Mercantile Bank
Member of CGD Group
Mercantile Bank Limited Reg. No. 1965/006706/06
An Authorised Financial Services Provider

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Directors' responsibility

In terms of the Companies Act of South Africa, 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 ended 31 December 2006 of Mercantile Bank Limited ("the Company", "the Bank" or "Mercantile").

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 Audit Committee 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 Company'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 Company's internal audit function conducts inspections, financial and specific audits and co-ordinates audit coverage with the external auditors.

The external auditors are responsible for reporting on the Company's annual financial statements.

The Company's annual financial statements are prepared in accordance with International Financial Reporting Standards and incorporate responsible disclosures in line with the accounting policies of the Company. The Company's annual financial statements are based on appropriate accounting policies consistently applied, except as otherwise stated and supported by reasonable and prudent judgements and estimates. The Board believes that the Company 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 5 to 38, have been approved by the Board and are signed on their behalf by:

J A S de Andrade Campos
Chairman
27 February 2007

D J Brown
Chief Executive Officer
27 February 2007

Certificate from the Company Secretary

In terms of section 268G(d) of the Companies Act, 1973, as amended ("the Act"), I certify that, to the best of my knowledge and belief, the Company has lodged with the Registrar of Companies ("Registrar") for the financial year ended 31 December 2006 all such returns as are required of a public company in terms of the Act, and that all such returns are true, correct and up-to-date, with the exception of the following return:

The submission of a copy of the audited financial statements of one of the subsidiaries of the Company in terms of section 302(4)(b) of the Act which is not deemed a material omission as the revenue from the said subsidiary is accounted for in the Company, and the Company applied for exemption to submit audited financial statements of subsidiaries of the Company, other than public companies, to the Registrar from 2007, which exemption has been granted. The exemption is renewable by way of application to the Registrar every two years.

R van Rensburg
Company Secretary
27 February 2007

Independent auditor's report

To the member of Mercantile Bank Limited

Report on the financial statements

We have audited the annual financial statements of Mercantile Bank Limited, which comprise the directors' report and the balance sheet at 31 December 2006, the income statement, the statement of changes in equity and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory notes as set out on pages 5 to 38.

Directors' responsibility for the financial statements

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

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall financial statement presentation. We believe that the audit evidence 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 at 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards and in the manner required by the Companies Act of South Africa.

DELOITTE & TOUCHE

Deloitte & Touche
Per Lito Nunes
Partner
27 February 2007

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

National Executive: G G Gelink Chief Executive, A E Swiegers Chief Operating Officer, G M Pinnock Audit, D L Kennedy Tax, L Geeringh Consulting, MG Crisp Financial Advisory, L Bam Strategy, C R Beukman Finance, T J Brown Clients & Markets, S J C Sibisi Public Sector and Corporate Social Responsibility, N T Mtoba Chairman of the Board, J Rhynes Deputy Chairman of the Board

A full list of partners and directors is available on request

Directors' report
for the year ended 31 December 2006

The directors have pleasure in presenting their report, which forms part of the audited annual financial statements of the Company for the year ended 31 December 2006.

1. Nature of business

The Company is a registered bank, incorporated in the Republic of South Africa ("South Africa"), and provides its clients with a full range of domestic and international banking services. In addition, it provides a full range of specialised financing, savings and investment facilities to the retail, commercial, corporate and alliance banking niche markets.

2. Holding company

Mercantile Bank Holdings Limited ("MBH"), a company incorporated in South Africa, wholly owns the Company. The ultimate holding company is Caixa Geral de Depósitos S.A. ("CGD"), a company registered in Portugal.

3. Financial results

Details of the financial results are set out on pages 6 to 38 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. The authorised and issued share capital of the Company is detailed in note 10 to the annual financial statements.

5. Dividends

No dividend was declared during the year under review (2005: nil).

6. 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 ∞
M J M Figueira *# (resigned effective 28 February 2007)
L Hyne ∞
A T Ikalafeng ∞
J P M Lopes *#
A M Osman ^+
S Rapeti ∞
K B Motshabi ∞(resigned 10 November 2006)

The Company Secretary is Ms R van Rensburg (appointed 23 March 2006) and the registered addresses are:

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

* Portuguese, ^ Mozambican, # Executive,
\+ Non-Executive, ∞Independent Non-Executive

7. Consolidated annual financial statements

Consolidated annual financial statements have not been presented as the Company is wholly owned by MBH, which is a company incorporated in South Africa.

8. Going concern

The Company's annual financial statements have been prepared on the going concern basis.

9. Special resolutions

No special resolutions were passed during the year under review.

10. Post-balance sheet events

No material events have occurred between the accounting date and the date of this report.

Accounting policies
for the year ended 31 December 2006

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

1. Basis of presentation

The Company's annual financial statements have been prepared in accordance with International Financial Reporting Standards and interpretations ("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.

2. Recognition of assets and liabilities

2.1 Assets

The Company 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 Company.

2.2 Liabilities

The Company 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.

2.3 Contingent liabilities

The Company 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 Company, 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.

3. Financial instruments

Financial assets and financial liabilities are recognised on the Company's balance sheet when the Company 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. Initial recognition is at cost, including transaction costs.

The Company derecognises a financial asset when:

- the contractual rights to the cash flows arising from the financial assets have expired or been forfeited by the Company; 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.

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

3.1 Derivative financial instruments

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

The Company uses the following derivative financial instruments to reduce its underlying financial risks:

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

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

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

Accounting policies
for the year ended 31 December 2006 (continued)

3. **Financial instruments** (continued)

3.1 **Derivative financial instruments** (continued)

- 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;
- the combined instrument is not measured at fair value with changes in fair value reported in income.

A derivative's notional principal reflects the value of the Company'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.

3.2 **Financial assets**

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

Cash and cash equivalents

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

Investments

Investments comprise negotiable securities and other investments. Negotiable securities consist of Government stock, Treasury bills, Landbank bills, corporate bonds and debentures while other investments consist of unlisted equity investments.

Negotiable securities for which there is no active secondary market are classified as loans and receivables and are carried at amortised cost subject to impairment.

Negotiable securities for which an active secondary market exists are designated as fair value through profit and loss.

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

Loans and advances

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

Other accounts receivable

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

3.3 **Financial liabilities**

The Company's financial liabilities include deposits and other accounts payable consisting of repurchase agreements, accruals, product-related credits and sundry creditors. All financial liabilities, other than liabilities designated at fair value and derivative instruments, are measured at amortised cost. Financial liabilities designated at fair value and derivative instruments are measured at fair value and the resultant gains and losses are included in income.

3.4 **Fair value estimation**

The fair value of publicly traded derivatives, securities and investments is based on quoted market values at the balance sheet date. In the case of an asset held by the Company, the current bid price is used as a measure of fair value.

Accounting policies
for the year ended 31 December 2006 (continued)

3. Financial instruments (continued)

3.4 Fair value estimation (continued)

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

3.5 Amortised cost

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

3.6 Impairments

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

Advances which are deemed uncollectible are written-off against the specific impairments. Loans previously written-off which subsequently become fully performing are re-incorporated in the advances portfolio. Both the specific and portfolio impairments raised during the year less the recoveries of advances previously written-off, are charged to income.

The Company reviews the carrying amounts of its advances to determine whether there is any indication that those advances have suffered an impairment loss. Where it is not possible to estimate the recoverable amount of an individual advance, the Company estimates the recoverable amount on a portfolio basis for a group of similar financial assets.

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' original effective interest rate.

