Mercantile Bank Limited

Member of CGD Group

The Business Bank inspired by entrepreneurs

Mercantile Bank Limited
Registration Number: 1965/006706/06
An Authorised Financial Services
and Credit Provider NCRCP19
Member of CGD Group

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In terms of section 29(1)(e)(ii) of the Companies Act, it is confirmed that the preparation of these annual financial statements is the responsibility of M E L Teixeira (CA)SA, the Chief Financial Officer of the Bank.

These annual financial statements have been audited in compliance with the requirements of section 29(1)(e)(i) of the Companies Act.

GLOSSARY OF TERMS

ABBREVIATION:	DEFINITION/DESCRIPTION:
AC	Audit Committee
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
CGD	Caixa Geral de Depósitos S.A., a company registered in Portugal and the ultimate holding company
Companies Act	Companies Act, No. 71 of 2008
CREDCOM	Credit Committee
IFRS	International Financial Reporting Standards and Interpretations
MBHL	Mercantile Bank Holdings Limited, the holding company
Mercantile	Mercantile Bank Limited
RMC	Risk and Capital Management Committee
SARB	South African Reserve Bank
the Bank	Mercantile Bank Limited
the Board	The Board of Directors
the Company	Mercantile Bank Limited

DIRECTORS' RESPONSIBILITY

In terms of the Companies Act, the Directors are required to maintain adequate accounting records and 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 2013 of the Company.

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, and 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's annual financial statements.

The Company's annual financial statements are prepared in accordance with IFRS issued by the International Accounting Standards Board 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 are 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 56, have been approved by the Board and are signed on their behalf by:

J A S de Andrade Campos
Chairman

K R Kumbier
Chief Executive Officer

26 March 2014

CERTIFICATE FROM THE COMPANY SECRETARY

In terms of the provisions 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 2013, 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.

F J Schutte
Company Secretary

26 March 2014

INDEPENDENT AUDITOR'S REPORT

to the shareholder of Mercantile Bank Limited

REPORT ON THE FINANCIAL STATEMENTS

We have audited the annual financial statements of the Company, which comprise the statement of financial position as at 31 December 2013, the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, a summary of significant accounting policies and other explanatory information as set out on pages 7 to 56.

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 the requirements of 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 mis-statement, 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 mis-statement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls 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, these financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2013, and of its financial performance and its cash flows for the year then ended in accordance with IFRS and the requirements of the Companies Act of South Africa.

OTHER REPORTS REQUIRED BY THE COMPANIES ACT

As part of our audit of the financial statements for the year ended 31 December 2013, we have read the Audit Committee report and the Directors' report for the purpose of identifying whether there are material inconsistencies between the reports and the audited financial statements. The reports are the responsibility of the respective preparers. Based on reading the reports, we have not identified material inconsistencies between the reports and the audited financial statements. However, we have not audited the reports and accordingly do not express an opinion on the reports.

Deloitte & Touche

Deloitte & Touche
Registered Auditors

Per Danie Crowther
Partner

26 March 2014

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

AUDIT COMMITTEE REPORT

for the year ended 31 December 2013

The AC is a committee of the Board and has assumed the responsibilities of an audit committee in respect of all subsidiaries of MBHL, and therefore a separate AC has not been formed for the Bank. The AC assists the Board in fulfilling its monitoring and controlling responsibilities in terms of applicable legislation.

TERMS OF REFERENCE

The AC is a Board Committee appointed by the Board and is accountable to it. Its powers and terms of reference are delegated to it by the Board, and are formalised in its charter which is reviewed annually and approved by the Board.
The AC has executed its duties during the past financial year in accordance with its charter and the Companies Act.

COMPOSITION

The AC comprises three independent Non-Executive Directors. At 31 December 2013 the members were:

- L Hyne (Chairman) CA(SA)
- G P de Kock
- T H Njikizana CA(SA)

The Chief Executive Officer, Executive Officer, Chief Financial Officer, heads of Risk and Internal Audit, and representatives from the External Auditors attend the committee meetings by invitation. The External and Internal Auditors have unrestricted access to the AC Chairman or any other member of the Committee, as required.

MEETINGS

The AC held five meetings during the period under review. During their tenure as members of the Committee, all members attended each of these meetings.

STATUTORY DUTIES

In execution of its statutory duties during the financial year under review, the AC:

- nominated for appointment, as external auditor, Deloitte & Touche which, in its opinion, is independent of the Company;
- determined the fees to be paid to Deloitte & Touche as disclosed in note 25 to the annual financial statements;
- determined Deloitte & Touche's terms of engagement;
- believes the appointment of Deloitte & Touche complies with the relevant provisions of the Companies Act and King III;
- pre-approved all non-audit service contracts with Deloitte & Touche in accordance with its policy;
- received no complaints with regard to accounting practices and the internal audit of the Company, the content or auditing of its financial statements, the internal financial controls of the Company, and any other related matters; and
- advised the Board that regarding matters concerning the Company's accounting policies, financial control, records and reporting, it concurs that the adoption of the going concern premise in the preparation of the financial statements is appropriate.

INTERNAL FINANCIAL CONTROL AND INTERNAL AUDIT

In the execution of its delegated duties in this area, the AC has:

- reviewed and recommended the internal audit charter for approval;
- evaluated the independence, effectiveness and performance of the internal audit function;
- reviewed the effectiveness of the Company's system of internal financial controls;
- reviewed significant issues raised by the external and internal audit process, and the adequacy of corrective action in response to such findings; and
- reviewed policies and procedures for preventing and detecting fraud.

The head of Internal Audit functionally reported to the AC and had unrestricted access to the AC Chairman, and is of the opinion that significant internal financial controls operated effectively during the period under review.

Based on the processes and assurances obtained, the AC believes that significant internal financial controls are effective.

REGULATORY COMPLIANCE

The AC has complied with all applicable legal, regulatory and other responsibilities.

EXTERNAL AUDIT

Based on processes followed and assurances received, the AC is satisfied that both Deloitte & Touche and the partner, Danie Crowther, are independent of the Bank. The AC confirmed that no reportable irregularities were identified and reported by the external auditors in terms of the Auditing Professions Act, No. 26 of 2005.

Based on our satisfaction with the results of the activities outlined above, the AC has recommended to the Board that Deloitte & Touche should be reappointed for 2014.

FINANCE FUNCTION

The AC believes that Ms M E L Teixeira, the Chief Financial Officer, who is responsible for Finance, possesses the appropriate expertise and experience to meet her responsibilities in that position. We are also satisfied with the expertise and adequacy of resources within the finance function.

In making these assessments, we have obtained feedback from both external and internal audit.

Based on the processes and assurances obtained, we believe that the accounting practices are effective.

FINANCIAL STATEMENTS

Based on the processes and assurances obtained, we recommend the current annual financial statements be approved by the Board.

On behalf of the AC

L Hyne
Chairman of the AC

26 March 2014

DIRECTORS' REPORT

for the year ended 31 December 2013

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 2013.

1. NATURE OF BUSINESS

The Company is a registered bank, incorporated in the Republic of 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 commercial, business, corporate and alliance banking niche markets.

2. HOLDING COMPANY

MBHL, a company incorporated in the Republic of South Africa, wholly owns the Company. The ultimate holding company is CGD, a company registered in Portugal.

3. FINANCIAL RESULTS

Details of the financial results are set out on pages 7 to 56 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 (2012: nil). The authorised and issued share capital of the Company is detailed in note 14 to the annual financial statements.

5. DIVIDENDS

A dividend of R25.701 million was declared on 26 February 2014 in respect of the year ended 31 December 2013 (2012: R29.672 million).

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)
K R Kumbier #	(Chief Executive Officer)
D J Brown (resigned 19 August 2013) °	
G P de Kock °	
L Hyne °	
A T Ikalafeng °	
J P M Lopes *#	
T H Njikizana ^°	
D Naidoo (resigned 23 August 2013) °	

**Portuguese, ^Zimbabwean, #Executive, +Non-Executive, °Independent Non-Executive*

F J Schutte, who was serving as Acting Company Secretary, was appointed as Company Secretary with effect from 12 April 2013.

The registered addresses of the Company are:

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

7. GOING CONCERN

The Directors, in performing their assessment of the 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 Company. The Directors believe the Company will have sufficient capital and cash resources to operate as a going concern in the year ahead.

8. SPECIAL RESOLUTIONS

On 23 May 2013, to approve and adopt the Company's Memorandum of Incorporation to ensure alignment to the requirements of the Companies Act, 71 of 2008.

On 28 May 2013, to approve the disposal of the majority of the assets of the subsidiary, Custom Capital (Pty) Ltd to a Special Purpose Vehicle in terms of an International Finance Corporation supported securitisation programme to the extent of R240 million.

9. EVENTS AFTER THE REPORTING PERIOD

Following the establishment of a special purpose vehicle in 2013, on 5 February 2014, R260 million of rental assets of the Bank's subsidiary, Custom Capital (Pty) Ltd, were securitised and notes to this value were issued.
The A class notes (R180 million) were issued to the International Finance Corporation and the D class notes (R80 million) to Custom Capital (Pty) Ltd.

ACCOUNTING POLICIES

for the year ended 31 December 2013

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 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.

IAS19 Employee Benefits (as revised in 2011), which became effective in the current reporting period, had an impact on the Company and was consequently applied. Detail of the changes are set out in note 29 to the annual financial statements. Other IFRS' that became effective in the current reporting period have had no impact on the Company.

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 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.

2.4 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 statement of financial position when the Company has become a party to the contractual provisions of that instrument. Regular 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 Company de-recognises a financial asset when:

- the contractual rights to the cash flows arising from the financial assets have expired or have 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 retaining control of the asset.

A financial liability is de-recognised 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 profit and loss.

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 and/or to enhance yields:

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

Derivative financial instruments ("derivatives") are not entered into for trading or speculative purposes. All derivatives are recognised on the statement of financial position. Derivative financial instruments are recorded at cost and are measured to fair value, excluding transaction costs, at each reporting date. Changes in the fair value of derivatives are recognised in profit and loss.

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

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.

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, bank term deposits, other investments, negotiable securities, loans and advances, and other accounts receivable.

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 Company seeks to demonstrate that by applying the fair value option, which measures fair value gains and losses in profit and loss, it significantly reduces measurement inconsistency that would otherwise arise from measuring derivatives and such designated financial assets, at amortised cost.

Available-for-sale financial assets

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 Company 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 Company 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.

Other investments

Investments consist of unlisted and listed equity investments. Other investments, which are an integral part of the Company'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 or disposed of. 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 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.

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

3.3 FINANCIAL LIABILITIES

The Company's financial liabilities include deposits 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.

3.4 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 Company, 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 Company 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.

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 to 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 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 Company writes off an impaired account. The Company's write-off policy sets out the criteria for write-offs which involve an assessment of the likelihood of commercially viable recovery of the carrying amount of an impaired financial asset. 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 in profit and loss immediately, except for the reversal of an impairment of equity instruments designated as available-for-sale, which is recognised in other comprehensive income.

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 profit and loss.

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

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

6. ASSOCIATED COMPANIES

Associated companies are those companies in which the Company exercises significant influence, but has no 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.

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

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 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.

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 profit and loss 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 for impairment where there are indicators of impairment and adjusted, if appropriate, at each reporting 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 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 de-recognised.

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

8. INTANGIBLE ASSETS

COMPUTER SOFTWARE

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

Computer software and licenses 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 10 years and are carried at cost less any accumulated amortisation and any accumulated impairment losses. The carrying amount of capitalised computer software and licenses 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.

9. 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 12 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.

10. TAX

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

10.1 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 Company’s liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting date.

10.2 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 are 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 Company 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 that 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.

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

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 when the Company intends to settle its current tax assets and liabilities on a net basis.

10.3 CURRENT AND DEFERRED TAX FOR THE PERIOD

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.

11. INSTALMENT SALES AND LEASES

11.1 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 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.

11.2 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. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

12. 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 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 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.

13. 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.

14. RETIREMENT FUNDS

The Company 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 Company. The Company contributions to the retirement funds are based on a percentage of the payroll and are charged to profit and loss as accrued.

15. 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 is 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. The interest cost and expected return on plan assets used in the previous version of IAS19 are replaced with a "net interest" amount under IAS19 (as revised in 2011), as well as the effect of settlements on the liability and plan assets are recognised immediately in profit and loss and any remeasurements of the defined benefit liability and assets (which includes actuarial gains and losses) are recognised immediately through other comprehensive income in order for the net post retirement asset or liability recognised in the consolidated statement of financial position to reflect the full value of the plan deficit or surplus.

