequent progress will remain on the Board's agenda for 2011.

The Board has taken cognisance of the provisions of the Companies Act, 2008 to ensure that it is appropriately informed and prepared for the implementation thereof.

The following is a summary of the corporate governance processes of the Group for the year ended 31 December 2010:

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 review and approve the non-executive Directors' remuneration and submit such for approval and ratification by shareholders at the AGM;
- annually review and approve executive Directors' remuneration and/or increases thereto and agree the remuneration of executive management;
- consider, approve, govern and review long-term incentive remuneration structures for the Group;
- annually approve the Group's financial budget (including 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;
- review and approve the audited financial statements and interim results;
- be responsible for ensuring that the Group complies with all relevant laws, regulations, 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 of 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, 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 and objective 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 upon termination of their term of office is conducted by the DAC. 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 retire on a three-year rotational basis. The service contract of the CEO, being three years, will expire in March 2012. The service contract of Mr Lopes, an executive Director seconded by the major shareholder, will be up for renewal in November 2011. Directors are required to retire from the Board at age 70 subject to the Board's discretion to allow a Director to continue in office beyond this age. Such Director is still subject to retirement by the rotation provisions as explained above.

Corporate governance
(continued)

1. Board of Directors (continued)
During the past year the Board appointed an executive Director of Finance, in accordance with the JSE Listings Requirements. Mr Kumbier, whose portfolio includes other executive areas of responsibility, took up his position on 1 June 2010. Ms S Rapeti, a black non-executive Director, resigned from the Board with effect 29 July 2010. Ms Rapeti brought valuable skills to the Board which will need to be replaced in due course.

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 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 2010, the Board, which has a unitary board structure, comprised of eight Directors, of which three were executives.

All the non-executive Directors are classified as independent. In accordance with King III an annual formal evaluation of the independence of non-executive Directors will be included in the performance evaluation of these Directors. Two of the non-executive 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 but will endeavour to attract a suitable black female to fill the vacancy left by the resignation of Ms Rapeti.

The Board has unrestricted access to all company information, records, documents, property and management. If required, Directors are entitled to obtain independent professional advice at the Group's expense.

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 and acts as custodian of good governance. The Group Secretary attends all Board and Board Committee meetings and has unfettered access to the Chairman. The Group Secretary provides a central source of advice and guidance on business ethics, compliance with good corporate governance and changes in legislation, 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.

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 responsibilities, 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. The Group Secretary is not a director of Mercantile.

3. Board Committees
The Board has appointed a number of Board Committees to assist the Board in carrying out its duties and responsibilities. This does not relieve the Board of any of its responsibilities and the Board critically evaluates the recommendations and reports of these committees before approving such recommendations or accepting such reports. These committees all operate in terms of Board approved charters, which define their roles. All Board Committees' charters are reviewed annually by the Board.

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 Board Committee meetings but will not be able to participate in the proceedings without the consent of the relevant chairman and will not have a vote.

All Directors who are not Board Committee members receive copies of all 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. The CEO and the executive Director Finance attend GAC meetings as permanent invitees. The Board is satisfied that the collective skills of the members of the GAC are appropriate relative to the size and circumstances of the Company.

Corporate governance
(continued)

3. Board Committees (continued)

3.1 GAC (continued)

GAC meetings are held at least four times per annum. The meetings of the GAC 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. 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, the executive Director Finance and the external auditors have unrestricted access to the chairman of the GAC. As defined in its charter, the primary objective of the GAC 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.

The GAC reviews, *inter alia*, accounting policies, the audited annual financial statements, interim results, internal and external auditors' reports, regulatory public disclosures required in terms of the Regulations to the Banks Act, the adequacy and efficiency of internal control systems, the effectiveness of management information systems, the internal audit process, 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 GAC 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 GAC and approved at the AGM. The GAC 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 meets with the external auditors separate from management at least annually.

The GAC carried out its function 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 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 has considered the expertise and experience of the executive Director Finance and confirm that it is satisfied that Mr K R Kumbier has the appropriate skills to adequately perform this function.

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 2010, in terms of IFRS, the Companies Act, the Banks Act and the JSE Listings Requirements.

3.2 RMC

The RMC comprises five members, three of whom are independent non-executive Directors, the CEO and an executive Director. The Chairman of the Board chairs the RMC. The Board has considered the position of the chair of the RMC in view of Principle 2.16 (45.1) of King III and is satisfied that the Chairman of the Board is the most appropriate Board member to act as chairman of the RMC, given his experience and individual skills set. This position will be reviewed on an annual basis.

RMC meetings are held at least four times per annum. The RMC meetings are attended by the head of Risk, the head of Treasury Middle Office 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, the 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 capital management; 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.

Corporate governance
(continued)

3. Board Committees (continued)

3.2 RMC (continued)

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 62 to 74.

3.3 DAC

The DAC comprises all the non-executive Directors on the Board. The Chairman of the Board chairs the DAC and the CEO attends the meetings by invitation. Meetings are held at least four times per annum.

As defined in its charter, the primary objectives of the DAC 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 applies good 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).

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

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 and the CEO attends the meetings by invitation. The Remuneration Committee must meet at least twice per annum.