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

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

4. Foreign currency transactions

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

5. Subsidiaries

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

Accounting policies
for the year ended 31 December 2006 (continued)

6. Associated companies

Associated companies are those companies in which the Company exercises significant influence, but not control or joint control, over their financial and operating policies and holds between 20% and 50% interest therein. These investments are designated as available-for-sale assets and are recognised at fair value. 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.

7. Property and equipment

7.1 Owner-occupied properties

Owner-occupied properties are held for use in the supply of services or for administrative purposes and are stated in the balance sheet at open-market fair value on the basis of their existing use at the date of revaluation, less any subsequent accumulated depreciation calculated using the straight-line method and subsequent accumulated impairment losses. The open-market fair value is based on the open market net rentals for each property. Revaluations are performed annually by independent registered professional valuators.

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

7.2 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 Company and the cost of the item can be measured reliably. All other repairs and maintenance are charged to income as they are incurred.

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

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

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

Leasehold improvements	5 – 10 years
Computer equipment	3 – 5 years
Furniture and fittings	10 years
Office equipment	5 – 10 years
Motor vehicles	5 years
Owner-occupied properties	50 years

Gains and losses on disposal of property and equipment are determined by comparing proceeds with the carrying amount and are recognised in income.

Accounting policies
for the year ended 31 December 2006 (continued)

8. Intangible assets

Computer software

Costs associated with developing or maintaining computer software programmes and the acquisition of software licenses are recognised as an expense as incurred. Costs that are directly associated with an identifiable and unique system controlled by the Company, and are expected to generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Costs include external software development and consultancy fees.

Direct computer software development costs 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 is reviewed annually for indication of impairment and is written down when the carrying amount exceeds the recoverable amount.

9. Provisions

Provisions are recognised when the Company has a present legal or constructive obligation, as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

10. Deferred income taxes

Deferred income tax is provided, using the balance sheet liability method, for all temporary differences arising between the tax values of assets and liabilities and their carrying values for financial reporting purposes. Expected tax rates are used to determine deferred income tax. Deferred tax assets relating to the carry forward of unused tax losses are recognised to the extent that it is probable that future taxable income will be available against which the unused tax losses can be utilised.

11. Sale and repurchase agreements and lending of securities

Securities sold subject to linked repurchase agreements ("repos") are reflected in the annual financial statements as cash and cash equivalents, when the transferee has the right to sell or repledge the collateral, and the counterparty liability is included in amounts due to other banks, deposits from banks, other deposits, or deposits due to customers, as appropriate. Securities purchased under agreements to resell ("reverse repos") are recorded as cash and cash equivalents. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective interest method. Securities lent to counterparties are also retained in the annual financial statements.

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

12. Instalment sales and leases

12.1 The Company as the lessee

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

12.2 The Company 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. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

Accounting policies
for the year ended 31 December 2006 (continued)

13. Interest income and interest expense

Interest income and expense are recognised in income for all interest bearing instruments measured at amortised cost using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Company estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and 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.

14. Fee, commission and dividend income

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

15. Retirement funds

The Company operates defined contribution funds, the assets of which are held in a separate trustee-administered fund. The retirement funds are funded by payments from employees and by the Company.

The Company contributions to the retirement funds are based on a percentage of the payroll and are charged to income as incurred.

16. Post-retirement medical benefits

The Company provides for post-retirement medical benefits to certain retired employees. These benefits are only applicable to employees who were members of the Company'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 Company provides for the present value of the obligations in excess of the fair value of the plan assets which are intended to offset the expected costs relating to the post-retirement medical benefits. The costs of the defined benefit plan are assessed using the projected unit credit method. Under this method, the cost of providing post-retirement medical benefits is charged to income so as to spread the regular cost over the service lives of employees in accordance with the advice of qualified actuaries, who value the plans at least every three years.

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 immediately. The Company's contributions to the post-retirement healthcare policy are charged to income in the year to which they relate.

17. Equity compensation plans

Share options in MBH are granted to employees of the Company at the discretion of the Remuneration Committee and approved by the Board of MBH. The Company has applied the requirements of IFRS 2 to share-based payments.

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

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

18. General credit-risk reserve

Banks Act circular 21/2004 requires that a general credit-risk reserve be recognised within Shareholders' equity for any shortfall between total impairments raised in terms of IAS 39 and the provisions required in terms of Regulation 28 of the Regulations relating to Banks. Such reserve is maintained through an appropriation of distributable reserves to a general credit-risk reserve.

19. Critical accounting estimates and judgements

The Company 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.

Accounting policies
for the year ended 31 December 2006 (continued)

19. Critical accounting estimates and judgements (continued)

19.1 Impairment losses on loans and advances

The Company reviews its loan portfolios to assess impairment on a monthly basis. In determining whether an impairment loss should be recorded in income, the Company makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in the Company, or national or local economic conditions that correlate with defaults on assets in the Company. 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 derivatives

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

19.3 Impairment of available-for-sale equity investments

The Company 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 Company evaluates, among other factors, the normal volatility in share price. In addition impairment may be appropriate when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology and 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 Company recognises liabilities for anticipated tax audit 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. Comparative figures

Where necessary, comparative figures have been restated to be consistent with the disclosure in the current year. Details of restatements are provided in note 26.

21. Recent accounting developments

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

IFRS 7 (Financial Instruments: Disclosures) was issued during June 2005 but is only effective for annual periods beginning on or after 1 January 2007.

Accounting policies
for the year ended 31 December 2006 (continued)

21. **Recent accounting developments** (continued)

The Company is subject to IFRS 7 as this standard supersedes IAS 30 (Disclosures in the Financial Statements of Banks and Similar Financial Institutions) and supplements the principles of IAS 32 and IAS 39. The Company will apply IFRS 7 from the year ending 31 December 2007.

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

IFRIC 8 (Scope of IFRS 2) was issued during January 2006 but is only effective for annual periods beginning on or after 1 May 2006. The Company will apply IFRIC 8 from the year ending 31 December 2007.

IFRIC 9 (Re-assessment of Embedded Derivatives) was issued during March 2006 but is only effective for annual periods beginning on or after 1 June 2006. The Company will apply IFRIC 9 from the year ending 31 December 2007.

IFRIC 10 (Interim Financial Reporting and Impairment) was issued during July 2006 but is only effective for annual periods beginning on or after 1 November 2006. The Company will apply IFRIC 10 from the year ending 31 December 2007.

IFRIC 11 (Interim Financial Reporting and Impairment) was issued during November 2006 but is only effective for annual periods beginning on or after 1 March 2007. The Company will apply IFRIC 11 from the year ending 31 December 2008.