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

16. 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.

16.1 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 profit and loss, 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 group, 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.

16.2 FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of financial instruments that are not quoted in active markets is 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 this 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.

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

16.4 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 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.

ACCOUNTING POLICIES

for the year ended 31 December 2013 (continued)

17. 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 Company, 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, and will be applied for years ending after 31 December 2013:

	Standard/Interpretation	**Effective date**
IFRS 3 IFRS13 IAS16 IAS 19 IAS 24 IAS 38 IAS 40	Amendments resulting from Annual Improvements 2010 – 2012 cycle	Annual periods beginning on or after 1 July 2014
IFRS 7	Financial Instruments: Disclosures	Unknown as the effective date has been removed but will not be early adopted by the Company
IFRS 8	Amendments resulting from Annual Improvements 2010 – 2012 cycle	Annual periods beginning on or after 1 July 2014
IFRS 9	Financial Instruments	Unknown as the effective date has been removed but will not be early adopted by the Company
IFRS 10	Consolidated financial statements: Amendments for investment entities	Annual periods beginning on or after 1 January 2014
IFRS 12	Disclosure of interest in other entities: Amendments for investment entities	Annual periods beginning on or after 1 January 2014
IFRS 14	Regulatory deferral accounts	Annual periods beginning on or after 1 January 2016
IAS 27	Consolidated and separate financial statements: Amendments for investment entities	Annual periods beginning on or after 1 January 2014
IAS 32	Financial instruments: Amendments relating to the off-setting of financial assets and financial liabilities	Annual periods beginning on or after 1 January 2014
IAS 36	Impairment of assets: Amendments arising from recoverable amount disclosures for non-financial assets	Annual periods beginning on or after 1 January 2014
IAS 39	Financial instruments: Recognition and Measurement: Amendments for novations of derivatives	Annual periods beginning on or after 1 January 2014
IFRIC 21	Levies	Annual periods beginning on or after 1 January 2014

STATEMENT OF FINANCIAL POSITION

at 31 December 2013

	Note	**2013 R'000**	2012 R'000 (restated)	2011 R'000 (restated)
ASSETS				
Intangible assets	2	**196 466**	197 823	206 817
Property and equipment	3	**27 254**	19 069	20 002
Tax	4	**1 220**	1 262	–
Other accounts receivable	5	**86 357**	61 447	69 577
Interest in subsidiaries	6	**154 790**	118 298	204 240
Other investments	7	**5 737**	19 822	69 162
Deferred tax	8	**–**	–	16 935
Non-current assets held for sale	9	**13 470**	13 453	–
Loans and advances	10	**5 083 585**	5 168 753	4 358 484
Derivative financial instruments	11	**10 630**	6 565	15 657
Negotiable securities	12	**496 608**	257 514	192 588
Cash and cash equivalents	13	**1 490 681**	1 218 714	936 911
Total assets		**7 566 798**	7 082 720	6 090 373
EQUITY AND LIABILITIES				
Shareholders' equity		**1 804 089**	1 685 877	1 649 695
Share capital and share premium	14	**1 483 300**	1 483 300	1 483 300
General reserve		**12 231**	12 231	12 231
Property revaluation reserve		**69**	69	69
Employee benefits reserve		**(6 186)**	(7 296)	(4 643)
Available-for-sale reserve		**45 619**	37 855	22 905
Retained earnings		**269 056**	159 718	135 833
Liabilities		**5 762 709**	5 396 843	4 440 678
Deferred tax	8	**34 204**	30 009	–
Long-term funding	15	**493 173**	491 876	–
Deposits	16	**5 048 268**	4 738 236	4 272 970
Derivative financial instruments	11	**11 459**	7 160	17 130
Provisions and other liabilities	17	**71 311**	70 654	48 703
Other accounts payable	19	**104 294**	58 908	101 875
Total equity and liabilities		**7 566 798**	7 082 720	6 090 373

STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2013

	Note	2013 R'000	2012 R'000 (restated)
Interest income	21	**567 889**	511 076
Interest expense	22	**(235 470)**	(205 825)
Net interest income		**332 419**	305 251
Net charge for credit losses	10,4	**(15 185)**	(27 992)
Net interest income after credit losses		**317 234**	277 259
Net gain on disposal of designated through profit and loss investments		**–**	26 555
Net gain on disposal of available-for-sale-investments		**16 310**	14 555
Net non-interest income		**203 358**	205 085
Non-interest income	23	**339 852**	332 160
Fee and commission expenditure	24	**(136 494)**	(127 075)
Net interest and non-interest income		**536 902**	523 454
Operating expenditure	25	**(347 154)**	(334 669)
Profit before tax		**189 748**	188 785
Tax	26	**(50 738)**	(47 217)
Profit after tax		**139 010**	141 568
Other comprehensive income			
Gains on remeasurement to fair value		**25 822**	30 668
Remeasurement of defined benefit obligation		**1 541**	(3 685)
Release to profit and loss on disposal of available-for-sale financial assets		**(16 310)**	(14 555)
Tax relating to other comprehensive income		**(2 179)**	(131)
Other comprehensive income net of tax		**8 874**	12 297
Total comprehensive income		**147 884**	153 865
Profit after tax attributable to:			
Equity holder of the Company		**139 010**	141 568
Total comprehensive income attributable to:			
Equity holder of the Company		**147 884**	153 865

STATEMENT OF CHANGES IN EQUITY

at 31 December 2013

	Share capital R'000	Share premium R'000	Employee benefits reserve R'000	General reserve R'000	Property revaluation reserve R'000	Available for-sale reserve R'000	Retained earnings R'000	Total R'000
Balance at 1 January 2012 (previously reported)	124 969	1 358 331	–	12 231	69	22 905	131 190	1 649 695
Adjustments (refer to note 29)	–	–	(4 643)	–	–	–	4 643	–
Balance at 1 January 2012 (restated)	124 969	1 358 331	(4 643)	12 231	69	22 905	135 833	1 649 695
Net movement for the year	–	–	(2 653)	–	–	14 950	23 885	36 182
Total comprehensive loss/income for the year	–	–	(2 653)	–	–	14 950	141 568	153 865
Profit after tax	–	–		–	–	–	141 568	141 568
Other comprehensive (loss)/income	–	–	(3 685)	–	–	16 113	–	12 428
Tax relating to other comprehensive loss/income	–	–	1 032	–	–	(1 163)	–	(131)
Dividend paid (in specie)	–	–	–	–	–	–	(117 683)	(117 683)
Balance at 31 December 2012 (restated)	**124 969**	**1 358 331**	**(7 296)**	**12 231**	**69**	**37 855**	**159 718**	**1 685 877**
Net movement for the year	**–**	**–**	**1 110**	**–**	**–**	**7 764**	**109 338**	**147 884**
Total comprehensive income for the year	**–**	**–**	**1 110**	**–**	**–**	**7 764**	**139 010**	**147 884**
Profit after tax	**–**	**–**	**–**	**–**	**–**	**–**	**139 010**	**139 010**
Other comprehensive income	**–**	**–**	**1 541**	**–**	**–**	**9 512**	**–**	**11 053**
Tax relating to other comprehensive income	**–**	**–**	**(431)**	**–**	**–**	**(1 748)**	**–**	**(2 179)**
Dividend paid	**–**	**–**	**–**	**–**	**–**	**–**	**(29 672)**	**(29 672)**
Shareholders' equity at 31 December 2013	**124 969**	**1 358 331**	**(6 186)**	**12 231**	**69**	**45 619**	**269 056**	**1 804 089**

STATEMENT OF CASH FLOWS

for the year ended 31 December 2013

	Note	2013 R'000	2012 R'000
Cash flows from operating activities			
Cash receipts from customers	27,1	**906 589**	868 539
Cash paid to customers, suppliers and employees	27,2	**(680 001)**	(610 078)
Cash generated from operations	27,3	**226 588**	258 461
Dividends received		**–**	434
Tax (paid)	27,4	**(48 682)**	(1 666)
Net (increase) in income-earning assets	27,5	**(169 423)**	(859 796)
Net increase in deposits and other accounts	27,6	**330 508**	430 429
Net cash inflow/(outflow) from operating activities		**338 991**	(172 138)
Cash flows from investing activities			
Purchase of intangible assets	2	**(25 402)**	(15 869)
Purchase of property and equipment	3	**(17 595)**	(9 565)
Acquisition of non-current assets held for sale		**(17)**	(13 453)
Dividends paid		**(29 672)**	(117 683)
Proceeds on disposal of investments		**16 310**	14 555
(Increase)/Decrease in interest in subsidiaries		**(11 945)**	104 080
Net cash (outflow) from investing activities		**(68 321)**	(37 935)
Cash flows from financing activities			
Increase in long-term funding	15	**1 297**	491 876
Net cash Inflow from financing activities		**1 297**	491 876
Net cash inflow for the year		**271 967**	281 803
Cash and cash equivalents at the beginning of the year		**1 218 714**	936 911
Cash and cash equivalents at the end of year	13	**1 490 681**	1 218 714

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013

	2013 Fair value R'000	2013 Carrying amount R'000	2012 Fair value R'000	2012 Carrying amount R'000
1. CATEGORIES AND FAIR VALUES OF FINANCIAL INSTRUMENTS				
1.1 Categories analysis of financial instruments				
ASSETS				
Available-for-sale	**177 863**	**177 863**	156 760	156 760
Other investments	**5 737**	**5 737**	19 822	19 822
Interest in subsidiaries	**154 790**	**154 790**	118 298	118 298
Negotiable securities – Government stock	**17 336**	**17 336**	18 640	18 640
Loans and receivables	**7 137 933**	**7 139 895**	6 656 699	6 656 699
Loans and advances				
Current accounts	**1 504 851**	**1 504 851**	1 313 069	1 313 069
Credit cards	**16 365**	**16 365**	17 607	17 607
Mortgage loans	**2 162 185**	**2 162 185**	2 395 456	2 395 456
Instalment sales and leases	**276 469**	**276 469**	276 567	276 567
Structured loans	**27 158**	**27 158**	35 228	35 228
Medium-term loans	**1 096 557**	**1 096 557**	1 099 737	1 099 737
Negotiable securities				
Treasury bills	**382 881**	**384 812**	238 874	238 874
Land Bank promissory notes	**94 429**	**94 460**	–	–
Cash and cash equivalents	**1 490 681**	**1 490 681**	1 218 714	1 218 714
Other accounts receivable	**86 357**	**86 357**	61 447	61 447
Designated at fair value through profit and loss	**23 636**	**23 636**	31 089	31 089
Loans and advances				
Mortgage loans	**22 741**	**22 741**	29 810	29 810
Medium-term loans	**895**	**895**	1 279	1 279
Held-for-trading				
Derivative financial instruments	**10 630**	**10 630**	6 565	6 565
	7 350 062	**7 352 024**	6 851 113	6 851 113
LIABILITIES				
Held-for-trading				
Derivative financial instruments	**11 459**	**11 459**	7 160	7 160
Amortised cost	**5 645 735**	**5 645 735**	5 289 020	5 289 020
Long-term funding	**493 173**	**493 173**	491 876	491 876
Deposits	**5 048 268**	**5 048 268**	4 738 236	4 738 236
Other accounts payable	**104 294**	**104 294**	58 908	58 908
	5 657 194	**5 657 194**	5 296 180	5 296 180

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (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 value.
- 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 value of loans and advances that are carried at amortised cost approximate the fair value reported, as they bear variable rates of interest. The fair value is adjusted for deterioration of credit quality through the application of the credit impairment models.
- Long-term funding is carried at amortised cost and approximates the fair value reported as it bears variable rates of interest.
- 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.
- Depending on the business and nature of the underlying investment, the fair value of other unlisted investments which are an integral part of the Banks's structured loan portfolio are valued in terms of the shareholders' agreement conditions, net asset value or an EBITDA multiple (based on the latest management accounts available). 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 and/or the underlying net asset value of its investment holdings.
- 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 value is 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 2013 (continued)