As defined in its charter, this 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);
- ensure alignment of the remuneration strategy/philosophy and policy with Mercantile's business strategy, desired culture, shareholders' interests, and commercial wellbeing;
- assist the Board in the consideration of performance-related incentive schemes, performance criteria and measurements, including allocations in terms of the Conditional Share Plan ("CSP")/other long-term awards;
- assist the Board in reviewing CEO performance against set management and performance criteria and approve guaranteed and performance-based individual remuneration including CSP allocations of the executive Directors, Company Secretary and senior management;
- ensure full disclosure of Director remuneration in the annual report on an individual basis, giving details of earnings, CSP awards, restraint payments and other benefits. Given the size and business activities of Mercantile, disclosure of the remuneration of the three most highly paid employees who are not Directors is not considered relevant and is therefore not applied, as no such employee is remunerated at a level higher than any executive Director; and
- assist the Board in reviewing the non-executive Directors' fees.

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

3.5 Transformation Committee

This committee comprises two independent non-executive Directors, one of whom acts as Chairman, and the CEO. This committee must meet at least four times per annum.

As defined in its charter, the Transformation 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

Corporate governance

(continued)

3. Board Committees (continued)

3.5 Transformation Committee (continued)

- assist the Board in determining which black individuals/ entities should be considered for direct ownership in the Group.

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

3.6 Technology Committee

This committee was constituted as a committee of the Bank in 2006 to specifically monitor and manage a special project of the Bank relating to the replacement of its core banking system. With the successful completion of the project in July 2010, the Technology Committee has been refocused to assist the Board in its duties with regard to the governance of Information Technology in accordance with the provisions of King III. The reconstituted Technology Committee, as a Board Committee, comprises two independent non-executive Directors and two executive Directors. An independent non-executive Director chairs this committee.

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

- ensure that prudent and reasonable steps have been taken in regard to Information Technology ("IT") governance by developing and implementing an IT governance framework;
- strategically align IT with the performance and sustainability objectives of the Bank;
- concentrate on optimising expenditure and enhancing the value of IT;
- address the safeguarding and security of IT assets, continuity of operations and disaster recovery; and
- adequately protect and manage information.

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

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:

- Group EXCO;
- ALCO;
- CREDCOM;
- Employment Equity Committee;
- Business and Commercial Management Committee,
- Treasury Management Committee;
- Alliance Banking Management Committee;
- Human Resources Committee;
- IT Steering Committee;
- New Product Committee; and
- Procurement Committee.

All these committees operate in terms of their charters, which define their duties and responsibilities. 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. It encapsulates five elements which include compensation, benefits, work-life balance, performance-based recognition and development of career opportunities to help attract, motivate and retain the talent needed to achieve the Company's objectives and optimise management, i.e. involved employees who are enthusiastic about work and hence further the Company's interest. Bonus pools and long-term incentives are reviewed and monitored to align with the Company's risk management strategy.

To attract, motivate and retain employees, the Group ensures that remuneration practices are fair, equitable and competitive. The three main components 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 an 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.

Short-term incentives are important to support the pay for performance philosophy and form an important component of variable pay. Periodic reviews of the short-term incentive scheme take place at the discretion of the Board Remuneration Committee and/or executive Directors to ensure market competitiveness and alignment to regulatory requirements/good governance.

Corporate governance
(continued)

5. Remuneration philosophy (continued)
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 long-term incentive scheme, the Conditional Share Plan, was introduced in 2008 to replace the previous share option scheme and was amended in 2009. If at a future date the Board wishes to use the share option scheme it would be able to do so.

The remuneration of non-executive Directors takes into account the responsibilities of the role and the skills and experience of the individual whilst not losing sight of the requirement for market related, fair and defendable compensation from a regulatory and stakeholder viewpoint. King III requires fair and responsible remuneration policies in relation to non-executive Director remuneration and hence our Remuneration Committee advises the Board on appropriate remuneration for non-executive Directors, incentives such as share options/plans or rewards geared to the Company's share price or performance does not form part of the remuneration of non-executive Directors and shareholders approve non-executive Directors' fees.

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 Chairman of the GAC and administratively to the CEO, performs a function independent from any other function in the Group. The head of Internal Audit has direct and unrestricted access to the CEO and the Chairmen of the GAC, the RMC and the Board.

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

The Internal Audit Charter, which governs Internal Audit activities in the Group, was reviewed and revised by the Board during the year. The charter defines the role, objectives, authority and responsibility of the Internal Audit function in line with the requirements of the International Professional Practices Framework ("IPPF") of the Institute of Internal Auditors ("IIA") as well as the requirements of Regulation 48 of the Banks Act.

All operations, business activities and support functions are subject to Internal Audit review. The annual internal audit plan is risk-based and is approved by the GAC. Audits are conducted according to a risk-based approach and the audit plan is updated quarterly or as needed to reflect any changes in the risk profile of the Group. Updated plans are then presented to the GAC for review and approval.

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 is then taken.

Internal Audit also works closely with Risk and Compliance to ensure that audit issues of an ethical, compliance or governance nature are made known and appropriately resolved. The Compliance and Risk functions are also reviewed by Internal Audit in accordance with the annual audit plan.

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 environment.