Balance sheet
at 31 December 2006

	Note	2006 R'000	2005 R'000
ASSETS			
Intangible assets	1	**11 549**	7 018
Property and equipment	2	**21 531**	25 764
Other accounts receivable	3	**161 901**	33 765
Interest in subsidiaries	4	**73 181**	65 611
Other investments	5	**10 813**	5 661
Loans and advances	6	**2 066 432**	1 458 677
Derivative financial instruments	7	**31 134**	36 757
Negotiable securities	8	**405 016**	379 028
Cash and cash equivalents	9	**1 683 974**	1 408 972
Total assets		**4 465 531**	3 421 253
EQUITY AND LIABILITIES			
Shareholder's equity		**682 772**	566 588
Share capital and share premium	10	**1 483 300**	1 483 300
General reserve		**12 231**	12 231
Property revaluation reserve		**69**	69
Available-for-sale reserve		**29 869**	11 786
General credit-risk reserve		**13 954**	10 835
Accumulated loss		**(856 651)**	(951 633)
Liabilities		**3 782 759**	2 854 665
Deposits	11	**3 542 031**	2 639 377
Derivative financial instruments	7	**29 189**	38 531
Provisions	12	**38 964**	31 618
Other accounts payable	14	**172 575**	145 139
Total equity and liabilities		**4 465 531**	3 421 253

Income statement
for the year ended 31 December 2006

	Note	2006 R'000	2005 R'000 (restated)
Interest income	17	361 270	254 204
Interest expenditure	18	(189 143)	(113 238)
Net interest income before recoveries		172 127	140 966
Net recovery of credit losses	6	1 425	22 182
Net interest income after recoveries		173 552	163 148
Net loss on disposal and revaluation of investments		(1 513)	(1 528)
Non-interest income	19	146 084	110 313
Net interest and non-interest income		318 123	271 933
Operating expenditure	20	(228 624)	(228 450)
Profit before taxation and exceptional item		89 499	43 483
Recovery of amounts previously written off in respect of the release of the CGD guarantee	6	8 602	23 119
Profit before taxation		98 101	66 602
Taxation	21	–	–
Attributable profit after taxation		98 101	66 602

Statement of changes in equity for the year ended 31 December 2006

	Share capital R'000	Share premium R'000	General reserve R'000	Property revaluation reserve R'000	Available for-sale reserve R'000	General credit-risk reserve R'000	Accumulated loss R'000	Total R'000
Shareholder's equity at 31 December 2004	124 969	1 358 331	12 231	95	4 278	31 668	(1 016 116)	515 456
Net movement for the year	–	–	–	(26)	7 508	(20 833)	64 483	51 132
Change in accounting policy – IAS 32 and 39 credit-risk impairments	–	–	–	–	–	–	(22 952)	(22 952)
Release of general credit-risk reserve on adoption of IFRS in respect of credit risk impairments	–	–	–	–	–	(22 952)	22 952	–
Gains and losses on remeasurement to fair value	–	–	–	–	5 950	–	–	5 950
Release to income on disposal of available-for-sale financial assets	–	–	–	–	1 558	–	–	1 558
Increase in general credit-risk reserve	–	–	–	–	–	2 119	(2 119)	–
Revaluation of property	–	–	–	(26)	–	–	–	(26)
Attributable profit after taxation	–	–	–	–	–	–	66 602	66 602
Shareholder's equity at 31 December 2005	**124 969**	**1 358 331**	**12 231**	**69**	**11 786**	**10 835**	**(951 633)**	**566 588**
Net movement for the year	**–**	**–**	**–**	**–**	**18 083**	**3 119**	**94 982**	**116 184**
Gains and losses on remeasurement to fair value	–	–	–	–	15 055	–	–	15 055
Release to income on disposal of available-for-sale financial assets	–	–	–	–	3 028	–	–	3 028
Increase in general credit-risk reserve	–	–	–	–	–	3 119	(3 119)	–
Attributable profit after taxation	–	–	–	–	–	–	98 101	98 101
Shareholder's equity at 31 December 2006	**124 969**	**1 358 331**	**12 231**	**69**	**29 869**	**13 954**	**(856 651)**	**682 772**

Cash flow statement
for the year ended 31 December 2006

	Note	2006 R'000	2005 R'000 (restated)
Operating activities			
Cash receipts from customers	22.1	**519 983**	397 785
Cash paid to suppliers and employees	22.2	**(395 367)**	(328 804)
Dividends received		**973**	509
Taxation paid	22.3	**–**	(44)
Net increase in income earning assets	22.4	**(641 037)**	(505 989)
Net increase in deposits and other accounts	22.5	**799 776**	715 427
Net cash inflow from operating activities		**284 328**	278 884
Investing activities			
Purchase of property, equipment and intangible assets		**(13 213)**	(18 644)
Proceeds on sale of property, equipment and intangible assets		**39**	384
Proceeds on disposal of other investments		**–**	900
Decrease/(Increase) in interests in subsidiaries		**3 848**	(1 413)
Net cash outflow from investing activities		**(9 326)**	(18 773)
Net cash inflow for year		**275 002**	260 111
Cash and cash equivalents at beginning of year		**1 408 972**	1 148 861
Cash and cash equivalents at end of year	9	**1 683 974**	1 408 972

Notes to the annual financial statements for the year ended 31 December 2006

1. Intangible assets

	2006 R'000	2005 R'000
Computer software		
Cost at beginning of year	44 066	39 051
Additions	7 647	5 015
Disposals	(42)	–
Cost at end of year	**51 671**	**44 066**
Accumulated amortisation and impairment losses at beginning of year	(37 048)	(32 250)
Amortisation	(3 107)	(4 798)
Disposals	33	–
Accumulated amortisation and impairment losses at end of year	**(40 122)**	**(37 048)**
Net carrying amount at end of year	**11 549**	**7 018**

2. Property and equipment

	Owner-occupied property R'000	Leasehold improve-ments R'000	Computer equipment R'000	Furniture and fittings R'000	Office equipment R'000	Motor vehicles R'000	Total R'000
2006							
Open market value/cost at beginning of year	164	17 166	67 062	8 404	18 975	422	112 193
Additions	–	963	2 049	49	2 505	–	5 566
Disposals	–	–	(643)	(85)	(356)	(83)	(1 167)
Open market value/cost at end of year	**164**	**18 129**	**68 468**	**8 368**	**21 124**	**339**	**116 592**
Accumulated depreciation and impairment losses at beginning of year	–	(11 550)	(54 901)	(6 582)	(13 066)	(330)	(86 429)
Depreciation	–	(1 275)	(5 858)	(627)	(1 967)	(40)	(9 767)
Disposals	–	–	634	80	338	83	1 135
Accumulated depreciation and impairment losses at end of year	**–**	**(12 825)**	**(60 125)**	**(7 129)**	**(14 695)**	**(287)**	**(95 061)**
Net carrying amount at end of year	**164**	**5 304**	**8 343**	**1 239**	**6 429**	**52**	**21 531**

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

2. Property and equipment (continued)

	Owner-occupied property R'000	Leasehold improve-ments R'000	Computer equipment R'000	Furniture and fittings R'000	Office equipment R'000	Motor vehicles R'000	Total R'000
2005							
Open market value/cost at beginning of year	190	15 568	61 545	8 201	17 460	722	103 686
Revaluations	(26)		–	–	–	–	(26)
Additions	–	3 941	7 968	205	1 515	–	13 629
Disposals	–	(2 343)	(2 451)	(2)	–	(300)	(5 096)
Open market value/cost at end of year	**164**	**17 166**	**67 062**	**8 404**	**18 975**	**422**	**112 193**
Accumulated depreciation and impairment losses at beginning of year	–	(12 324)	(49 485)	(5 909)	(11 824)	(586)	(80 128)
Depreciation	–	(1 432)	(7 477)	(674)	(1 242)	(44)	(10 869)
Disposals	–	2 206	2 061	1	–	300	4 568
Accumulated depreciation and impairment losses at end of year	**–**	**(11 550)**	**(54 901)**	**(6 582)**	**(13 066)**	**(330)**	**(86 429)**
Net carrying amount at end of year	**164**	**5 616**	**12 161**	**1 822**	**5 909**	**92**	**25 764**

Note:

The owner-occupied property comprises stand 624 Malvern, Johannesburg, with a building thereon. The property is valued at the offer to purchase amount received.