1. CATEGORIES AND FAIR VALUES OF FINANCIAL INSTRUMENTS (CONTINUED)

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

	Level 1 R'000	Level 2 R'000	Level 3 R'000	Total R'000
2013				
ASSETS				
Available-for-sale				
Other investments	**–**	**–**	**5 737**	**5 737**
Interest in subsidiaries	**–**	**154 790**	**–**	**154 790**
Negotiable securities – Government stock	**17 336**	**–**	**–**	**17 336**
Designated at fair value through profit and loss				
Loans and advances				
Mortgage loans	**–**	**22 741**	**–**	**22 741**
Medium-term loans	**–**	**895**	**–**	**895**
Held-for-trading				
Derivative financial instruments	**10 630**	**–**	**–**	**10 630**
	27 966	**178 426**	**5 737**	**212 129**
LIABILITIES				
Held-for-trading				
Derivative financial instruments	**11 459**	**–**	**–**	**11 459**
	11 459	**–**	**–**	**11 459**
2012				
ASSETS				
Available-for-sale				
Other investments	14 831	–	4 991	19 822
Interest in subsidiaries	–	118 298	–	118 298
Negotiable securities – Government stock	18 640	–	–	18 640
Designated at fair value through profit and loss				
Loans and advances				
Mortgage loans	–	29 810	–	29 810
Medium-term loans	–	1 279	–	1 279
Held-for-trading				
Derivative financial instruments	6 565	–	–	6 565
	40 036	149 387	4 991	194 414
LIABILITIES				
Held-for-trading				
Derivative financial instruments	7 160	–	–	7 160
	7 160	–	–	7 160

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

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
1. CATEGORIES AND FAIR VALUES OF FINANCIAL INSTRUMENTS (CONTINUED)		
1.4 Reconciliation of Level 3 fair value measurements of financial assets		
Available-for-sale		
Other investments – unlisted equities		
Balance at the beginning of the year	**4 991**	4 390
Gains on remeasurement to fair value in comprehensive income	**746**	601
Balance at the end of the year	**5 737**	4 991
Designated at fair value through profit and loss		
Other investments – unlisted equities		
Balance at the beginning of the year	**–**	39 849
Realisation	**–**	(39 849)
Balance at the end of the year	**–**	–
2. INTANGIBLE ASSETS		
Computer software		
Cost at the beginning of the year	**317 956**	302 173
Additions	**25 402**	15 869
Net transfer (to) property and equipment	**(8)**	–
Write-off of obsolete computer software	**(19 997)**	(86)
Cost at the end of the year	**323 353**	317 956
Accumulated amortisation and impairment losses at the beginning of the year	**(120 133)**	(95 356)
Amortisation	**(26 751)**	(24 863)
Write-off of obsolete computer software	**19 997**	86
Accumulated amortisation and impairment losses at the end of the year	**(126 887)**	(120 133)
Net carrying amount at the end of the year	**196 466**	197 823

During 2012 and 2013, the Bank identified no events or circumstances that would indicate that the Banks's intangible assets may need to be impaired.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (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
3. PROPERTY AND EQUIPMENT							
2013							
Open market value/cost at the beginning of the year	**164**	**18 509**	**91 821**	**9 837**	**28 446**	**438**	**149 215**
Additions	**–**	**1 433**	**10 189**	**2 393**	**3 468**	**112**	**17 595**
Disposals	**–**	**–**	**(1)**	**(6)**	**(299)**	**–**	**(306)**
Transfer*	**–**	**–**	**8**	**(414)**	**414**	**–**	**8**
Write-off of obsolete assets	**–**	**(4 069)**	**(3 283)**	**(2 061)**	**(3 473)**	**–**	**(12 886)**
Open market value/cost at the end of the year	**164**	**15 873**	**98 734**	**9 749**	**28 556**	**550**	**153 626**
Accumulated depreciation and impairment losses at the beginning of the year	**–**	**(16 431)**	**(82 495)**	**(9 446)**	**(21 338)**	**(436)**	**(130 146)**
Depreciation	**–**	**(618)**	**(5 216)**	**(120)**	**(2 899)**	**(25)**	**(8 878)**
Disposals	**–**	**–**	**–**	**5**	**225**	**–**	**230**
Transfer*	**–**	**–**	**–**	**266**	**(266)**	**–**	**–**
Write-off of obsolete assets	**–**	**4 030**	**2 934**	**2 087**	**3 371**	**–**	**12 422**
Accumulated depreciation and impairment losses at the end of the year	**–**	**(13 019)**	**(84 777)**	**(7 208)**	**(20 907)**	**(461)**	**(126 372)**
Net carrying amount at the end of the year	**164**	**2 854**	**13 957**	**2 541**	**7 649**	**89**	**27 254**
2012							
Open market value/cost at the beginning of the year	164	19 570	87 629	9 978	29 497	467	147 305
Additions	–	–	5 551	17	3 997	–	9 565
Transfer*	–	–	–	–	–	(29)	(29)
Write-off of obsolete assets	–	(1 061)	(1 359)	(158)	(5 048)	–	(7 626)
Open market value/cost at the end of the year	164	18 509	91 821	9 837	28 446	438	149 215
Accumulated depreciation and impairment losses at the beginning of the year	–	(16 822)	(77 593)	(9 478)	(22 964)	(446)	(127 303)
Depreciation	–	(670)	(6 261)	(126)	(2 545)	(19)	(9 621)
Transfer*	–	–	–	–	–	29	29
Write-off of obsolete assets	–	1 061	1 359	158	4 171	–	6 749
Accumulated depreciation and impairment losses at the end of the year	–	(16 431)	(82 495)	(9 446)	(21 338)	(436)	(130 146)
Net carrying amount at the end of the year	164	2 078	9 326	391	7 108	2	19 069

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

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

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
4. TAX		
South African Revenue Services		
Tax overpaid	**1 220**	1 262
	1 220	1 262
5. OTHER ACCOUNTS RECEIVABLE		
Items in transit	**52 604**	24 660
Loan to fellow subsidiary (refer to note 28.2)	**94**	25
Prepayments and deposits	**7 327**	9 273
Other receivables	**26 332**	27 489
	86 357	61 447
6. INTEREST IN SUBSIDIARIES		
Unlisted		
Shares at fair value		
Portion 2 of Lot 8 Sandown (Pty) Ltd	**50 834**	23 002
Loans to/(from) subsidiaries	**103 956**	95 296
Portion 2 of Lot 8 Sandown (Pty) Ltd	**(4 608)**	(7 128)
LSM (Troyeville) Properties (Pty) Ltd	**7 819**	7 618
Custom Capital (Pty) Ltd	**105 515**	96 291
Less: Provisions held against loan accounts	**(4 770)**	(1 485)
	154 790	118 298

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

The loans to/(from) Portion 2 of Lot 8 Sandown (Pty) Ltd and LSM (Troyeville) Properties (Pty) Ltd bear interest at the prevailing prime rate plus 2% (2012: prime rate plus 2%) and have no fixed terms of maturity.

The loan to Custom Capital (Pty) Ltd bears interest at 12% (2012: 5.5%) and has no fixed terms of maturity.

	2013 R'000	2012 R'000
7. OTHER INVESTMENTS		
Available-for-sale		
Unlisted equities	**5 737**	4 991
Listed equities – Visa Inc.*	**–**	14 831
	5 737	19 822

* 50% of the shareholding in Visa Inc. was sold during 2013 and the other 50% during 2012.

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 2013 (continued)

	2013 R'000	2012 R'000
8. DEFERRED TAX		
Balance at the beginning of the year	**(30 009)**	16 935
Movements relating to prior years provision	**(406)**	–
Current year charge		
Per the statement of comprehensive income (restated)	**(1 610)**	(46 813)
Per the statement of changes in equity/other comprehensive income (restated)	**(2 179)**	(131)
	(34 204)	(30 009)
Comprising		
Deferred tax liabilities	**(34 204)**	(30 009)
	(34 204)	(30 009)
Deferred tax is attributable to the following temporary differences		
Asset/(Liability)		
Intangible assets	**(48 398)**	(47 273)
Provisions and other liabilities	**16 879**	16 498
Impairments on loans and advances	**(14 212)**	(21 980)
Leased assets	**3 349**	2 622
Revaluations	**(6 715)**	(4 966)
Interest rate swaps	**150**	411
Current assets	**14 743**	24 679
	(34 204)	(30 009)
9. NON-CURRENT ASSETS HELD FOR SALE		
Properties in possession	**13 470**	13 453
	13 470	13 453

The Bank intended to dispose of a property during 2013 that was purchased as a result of a loan default. Due to unsatisfactory market conditions, the property was not sold. However, it remains the Bank's intention to dispose of it in the short term. The property has been valued based on an independent valuation obtained and allowing for cost of disposal.

10. LOANS AND ADVANCES

10.1 Product analysis

	2013 R'000	2012 R'000
Amortised cost	**5 100 205**	5 241 859
Current accounts	**1 527 609**	1 340 870
Credit cards	**19 521**	22 227
Mortgage loans	**2 144 070**	2 433 471
Instalment sales and leases	**279 677**	285 334
Structured loans	**27 535**	44 579
Medium-term loans	**1 101 793**	1 115 378
Fair value through profit and loss	**23 644**	2 145
Mortgage loans	**22 748**	2 011
Medium-term loans	**896**	134
Gross loans and advances	**5 123 849**	5 244 004
Less: Portfolio impairments for credit losses	**(7 072)**	(12 320)
Specific impairments for credit losses	**(33 192)**	(62 931)
	5 083 585	5 168 753

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

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

10. LOANS AND ADVANCES (CONTINUED)

10.2 Maturity analysis

	2013 R'000	2 012 R'000
Repayable on demand and maturing within one month	**1 590 178**	1 388 731
Maturing after one month but within six months	**36 812**	10 186
Maturing after six months but within 12 months	**234 551**	405 473
Maturing after 12 months	**3 262 308**	3 439 614
	5 123 849	5 244 004

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

10.3 Detailed product analysis of loans and advances

	Gross amount R'000	Portfolio impairments R'000	Specific impairments R'000	Net balance R'000
2013				
Current accounts	**1 527 609**	**2 733**	**20 025**	**1 504 851**
Credit cards	**19 521**	**1 115**	**2 041**	**16 365**
Mortgage loans	**2 166 818**	**695**	**3 938**	**2 162 185**
Instalment sales and leases	**279 677**	**493**	**2 715**	**276 469**
Structured loans	**27 535**	**377**	**–**	**27 158**
Medium-term loans	**1 102 689**	**1 659**	**4 473**	**1 096 557**
	5 123 849	**7 072**	**33 192**	**5 083 585**
2012				
Current accounts	1 340 870	5 067	22 734	1 313 069
Credit cards	22 227	1 282	3 338	17 607
Mortgage loans	2 435 482	1 212	9 004	2 425 266
Instalment sales and leases	285 334	495	8 272	276 567
Structured loans	44 579	403	8 948	35 228
Medium-term loans	1 115 512	3 861	10 635	1 101 016
	5 244 004	12 320	62 931	5 168 753

10.4 Impairments for credit losses

	Total R'000	Current accounts R'000	Credit cards R'000	Mortgage loans R'000	Instalment sales and leases R'000	Structured loans R'000	Medium-term loans R'000
2013							
Balance at the beginning of the year	**75 251**	**27 801**	**4 620**	**10 216**	**8 767**	**9 351**	**14 496**
Movements for the year:							
Credit losses written off	**(50 068)**	**(25 223)**	**(1 038)**	**(8 154)**	**(6 313)**	**(1 080)**	**(8 260)**
Net impairments raised/(released)	**15 081**	**20 180**	**(426)**	**2 571**	**754**	**(7 894)**	**(104)**
Balance at the end of the year	**40 264**	**22 758**	**3 156**	**4 633**	**3 208**	**377**	**6 132**
2012							
Balance at the beginning of the year	76 550	19 896	4 425	12 141	9 530	9 044	21 514
Movements for the year:							
Credit losses written off	(24 287)	(1 001)	(650)	(339)	(848)	(11 000)	(10 449)
Net impairments raised/(released)	22 988	8 906	845	(1 586)	85	11 307	3 431
Balance at the end of the year	75 251	27 801	4 620	10 216	8 767	9 351	14 496

	2013 R'000	2012 R'000
Net charge for credit losses in the statement of comprehensive income		
Net impairments raised	**(15 081)**	(22 988)
Amounts directly written off to other comprehensive income	**(495)**	(5 142)
Recoveries in respect of amounts previously written off	**391**	138
	(15 185)	(27 992)