An independent external quality assurance assessment of the Internal Audit function's conformance with the definition of internal auditing and the standards of the IPPF and whether the internal auditors apply the IIA Code of Ethics was conducted by Deloitte & Touche during the latter half of 2009. The overall assessment found that the function demonstrates some areas of good industry practice, as compared against local and international banking audit functions, while some areas require improvement. An action plan for implementing these improvements is progressing well and it is intended that another external quality assurance assessment shall be undertaken in 2012.

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;

Corporate governance
(continued)

7. External Auditor's services: outsourcing policy (continued)

- 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 ("the Engagement Letter") on the basis that the external auditors confirm in writing, prior to providing a service contained in the Engagement Letter, that such service does not impair their independence and that they may provide such service. The GAC has approved that 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 approval. 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 be submitted to the GAC for approval prior to the external auditors providing the service.

8. Compliance function

Compliance risk is the risk to earnings, capital and reputation arising from violations of, or non-compliance with laws, rules, regulations, supervisory requirements, prescribed practices or ethical standards. The role of the 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. The objective of the Compliance function is to ensure that the Group continuously manages and complies with existing and emerging regulations impacting on our business activities.

To ensure the independence of the Compliance function from the business activities of the Group, in accordance with the requirements stipulated in section 60A of the Banks Act, read with the provisions of regulation 49, 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 Board Committee, whenever necessary.

A Compliance Charter has been approved and is annually reviewed by the Board, 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. The Group's Compliance Officers are charged with developing and maintaining constructive working relationships with Regulators and Supervisors.

Compliance risk is managed within the organisation through the following key activities:

- creating awareness through training employees in respect of the impact and responsibilities related to legislative requirements;
- monitoring and reporting on the level of compliance with regulatory requirements, including reporting specific incidents of non-compliance to senior management and the Board;
- providing assurance that the risks relating to regulatory requirements are identified, understood and effectively managed; and
- consulting with the business units and providing compliance opinions with regard to new business ventures and processes.

Corporate governance
(continued)

8. Compliance function (continued)

The Compliance risk management tools provided to management include a comprehensive and consolidated Compliance Manual, Compliance Risk Management Plans, Compliance Opinions and Compliance Monitoring Reports.

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 considered by the GAC).

The challenge of the increasing pace and organisational impact of regulatory change continued in 2010, with a veritable raft of new regulation and regulatory changes, which has placed additional pressure on banks, and arguably, this increased workload has had a disproportionate impact on smaller banks.

The NCA, FICA, FAIS and the OHSA, were the key areas that the Compliance Department focused on during the year under review.

The NCA has imposed 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 carried out extensive training and monitoring reviews 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, international best practice and industry trends.

The ongoing implementation of FAIS was the other major imperative for business and the Compliance function during the year. To better regulate the quality of financial advice, the Financial Services Board has introduced amendments to the FAIS 'Fit and Proper' requirements, which deal with the qualifications and experience needed to perform a Representative or Key Individual role for a Financial Services Provider ("FSP"). Compliance, Business and Human Resources have developed a system to monitor and ensure compliance with the requirements of the 'Fit and Proper' status of Representatives and Key Individuals. In-house training is also provided to all relevant staff and comprehensive monitoring reviews are carried out 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. Compliance staff independently monitor the business units to ensure adherence to policies and procedures and business specific requirements.

No material incidents of non-compliance were reported during the year under review.

9. Dealing in securities of the Group

The Group's dealings in securities policy ("the policy") complies with the JSE Listings Requirements regarding dealings in the Group's securities by Directors and the Group Secretary. 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. During the year under review the Board decided to expand the policy to restrict trading by all employees of the Bank.

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

- when the Company is trading under a 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.

In addition, the policy emphasises that each individual (whether a Director or an employee) is obliged to comply with the provisions of the Securities Services Act No 36 of 2004, in regard to insider trading and inside information.

Corporate governance

(continued)

9. Dealing in securities of the Group (continued)

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 the appropriate disclosure, where relevant, is made on SENS in terms of the JSE Listings Requirements.

10. The Code

As a member of the Banking Association of South Africa the Group subscribes to the Code that promotes good banking practices by setting standards for disclosure and conduct, thereby providing valuable safeguards for its clients. The Group aims 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 veracity, 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)

The Group accepts conscious responsibility for a sustainable future. To this end the Group aims to incorporate its values in sustainable practices across the entire scope of its business activities, concerning the full spectrum of its stakeholders, both external and internal. During the period under review the Board considered and approved a Sustainability Policy in order to identify and document the themes, principles, strategy, objectives, management, performance and reporting of sustainability to enable the integration of sustainability into the culture of Mercantile.

The Sustainability themes are based on the recommendations set out in King III, read with the JSE Sustainability Reporting Index criteria and taking into account the size of our business and the community and industry that the Group operates in. The broad categories are:

- environment;
- society; and
- governance and related sustainability concerns.

The Board is responsible for ensuring that the Company operates as a responsible corporate citizen and will set the strategic guidelines for meeting Sustainability requirements recognised by the Company and has identified the following Sustainability objectives:

- adoption and implementation of a Sustainability strategy;
- incorporation of Sustainability principles into Mercantile's Corporate Governance practices, Code of Ethics, HR practices and Risk management;
- future definition of an Environmental Policy;
- future definition of a Social Responsibility Policy;
- introduction of products and services that have positive environmental and social impact; and
- reporting on Sustainability practices by means of a comprehensive Sustainability Report, in accordance with the principles of King III.