	2006 R'000	2005 R'000
3. Other accounts receivable		
Items in transit	**7 743**	4 396
Loans to fellow subsidiaries and holding company (refer to note 24.2)	**13 532**	18 542
Loan to the Mercantile Share Incentive Trust (refer to note 24.2)	**3 097**	3 111
Pre-payments and deposits	**4 140**	3 692
Other receivables	**133 389**	4 024
	161 901	33 765

Other receivables includes amounts due from Alliance Partners which have been settled after year-end.

4. Interest in subsidiaries

	2006 R'000	2005 R'000
Unlisted		
Shares at fair value	**24 458**	15 202
Loans (refer to note 24.2)	**48 723**	50 409
	73 181	65 611

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

The loans bear interest at market related rates and have no fixed terms of maturity.

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

	2006 R'000	2005 R'000
5. Other investments		
Available-for-sale		
Unlisted – associated company	**3 626**	3 323
– other	**7 187**	2 338
	10 813	5 661
Directors' valuation of unlisted investments	**10 813**	5 661

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

	2006 R'000	2005 R'000
6. Loans and advances		
Category analysis		
Amortised cost	**2 053 778**	1 758 930
Current accounts	**460 389**	318 177
Credit card	**29 002**	137 638
Mortgage loans	**699 122**	529 247
Instalment sales and leases	**299 284**	209 642
Other advances	**565 981**	564 226
Fair value		
Other advances	**114 205**	129 292
	2 167 983*	1 888 222
Less: Impairment for credit losses	**(64 394)***	(268 665)
Less: Interest in suspense	**(37 157)***	(160 880)
	2 066 432	1 458 677

All loans and advances are denominated in South African Rand.

	2006 R'000	2005 R'000
Maturity analysis		
Repayable on demand	**701 009**	696 215
Maturing within six months	**105 259**	61 884
Maturing after six months but within 12 months	**119 327**	55 798
Maturing after 12 months	**1 242 388**	1 064 325
	2 167 983	1 888 222

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

	2006 R'000	2005 R'000
Impairment for credit losses		
Balance at beginning of year	**268 665**	294 264
Movements for year:		
Credit losses written-off	**(5 090)**	(39 826)
Impairments utilised in writing off sold legacy loans and advances	**(214 578)***	–
Net impairments raised	**15 397**	14 227
Creation of credit-risk impairments on adoption of IFRS	**–**	22 952
Other net impairments raised/(released)	**15 397**	(8 725)
Balance at end of year	**64 394**	268 665

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

	2006 R'000	2005 R'000
6. Loans and advances (continued)		
Comprising:		
Portfolio impairment	31 682	4 238
Specific impairment	32 712	264 427
Balance at end of year	64 394	268 665
Net recovery of credit losses		
Net impairments (raised)/released	(15 397)	8 725
Recoveries in respect of sold legacy loans and advances	7 345	–
Recoveries in respect of amounts previously written off	9 477	9 705
Other credit risk related provisions released	–	3 752
	1 425	22 182
Exceptional items as per income statement		
Recovery of amounts previously written off in respect of the release of the CGD guarantee	8 602	23 119

* Effective 1 December 2006, legacy loans and advances of R377.4 million were sold to a third party. Specific impairments and interest in suspense of R214.6 million and R157.3 million, respectively, were utilised in writing off this debt.

	Balance after interest in suspense R'000	Specific impairment R'000	Net balance R'000
Non-performing loans			
2006			
Category analysis			
Current accounts	9 159	5 959	3 200
Credit card	6 588	6 446	142
Mortgage loans	4 257	1 134	3 123
Instalment sales and leases	6 737	5 638	1 099
Other advances	19 668	13 535	6 133
	46 409	32 712	13 697
2005			
Category analysis			
Current accounts	1 830	–	1 830
Credit cards	67 826	67 579	247
Mortgage loans	28 729	12 182	16 547
Instalment sales and leases	52 355	51 186	1 169
Other advances	145 220	133 480	11 740
	295 960	264 427	31 533

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

7. 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
2006				
Held-for-trading				
Foreign exchange contracts	**1 022 312**	**30 402**	**461 355**	**13 350**
Interest rate swaps	**30 700**	**732**	**172 699**	**15 839**
	1 053 012	**31 134**	**634 054**	**29 189**
2005				
Held-for-trading				
Foreign exchange contracts	1 118 646	36 757	401 219	8 937
Interest rate swaps	100 000	–	315 832	29 594
	1 218 646	36 757	717 051	38 531

8. Negotiable securities

	2006 R'000	2005 R'000
Loans and receivables		
Treasury bills	**184 539**	129 509
Landbank bills	**9 867**	–
Debentures	**26 105**	58 226
Non-liquid bills and acceptances	**–**	56
Held as fair value through profit and loss		
Corporate bonds	**184 505**	191 237
	405 016	379 028
Maturity analysis		
Repayable within one month	**56 061**	153 175
Maturing within six months	**164 450**	34 616
Maturing after six months but within 12 months	**152 607**	–
Maturing after 12 months but within five years	**31 898**	191 237
	405 016	379 028

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

9. Cash and cash equivalents

	2006 R'000	2005 R'000
Cash and bank notes	**28 350**	19 946
Central Bank balances	**49 325**	35 719
Domestic bank balances	**88 011**	151 785
Foreign bank balances	**1 518 288**	1 201 522
	1 683 974	1 408 972

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

10. Share capital and share premium

	Number of issued ordinary shares	Share capital R'000	Share premium R'000	Total R'000
Opening and closing balance	**62 484 352**	**124 969**	**1 358 331**	**1 483 300**

Notes:

1. The total authorised number of ordinary shares is 62 630 000 shares (2005: 62 630 000 shares) with a par value of R2.00 per share.
2. No shares were issued during the financial years ended 31 December 2005 and 31 December 2006.
3. The unissued shares are under the control of the directors until the next annual general meeting.

11. Deposits

	2006 R'000	2005 R'000
Call deposits and current accounts	**1 483 034**	946 684
Savings accounts	**158 521**	155 853
Term and notice deposits	**1 817 336**	1 411 088
Negotiable certificates of deposit	**25 151**	35 472
Foreign bank deposits and loans	**57 989**	90 280
	3 542 031	2 639 377
Maturity analysis		
Repayable on demand and within one month	**2 106 799**	1 516 731
Maturing after one month but within six months	**1 205 089**	966 723
Maturing after six months but within 12 months	**216 378**	155 623
Maturing after 12 months	**13 765**	300
	3 542 031	2 639 377

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

12. Provisions

	Staff incentives R'000	Audit fees R'000	Post-retirement medical benefits R'000	Leave pay R'000	Onerous lease contracts R'000	Other risks R'000	Total R'000
At 31 December 2004	4 000	2 400	15 949	8 042	–	4 878	35 269
Additional provision raised	9 000	3 244	2 234	2 818	428	3 295	21 019
Charged to provision	(4 000)	(2 400)	(7 769)	(2 949)	–	(577)	(17 695)
Unutilised provision reversed	–	–	–	–	–	(6 975)	(6 975)
At 31 December 2005	9 000	3 244	10 414	7 911	428	621	31 618
Additional provision raised	9 553	2 100	2 439	2 522	–	5 000	21 614
Charged to provision	(8 171)	(3 244)	–	(2 134)	–	–	(13 549)
Unutilised provision reversed	–	–	–	–	(428)	(291)	(719)
At 31 December 2006	**10 382**	**2 100**	**12 853**	**8 299**	**–**	**5 330**	**38 964**

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

12. Provisions (continued)

Post-retirement medical benefits

Refer to note 13 for detailed disclosure of this provision.