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

10. LOANS AND ADVANCES (CONTINUED)

10.5 Product analysis of performing loans and advances

	Gross amount R'000	Portfolio impairment R'000	Net balance R'000
2013			
Current accounts	**1 487 222**	**2 733**	**1 484 489**
Credit cards	**17 480**	**1 115**	**16 365**
Mortgage loans	**2 067 916**	**695**	**2 067 221**
Instalment sales and leases	**272 695**	**493**	**272 202**
Structured loans	**27 535**	**377**	**27 158**
Medium-term loans	**1 064 046**	**1 659**	**1 062 387**
	4 936 894	**7 072**	**4 929 822**
2012			
Current accounts	1 301 685	5 067	1 296 618
Credit cards	18 889	1 282	17 607
Mortgage loans	2 360 976	1 212	2 359 764
Instalment sales and leases	276 755	495	276 260
Structured loans	29 447	403	29 044
Medium-term loans	1 084 349	3 861	1 080 488
	5 072 101	12 320	5 059 781

	2013 R'000	2012 R'000
10.6 Product analysis of performing loans and advances excluding loans and advances with renegotiated terms		
Current accounts	**1 487 222**	1 301 189
Credit cards	**16 276**	18 889
Mortgage loans	**2 057 189**	2 353 378
Instalment sales and leases	**272 695**	276 755
Structured loans	**27 535**	29 447
Medium-term loans	**934 797**	1 080 869
	4 795 714	5 060 527
10.7 Product analysis of loans and advances with renegotiated terms that would otherwise be past due or impaired		
Current accounts	**–**	496
Credit cards	**1 204**	–
Mortgage loans	**10 727**	7 598
Instalment sales and leases	**–**	–
Structured loans	**–**	–
Medium-term loans	**129 249**	3 480
	141 180	11 574

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

10. LOANS AND ADVANCES (CONTINUED)

10.8 Product 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
2013					
Current accounts	**–**	**–**	**–**	**–**	**–**
Credit cards	**–**	**–**	**–**	**–**	**–**
Mortgage loans	**22 037**	**1 505**	**40 291**	**63 833**	**70 899**
Instalment sales and leases	**713**	**–**	**–**	**713**	**359**
Structured loans	**–**	**–**	**–**	**–**	**–**
Medium-term loans	**4 395**	**51 602**	**515**	**56 512**	**9 973**
	27 145	**53 107**	**40 806**	**121 058**	**81 231**
2012					
Current accounts	–	–	–	–	–
Credit cards	–	–	–	–	–
Mortgage loans	24 077	8 755	54 184	87 016	78 893
Instalment sales and leases	242	62	115	419	255
Structured loans	–	–	–	–	–
Medium-term loans	5 590	5 185	7 702	18 477	7 693
	29 909	14 002	62 001	105 912	86 841

10.9 Product 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
2013				
Current accounts	**40 387**	**20 025**	**20 362**	**16 829**
Credit cards	**2 041**	**2 041**	**–**	**–**
Mortgage loans	**98 902**	**3 938**	**94 964**	**95 236**
Instalment sales and leases	**6 982**	**2 715**	**4 267**	**2 145**
Structured loans	**–**	**–**	**–**	**–**
Medium-term loans	**38 643**	**4 473**	**34 170**	**27 112**
	186 955	**33 192**	**153 763**	**141 322**
2012				
Current accounts	39 185	22 734	16 451	11 353
Credit cards	3 338	3 338	–	–
Mortgage loans	74 506	9 004	65 502	66 017
Instalment sales and leases	8 579	8 272	307	329
Structured loans	15 132	8 948	6 184	6 850
Medium-term loans	31 163	10 635	20 528	19 138
	171 903	62 931	108 972	103 687

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

10. LOANS AND ADVANCES (CONTINUED)

10.10 Collateral held as security and other credit enhancements

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

All customers of the Bank are accorded a client risk grading. The risk grading is dependent upon the client's creditworthiness and standing with the Bank, and is subject 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 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	50% of listed shares value; nil for unlisted shares
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	100% of asset value
Vacant land	50% of professional valuation
Residential properties	80% of official 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
Earthmoving 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 Bank has acquired zero cost equity options attached to certain structured loans that have been recognised at cost in accordance with accounting policy 3.1.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	Notional principal of assets R'000	Fair value of assets R'000	Notional principal of liabilities R'000	Fair value of liabilities R'000
11. DERIVATIVE FINANCIAL INSTRUMENTS				
2013				
Held-for-trading				
Foreign exchange contracts	**422 370**	**10 561**	**507 193**	**10 856**
Interest rate swaps	**–**	**69**	**25 203**	**603**
	422 370	**10 630**	**532 396**	**11 459**
2012				
Held-for-trading				
Foreign exchange contracts	395 050	6 565	386 522	5 620
Interest rate swaps	–	–	31 237	1 540
	395 050	6 565	417 759	7 160

	2013 R'000	2012 R'000
12. NEGOTIABLE SECURITIES		
Loans and receivables		
Treasury bills	**384 812**	238 874
Land Bank promissory notes	**94 460**	–
Available-for-sale		
Government stock	**17 336**	18 640
	496 608	257 514
Maturity analysis		
Maturing within one month	**36 940**	2 329
Maturing after one month but within six months	**317 236**	125 058
Maturing after six months but within 12 months	**125 096**	111 487
Maturing after one year but within five years	**17 336**	18 640
	496 608	257 514

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

	2013 R'000	2012 R'000
13. CASH AND CASH EQUIVALENTS		
Cash on hand	**46 949**	34 415
Central Bank balances	**148 284**	125 565
Money Market funds	**1 084 222**	854 068
Rand denominated domestic bank balances	**3 969**	83 966
Foreign currency denominated bank balances	**207 257**	120 700
	1 490 681	1 218 714

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

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

The total authorised number of ordinary shares is 62 630 000 shares (2012: 62 630 000 shares) with a par value of R2.00 per share.

No shares were issued during the financial years ended 31 December 2013 and 31 December 2012.

The unissued shares are under the control of the shareholder until the next Annual General Meeting of MBHL.

	2013 R'000	2012 R'000
15. LONG-TERM FUNDING		
International Finance Corporation (IFC)	**493 173**	491 876
Short-term portion payable in the next 12 months	**30 000**	–
Portion payable after 12 months but within five years	**463 173**	491 876
	493 173	491 876

The loan obtained from the IFC in 2011, with interest repayable quarterly and linked to JIBAR, is repayable between 15 September 2014 and 15 September 2018.

	2013 R'000	2012 R'000
16. DEPOSITS		
Call deposits and current accounts	**2 299 586**	2 269 800
Savings accounts	**174 507**	186 767
Term and notice deposits	**2 455 212**	2 145 666
Negotiable certificates of deposit	**30 542**	29 560
Foreign deposits	**88 421**	106 443
	5 048 268	4 738 236
Maturity analysis		
Repayable on demand and maturing within one month	**2 905 385**	2 891 750
Maturing after one month but within six months	**1 320 124**	1 280 268
Maturing after six months but within 12 months	**451 996**	528 932
Maturing after 12 months	**370 763**	37 286
	5 048 268	4 738 236

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 2013 (continued)

17. PROVISIONS AND OTHER LIABILITIES

	Deferred bonus scheme R'000	Staff incentives R'000	Audit fees R'000	Post-retirement medical benefit R'000	Leave pay R'000	Other risks R'000	Total R'000
At 1 January 2012	5 793	12 000	3 710	16 049	9 608	1 543	48 703
Provision raised	3 913	16 000	6 175	3 423	2 116	12 936	44 563
Charged to provision	(1 677)	(12 000)	(6 181)	–	(1 729)	(1 025)	(22 612)
At 31 December 2012	**8 029**	**16 000**	**3 704**	**19 472**	**9 995**	**13 454**	**70 654**
Provision raised	**5 733**	**16 000**	**7 305**	**–**	**2 517**	**6 162**	**37 717**
Charged to provision	**(6 655)**	**(16 000)**	**(7 087)**	**(1 202)**	**(1 702)**	**(4 414)**	**(37 060)**
At 31 December 2013	**7 107**	**16 000**	**3 922**	**18 270**	**10 810**	**15 202**	**71 311**

Post-retirement medical benefits

Refer to note 18 for detailed disclosure of this provision.

Leave pay

In terms of Bank's 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 Bank, the outcome of which cannot 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 2013 (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 Bank's assets in a separate trustee-administered fund. Independent actuaries value this scheme annually (the last valuation was carried out at 31 December 2013). The actuary's opinion is that the plan is in a sound financial position.

	2013 R'000	2012 R'000 (restated)	2011 R'000 (restated)	2010 R'000 (restated)	2009 R'000 (restated)
The amounts recognised in the statement of financial position are as follows (refer to note 17):					
Present value of total service liabilities	**19 900**	21 575	18 577	20 648	19 370
Fair value of plan assets	**(1 630)**	(2 103)	(2 528)	(5 499)	(5 507)
Provident fund	**(782)**	(1 315)	(1 800)	(1 832)	(1 674)
Endowment bond	**(848)**	(788)	(728)	(2 530)	(2 718)
Annuities	**–**	–	–	(1 137)	(1 115)
Liability in the statement of financial position	**18 270**	19 472	16 049	15 149	13 863
The amounts recognised in the statement of comprehensive income are as follows:					
Staff cost (refer to note 25):	**(1 030)**	(1 494)	(994)	(1 391)	(1 267)
Current service cost	**22**	13	53	50	92
Payments from plan assets	**540**	–	–	–	–
Employer benefit payments	**(1 592)**	(1 507)	(1 533)	(1 441)	(1 359)
Discharge of liability and related plan asset	**–**	–	486	–	–
Net interest cost (refer to note 22):	**1 369**	1 232	1 127	1 189	1 259
Interest costs	**1 502**	1 466	1 636	1 767	1 785
Expected return on plan assets	**(133)**	(234)	(509)	(578)	(526)
Total included in comprehensive income	**339**	(262)	133	(202)	(8)
The amounts recognised in the statement of other comprehensive income, are as follows:					
Remeasurement of defined benefit obligation	**(1 541)**	3 685	767	1 488	(660)
Total included in other comprehensive income	**(1 541)**	3 685	767	1 488	(660)
Reconciliation of the movement in the present value of total service liabilities:					
At the beginning of the year	**21 575**	18 577	20 648	19 370	19 664
Current service cost	**22**	13	53	50	92
Interest costs	**1 502**	1 466	1 636	1 767	1 785
Discharge of liability	**–**	–	(1 891)	–	–
Remeasurement of defined benefit obligation	**(1 607)**	3 026	(336)	902	(812)
Employer benefit payments	**(1 592)**	(1 507)	(1 533)	(1 441)	(1 359)
At the end of the year	**19 900**	21 575	18 577	20 648	19 370
Reconciliation of the movement in the fair value of plan assets:					
At the beginning of the year	**2 103**	2 528	5 499	5 507	5 133
Expected return on plan assets	**133**	234	509	578	526
Payments from plan assets	**(540)**	–	–	–	–
Non-qualifying plan assets as a result of discharge of liability	**–**	–	(2 377)	–	–
Remeasurement of defined benefit obligation	**(66)**	(659)	(1 103)	(586)	(152)
At the end of the year	**1 630**	2 103	2 528	5 499	5 507

The principal actuarial assumptions used were as follows:

Discount rate	**8,60%**	(2012: 7.25%) compounded annually
Investment return	**8,60%**	(2012: 8.25%) compounded annually
Rate of medical inflation	**8,30%**	(2012: 7.75%) compounded annually
Salary inflation	**7,80%**	(2012: 7.25%) 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 R1.806 million (2012: R1.674 million) and a decrease of R1.524 million (2012: R1.394 million), respectively.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
19. OTHER ACCOUNTS PAYABLE		
Loan from the holding company (refer to note 28.2)	**460**	504
Accruals	**21 503**	11 949
Product-related credits	**47 399**	39 510
Sundry creditors	**34 932**	6 945
	104 294	58 908

20. CONTINGENT LIABILITIES AND COMMITMENTS

20.1 Guarantees, letters of credit and committed undrawn facilities

	2013 R'000	2012 R'000
Guarantees	**400 147**	300 496
Shipping	**117**	117
Lending related	**6 914**	8 219
Mortgage	**111 670**	81 526
Performance	**281 446**	210 634
Letters of credit	**16 024**	15 634
Committed undrawn facilities	**105 747**	66 314
	521 918	382 444

20.2 Commitments under operating leases

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

	2013 R'000	2012 R'000
Property rentals		
Due within one year	**21 306**	20 605
Due between one and five years	**63 732**	82 163
	85 039	102 768
After tax effect on operating leases	**61 228**	73 993

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.