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 and honesty in all aspects of their activities, to be accountable for their actions and to comply with all applicable laws, regulations and the Group's policies in the performance of its banking activities. These activities are modelled on principles of ethics, thoroughness, honesty, transparency, stability and security in terms of its relationship with customers.

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 and a source of competitive advantage.

The standards as set out in the Code are designed to preserve the highest standards of professional confidentiality in terms of access to, management and processing of all information and, in general, in performance of our banking activity as a whole and ensure the adoption of best banking and financial practice and transparent, responsible and prudent business management.

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

11.2 Talent management

In 2008 the first graduate programme (Mercantile Trainee Programme) was implemented and the Group has successfully placed those individuals who remained on the programme. The second group of graduate trainees employed in 2009 will be finishing their programme in 2011.

Corporate governance
(continued)

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

11.2 Talent management (continued)

Following extensive research and consultation with employees, an Employee Value Proposition ("EVP") relating to Personal Growth and Career Development was launched in 2009. The EVP allows for the creation of opportunities for employees to improve their knowledge and to become multi-skilled. Those employees who embrace this opportunity are encouraged to apply for vacant positions that may arise within the organisation or explore other career opportunities within the Group in pursuit of their career goals. The incorporation of this initiative in our recruitment process, retention strategies for talent and performance management processes should result in more successful and targeted recruitment, motivated employees, improved performance and retention of employees.

The Alumni Talent programme implemented in 2010 will add value in terms of ex-employees acting as ambassadors by referring candidates and potentially rejoining the Company in the future after gaining new skills and experiences.

11.3 Employee satisfaction and commitment

The flexible work arrangement policy was introduced in 2009 following the employee satisfaction and commitment survey which was conducted in 2008. With the implementation of the flexible work schedules employees have the flexibility to meet family needs, personal obligations, avoid traffic and the stress of commuting during peak hours, thereby increasing personal control over their work schedule, reducing potential burnout and allowing employees to work when they accomplish the most. For the Company employee the policy increases morale, engagement and commitment, while absenteeism and turnover of valued employees are reduced.

The attrition rate is monitored on a quarterly basis. There has been a consistent decline in the attrition rate since 2007 from 19.6% to 15.8% in 2010, a decline of 3.8%.

11.4 Brand values and culture transformation

The Mercantile Brand values underpin and drive the culture transformation process and customer experience and satisfaction. With the recruitment of new employees and as the environment in which the Company operates changes, the Company culture may change.

The EVP and Employee Survey processes referred to are some of the mechanisms used to shape and measure progress in refining the culture.

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

11.5 Employee wellness

The overall wellbeing of our employees is regarded as very important and the Group offers a comprehensive Employee Assistance Programme, provided by an external company, to all our staff. This programme contributes to the reduction in health care costs and absenteeism thus potentially increasing productivity. 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. Employees receive health and wellness information on a monthly basis via email.

The absenteeism management programme implemented in 2009 aims to assist management and employees in understanding the impact of absenteeism, actively monitoring trends and engaging employees to potentially reduce the impact. This programme also supports the effective utilisation of the Employee Assistance Programme to address potential external drivers causing absenteeism, timeous identification of incapacity cases, reducing direct and indirect costs of absenteeism and working towards creating a wellness-culture.

11.6 Safety, health and environmental principles

The Group is, on an ongoing basis, striving to improve its facilities to ensure the safety and well being 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.

Corporate governance

(continued)

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

11.6 Safety, health and environmental principles (continued)

The Group acknowledges that the sound management of natural resources is a cornerstone of sustainable development. As a financial institution the Group recognises that its direct environmental impacts are associated primarily with the operation of the Group's office infrastructure. Systems aimed at reducing resource consumption over time are in place. The Group continuously explores ways in which to reduce paper, energy and water usage. The Group is cognisant that our business, through its 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 the Group is adhering to its Environmental Risk Management Policy.

The Group 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 Mastercard and Visa 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 prescribed by the card association 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.

The SMS service notifying cardholders of their above floor limit transactions is now offered to all credit card holders. The Group is aiming to offer the same service to all its debit card cardholders in 2011. The SMS service is expected to contribute to the existing fraud prevention measures.

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, 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.

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

Fraud other than credit card fraud:

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

The Forensic Investigator within Compliance investigates all incidents relating to fraud.

An incident is investigated when reported and all related evidence and statements are 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 South African Police Service.

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 business centre employees and affected head office employees receive training on what to report on and how to do the reporting. Training is repeated annually. The Policy caters for anonymous reporting, should the employee wish not to disclose his/her name.

An enhanced anonymous reporting system is in place. This allows all employees to report directly to Compliance 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.

Corporate governance

(continued)

12. Transformation (continued)

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:

12.1 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, Basic Conditions of Employment and Labour Relations legislation are 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 business/support service unit's key result areas. Targets were set 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 representation of black people has increased from 35% in 2004 to 59% in 2010. Although some progress has been made on the senior and middle management levels, 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.

The table below illustrates the number of staff per race category (as defined by the Department of Labour) as at 31 December 2010.