Leave pay

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

Other risks

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

13. Post-retirement medical benefits

The Company operates a partly funded post-retirement medical scheme. The assets of the funded plans are held independently of the Company's assets in a separate trustee-administered fund. Independent actuaries value this scheme at least every three years. The last actuarial valuations were carried out at 31 December 2006.

A buy-out of member's post-retirement medical liability took place in 2005, during which some eligible members accepted the offer. Members that did not accept the offer remain eligible for post-retirement medical benefits.

	2006 R'000	2005 R'000
The amounts recognised in the balance sheet are as follows (refer to note 12):		
Present value of total service liabilities	18 989	16 651
Fair value of plan assets	(6 136)	(6 237)
Provident fund	(1 457)	(1 624)
Endowment bond	(3 729)	(4 104)
Annuities	(950)	(509)
Liability in the balance sheet	12 853	10 414
The amounts recognised in the income statement are as follows (refer to note 20):		
Current service cost	115	414
Interest costs	1 365	1 659
Expected return on plan assets	(396)	(575)
Actuarial loss	1 957	1 736
Employer benefit payments	(1 168)	(1 085)
Payments from plan assets	846	540
Effect on curtailment	(280)	(455)
Total included in staff costs	2 439	2 234
Reconciliation of the movement in the present value of total service liabilities:		
At beginning of year	16 651	22 277
Current service cost	115	414
Interest costs	1 365	1 659
Actuarial loss	2 306	1 610
Employer benefit payments	(1 168)	(1 085)
Net effect of settlements	–	(7 769)
Effect of curtailment	(280)	(455)
At end of year	18 989	16 651
Reconciliation of the movement in the fair value of plan assets:		
At beginning of year	6 237	6 328
Expected return on plan assets	396	575
Actuarial gain/(loss)	349	(126)
Payments from plan assets	(846)	(540)
At end of year	6 136	6 237

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

13. Post-retirement medical benefits (continued)

The principal actuarial assumptions used were as follows:

Discount rate	8.25% (2005: 8.5%) compounded annually
Investment return	9.25% (2005: 6.5%) compounded annually
Rate of medical inflation	7.25% (2005: 7.0%) compounded annually
Salary inflation	6.75% (2005: 6.5%) compounded annually

	2006 R'000	2005 R'000
14. Other accounts payable		
Accruals	6 949	5 380
Loans from fellow subsidiaries (refer to note 24.2)	189	121
Repurchase agreements	126 343	109 461
Product-related credits	26 081	11 606
Sundry creditors	13 013	18 571
	172 575	145 139

15. Contingent liabilities and commitments

15.1 Conditional buy-back obligation

In terms of a sale agreement, wherein the Company disposed of its asset finance book, the Company has an obligation to buy-back the credit agreement rights and obligations of customers that fail to meet their repayments. In 2006, by agreement, this obligation to repurchase was terminated.

	2006 R'000	2005 R'000
Capital balance outstanding	–	7 707

15.2 Guarantees and letters of credit

	2006 R'000	2005 R'000
Guarantees	269 402	261 763
Lending related	16 201	34 860
Mortgage	66 618	70 173
Performance	186 583	156 730
Letters of credit	11 662	26 058
	281 064	287 821

15.3 Commitments under operating leases

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

	2006 R'000	2005 R'000
Property rentals:		
Due within one year	4 042	3 852
Due between one and five years	6 191	9 721
	10 233	13 573
Motor vehicle rentals:		
Due within one year	55	103
Due between one and five years	–	66
	55	169

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.

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

16. Deferred taxation

A deferred tax asset has not been recognised for the deductible temporary differences and unutilised calculated tax losses of R939.6 million (2005: R980.3 million) due to the uncertain timing of the reversal of these losses and availability of future taxable income.

	2006 R'000	2005 R'000
17. Interest income		
Interest on:		
Cash and cash equivalents	126 688	82 325
Negotiable securities	31 139	27 957
Loans and advances	203 443	143 922
Amortised cost	187 547	134 230
Fair value	15 896	9 692
	361 270	254 204
18. Interest expenditure		
Interest on:		
Deposits	180 210	112 325
Repurchase agreements	8 933	913
	189 143	113 238
19. Non-interest income		(restated)
Transactional income	106 375	80 618
Fees and commission	95 920	78 896
Knowledge-based fees	10 455	1 722
Trading income	38 736	29 186
Foreign currency	29 141	24 758
Foreign currency commissions	6 658	5 698
Treasury operational gain/(loss)	2 937	(1 270)
Investment income – dividends	973	509
Associated company	966	429
Other	7	80
	146 084	110 313

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

	2006 R'000	2005 R'000 (restated)
20. Operating expenditure		
Auditor's remuneration		
Audit fees – current	5 250	5 163
– prior	121	200
Fees for other services – taxation	597	1 047
– IFRS consulting	100	230
– controls and processes review	–	181
	6 068	6 821
Professional fees		
Collections	1 155	3 329
Consulting	14 372	10 276
Legal	911	1 588
Technical and other	18 241	19 184
	34 679	34 377
Depreciation and amortisation (refer to notes 1 and 2)	12 874	15 667
Directors' emoluments (refer to note 24.3)		
Executive directors	8 499	5 899
Non-executive directors' fees	3 044	2 520
Share-based payments	849	311
	12 392	8 730
Lease charges		
Motor vehicles	36	37
Equipment	38	78
	74	115
Staff costs		
Salaries, wages and allowances	89 947	89 874
Post-retirement medical benefits (refer to note 13)	2 439	2 234
Contributions to retirement funds	5 776	5 746
Share-based payments excluding directors	1 329	413
Other	4 879	4 190
	104 370	102 457
Impairment and loss on sale of property and equipment	2	144
Operating leases – premises	14 068	15 972
Marketing and communication	5 616	7 212
Indirect taxation		
Non-claimable Value-Added Tax	7 291	7 942
Skills development levy	277	486
Regional Services Council levies	554	959
	8 122	9 387
Other operating costs	30 359	27 568
Total operating expenditure	228 624	228 450
Number of persons employed by the Company at year-end	411	413

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

	2006 R'000	2005 R'000
21. Taxation		
Direct taxation		
South African normal taxation	–	–
South African tax rate reconciliation		
South African standard tax rate (%)	29.0	29.0
Exempt income (%)	(1.0)	(0.8)
Deferred taxation not raised (%)	(292.6)	(227.2)
Tax losses (%)	264.6	199.0
Effective tax rate (%)	0.0	0.0
Estimated tax losses available for set-off against future taxable income	939 601	980 313

22. Cash flow notes

	2006 R'000	2005 R'000
22.1 Cash receipts from customers		(restated)
Interest income	361 270	254 204
Non-interest income and net loss on disposal and revaluation of investments	144 571	108 785
Adjusted for: Dividends received	(973)	(509)
Net loss on disposal and revaluation of investments	1 513	1 528
Revaluation of held-for-trading financial instruments	(11 822)	953
Net recoveries of credit losses	25 424	32 824
Total cash receipts from customers	519 983	397 785
22.2 Cash paid to suppliers and employees		
Interest expenditure	(189 143)	(113 238)
Operating expenditure	(228 624)	(228 450)
Adjusted for: Depreciation and amortisation	12 874	15 667
Loss on sale of property and equipment	2	144
Share-based payments	2 178	724
Increase/(Decrease) in provisions	7 346	(3 651)
Total cash paid to suppliers and employees	(395 367)	(328 804)
22.3 Taxation paid		
Amounts unpaid at beginning of year	–	(44)
Income statement charge	–	–
Less: Amounts unpaid at end of year	–	–
Total taxation paid	–	(44)