21. INTEREST INCOME

	2013 R'000	2012 R'000
Loans to subsidiaries and fellow subsidiaries	**35 392**	20 599
Loans and receivables	**529 773**	486 288
Cash and cash equivalents	**62 339**	45 627
Negotiable securities	**17 187**	13 381
Loans and advances	**450 247**	427 280
Loans and receivables designated at fair value through profit and loss		
Loans and advances	**2 724**	4 189
	567 889	511 076

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
22. INTEREST EXPENSE		(restated)
Deposits	**195 047**	179 220
Long-term funding	**38 228**	24 051
Held-for-trading		
Interest rate swaps	**816**	1 304
Net interest on defined benefit obligation	**1 369**	1 232
Other	**10**	18
	235 470	205 825
23. NON-INTEREST INCOME		
Fee and commission income		
Loans and receivables	**270 120**	260 442
Trading income	**69 732**	71 284
Held-for-trading	**70 315**	71 295
Foreign currency	**69 401**	70 950
Derivative assets	**–**	70
Derivative liabilities	**914**	275
Designated at fair value through profit and loss		
Loans and advances	**(583)**	(11)
Investment income		
Dividends	**–**	434
	339 852	332 160
24. FEE AND COMMISSION EXPENDITURE		
Foreign currency	**29 926**	26 999
Commissions and transactions	**106 568**	100 076
	136 494	127 075

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
25. OPERATING EXPENDITURE		(restated)
Amortisation (refer to note 2)	**26 751**	24 863
Auditors' remuneration		
Audit fees – current year	**7 075**	6 175
Fees for other services – Tax advisory fees	**207**	180
– Regulatory reviews	**58**	–
– Accounting services	**382**	–
– Other	**44**	20
	7 766	6 375
Depreciation (refer to note 3)	**8 878**	9 621
Directors' remuneration (refer to note 28.3)		
Executive Directors	**16 350**	14 388
Non-Executive Directors' fees	**8 482**	4 429
	24 832	18 817
Indirect tax		
Non-claimable Value-Added Tax	**9 911**	9 271
Skills development levy	**1 569**	1 433
	11 480	10 704
Loss/(Profit) on sale of property and equipment	**100**	(6)
Marketing	**2 343**	1 862
Operating leases for premises and related costs	**26 399**	25 112
Other operating costs	**42 480**	49 107
Professional fees		
Consulting	**2 242**	2 532
Legal and collection	**2 387**	1 169
Computer consulting and services	**36 122**	37 867
	40 751	41 568
Staff costs		
Salaries, allowances and incentives	**148 771**	140 143
Post-retirement medical benefits (refer to note 17)	**(1 030)**	(1 494)
Deferred bonus scheme expense including Directors	**5 113**	3 864
Other	**2 520**	4 133
	155 374	146 646
Total operating expenditure	**347 154**	334 669
Number of persons employed by the Company at year-end	**389**	403

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
26. TAX		(restated)
South African normal tax	**49 128**	404
Current year	**49 128**	404
Prior year	**–**	–
Deferred tax	**1 610**	46 813
Current year	**1 207**	46 844
Prior year	**403**	(31)
	50 738	47 217
Direct tax		
South African normal tax	**49 128**	404
South African tax rate reconciliation		
South African standard tax rate (%)	**28.00**	28.00
Exempt income (%)	**0.00**	(0.05)
Expenses not deductible for tax purposes (%)	**0.00**	1.19
Additional allowances for tax purposes (%)	**(0.67)**	(0.06)
Capital gain not taxable on realised portion (%)	**(0.80)**	(4.13)
Under provision prior year (%)	**0.21**	–
Effective tax rate (%)	**26.74**	24.95

27. NOTES TO STATEMENT OF CASH FLOWS

27.1 Cash receipts from customers

		2013 R'000	2012 R'000
Interest income		**567 889**	511 076
Non-interest income and gains on disposal of investments		**356 162**	373 270
Adjusted for:	Dividends received	**–**	(434)
	Net (gain) on disposal of investments	**(16 310)**	(14 832)
	Revaluation of fair value financial instruments	**(1 543)**	(679)
Recoveries in respect of amounts previously written off		**391**	138
		906 589	868 539

27.2 Cash paid to customers, suppliers and employees

		2013 R'000	2012 R'000 (restated)
Interest expense		**(235 470)**	(205 825)
Operating expenditure and fee and commission expenditure		**(483 648)**	(461 744)
Adjusted for:	Amortisation	**26 751**	24 863
	Depreciation	**8 878**	9 621
	Write-off of obsolete property and equipment	**464**	877
	Loss/(Profit) on sale of property and equipment	**100**	(6)
	Deferred bonus scheme expense	**5 113**	3 864
	Remeasurement of defined benefit obligation	**–**	(3 685)
	(Decrease)/Increase in provisions and other liabilities	**(2 189)**	21 957
		(680 001)	(610 078)

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000
27. NOTES TO STATEMENT OF CASH FLOWS (CONTINUED)		(restated)
27.3 Reconciliation of profit before tax to cash generated from operations		
Profit before tax	**189 748**	188 785
Profit before tax adjusted for:		
Dividends received	**–**	(434)
Net (gain) on disposal of investments	**(16 310)**	(14 832)
Revaluation of fair value financial instruments	**(1 543)**	(679)
Net impairments raised	**15 576**	28 130
Amortisation	**26 751**	24 863
Depreciation	**8 878**	9 621
Write-off of obsolete property and equipment	**464**	877
Loss/(Profit) on sale of property and equipment	**100**	(6)
Deferred bonus scheme expense	**5 113**	3 864
Remeasurement of defined benefit obligation	**–**	(3 685)
(Decrease)/Increase in provisions and other liabilities	**(2 189)**	21 957
Cash generated from operations	**226 588**	258 461
27.4 Tax		
Amounts paid at the beginning of the year	**1 666**	–
Statement of comprehensive income (charge)	**(49 128)**	(404)
Less: Amounts (overpaid) at the end of the year	**(1 220)**	(1 262)
Total tax (paid)	**(48 682)**	(1 666)
27.5 Net movement in income-earning assets		
(Increase) in negotiable securities	**(239 346)**	(64 652)
Decrease/(Increase) in loans and advances	**69 923**	(795 144)
Net (increase) in income-earning assets	**(169 423)**	(859 796)
27.6 Net movement in deposits and other accounts		
Increase in deposits	**310 032**	465 266
(Increase)/Decrease in other accounts receivable	**(24 910)**	8 130
Increase/(Decrease)I in other accounts payable	**45 386**	(42 967)
Net increase in deposits and other accounts	**330 508**	430 429

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

28. RELATED PARTY INFORMATION

28.1 Identity of related parties with whom transactions have occurred

The ultimate holding company (CGD), holding company (MBHL), direct and fellow subsidiaries, a joint venture (Mercantile E-Bureau (Pty) Ltd) and Directors are related parties. There are no other related parties with whom transactions have taken place, other than as listed below.

28.2 Related party balances and transactions

The Company, in the ordinary course of business, enters into various financial services transactions with related parties. Except for the interest-free loan between the Bank and MBHL, transactions are governed by commercial terms.

Balances with the holding company, direct and fellow subsidiaries: and joint venture

	% Held	2013 R'000	2012 R'000
Loans to/(from) subsidiaries			
Portion 2 of Lot 8 Sandown (Pty) Ltd	100	**(4 608)**	(7 128)
LSM (Troyeville) Properties (Pty) Ltd	100	**7 819**	7 618
Custom Capital (Pty) Ltd	74,9	**391 718**	328 599
Shareholder loan (refer to note 6)		**105 515**	96 291
Current account (included as part of loans and advances – refer to note 10)		**286 203**	232 308
Less: Provisions held against loan accounts		**(4 770)**	(1 485)
		390 159	327 604
Loans to/(from) the holding company, fellow subsidiary and joint venture			
Mercantile Bank Holdings Limited		**(460)**	(504)
Mercantile Insurance Brokers (Pty) Ltd		**94**	25
Mercantile E-Bureau (Pty) Ltd		**1 556**	1 367
		1 190	888
Deposits from the holding company, subsidiary, fellow subsidiary and joint venture			
Mercantile Bank Holdings Limited		**4 292**	222
The Mercantile Bank Foundation (NPC)		**65**	–
Mercantile Insurance Brokers (Pty) Ltd		**2 262**	2 055
Mercantile E-Bureau (Pty) Ltd		**446**	27
		7 065	2 304

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

28. RELATED PARTY INFORMATION (CONTINUED)

28.2 Related party balances and transactions (continued)

	2013 R'000	2012 R'000
Transactions with the holding company, direct and fellow subsidiaries and joint venture:		
Interest received from:		
Portion 2 of Lot 8 Sandown (Pty) Ltd	–	1 295
LSM (Troyeville) Properties (Pty) Ltd	**810**	805
Custom Capital (Pty) Ltd	**34 582**	18 108
Multi Risk Investment Holdings (Pty) Ltd (disposed of effective 29 June 2012)	–	391
Interest paid to:		
Portion 2 of Lot 8 Sandown (Pty) Ltd	**984**	363
Mercantile Insurance Brokers (Pty) Ltd	**79**	78
Custom Capital (Pty) Ltd	–	–
Non-interest income earned from:		
Mercantile Insurance Brokers (Pty) Ltd	**1**	9
Custom Capital (Pty) Ltd	**281**	163
Multi Risk Investment Holdings (Pty) Ltd (disposed of effective 29 June 2012)	–	31
Mercantile E-Bureau (Pty) Ltd	**29 553**	25 521
Dividends paid to:		
Mercantile Bank Holdings Limited	**29 672**	117 683
Donations received by:		
The Mercantle Bank Foundation (NPC)	**1 000**	–
Operating expenditure paid to:		
Portion 2 of Lot 8 Sandown (Pty) Ltd	**17 345**	16 648
LSM (Troyeville) Properties (Pty) Ltd	**1 188**	1 134
Balances and transactions with the ultimate holding company (CGD) and its subsidiary:		
CGD – Lisbon (Branch of CGD)	**64 950**	(960)
Nostro accounts	**3 500**	400
Vostro accounts	**(934)**	(1 360)
Deposits	**(149)**	–
Foreign currency placements	**62 533**	–
CGD – Paris (Branch of CGD)	**(28)**	(36)
Nostro accounts	–	–
Vostro accounts	**(28)**	(36)
CGD – London (Branch of CGD)		
Vostro accounts	**(12)**	(14)
CGD	**64 910**	(1 010)
Banco Comercial e de Investimentos (BCI) – Mozambique (Subsidiary of CGD)	**(100 662)**	(133 984)
Vostro accounts	**(405)**	(3 656)
Fixed deposits	**(100 256)**	(130 085)
Call and notice deposits	**(1)**	(243)
Total CGD	**(35 752)**	(134 994)
Transactions between the ultimate holding company (CGD) and the Bank:		
Interest paid by the Bank to BCI	**6 569**	8 708
Interest paid by the Bank to CGD	**2**	–
Interest received by the Bank from CGD	**7**	–

NOTES TO THE ANNUAL FINANCIAL STATEMENTS
for the year ended 31 December 2013 (continued)

28. RELATED PARTY INFORMATION (CONTINUED)

28.3 Director and Director-related activities

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
2013						
Non-Executive Directors						
J A S de Andrade Campos	**1 712**	**–**	**–**	**–**	**–**	**1 712**
D J Brown (resigned 19 August 2013)	**3 782**	**–**	**–**	**–**	**–**	**3 782**
G P de Kock	**704**	**–**	**–**	**–**	**–**	**704**
L Hyne	**664**	**–**	**–**	**–**	**–**	**664**
A T Ikalafeng	**562**	**–**	**–**	**–**	**–**	**562**
T H Njikizana	**633**	**–**	**–**	**–**	**–**	**633**
D Naidoo (resigned 23 August 2013)	**425**	**–**	**–**	**–**	**–**	**425**
Executive Directors						
D J Brown (tenure as CEO ended 31 March 2013)	**–**	**892**	**–**	**272**	**6 400**	**7 564**
K R Kumbier	**–**	**2 900**	**–**	**294**	**2 500**	**5 694**
J P M Lopes	**–**	**2 010**	**496**	**86**	**500**	**3 092**
	8 482	**5 802**	**496**	**652**	**9 400**	**24 832**
2012						
Non-Executive Directors						
J A S de Andrade Campos	1 625	–	–	–	–	1 625
G P de Kock	667	–	–	–	–	667
L Hyne	629	–	–	–	–	629
A T Ikalafeng	533	–	–	–	–	533
T H Njikizana	600	–	–	–	–	600
D Naidoo (appointed 23 May 2012)	375	–	–	–	–	375
Executive Directors						
D J Brown	–	3 186	–	341	3 570	7 097
K R Kumbier	–	2 464	–	260	1 950	4 674
J P M Lopes	–	1 977	463	77	100	2 617
	4 429	7 627	463	678	5 620	18 817

	2013 R'000	2012 R'000
Deferred bonus scheme expense relating to Executive Directors		
D J Brown (tenure as CEO ended 31 March 2013)	**806**	1 039
K R Kumbier	**1 220**	995
Loans to Executive Directors		
J P M Lopes	**165**	154
Amounts paid by CGD to Executive Directors		
J P M Lopes	**736**	544

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

28. RELATED PARTY INFORMATION (CONTINUED)

28.3 Director and Director-related activities (continued)

Service agreements and deferred bonus scheme awards

D J Brown, CEO

D J Brown's tenure as CEO of the Bank ended on 31 March 2013 and he remained on the Board as a Non-Executive Director until 19 August 2013.