Occupational levels	Male				Female				Foreign nationals		Total
	A	C	I	W	A	C	I	W	Male	Female	
Top management	2	0	0	3	0	0	0	0	3	0	8
Senior management	1	1	0	12	0	0	0	4	0	0	18
Middle management	7	3	7	34	5	2	5	39	0	0	102
Junior management	14	4	6	13	19	17	6	52	0	0	131
Semi-skilled	27	16	7	2	62	36	9	19	0	0	178
Unskilled	6	0	0	0	0	0	0	0	0	0	6
Total permanent	57	24	20	64	86	55	20	114	3	0	443
Temporary employees	0	0	0	0	0	0	0	1	0	0	1
Grand total	57	24	20	64	86	55	20	115	3	0	444

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. In addition to the existing management training, more interventions for the senior managers as well as other managers will be implemented in 2011.

Corporate governance
(continued)

12. Transformation (continued)

12.2 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	98
• Corrective Counselling and Positive Discipline	15
• Absenteeism management training	26
2. Functional/Technical/Legislative	
• FAIS	72
3. Systems Training – BaNCS Classroom training	
• Course transaction and history data	72
• Manage instruments functionality on BaNCS	5
• Forex inward	8
• Forex outward	16
• Vostro payments/ STP/STP bulk payments	12
• Manage instructions	5
• Super user training	22
• Letters of credit	11
• OLLRR Queue	14
• Statements and certificates	45
• Credit management collections	20
• Fees and charges	5
4. Other	
• Safety first/First aid	24
• Induction	15
5. Various external training programmes	27
6. Study loans granted to staff	11 totalling R54 957

Participation in the BANKSETA Learnership programme commenced in 2004 and another two groups of learners – graduates and matriculants were up-skilled within the various business/support service units in the Company during 2010. The employment and retention of learners from previous programmes has been very successful.

Corporate governance
(continued)

12. Transformation (continued)

12.3 Corporate Social Investment

The Group is committed to the upliftment and transformation of communities and has participated in a number of projects initiated by the employees and/or the Bank. The initiatives which employees contributed to include the Sunshine Association, which supports children with disabilities, and the Heart & Stroke Foundation of SA annual fundraising and awareness campaign. Furthermore, the Group's Corporate Social Investment spend is aligned with our core business objectives in the form of sponsorships and/or donations to community initiatives identified by the Group.

12.4 Procurement

A targeted procurement strategy to enhance Broad Based Black Economic Empowerment ("BBBEE") has been adopted. The principles are detailed in the Group's Procurement Policy. The objective is to actively promote the effective support of suppliers and contractors from historically disadvantaged South African enterprises. Since 2008, the Group has achieved the targets as set out by the Department of Trade and Industry ("DTI") and the FSC. The Group envisages meeting the DTI 2014 target of 70% of procurement spend with BEE enterprises.

12.5 Loan approval to black SMEs

For purposes of the target setting the following definition of a BEE SME has been used:

- Black SME means a small or medium enterprise (with a turnover ranging from R500 000 per annum to R20 million per annum) which is a black company or a black empowered company;
- Black companies* mean companies that are more than 50% owned and are controlled by black people;
- Black empowered companies** mean companies that are more than 25% owned by black people and where substantial participation in control is vested in black people; and
- Black influenced companies*** mean companies that are between 5% and 25% owned by black people and with participation in control by black people.

The draft Financial Sector Code was published on 10 December 2010 for comment and is expected to be finalised during the course of 2011.

Based on previous objectives, growth targets, and actual performance the Group has projected a target of R600 million for 2011.

12.6 Ownership and control

On 5 October 2010 shareholders were advised that discussions with the short-listed candidates for the sale of 10% of the Group's equity were terminated based on the prevailing uncertain international market conditions. No further developments have taken place since then in this regard, but the Group remains committed to empowerment at shareholder level.

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 Bank Supervision Division of the SARB is the lead regulator for the Group. The Financial Services Board, the National Credit Regulator, the Registrar of Companies and the JSE regulate the various activities of the Group. The Group strives to establish and maintain open and active dialogue with regulators and supervisors. Processes are in place to respond proactively and pragmatically to emerging issues and the Group regularly reports to regulators and supervisory bodies. Where appropriate the Group participates in industry associations and discussion groups to maintain and enhance the regulatory environment in which the Group operates.

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 the press and 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

Name	Appointment date	Board (joint meetings)	Board Committees					
			GAC	RMC	DAC	Remuneration	Transformation	Technology
Number of meetings held during the year under review		◆ 6	5	4	4	3	4	6
Directors								
J A S de Andrade Campos	26.07.2002	C 6/6	▲	C 4/4	C 4/4	▲	4/4	▲
D J Brown	29.03.2004	6/6	▲	4/4	▲	▲	4/4	6/6
G P de Kock	23.11.2000	6/6	5/5	4/4	4/4	C 3/3	▲	6/6
L Hyne	1.06.2003	5/6	C 5/5	3/4	3/4	2/3		
A T Ikalafeng	16.11.2004	6/6	▲	▲	4/4	3/3	C 4/4	▲
K R Kumbier ¤	1.06.2010	2/6	▲	1/4 ❊	▲	▲	▲	▲
J P M Lopes	9.11.2005	6/6	▲	3/4 ❊	▲	▲	▲	6/6
T H Njikizana*	6.11.2008	6/6	5/5	▲	4/4	3/3	▲	C 1/6
S Rapeti ▼	29.07.2005	5/6	▲	▲	3/4	1/3	3/4	C 5/6

▲ Non-member of committee/permanent invitee. The ad hoc attendance by a Director of a meeting that he/she is not a member of is not disclosed.