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

	2006 R'000	2005 R'000
22. Cash flow notes (continued)		
22.4 Net increase in income earning assets		
Increase in negotiable securities	**(25 988)**	(8 749)
Increase in loans and advances	**(615 049)**	(497 240)
Net increase in income earning assets	**(641 037)**	(505 989)
22.5 Net increase in deposits and other accounts		
Increase in deposits	**902 654**	523 859
(Decrease)/Increase in other accounts	**(102 878)**	191 568
Net increase in deposits and other accounts	**799 776**	715 427

23. Financial risk management

23.1 Foreign currency risk management

The Bank, in terms of approved policy limits, manages short-term foreign currency exposures relating to trade imports, exports and interest flows on foreign liabilities. The transaction exposures and material forward exchange contracts at year-end are summarised as follows:

	US Dollar R'000	Euro R'000	Pound Sterling R'000	Other R'000	Total R'000
2006					
Total foreign exchange assets	**1 459 295**	**37 348**	**28 834**	**4 285**	**1 529 762**
Total foreign exchange liabilities	**(24 402)**	**(10 890)**	**(22 193)**	**(329)**	**(57 814)**
Commitments to purchase foreign currency	**153 361**	**61 023**	**4 753**	**12 827**	**231 964**
Commitments to sell foreign currency	**(1 588 540)**	**(87 718)**	**(11 911)**	**(16 601)**	**(1 704 770)**
Year-end effective net open foreign currency positions	**(286)**	**(237)**	**(517)**	**182**	**(858)**
2005					
Total foreign exchange assets	1 133 799	61 959	26 848	2 708	1 225 314
Total foreign exchange liabilities	(17 685)	(49 082)	(22 324)	(1 057)	(90 148)
Commitments to purchase foreign currency	83 036	52 113	–	40 072	175 221
Commitments to sell foreign currency	(1 199 681)	(65 521)	(5 435)	(41 635)	(1 312 272)
Year-end effective net open foreign currency positions	(531)	(531)	(911)	88	(1 885)

The forward exchange contracts above have maturity dates within 12 months of the year-end. The highest and lowest rates inherent in the above contracts have been set out per foreign currency below:

	Highest rate		Lowest rate	
Foreign currency	**2006**	2005	**2006**	2005
US Dollar	**8.08**	7.00	**6.09**	6.25
Euro	**10.31**	8.60	**9.03**	7.49
Pound Sterling	**14.62**	11.70	**13.13**	11.12
Swiss Franc	**6.45**	5.26	**5.81**	5.00
Australian Dollar	**0.17**	0.22	**0.18**	0.22

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

23. Financial risk management (continued)

23.2 Credit risk management

Potential concentrations of credit risk consist mainly of short-term cash, cash equivalent investments, advances and other receivables.

The Company limits its counterparty exposures to its money market investment operations by only dealing with well-established financial institutions of high credit standing. The credit exposure to any one counterparty is managed by setting transaction/exposure limits, which are reviewed by the Risk Management Committee.

Advances and other receivables comprise a large number of customers, dispersed across different industries and geographical areas. Ongoing credit evaluations are performed on the financial condition of these customers. Advances and other receivables are presented net of impairment for credit losses and interest in suspense.

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

At year-end, the Company did not consider there to be any significant concentration of risk, which had not been insured or adequately provided for. There were no material credit exposures in advances made to foreign entities at year-end, except for the deposits with CGD as disclosed in note 24.2.

23.3 Liquidity risk management

The Company is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs and guarantees. The Company maintains cash resources to cover these exposures. The table below summarises assets and liabilities at balance sheet date of the Company into relevant maturity groupings, based on the remaining period to the contractual maturity date:

	Assets R'000	Liabilities R'000	Total mismatch R'000
2006			
Maturing up to one month	**1 841 358**	**2 347 528**	**(506 170)**
Maturing between one and three months	**484 548**	**804 066**	**(319 518)**
Maturing between three and six months	**419 297**	**401 022**	**18 275**
Maturing between six months and one year	**328 967**	**216 378**	**112 589**
Maturing after one year	**1 391 361**	**13 765**	**1 377 596**
	4 465 531	**3 782 759**	**682 772**
2005			
Maturing up to one month	1 472 282	1 711 069	(238 787)
Maturing between one and three months	500 391	688 265	(187 874)
Maturing between three and six months	310 798	280 868	29 930
Maturing between six months and one year	130 699	158 515	(27 816)
Maturing after one year	1 007 083	15 948	991 135
	3 421 253	2 854 665	566 588

23.4 Fair value of financial instruments

All financial instruments have been recognised in the balance sheet at fair value, other than assets classified as loans and receivables as well as liabilities that are not derivatives. Such assets and liabilities are carried at amortised cost which approximates fair value.

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

23. Financial risk management (continued)

23.5 Interest rate risk management

The Company takes on exposures that are subject to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Mismatches of interest rate repricing are monitored regularly by the Asset and Liability Committee. The table below summarises the Company's exposure to interest rate risks. Assets and liabilities are included at carrying amounts, categorised by the earlier of contractual repricing or maturity dates and also indicate their effective interest rates at year-end:

	Up to 1 month R'000	1 – 3 months R'000	3 – 12 months R'000	1 – 5 years R'000	Over 5 years R'000	Non-interest bearing R'000	Total R'000	Effective interest rate %
2006								
ASSETS								
Intangible assets	–	–	–	–	–	11 549	11 549	–
Property and equipment	–	–	–	–	–	21 531	21 531	–
Other accounts receivable	–	–	–	–	–	161 901	161 901	–
Interest in subsidiaries	–	–	–	–	–	73 181	73 181	–
Other investments	–	–	–	–	–	10 813	10 813	–
Loans and advances	1 952 227	–	–	31 074	83 131	–	2 066 432	11.74
Derivative financial instruments	31 134	–	–	–	–	–	31 134	–
Negotiable securities	56 060	164 450	152 607	31 899	–	–	405 016	8.72
Cash and cash equivalents	915 131	277 851	413 317	–	–	77 675	1 683 974	8.24
Total assets	2 954 552	442 301	565 924	62 973	83 131	356 650	4 465 531	
EQUITY AND LIABILITIES								
Shareholder's equity	–	–	–	–	–	682 772	682 772	–
Deposits	2 212 541	640 336	617 400	13 765	–	57 989	3 542 031	6.18
Derivative financial instruments	29 189	–	–	–	–	–	29 189	–
Provisions	–	–	–	–	–	38 964	38 964	–
Other accounts payable	126 343	–	–	–	–	46 232	172 575	–
Total equity and liabilities	2 368 073	640 336	617 400	13 765	–	825 957	4 465 531	
On balance sheet interest sensitivity gap	586 479	(198 035)	(51 476)	49 208	83 131	–	469 307	–
Derivative financial instruments	94 279	89 119	(10 700)	(105 899)	(66 799)	–	–	–
Total net interest sensitivity gap	680 758	(108 916)	(62 176)	(56 691)	16 332	–	469 307	–