In consideration for the rendering of his services under the service agreement as CEO, Mr Brown received a bonus payment of R6.4 million. In terms of the change in the contractual conditions relating to Mr Brown's employment contract, the unvested deferred bonus scheme awards were settled for a consideration of R2.8 million in April 2013.

K R Kumbier, CEO

Mr Kumbier was employed by Mercantile as Executive Director: Finance and Business on 1 June 2010. He was subsequently appointed as Deputy CEO (effective 1 April 2012), and was appointed as CEO from 1 April 2013.

During 2013, of the 10 000 000 phantom awards granted in 2010 to K R Kumbier, 2 500 000 phantom awards were settled at a proxy price of 64.2 cents each. The balance of awards (7 500 000) were forfeited as performance conditions in terms of the plan were not achieved.

In terms of the deferred bonus scheme, phantom awards in MBHL granted to K R Kumbier, which have not yet vested as at 31 December 2013, are as follows:

- 5 000 000 at an estimated proxy price of 69 cents each (of which approximately 35% will vest in 2014);
- 3 500 000 at an estimated proxy price of 71 cents each (vesting in 2015); and
- 5 000 000 at an estimated proxy price of 80 cents each (vesting in 2016).

J P M Lopes, Executive Director

Mr Lopes has been seconded to Mercantile by CGD.

Mr Lopes' employment contract was extended by the Board in 2011 to July 2014. In terms of his service agreement, Mr Lopes has 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.

29. APPLICATION OF NEW AND REVISED IFRSs

29.1. New and revised IFRSs affecting amounts reported and/or disclosures in the financial statements

Amendments to IAS 1 Presentation of Financial Statements.

(as part of the Annual Improvements to IFRSs 2009 – 2011 Cycle issued in May 2012)

The Annual improvements to IFRSs 2009 – 2011 have made a number of amendments to IFRSs. The amendments that are relevant to the Bank are the amendments to IAS 1 regarding when a statement of financial position as at the beginning of the preceding period (third statement of financial position is required when a) an entity applies an accounting policy retrospectively, or makes a retrospective restatement or reclassification of items in its financial statements, and b) the retrospective application, restatement or reclassification has a material effect on the information in the third statement of financial position. The amendments specify that the related notes are not required to accompany the third statement of financial position.

IAS19 Employee Benefits (as revised in 2011)

In the current year, the Bank has applied one new revised IFRS (IAS19), Employee Benefits (as revised in 2011) and the related consequential amendments for the first time, which has had an effect on the information in the consolidated statement of financial position as at 1 January 2012. In accordance with the amendments to IAS1, the Bank has presented a third statement of financial position as at 1 January 2012 without the related notes except for the disclosure requirements of IAS 8, Accounting policies, changes in Accounting Estimates and Errors, as detailed below.

IAS 19 (as revised in 2011) changes the accounting for defined benefit plans and termination benefits. The most significant accounting changes related to defined benefit obligations and plan assets. The amendments require all actuarial gains and losses to be recognised immediately through other comprehensive income in order for the net post retirement asset or liability recognised in the consolidated statement of financial position to reflect the full value of the plan deficit or surplus.

Furthermore, the interest cost and expected return on plan assets used in the previous version of IAS19 are replaced with a "net interest" amount under IAS19 (as revised in 2011), which is calculated by applying the discount rate to the net defined benefit liability or asset. These changes have had no impact on the amounts recognised in profit or loss and other comprehensive income in prior years, except that they are no longer accounted for under staff costs, but rather under other interest expenses.

Specific transitional provisions are applicable to first-time application of IAS19 (as revised in 2011). The Bank has applied the relevant transitional provisions and restated the comparative amounts on a retrospective basis, as set out in notes 29.2 and 29.3.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2013 (continued)

	2013 R'000	2012 R'000

29. APPLICATION OF NEW AND REVISED IFRSs (CONTINUED)

29.2 Impact on total comprehensive income for the year of application of IAS19 (as revised in 2011)

	2013 R'000	2012 R'000
Impact on profit for the year:		
(Increase)/Decrease in staff costs expenses - related to actuarial (gains)/losses	**(1 541)**	3 685
Decrease in staff costs expenses - related to reallocation as other interest expense	**(1 369)**	(1 232)
Increase in other interest expense	**1 369**	1 232
Decrease/(Increase) in tax expenses	**431**	(1 032)
Net (decrease)/increase in profit for the year	**(1 110)**	2 653
Impact on other comprehensive income for the year:		
Increase/(Decrease) in remeasurement of defined benefit obligation - related to actuarial (gains)/losses	**1 541**	(3 685)
(Decrease)/Increase in tax relating to other comprehensive income	**(431)**	1 032
Net increase(decrease) in other comprehensive income for the year	**1 110**	(2 653)
Change in total comprehensive income for the year	**–**	–
(Decrease)/Increase in profit for the year attributable to:	**(1 110)**	2 653
Equity holder of the parent:	**(1 110)**	2 653
Non-controlling interests:	**–**	–
Increase/(Decrease) in total comprehensive income for the year attributable to:	**1 110**	(2 653)
Equity holder of the parent:	**1 110**	(2 653)
Non-controlling interests:	**–**	–

29.3 Impact on assets, liabilities and equity as at 1 January 2012 of the application of IAS19 (as revised in 2011)

	As at 1 January 2012 previously reported R'000	IAS19 adjustments R'000	As at 1 January (restated) R'000
Employee benefits reserve	–	(4 643)	(4 643)
Retained earnings	380 836	4 643	385 479
Total effect on equity	380 836	–	380 836

The accumulated actuarial loss adjustment as at 1 January 2012, related to the net defined benefit liability, was R6.448 million that was no longer recognised as profit or loss, but rather through other comprehensive income as an "employee benefits reserve". After the recognition of deferred tax on the employee benefits reserve of R1.806 million, the net opening balance adjustment amounted to R4.643 million.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013

BANK RISK MANAGEMENT PHILOSOPHY

The Bank 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 extended global financial crisis. Risk management is a key focus of the Bank, 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 downturns than others. Changing 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, the Bank acknowledges the potential of concentration risk in being a niche bank – 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 Bank remains well positioned to effectively manage identified threats in a way that minimises risks to the Bank. Continuous risk management and control reviews are undertaken by senior staff members to identify material control weaknesses and action is taken as required to address any areas of weakness.

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 essentially conservative, with proper regard to the mix of risk and reward. Existing policies, methodologies, processes, systems and infrastructure are frequently evaluated for relevance, to ensure that they remain at the forefront of risk management, and in line with regulatory developments and emerging best practices. The Bank takes all necessary steps to safeguard its depositors' funds, its own asset base, and shareholder's funds.

A number of risk initiatives were implemented and others further entrenched during the year. These included:

- further enhancements to the Asset Liability Management monitoring and reporting process;
- enhancements to the Risk Tolerance Framework approved by the Board;
- additions to the prudential management schedule, wherein all risk-related ratios are monitored and reported to the ALCO and Board on a monthly basis;
- enhancements to the Card and Treasury Back Office risk control self-assessment templates;
- streamlining of risk management methodologies and techniques in subsidiary companies together with rewrites of processes and procedures in use;
- expansion of stress testing;
- review and enhancement to the application of the Principles for the Sound Management of Operational Risk;
- expanded utilisation of an online training application to ensure that staff stay abreast with regulatory and other changes;
- re-engineering and review of Treasury back office processes to ensure effective mitigation of identified risks
- Bank-wide review of the Enterprise-Wide Risk Management Framework to factor in changes in risk profiles; and
- review of the Funding Policy and Contingent Funding plan.

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 in line with changing circumstances. Risk dimensions vary in importance, depending 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 risk-taking behaviour to be more closely aligned with strategic objectives.

Risk management is performed on a Bank-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 support from information technology. Independent oversight and validation by internal audit functions ensure a high standard of assurance across methodology, operational and process components of the Bank's risk and capital management processes.

RISK MANAGEMENT LIFECYCLE/ PROCESS

All of the Bank'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 Bank's governance structure and risk management profile, reflecting the expectations and requirements of the Board in respect of key areas of control. The standards and effective maintenance of the risk control self-assessment process ensures alignment and consistency in the way that prevalent risk types are identified and managed, and form part of the various phases of the risk management lifecycle, 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 MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

RISK MEASUREMENT (AND EVALUATION USING A RANGE OF ANALYTICAL TOOLS)

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

To consider risk appetite and the alignment against broader financial targets, the Bank mainly considers the level of earnings, growth and volatility that it is willing to accept from certain risks that are core to its business. Economic and regulatory capital required for such transactions is also considered, together with the resultant return on the required capital. The Bank also maintains a capital buffer for unforeseen events and business expansion.

RISK MANAGEMENT (AS AN INDEPENDENT FUNCTION)

The Bank'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, establish how much risk is acceptable, and to decide how the Bank will stay within targets laid down in risk tolerance thresholds.

RISK MONITORING (AND COMPLIANCE WITH DOCUMENTED POLICIES)

Open, two-way communication between the Bank 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 (through Banks Act returns and periodic meetings).

RISK CONTROL (STRESS AND BACK-TESTING)

The Bank 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 Bank'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 deployed within the Bank.

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 unit within the Bank, 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 Bank's reputation and success. These decisions are usually intended to enhance the Bank's long-term viability or success and are therefore 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 Bank, 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 Bank'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 it is 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 Bank 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 are approved by the RMC. Business and Operating units are integrally involved in the process in both risk identification and evaluation.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

The Bank subscribes to the Principles for the Sound Management of Operational Risk as defined by the Basel Committee on Banking Supervision.

Business Continuity Management continues to be an area of focus. Business Continuity Management ensures the availability of key staff and processes required to support essential activities in the event of an interruption to or disruption of business. Business Continuity Management 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 Bank 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 Bank. The outcome of these assessments resulted in the Bank identifying different levels of risk related to specific characteristics of the business where it was deemed prudent to hold a capital buffer in addition to the regulatory capital requirements. Such buffer requirements are re-evaluated half-yearly and adjusted where appropriate.

The Bank employs a size-appropriate approach to stress testing that is a component of business planning. Stress testing measures potential volatility of earnings under various scenarios.

Under the Enterprise-wide Risk Management Framework, the direct risks of the Bank have been categorised and those deemed to be of the most significance are reported on below:

CREDIT RISK

Credit parameters and tolerance levels are clearly defined and reflected in governing procedures and policies. The Bank offers a spread of banking products common to the banking industry, with a specific focus on small- and medium-sized businesses, across a wide variety of industries. While 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 Bank to credit-related losses in the event of non-performance. The counterparties to these contracts are financial institutions. The Bank 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 Bank did not have any significant concentration of risk that had not been adequately provided for. There were no material exposures in advances made to foreign entities at year end.

A portfolio analysis report is prepared and presented to the RMC analysing the performance and make-up of the book, including customer, geographic and segment concentration.

The Bank 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 aggregate). 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.