C Chairman of meeting

◆ One of which was a two day Strategy Board meeting.

* Appointed Chairman of the Technology Committee effective 16 November 2010.

¤ Appointed as an executive Director effective 1 June 2010.

▼ Resigned as a Board member effective 29 July 2010.

❊ K R Kumbier replaced J P M Lopes as a member of the Risk and Capital Management Committee with effect from 15 November 2010.

Bank regulations public disclosure

The December 2010 bi-annual disclosure required in terms of Regulation 43 of the Bank Regulations is published on the Group's website.

Home Loan and Mortgage disclosure

The HLAMDA aims:

- to promote fair lending practices;
- disclosure by Financial Institutions of information regarding the provision of home loans; and
- to establish an Office of Disclosure to oversee compliance with legislation.

The following tables summarise the home loan statistics for 2010 per province and per race group:

Statistics per province

	Gauteng		KwaZulu Natal		Western Cape		Total	
	R'000	**Count**	**R'000**	**Count**	**R'000**	**Count**	**R'000**	**Count**
Received	211 798	157	694	2	3 000	3	215 492	162
Approved and taken up	150 116	136	694	2	3 000	3	153 810	141
Approved and not taken up	–	–	–	–	–	–	–	–
Declined	61 682	21	–	–	–	–	61 682	21
Pending, taken up but not disbursed	22 123	20	–	–	600	1	22 723	21
Disbursed	127 993	116	694	2	2 400	2 400	131 087	120

Statistics per race group

	African		Coloured		Indian		White		Total	
	R'000	**Count**	**R'000**	**Count**	**R'000**	**Count**	**R'000**	**Count**	**R'000**	**Count**
Received	2 356	7	1 304	7	9 797	8	202 035	140	215 492	162
Approved and taken up	1 810	6	1 304	7	9 797	8	140 899	120	1 532 810	141
Approved and not taken up	–	–	–	–	–	–	–	–	–	–
Declined	546	1	–	–	–	–	61 136	20	61 682	21
Pending, taken up but not disbursed	–	–	180	2	3 540	2	19 003	17	22 723	21
Disbursed	1 810	6	1 124	5	6 257	6	121 986	103	131 087	120

Analysis of shareholders

at 31 December 2010

Shareholders' spread

	2010	2009
Number of public shareholders	**6 246**	6 471

Percentage of shares held by:

	2010 Number	2010 %	2009 Number	2009 %
Public	**295 812 879**	**7.51**	296 985 329	7.54
Non-public	**3 643 105 545**	**92.46**	3 641 933 195	92.46
– Directors	**2 016 851**	**0.051**	–	–
– Employees	**110 600**	**0.003**	110 600	0.003
– Trustees of share incentive scheme	**26 959 899**	**0.684**	27 804 400	0.707
– Holders of 10% or more of shares	**3 614 018 195**	**91.75**	3 614 018 195	91.75
	3 938 918 524	**100**	3 938 918 524	100

Major shareholders holding in excess of 5% of the Company's share capital

	Number of shares	%
2010		
Caixa Geral de Depósitos SA	**3 614 018 195**	**91.75**
2009		
Caixa Geral de Depósitos SA	3 614 018 195	91.75

Performance on the JSE during the year

	2010	2009
Number of shares issued	**3 938 918 524**	3 938 918 524
Share price (cents)		
Year-end	**20**	23
Highest	**30**	28
Lowest	**19**	19
Number of shares traded	**53 711 509**	59 768 353
Value of shares traded (R'000)	**11 379**	13 134
Average price (cents)	**21**	23
Market capitalisation (R'000)	**787 784**	905 951
Market capitalisation net of treasury shares (R'000)	**782 392**	899 556

Group addresses

Mercantile Bank Group
Head Office
142 West Street, Sandown, 2196
PO Box 782699, Sandton, 2146
Tel: +27 11 302 0300
Fax: +27 11 883 776

Mercantile Insurance Brokers
Head Office
Mercantile Bank
142 West Street, Sandown, 2196
PO Box 782699, Sandton, 2146
Tel: +27 11 302 0300
Fax: +27 11 883 7765

Boksburg Business Centre
North Atlas Centre, cnr Atlas and
North Rand Roads, Boksburg, 1459
PO Box 31558, Braamfontein, 2017
Tel: +27 11 918 5276
Fax: +27 11 918 4159

Bruma Business Centre
11 Ernest Oppenheimer Boulevard,
Bruma, 2198
PO Box 31558, Braamfontein, 2017
Tel: +27 11 622 0916
Fax: +27 11 622 8833

Cape Town City Business Centre
Ground Floor, M&B House, Pier Place,
Foreshore, Cape Town, 8001
PO Box 51, Cape Town, 8000
Tel: +27 21 419 9402
Fax: +27 21 419 5929