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

23. Financial risk management (continued)

23.5 Interest rate risk management (continued)

	Up to 1 month R'000	1 – 3 months R'000	3 – 12 months R'000	1 – 5 years R'000	Over 5 years R'000	Non-interest bearing R'000	Total R'000	Effective interest rate %
2005								
ASSETS								
Intangible assets	–	–	–	–	–	7 018	7 018	–
Property and equipment	–	–	–	–	–	25 764	25 764	–
Other accounts receivable	18 878	–	–	–	–	14 887	33 765	–
Interest in subsidiaries	–	–	–	–	53 102	12 509	65 611	–
Other investments	–	–	–	–	–	5 661	5 661	–
Loans and advances	1 331 406	2 783	12 805	–	111 683	–	1 458 677	9.75
Derivative financial instruments	36 757	–	–	–	–	–	36 757	–
Negotiable securities	153 175	34 560	56	–	191 237	–	379 028	6.96
Cash and cash equivalents	580 163	440 032	335 293	–	–	53 484	1 408 972	6.51
Total assets	2 120 379	477 375	348 154	–	356 022	119 323	3 421 253	
EQUITY AND LIABILITIES								
Shareholder's equity	–	–	–	–	–	566 588	566 588	–
Deposits	1 696 340	507 693	435 044	300	–	–	2 639 377	4.58
Derivative financial instruments	38 531	–	–	–	–	–	38 531	–
Provisions	–	–	–	–	–	31 618	31 618	–
Other accounts payable	109 461	–	–	–	–	35 678	145 139	–
Total equity and liabilities	1 844 332	507 693	435 044	300	–	633 884	3 421 253	
On balance sheet interest sensitivity gap	276 047	(30 318)	(86 890)	(300)	356 022	–	514 561	–
Derivative financial instruments	94 279	89 119	(10 700)	(105 899)	(66 799)	–	–	–
Total net interest sensitivity gap	370 326	58 801	(97 590)	(106 199)	289 223	–	514 561	–

24. Related-party information

24.1 Identity of related parties with whom material transactions have occurred

The holding company and ultimate holding company is identified on page 5 in the Directors' report. Material subsidiaries of the Company are identified below. All of these entities and the directors are related parties. There are no other related parties with whom material transactions have taken place, other than as listed below.

24.2 Material related-party balances and transactions

The Company, in the ordinary course of business, enters into various financial services transactions with the ultimate holding company and its subsidiaries, the holding company, fellow subsidiaries, the share incentive trust and the Company's subsidiaries. These transactions are governed by terms no less favourable than those arranged with third parties. Loans to and from fellow subsidiaries and other transactions are detailed hereafter.

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

24. Related-party information (continued)

24.2 Material related-party balances and transactions (continued)

Balances with the holding company, subsidiaries, fellow subsidiaries and associated company:

	% Held	2006 R'000	2005 R'000
Loans to subsidiaries			
Portion 2 of Lot 8 Sandown (Pty) Limited	100	45 719	47 600
Lisabank Corporate Finance Limited	–	–	3 360
LSM (Troyeville) Properties (Pty) Limited	100	5 827	5 502
Less: Provisions held against loan accounts		(2 823)	(6 053)
		48 723	50 409
Loans to fellow subsidiaries and holding company			
Mercantile Insurance Brokers (Pty) Limited		622	596
Mercantile Bank Holdings Limited		12 901	13 754
Mercantile Registrars Limited		3 045	8 314
Weskor Beleggings (Pty) Limited		–	784
Less: Provisions held against loan accounts		(3 036)	(4 906)
		13 532	18 542
Loan from fellow subsidiary			
Mercantile Nominees (Pty) Limited		189	121
Loan to Share Incentive Trust		3 097	3 111
Loan to associated company			
Statman Investments (Pty) Limited		533	288
Deposits from fellow subsidiaries			
Mercantile Insurance Brokers (Pty) Limited		1 986	2 109
Mercantile Nominees (Pty) Limited		752	531
Mercantile Bank Holdings Limited		138	87
Mercantile Registrars Limited		7	53
Weskor Beleggings (Pty) Limited		–	50
		2 883	2 830

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

24. Related-party information (continued)

24.2 Material related-party balances and transactions (continued)

Transactions with the holding company, subsidiaries, fellow subsidiaries and associated company:

	2006 R'000	2005 R'000
Interest received from:		
Portion 2 of Lot 8 Sandown (Pty) Limited	5 175	5 249
LSM (Troyeville) Properties (Pty) Limited	638	586
Weskor Beleggings (Pty) Limited	21	79
Statman Investments (Pty) Limited	38	10
Interest paid to:		
Mercantile Insurance Brokers (Pty) Limited	99	95
Non-interest income earned from:		
Mercantile Insurance Brokers (Pty) Limited	247	595
Operating expenditure with:		
Portion 2 of Lot 8 Sandown (Pty) Limited	8 594	8 420
LSM (Troyeville) Properties (Pty) Limited	938	910

Balances and transactions with the ultimate holding company (CGD) and its subsidiary:

	2006 R'000	2005 R'000
Caixa Geral de Depósitos – Lisbon (Branch of CGD)	1 455 338	1 144 962
Nostro accounts	3 721	917
Vostro accounts	(4 734)	(8 722)
Deposit accounts	1 456 351	1 152 767
Caixa Geral de Depósitos – Paris (Branch of CGD)	429	525
Nostro accounts	440	536
Vostro accounts	(11)	(11)
Caixa Geral de Depósitos – London (Branch of CGD)		
Vostro accounts	(19)	(19)
Caixa Geral de Depósitos (CGD)	1 455 748	1 145 468
Banco Comercial e de Investimentos (BCI) – Mozambique (Subsidiary of CGD)	(117 288)	(62 487)
Vostro accounts	(1 118)	(23)
Fixed deposits	(114 427)	–
Call and notice deposits	(1 743)	(62 464)
	1 338 460	1 082 981

Interest was paid to BCI – Mozambique amounting to R7.8 million (2005: R3.0 million).

Interest received from BCI – Mozambique and CGD in respect of the above balances during the year amounted to nil (2005: R0.1 million) and R80.4 million (2005: R35.0 million), respectively.

Post-retirement medical plan

Details of the post-retirement medical plan are disclosed in note 13.

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

24. Related-party information (continued)

24.3 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	Incentive* R'000	Share-based payments R'000	Total R'000
Director							
2006							
J A S de Andrade Campos	**1 014**	**–**	**–**	**–**	**–**	**–**	**1 014**
D J Brown	**–**	**1 973**	**–**	**211**	**2 215**	**849**	**5 248**
G P de Kock	**392**	**–**	**–**	**–**	**–**	**–**	**392**
M J M Figueira	**–**	**1 533**	**265**	**–**	**300**	**–**	**2 098**
L Hyne	**403**	**–**	**–**	**–**	**–**	**–**	**403**
A T Ikalafeng	**318**	**–**	**–**	**–**	**–**	**–**	**318**
J P M Lopes	**–**	**1 363**	**302**	**37**	**300**	**–**	**2 002**
K B Motshabi (resigned 10 November 2006)	**352**	**–**	**–**	**–**	**–**	**–**	**352**
A M Osman	**228**	**–**	**–**	**–**	**–**	**–**	**228**
S Rapeti	**337**	**–**	**–**	**–**	**–**	**–**	**337**
	3 044	**4 869**	**567**	**248**	**2 815**	**849**	**12 392**
2005							
J A S de Andrade Campos	888	–	–	–	–	–	888
D J Brown	–	1 891	–	151	1 881	311	4 234
G P de Kock	335	–	–	–	–	–	335
M J M Figueira	–	1 432	41	–	300	–	1 773
L Hyne	377	–	–	–	–	–	377
A T Ikalafeng	287	–	–	–	–	–	287
J P M Lopes (appointed 9 November 2005)	–	203	–	–	–	–	203
K B Motshabi	348	–	–	–	–	–	348
A M Osman	213	–	–	–	–	–	213
S Rapeti (appointed 29 July 2005)	72	–	–	–	–	–	72
	2 520	3 526	41	151	2 181	311	8 730

* The incentive relates to the current financial year but is only paid in the following financial year.