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

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 Bank takes all necessary steps to safeguard its depositors' funds, its own asset base, and shareholder funds.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

The table below summarises the Bank'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
2013				
Current accounts	**19 521**	**–**	**–**	**19 521**
Credit cards	**2 144 070**	**13 019**	**–**	**2 157 089**
Mortgage loans	**280 573**	**92 728**	**–**	**373 301**
Installment sales and leases	**27 535**	**–**	**–**	**27 535**
Structured loans	**1 101 793**	**–**	**–**	**1 101 793**
Medium-term loans	**23 644**	**–**	**–**	**23 644**
Negotiable securities	**–**	**–**	**496 608**	**496 608**
Cash and cash equivalents	**–**	**–**	**1 490 681**	**1 490 681**
Guarantees	**–**	**–**	**400 147**	**400 147**
Letters of credit	**–**	**–**	**16 024**	**16 024**
	3 597 136	**105 747**	**2 403 460**	**6 106 343**
2012				
Current accounts	1 340 870	–	–	1 340 870
Credit cards	22 227	13 702	–	35 929
Mortgage loans	2 435 482	52 612	–	2 488 094
Installment sales and leases	285 334	–	–	285 334
Structured loans	44 579	–	–	44 579
Medium-term loans	1 115 512	–	–	1 115 512
Negotiable securities	–	–	257 514	257 514
Cash and cash equivalents	–	–	1 218 714	1 218 714
Guarantees	–	–	300 496	300 496
Letter of credit	–	–	15 634	15 634
	5 244 004	66 314	1 792 358	7 102 676

OPERATIONAL RISK

Operational risks faced by the Bank are extensive and include robbery, fraud, theft of data, unauthorised systems access, legal challenges, statutory and legislative non-compliance, ineffective operational processes, and business continuity. Operational risk can also cause reputational damage and, therefore, efforts to identify, manage and mitigate operational risk are equally sensitive to reputational risk, as well as the risk of financial loss.

Operational risk management's aim is to enhance the level of risk maturity across the Bank, by implementing and embedding process-based risk and control identification and assessments, and integrating the operational risk management process in all business units to ensure adequate risk management in an ever-changing business and financial industry. The Operational Risk Committee meets at least quarterly and has representation from all business units.

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 internal operational loss database, 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 monitoring and reviews by both the Compliance and Internal Audit functions, in line with annual plans approved by the Board;
- comprehensive data security and protection;

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

- ongoing review of the Bank-wide risk control self-assessment process, rolled out to job functional level in high-risk operational processing areas;
- ongoing review of key risk indicators, as a tool to further assist with risk identification and assessment;
- limiting access to systems and enforcing strong password controls; and
- a comprehensive insurance programme to safeguard the Bank's financial and non-financial assets.

Disaster recovery and business continuity management facilities were outsourced to specialist service providers during the year.

The Bank further benchmarks itself and stays abreast with developments regarding operational risk by actively participating as a member of the Banking Association of South Africa's operational risk forum and task group as well as being a member of the industry working group on accounting impact events.

The Bank subscribes to the Principles for the Sound Management of Operational Risk. Compliance with the principles has been reviewed, and action plans put in place to ensure compliance with the principles.

TECHNOLOGY RISK

Technology risk management forms a key component of the Enterprise-wide Risk Management Framework, and is effectively managed under the auspices of the IT Steering Committee, a Board-appointed committee. The compliance and governance aspects are independently managed within the risk environment and are reported on independently to the Technology Committee.

The Bank successfully implemented a new treasury system (BaNCS Treasury) during March 2013. This system interfaces with the core banking system (BaNCS).

The Bank replaced its IT services partners during the year under review and also outsourced the disaster recovery and business continuity facilities to specialist service providers.

A number of IT-related initiatives were implemented, and others further entrenched during the year. These included:

- enhancement of IT governance and information security frameworks;
- new DR documentation standard;
- comprehensive revamp of a portion of the head office infrastructure;
- ODS enhancement project in progress;
- relocation of the Bank's disaster-recovery capabilities to a specialist environment;
- new treasury system;
- evaluation and review of PCI-DSS compliance on card applications;
- replacement of desktop computers;
- upgrade of Prime (credit card system) software in progress; and
- new service partners.

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, depending on market events.

The Bank does not currently take proprietary trading positions and therefore has minimal exposure to market risk. Should the Bank consider entering into a proprietary trading position, the Trading Committee and RMC will have to evaluate and approve entering into such positions. The Trading Committee will ensure that the Bank 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 Bank enters into derivative financial instruments to manage its exposure to interest rate and foreign currency risk, including:

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

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, and it is immediately corrected and reported to the ALCO, which is a management committee accountable to the RMC.

The Bank 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 Bank 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 on pages 49 to 53).

There has been no significant change to the Bank's exposure to market risks, or the manner in which it manages and measures the risk. Additional controls were put in place to monitor foreign exchange exposures on a real-time basis subsequent to the implementation of BaNCS Treasury. Various conservative prudential risk limits are in place. Exposures under prudential risk limits and various sensitivities relating thereto are reported to the ALCO, RMC and Board on a regular basis.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

FOREIGN CURRENCY RISK

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

The Bank 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 R53.6 million (2012: R7.5 million). An adverse movement in the exchange rate of 10% would reduce the Bank's income by R5.4 million (2012: R0.6 million).

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
2013					
Total foreign exchange assets	**199 414**	**568**	**4 608**	**3 849**	**208 439**
Total foreign exchange liabilities	**(79 672)**	**(8 542)**	**(1 428)**	**–**	**(89 642)**
Commitments to purchase foreign currency	**87 414**	**70 641**	**5 208**	**2 752**	**166 015**
Commitments to sell foreign currency	**(207 672)**	**(62 630)**	**(6 877)**	**(4 256)**	**(281 435)**
Year-end effective net open foreign currency positions	**(516)**	**37**	**1 511**	**2 345**	**3 377**
2012					
Total foreign exchange assets	86 031	23 781	3 724	7 164	120 700
Total foreign exchange liabilities	(87 604)	(16 970)	(1 773)	(96)	(106 443)
Commitments to purchase foreign currency	143 367	42 352	17 271	4 480	207 470
Commitments to sell foreign currency	(141 499)	(50 117)	(18 861)	(7 079)	(217 556)
Year-end effective net open foreign currency positions	295	(954)	361	4 469	4 171

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 re-pricing on a daily basis, and reports back to the ALCO, RMC and the Board.

The Bank is exposed to interest rate risk as it takes deposits from clients at both fixed- and floating interest rates. The Bank manages the risk by maintaining an appropriate mix between fixed- and floating rate funds, as well as by using interest rate swap contracts, and matching the maturities of deposits and assets, as appropriate.

The objective in 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 Bank agrees to exchange the difference between fixed- and floating interest rate amounts, calculated on agreed notional principal amounts. Such contracts enable the Bank 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 Bank 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 rate-sensitive assets and liabilities. The Bank is also exposed to basis risk, which is the difference in re-pricing characteristics of two floating-rate indices, such as the South African prime rate and three-month JIBAR.

To measure interest rate risk, the Bank aggregates interest rate-sensitive assets and liabilities into fixed-time bands, in accordance with the respective interest re-pricing dates. The Bank 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.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

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.

The yield on assets remained under pressure during 2013, as a result of the low interest rate environment in South Africa. South Africa was also not immune to the global credit and liquidity crisis or market uncertainty in respect of the longer-term interest rate trends. Net interest income was adversely impacted by the negative endowment effect due to the current high levels of excess capital of the Bank and the high level of non-interest-bearing customer deposits. Pressure on margins is likely to continue during 2014.

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 in 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 by the ALM forum. Various approved prudential limits are in place and monitored by the ALM forum. The results are reported to the ALCO and Board regularly.

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 Bank's net profit and equity at year-end would increase by R8.4 million, or decrease by R11.9 million (2012: increase/decrease by R8.9 million/ R5.1 million). This is mainly attributable to the Bank's exposure to interest rates on its surplus capital and lending and borrowings in the banking book.

The table below summarises the Bank'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 re-pricing profile indicates that the Bank remains asset-sensitive as interest-earning assets re-price 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.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

	Up to 1 month R'000	1 – 3 months R'000	3 – 12 months R'000	1 – 5 years R'000	Non–interest sensitive R'000	Total R'000	Effective interest rate %
2013							
Assets							
Intangible assets	–	–	–	–	196 466	196 466	–
Property and equipment	–	–	–	–	27 254	27 254	–
Tax	–	–	–	–	1 220	1 220	–
Other accounts receivable	–	–	–	–	86 357	86 357	–
Interest in subsidiaries	108 726	–	–	–	46 064	154 790	–
Other investments	–	–	–	–	5 737	5 737	–
Non-current assets held for sale	–	–	–	–	13 470	13 470	–
Loans and advances	5 125 111	–	–	21 451	(62 977)	5 083 585	9.24
Derivative financial instruments	–	–	–	–	10 630	10 630	–
Negotiable securities	36 940	106 820	335 512	17 336	–	496 608	5.52
Cash and cash equivalents	1 087 234	62 533	–	–	340 914	1 490 681	4.61
Total assets	**6 358 011**	**169 353**	**335 512**	**38 787**	**665 135**	**7 566 798**	
Equity and liabilities							
Total equity	–	–	–	–	1 804 090	1 804 090	–
Deferred tax liabilities	–	–	–	–	34 204	34 204	–
Long-term funding	–	495 103	–	–	(1 930)	493 173	7.71
Deposits	3 128 656	477 580	512 813	55 522	873 697	5 048 268	3.95
Derivative financial instruments	–	–	–	–	11 459	11 459	–
Provisions and other liabilities	–	–	–	–	71 311	71 311	–
Other accounts payable	–	–	–	–	104 293	104 293	–
Total equity and liabilities	**3 128 656**	**972 683**	**512 813**	**55 522**	**2 897 124**	**7 566 798**	
Financial position interest sensitivity gap	**3 229 355**	**(803 330)**	**(177 301)**	**(16 735)**		**2 231 989**	
Derivative financial instruments	**(232)**	**21 504**	**–**	**(21 272)**		**–**	
Total net interest sensitivity gap	**3 229 123**	**(781 826)**	**(177 301)**	**(38 007)**		**2 231 989**	
2012							
Assets							
Intangible assets	–	–	–	–	197 823	197 823	–
Property and equipment	–	–	–	–	19 069	19 069	–
Tax	–	–	–	–	1 262	1 262	–
Other accounts receivable	–	–	–	–	61 447	61 447	–
Interest in subsidiaries	96 781	–	–	–	21 517	118 298	–
Other investments	–	–	–	–	19 822	19 822	–
Non-current assets held for sale	–	–	–	–	13 453	13 453	–
Loans and advances	5 235 545	–	–	28 962	(95 754)	5 168 753	9.37
Derivative financial instruments	–	–	–	–	6 565	6 565	–
Negotiable securities	2 330	36 076	200 468	18 640	–	257 514	5.77
Cash and cash equivalents	1 021 921	–	–	–	196 793	1 218 714	4.24
Total assets	6 356 577	36 076	200 468	47 602	441 997	7 082 720	
Equity and liabilities							
Total equity	–	–	–	–	1 685 877	1 685 877	–
Deferred tax liabilities	–	–	–	–	30 009	30 009	–
Long-term funding	494 983	–	–	–	(3 107)	491 876	7.80
Deposits	3 038 643	370 941	465 216	26 674	836 762	4 738 236	4.01
Derivative financial instruments	–	–	–	–	7 160	7 160	–
Provisions and other liabilties	–	–	–	–	70 654	70 654	–
Other accounts payable	–	–	–	–	58 908	58 908	
Total equity and liabilities	3 533 626	370 941	465 216	26 674	2 686 263	7 082 720	
Financial position interest sensitivity gap	2 822 951	(334 865)	(264 748)	20 928		2 244 266	
Derivative financial instruments	2 273	27 814	–	(30 087)		–	
Total net interest sensitivity gap	2 825 224	(307 051)	(264 748)	(9 159)		2 244 266	

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (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 Bank is exposed to daily cash needs from overnight deposits, current accounts, maturing deposits, loan drawdowns and guarantees.

To measure liquidity risk, the Bank aggregates assets and liabilities into fixed time-bands in accordance with the respective maturity dates, which measure 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 Bank's short-, medium- and long-term funding and liquidity requirements.