Cape Town Tygerberg Business Centre
Ground Floor, Tygerpoort Building,
7 Mispel Street, Belville, 7530
PO Box 5436, Tygervalley, 7536
Tel: +27 21 910 0161
Fax: +27 21 910 0163

Comaro Crossing Business Centre
Shop FF9, Comaro Crossing Shopping
Centre, Orpen and Comaro Roads,
Oakdene, 2190
PO Box 31558, Braamfontein, 2017
Tel: +27 11 435 0640
Fax: + 27 11 435 1586

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

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

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

Sandton Business Centre
Ground Floor, 142 West Street,
Sandown, 2196
PO Box 31558, Braamfontein, 2017
Tel: +27 11 302 0775
Fax: +27 11 884 1821

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

Vanderbijlpark Business Centre
Shop 1 & 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 Business Centre
Tulbagh House, 11 Tulbagh Street,
Welkom, 9459
PO Box 2207, Welkom, 9460
Tel: +27 57 357 3143
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 12h30 on Wednesday, 1 June 2011 in the Boardroom, First Floor, Mercantile Bank, 142 West Street, Sandown, Sandton for the following purposes:

SPECIAL RESOLUTIONS

1 AMENDMENT TO THE ARTICLES OF ASSOCIATION OF THE COMPANY:

RESOLVED as a special resolution that the articles of association of the Company be and are hereby amended, with or without modification, by the deletion of the existing article 60 and the replacement thereof with a new article 60:

"At the annual general meeting held each year one-third of the non-executive directors, or if their number is not a multiple of three, then the number nearest to, but not less than one-third shall retire from office, provided that in determining the number of directors to retire no account shall be taken of any director appointed in terms of Article 48. The directors so to retire at each annual general meeting shall be firstly those retiring in terms of Article 58 and secondly those who have been longest in office since their last election or appointment. As between directors of equal seniority, the directors to retire shall, in the absence of agreement, be selected from among them by lot: provided that notwithstanding anything herein contained, if, at the date of any annual general meeting any director will have held office for a period of three years since his last election or appointment, he shall retire at such meeting; either as one of the directors to retire in pursuance of the foregoing or additionally thereto. A retiring director shall act as a director throughout the meeting at which he retires. The length of time a director has been in office shall, save in respect of directors appointed or elected in terms of the provisions of articles 48 and 58 of these presents, be computed from the date of his last election or appointment."

The reason for the amendment is to ensure that executive Directors, who are appointed by the Board of Directors and provide their services in terms of employment contracts with the Company, do not retire by rotation; and to align the articles with the provisions of the JSE Listings Requirements and the principles of the King Report on Governance for South Africa 2009 ("King III").

The effect of the amendment is to allow continuity of executive Directors on the Board of Directors.

Notice of Annual General Meeting
(continued)

2 AMENDMENT TO THE ARTICLES OF ASSOCIATION OF THE COMPANY:

RESOLVED as a special resolution, subject to the passing of Special Resolution 1 by the required majority of votes, that the articles of association of the Company be and are hereby amended, with or without modification, by the deletion of the existing article 65 and the replacement thereof with a new article 65:

"A managing director may be appointed by contract for a maximum of five years at any one time, provided always that the number of directors appointed in terms of this Article 65, plus those appointed in terms of Article 57 and Article 64, shall at no time constitute a majority of directors. The managing director shall be eligible for re-appointment by contract at the expiry of any period of appointment. Subject to the terms of his contract, he shall be subject to the same provisions as to removal as the other directors and if he ceases to hold the office of director from any cause he shall *ipso facto* cease to be a managing director."

The reason for and effect of the amendment is to bring it into line with the amendment of article 60.

3 AMENDMENT TO THE ARTICLES OF ASSOCIATION OF THE COMPANY:

RESOLVED as a special resolution that the articles of association of the Company be and are hereby amended, with or without modification, by the deletion of the following words from the existing article 64:

"…including for the purposes of these articles the office of chairman.."

The reason for the amendment is to align the articles with the provisions of the JSE Listings Requirements and the principles of King III, ensuring that the office of chairman is independent.

The effect of the amendment is to ensure that the office of chairman and that of the managing Director or executive Director is split.

4 AMENDMENT TO THE ARTICLES OF ASSOCIATION OF THE COMPANY:

RESOLVED as a special resolution that the articles of association of the Company be and are hereby amended, with or without modification, by inserting a new article 101A:

"101A Any document required to be sent by the Company in terms of article 100 and 101 may be made available in electronic format to persons who have agreed thereto in writing."

The reason for the amendment is to align the articles with the provisions of the Companies Amendment Act 35 of 2001 and to minimise the printing of Annual and Interim Reports.

The effect of the amendment is to allow members electronic access to the Company's financial statements.

The quorum for the consideration of Special resolutions is the presence or representation of members holding not less than 25% of the total votes and approval by a 75% majority of the votes cast by shareholders present or represented by proxy at this meeting is required for these resolutions to be passed.

Notice of Annual General Meeting

(continued)

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 2010.

Explanatory note:
At the Annual General Meeting the Directors must present the audited annual financial statements for the year ended 31 December 2010 to shareholders together with the reports of the Directors and auditors as contained in the 2010 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 2011 to 31 March 2012 for serving as a Director on the Board and Board Committees.