	2006 R'000	2005 R'000
Amounts paid by CGD to:		
M J M Figueira	**845**	851
J P M Lopes (appointed 9 November 2005)	**381**	58
	1 226	909

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

24. Related-party information (continued)

24.3 Director and director-related activities (continued)

Service agreements

D J Brown, Chief Executive Officer

Mr Brown's employment as Chief Executive Officer commenced on 31 March 2004 and is for a maximum period of five years. Mercantile may re-appoint Mr Brown at the expiry of the five-year period, provided that agreement is reached on the terms and conditions for his re-appointment.

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 of Directors of Mercantile from time to time.

M J M Figueira, Executive Director

Mr Figueira has been seconded to Mercantile by CGD.

Mr Figueira's employment in Mercantile commenced on 26 May 2004 for a period of three years. In terms of the service agreement Mr Figueira agreed to perform such duties, functions and services as are assigned to him from time to time by the Board of Directors and which are consistent and commensurate with his position as Executive Director. Mr Figueira resigned with effect from 28 February 2007 to return to Portugal.

J P M Lopes, Executive Director

Mr Lopes has been seconded to Mercantile by CGD.

Mr Lopes's employment in Mercantile commenced on 9 November 2005 and it will last for a period of three years. In terms of the service agreement Mr Lopes agreed to perform such duties, functions and services as are assigned to him from time to time by the Board of Directors and which are consistent and commensurate with his position as Executive Director.

Share options

On 5 October 2004, 5 000 000 share options in Mercantile Bank Holdings Limited were granted to D J Brown at an exercise price of 18 cents each. A further 7 000 000 share options were granted on 22 March 2006 at an exercise price of 40 cents each (refer to note 25).

Directors' interests

No directors held beneficial and/or non-beneficial interests, directly or indirectly, in shares issued by Mercantile Bank Holdings Limited.

25. Share incentive scheme

The options granted are in respect of the holding company, Mercantile Bank Holdings Limited, to the employees of the Bank.

Options may be exercised in respect of 33% of the option shares after the expiration of two years from the offer date, in respect of a further 33% after the expiration of three years from the offer date and the remaining option shares after the expiration of four years from the offer date. Such percentages are to be carried forward on a cumulative basis. Should the options not be exercised by the fifth anniversary date of the offer, the option holder is 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 will lapse. The same rule applies for the seventh, eighth, ninth and tenth anniversary of the offer date until the options in question have either lapsed or been exercised.

The number of shares, which could be utilised for the purposes of the scheme are 393 891 852 (2005: 787 783 705), which is 10% (2005: 20%) of the issued share capital of the Mercantile Bank Holdings Limited at year-end. The number of scheme shares that may be issued to a single participant is 59 083 778, or 1.5% of the total number of issued shares. The table below sets out the movements in the options:

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

25. Share incentive scheme (continued)

Grant date	Exercise price (cents)	Options at beginning of year	Granted during year	Forfeited during year	Exercised during year	Options at end of year	Exercisable options at end of year	Relating to directors[1]
2006								
20 November 2001	32	5 343 000	–	(1 400 000)	–	3 943 000	3 943 000	–
11 February 2002	32	200 000	–	–	–	200 000	200 000	–
5 October 2004	18	5 000 000	–	–	–	5 000 000	1 650 000	5 000 000
7 October 2004	17	2 600 000	–	(100 000)	(500 000)	2 000 000	660 000	–
3 January 2005	15	700 000	–	–	–	700 000	–	–
11 February 2005	20	500 000	–	–	–	500 000	–	–
1 April 2005	39	1 000 000	–	–	–	1 000 000	–	–
27 July 2005	32	750 000	–	–	–	750 000	–	–
2 January 2006	31	–	350 000	–	–	350 000	–	–
9 February 2006	41	–	750 000	–	–	750 000	–	–
3 March 2006	38	–	500 000	–	–	500 000	–	–
22 March 2006	40	–	16 200 000	(1 400 000)	–	14 800 000	–	7 000 000
		16 093 000	**17 800 000**	**(2 900 000)**	**(500 000)**	**30 493 000**	**6 453 000**	**12 000 000**
2005								
20 November 2001	32	6 293 000	–	(950 000)	–	5 343 000	5 343 000	–
11 February 2002	32	350 000	–	(150 000)	–	200 000	133 333	–
5 October 2004	18	5 000 000	–	–	–	5 000 000	–	5 000 000
7 October 2004	17	3 100 000	–	(500 000)	–	2 600 000	–	–
3 January 2005	15	–	700 000	–	–	700 000	–	–
11 February 2005	20	–	500 000	–	–	500 000	–	–
1 April 2005	39	–	1 000 000	–	–	1 000 000	–	–
27 July 2005	32	–	750 000	–	–	750 000	–	–
		14 743 000	2 950 000	(1 600 000)	–	16 093 000	5 476 333	5 000 000

(1) Refer to note 24.3.

Inputs into the Black-Scholes model in determining the charge for share-based payments are as follows:

	2006	2005
Weighted average fair value share price	38 cents	31 cents
Weighted average exercise price	40 cents	28 cents
Expected volatility	92.3% – 98.7%	103.0%–127.2%
Option life	6 – 10 years	6 – 10 years
Risk free rate	7.3%	6.7% – 7.3%
Expected dividends	Nil	Nil

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

The Company recognised total expenses of R2.178 million (2005: R0.724 million) related to equity-settled share-based payment transactions.

Notes to the annual financial statements for the year ended 31 December 2006 (continued)

26. Prior year restatement

Non-interest income and operating expenditure in the income statement has been restated for 2005 in order to be consistent with the disclosure in the current year.

Certain costs incurred by Alliance partners are settled by Mercantile on their behalf and subsequently reimbursed by these Alliance partners to Mercantile. The reimbursements were previously treated as non-interest income and the costs as operating expenditure. The accounting treatment for 2006 has been changed whereby the reimbursements received are offset against the costs incurred.

	2005 R'000
Group	
Income statement	
Non-interest income	
Amount previously reported	116 504
Reimbursable expenses	(6 191)
Restated non-interest income	110 313
Operating expenditure	
Amount previously reported	234 641
Reimbursable expenses	(6 191)
Restated operating expenditure	228 450

Capital adequacy statement at 31 December 2006

	Risk weighting	Average assets 2006 R'000	Risk-weighted assets 2006 R'000	Risk-weighted assets 2005 R'000
Banking book				
Cash, off-balance sheet activities and central government transactions	0%	**2 101 793**	**–**	–
Landbank bonds	10%	**151 927**	**15 193**	14 726
Letters of credit and other bank advances	20%	**131 777**	**26 355**	31 059
Residential mortgage loans and performance-related guarantees	50%	**723 483**	**361 742**	294 388
Other assets including counterparty risk exposure	100%	**1 859 929**	**1 859 929**	1 292 550
		4 968 909	**2 263 219**	1 632 723

	2006 R'000	2005 R'000
Primary capital	**1 495 530**	1 495 530
Secondary capital	**43 259**	21 001
Impairments	**(856 650)**	(952 984)
Net qualifying capital and reserves	**682 139**	563 547

	2006 %	2005 %
Capital adequacy ratio	**30.1**	34.5
Primary capital	**28.2**	33.2
Secondary capital	**1.9**	1.3