Through active liquidity management, the Bank 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 Bank performs, among others, the following:

- the maintenance of a stock of readily available, high-quality liquid assets in excess of the statutory requirements, as well as a strong statement of financial position liquidity ratios;
- an assumptions-based sensitivity analysis to assess potential cash flows at risk;
- the management of concentration risk (i.e. undue reliance on any single counterparty or counterparty group, sector, market, product, instrument, currency and tenor;
- the maintenance of sources of funding for contingency funding needs;
- the monitoring of daily cash flow movements/cash flow requirements, including daily settlements and collateral management processes;
- targeting a diversified funding base to avoid undue concentrations by investor, market source and maturity;
- the creation and monitoring of prudential liquidity risk limits; and
- the maintenance of an appropriate term mix of funding.

Overall, the Bank'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 Bank continues to actively manage its stress funding sources and liquidity buffers, to ensure that it exceeds the estimated stress funding requirements that could emanate from moderate- to high-stressed liquidity events. The Bank subscribe to BIS's Principles for Sound Liquidity Risk Management and Supervision. Overall, the Bank's liquidity position remains strong.

Macro-economic conditions continued to hinder growth in advances and specifically in deposits as the banking sector in South Africa is characterised by certain structural features, such as a low discretionary savings rate, and a higher degree of contractual savings that are captured by institutions such as pension funds, provident funds and providers of asset management services. The Bank will continue to focus on gathering retail customer and longer-term deposits to reshape the structure of the balance sheet, and to ensure compliance with the Basel III liquidity requirements, which will be effective in 2015.

The two key liquidity ratios that were introduced by Basel III are the Liquidity Coverage Ratio ("LCR"), which is designed to promote short-term resilience of the one-month liquidity profile by ensuring that banks have sufficient high-quality liquid assets to meet potential outflows in a stressed environment; and the Net Stable Funding Ratio ("NSFR"), which is designed to measure the stability of long-term structural funding.

Both the LCR and the NSFR are subject to a monitoring period, which commenced in January 2013, with full implementation and compliance of the LCR and NSFR in 2015 and 2018 respectively. The Bank also monitors other Basel III-related ratios, such as the Leverage Ratio, which is a measure of qualifying capital to both on- and off-balance-sheet exposures. The Bank currently meets all the requirements of the new regulations.

There were no significant changes in the Bank's liquidity position during the current financial year, or in the manner in which it manages and measures the risk. The Bank is adequately funded and able to meet all of its current and future obligations. During 2011, the Bank entered into a R491 million seven-year term loan with the IFC. The facility has been fully utilised.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

The table below summarises assets and liabilities of the Bank 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
2013			
Maturing up to one month	**3 149 945**	**3 088 400**	**61 545**
Maturing between one and three months	**186 505**	**1 035 231**	**(848 726)**
Maturing between three and six months	**232 649**	**287 410**	**(54 761)**
Maturing between six months and one year	**360 089**	**452 466**	**(92 377)**
Maturing after one year	**3 279 728**	**864 539**	**2 415 189**
Non-contractual	**357 882**	**34 662**	**323 220**
	7 566 798	**5 762 708**	**1 804 090**
2012			
Maturity up to one month	2 675 488	3 023 862	(348 374)
Maturing between one and three months	41 836	964 353	(922 517)
Maturing between three and six months	96 296	318 340	(222 044)
Maturing between six months and one year	517 537	529 075	(11 538)
Maturing after one year	3 458 326	530 701	2 927 625
Non-contractual	293 237	30 512	262 725
	7 082 720	5 396 843	1 685 877

The remaining period to contractual maturity of financial liabilities of the Bank at the reporting date, which includes the interest obligation on un-matured 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	4 – 5 months R'000	7 – 12 months R'000	Over 1 year R'000
2013					
Deposits	**2 891 727**	**1 040 249**	**292 350**	**472 154**	**401 990**
Long-term funding	**–**	**–**	**–**	**–**	**594 275**
Derivative financial instruments	**7 869**	**1 581**	**936**	**470**	**603**
Other accounts payable	**104 293**	**–**	**–**	**–**	**–**
Guarantees, letters of credit and committed undrawn facilities	**521 918**	**–**	**–**	**–**	**–**
Operating lease commitments	**1 835**	**3 597**	**5 352**	**10 522**	**63 732**
	3 527 642	**1 045 427**	**298 638**	**483 146**	**1 060 600**
2012					
Deposits	2 892 296	969 078	324 947	552 727	41 160
Long-term funding	–	–	–	–	703 131
Derivative financial instruments	3 054	2 329	96	142	1 540
Other accounts payable	58 407	–	–	–	–
Guarantees, letters of credit and committed undrawn facilities	382 444	–	–	–	–
Operatinglease commitments	1 868	3 704	5 296	9 737	82 163
	3 338 069	975 111	330 339	562 606	827 994

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

BASEL III – INFLUENCING RISK MANAGEMENT DEVELOPMENTS

In today's complex environment, combining effective bank-level management with market discipline and regulatory supervision best achieves systemic safety and soundness. The Bank recognises the significance of Basel III in aligning regulatory capital to risk, and further entrenching risk-reward principles and practices in bank management and decision-making. This framework focuses on strengthening and harmonising global liquidity standards to ensure that internationally active banks are adequately capitalised.

South Africa embraced the principles of the Basel III capital framework, which was successfully implemented by the Bank on 1 January 2013. Full compliance with all the regulations will only be required in January 2019.

The Bank's capital adequacy was largely unaffected by the new regulations, which impose tighter restrictions on the quality and type of capital that qualifies as Tier 1 capital. The Bank's capital still consists almost entirely of Tier 1 capital. The new regulations also increase the required minimum regulatory capital. The Bank's internal capital targets remains well in excess of the new minimum requirements.

The other most significant changes introduced by Basel III are the Liquidity Coverage Ratio ("LCR") and the Net Stable Funding Ratio ("NSFR"). The banking industry in South Africa will find it difficult to fully meet the new liquidity ratios ("LCR" and the "NSFR") as a result of the structural characteristics and constraints with regards to qualifying liquid assets in South African.

The SARB made committed liquidity facilities available to banks with insufficient High Quality Liquid Assets ("HQLA") due to the fact that South Africa has virtually no Level II HQLA. This will enable banks to meet the LCR requirement by 2015. The cost for this facility ranges from 15 to 30 basis points if not utilised. Utilisation of this facility will be limited to 30 days at a cost of SARB's repo rate plus 100 basis points for the utilisation period.

The Bank currently complies with the requirements of the LCR and NSFR but continues to monitor these ratios on a monthly basis. The Bank also calculates various sensitivities on these ratios to identify potential constraints in meeting the requirements timeously.

The Bank will continue to seek and adopt market best-practice in accordance with these regulatory requirements. The focus in 2014 will remain on lengthening the maturity of the Bank's deposits and putting appropriate funding structures in place to further enhance these ratios.

CAPITAL MANAGEMENT

The Bank is subject to minimum capital requirements, as defined in the Banks Act and Regulations. The management of the Bank'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 while ensuring sufficient capital is available to support the growth objectives of the Bank. 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 on a regular basis as part of the Internal Capital Adequacy Assessment Process and strategic planning review. The RMC considers the various risks faced by the Bank and analyses the need to hold capital against these risks while 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 Bank Regulations 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 Bank 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 Bank 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 assessed operational risk profile and targeted growth requirements.

Capital to support the Bank's needs is currently generated by retained earnings and the surplus capital held.

The approach to capital management has been further enhanced over the past year in line with Basel III, and will remain a focus area for the future. The Bank was largely unaffected by the new regulations, which impose tighter restrictions on the quality and type of capital that qualifies as Tier 1 capital and raised the minimum required regulatory capital. The Bank's capital still consists almost entirely of Tier 1 capital.

The Bank complies with the provisions of section 46 of the Companies Act, whereby all dividends and distributions are authorised by the Board. The Board authorises a distribution after satisfying itself that the Bank will satisfy the solvency and liquidity test immediately after completing the distribution.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

The level of capital for the Bank is as follows:

	2013 R'000	2012 R'000
Risk-weighted assets – Banking book		
Credit risk	**6 584 195**	4 993 711
Operational risk	**1 019 149**	952 817
Market risk	**59 925**	33 813
Equity	**5 737**	19 822
Other assets	**138 997**	126 424
	7 808 003	6 126 587
Net qualifying capital and reserves		
Primary capital	**1 587 623**	1 450 291
Share capital and share premium	**1 483 300**	1 483 300
Retained earnings	**249 058**	152 583
Other reserves	**51 731**	12 231
Less: Deductions	**(196 466)**	(197 823)
Secondary capital	**5 587**	9 054
General allowance for credit impairment	**5 587**	9 020
Surplus resulting from a revaluation of specified assets	**–**	34
	1 593 210	1 459 345
Capital adequacy ratio (%)	**20.4**	23.8
Primary capital (%)	**20.3**	23.7
Secondary capital (%)	**0.1**	0.1

FRAUD

PAYMENT CARD FRAUD

The Bank is an issuer of MasterCard and Visa cards and has, in line with the card associations' regulations, adopted proactive measures to prevent fraudulent use of these products. The Bank makes use of monitoring fraud reports, based on a set of parameters prescribed by the card associations, and which are reviewed on a daily basis with the aim of identifying suspicious transactional behaviour.

In addition to standard monitoring measures, the Bank offers an SMS notification service on both its credit and debit card products. Since its introduction, this service has contributed to the early detection of fraudulent transactions and mitigation of losses.

If fraudulent activity is confirmed, action is taken to prevent further use of the card/card number. Confirmed fraudulent transactions are investigated and reported to the relevant card associations and the South African Banking Risk Information Centre ('SABRIC"), which determines common trends and then alerts the industry accordingly.

The Bank will start issuing integrated circuit cards (also known as "smart" or "chip" cards) during the second quarter of 2014. These cards use advanced encryption, embedded card risk analysis capabilities, and online and offline authentication. The traditional methods used to steal card data or to clone cards using magstripe technology are rendered worthless by implementing these cards. Another functionality to be implemented at the end of the first quarter is Verified by Visa. Verified by Visa is a unique service offered by Visa International that uses a One Time PIN (OTP) or personal password to protect a cardholder against unauthorised use when making online purchases (also known as e-Commerce transactions).

The Bank recently launched merchant acquiring, and offers merchants point-of-sale devices to acquire transactions on behalf of VISA and MasterCard. In order to address the fraud risks associated with merchant acquiring, the Bank has implemented fraud prevention systems and merchant account monitoring tools that comply with the relevant card associations' requirements.

RISK MANAGEMENT AND CONTROL

for the year ended 31 December 2013 (continued)

FRAUD OTHER THAN PAYMENT CARD FRAUD

The Bank has adopted a zero tolerance approach toward all types of fraud and theft. The Forensic Investigator investigates all incidents relating to external fraud while internal fraud is investigated by the Internal Audit function.

If an incident of fraud is brought to the Bank's attention, it is investigated immediately, evidence is collected, 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 the SABRIC and the South African Police Service.

FRAUD AWARENESS

Fraud awareness training is conducted on a regular basis and awareness newsletters are compiled and disseminated to all staff. These newsletters address a wide range of topics and are not limited to payment card fraud only. Fraud awareness newsletters are also compiled and distributed to clients. Fraud awareness material on prevalent modus operandi is also made available to clients and staff members on the Bank's website in the Fraud Prevention webpage.

During 2013, the Fraud Department discarded the issuance of additional modules of the Fraud Awareness User Guide and replaced it with Fraud Alerts. These Fraud Alerts contain warnings of the recently identified fraud trends as well as relevant Fraud Prevention and Awareness material related to the incident. The aim of the Fraud Alerts is to cover specific and current fraud trends as, and when, they are identified as well as create awareness on the most prevalent fraud incidents.

Fraud Department staff members attend meetings of industry role players and use Internet-based sources to stay abreast of fraud trends and the prevention thereof. The Bank also works closely with SABRIC, the Payment Association of South Africa, and card associations.

WHISTLE-BLOWING

The Bank has a comprehensive Protected Disclosures Policy based on the Act of the same name. The policy addresses the reporting of corrupt activities, as well as any improper conduct, under a section on whistle-blowing. Employees are encouraged to make disclosures in good faith and on reasonable grounds.

All employees receive, twice annually, an electronic step-by-step guide on what to report and how to report it.

To this end, an enhanced anonymous reporting system is in place to enable employees to report directly to Compliance and Internal Audit, using a web-based tool. This system simplifies the anonymous reporting procedure, and encourages employees to make use of the process.