2.1 Chairman of the Mercantile Board: R1 565 000 per annum

2.2 Director of the Mercantile Board: R215 000 per annum

2.3 Director of Mercantile Bank Limited ("the Bank"), the major subsidiary of the Company: R46 000 per annum

2.4 Chairman of the Group Audit Committee: R85 000 per annum

2.5 Member of the Group Audit Committee: R65 000 per annum

2.6 Chairman of the Remuneration Committee: R57 000 per annum

2.7 Member of the Remuneration Committee: R65 000 per annum

2.8 Member of the Risk and Capital Management Committee: R65 000 per annum

2.9 Chairman of the Transformation Committee: R57 000 per annum

2.10 Member of the Transformation Committee: R65 000 per annum

2.11 Member of the Directors' Affairs Committee: R65 000 per annum

2.12 Chairman of the Technology Committee: R57 000 per annum

2.13 Member of the Technology Committee: R65 000 per annum

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 89 for the Board and Board Composition as at 31 December 2010.

Notice of Annual General Meeting
(continued)

3 AFFIRMATION OF THE APPOINTMENT OF A DIRECTOR TO FILL A VACANCY

"RESOLVED as an ordinary resolution to affirm the appointment of K R Kumbier, appointed as Executive Director: Finance and Business on 1 June 2010."

An abbreviated *curriculum vitae* of K R Kumbier is contained on page 99 of the Annual Report

Explanatory note:
The appointment of a Financial Director is required in terms of the JSE Listings Requirements. Article 48 of the Articles of Association determines that the directors shall have the power to fill any vacancy on the Board of Directors provided that such appointment be affirmed at the next annual general meeting.

4 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:

L Hyne (appointed 1 January 2003)
T A Ikalafeng (appointed 16 November 2004)

and being eligible offer themselves for re-election.

An abbreviated *curriculum vitae* of each Director offering themselves for re-election is contained on page 99 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.

5 AUDITORS

To recommend the re-appointment of Deloitte & Touche as independent auditors of the Company and to appoint R Eksteen as the designated auditor to hold office for the ensuing year.

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 2010 are contained on page 51.

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 and 8.

Notice of Annual General Meeting

(continued)

6 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.

7 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.

8 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."

Notice of Annual General Meeting
(continued)

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 Monday, 30 May 2011. The detail of these addresses are on page 3.

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 A de Villiers
Company Secretary
Sandton

22 March 2011

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

K R Kumbier, age 39, holds a BCompt degree from the University of South Africa and PGDA from the University of Cape Town. He is a Chartered Accountant (SA) and a Chartered Financial Analyst (CFA Institute). K R Kumbier was employed with the Standard Bank Group since 2001 in various positions, most recently as Provincial Director, Western Cape and Chief Operating Officer of Stanbic Bank Ghana Limited.

L Hyne, age 67, is a Chartered Accountant (SA). He attended Executive Programmes at Witwatersrand Graduate School of Business and Stanford University in the USA. He was admitted as a partner with Deloitte & Touche in 1970 and later became Chief Operating Officer and Deputy Chairman, from which position he retired in May 2003. He holds non-executive directorships with various companies.

T A Ikalafeng, age 44, holds a BSc (Business Administration) and MBA degrees from Marquette University in the USA, and completed executive development courses in Finance at Wits and Harvard Business School. A chartered marketer (CM(SA)), he has held various Marketing positions in the USA and Africa. He is founder and Managing Director of Brand Leadership Group and a member of the Vega School of Brand Communications advisory council.

Notes

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 12h30 on Wednesday, 1 June 2011 ("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 Wednesday, 1 June 2011 at 12h30 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. Special resolutions: Amendment to Articles of Association			
1.1. Special resolution 1: Amendment to Articles of Association – Article 60			
1.2. Special resolution 2: Amendment to Articles of Association – Article 65			
1.3. Special resolution 3: Amendment to Articles of Association – Article 64			
1.4. Special resolution 4: Amendment to Articles of Association – Article 101A			
2. Ordinary resolution number 1: Adoption of annual financial statements			
3. Ordinary resolution number 2: Non-executive Directors' remuneration			
4. Ordinary resolution number 3: Confirmation of the appointment of K R Kumbier to the Board on 1 June 2010			
5. Re-election of Directors			
5.1 Ordinary resolution number 4: Re-election of L Hyne			
5.2 Ordinary resolution number 4: Re-election of T A Ikalafeng			
6. Ordinary resolution number 5: Re-appointment of auditors			
7. Ordinary resolution number 6: Control of authorised but unissued shares			
8. Ordinary resolution number 7: General authority to issue shares for cash			
9. Ordinary resolution number 8: Signature of documents			

I hereby elect to receive all documents required to be sent by the Company in terms of Article 100 and 101 in electronic format, provided that the new Article 101A is adopted at the AGM, as set out above.	Yes	No

Signed this ______________ day of ______________ 2011

Signature of member(s) ______________________________

Assisted by me (where applicable) ______________________________

Please read the notes and instructions on the reverse hereof.

Form of proxy

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 Monday, 30 May 2011.

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 Monday, 30 May 2011.

Mercantile Bank
Holdings Limited
Member of CGD Group

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