Mercantile Bank Limited

The Business Bank inspired by entrepreneurs

2020 AUDITED FINANCIAL STATEMENTS

for the 14-month period ended 29 February

CONTENTS

In terms of section 29(1)(e)(ii) of the Companies Act, it is confirmed that the preparation of these financial statements is the responsibility of MEL Teixeira (Chartered Accountant) South Africa, the Financial Director of the Company.

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

Registration number: 1965/006706/06 | An Authorised Financial Services and Credit Provider

NCRCP19 | Web: **mercantile.co.za**

GLOSSARY OF TERMS

ABBREVIATION	DEFINITION OR DESCRIPTION
ALCO	Asset and Liability Committee (a Management Committee accountable to the RCMC)
ALM	Asset and liability management
Bank Regulations	Regulations relating to banks issued in terms of section 90 of the Banks Act, No. 94 of 1990, as amended
Banks Act	Banks Act, No. 94 of 1990, as amended
BASA	Banking Association of South Africa
Capitec Bank Holdings	Capitec Bank Holdings Limited, Mercantile's ultimate holding company
Capitec Bank	Capitec Bank Limited, a wholly-owned subsidiary of Capitec Bank Holdings Limited and Mercantile's holding company
CEO	Chief Executive Officer
CGD	Caixa Geral de Depósitos S.A., a company registered in Portugal and the ultimate holding company of Mercantile Bank Limited prior to 7 November 2019
Companies Act	Companies Act, No. 71 of 2008
COVID-19	Coronavirus Disease 2019
CREDCOM	Credit Committee
EAD	Exposure at default
ECL	Expected credit loss(es)
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
IRBA	Independent Regulatory Board for Auditors
ISA	International Standards for Auditing
ISF SoGP 2018	Information Security Framework Standard of Good Practice 2018
IT	Information technology
JIBAR	Johannesburg Interbank Average Rate
King IV	King IV Report on Corporate Governance for South Africa 2016
LGD	Loss given default
Mercantile	Mercantile Bank Limited
PD	Probability of default
RDARR	Principles for Effective Risk Data Aggregation and Risk Reporting as published by the Bank for International Settlements (publication BCBS 239)
RCMC	Risk and Capital Management Committee
SARB	South African Reserve Bank
SICR	Significant increase in credit risk
the Bank	Mercantile Bank Limited
the Board	The Board of Directors
the Company	Mercantile Bank Limited

DIRECTORS' RESPONSIBILITY STATEMENT

In terms of the Companies Act, the Directors are required to maintain adequate accounting records and prepare financial statements that fairly present the Company's financial position as at 29 February 2020, and the results and cash flows for the 14-month period ended 29 February 2020.

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, though 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 risk-based audits.

The External Auditor is responsible for reporting on the fair presentation of the Company's financial statements.

The Company's financial statements are prepared in accordance with the Companies Act and IFRS, as issued by the International Accounting Standards Board, and incorporate responsible disclosures in line with the accounting policies of the Company. The Company's financial statements are based on consistently applied, appropriate accounting policies, except as otherwise stated, and are supported by reasonable and prudent judgements and estimates. The financial statements of the Company were prepared on a going concern basis. The Board of Directors has performed a formal review of the Company's results and its ability to continue as a going concern in the foreseeable future and confirm that they are satisfied that the Company has adequate resources to continue in business for the foreseeable future. The going concern status of the Company has also been considered in light of recent COVID-19 developments and the Board of Directors remain satisfied that the Company has adequate resources to continue business in the foreseeable future.

These financial statements, set out on pages 9 to 64, have been approved by the Board of Mercantile Bank Limited and are signed on its behalf by:

SL Botha	KR Kumbier
Chairman	*CEO*

9 April 2020

COMPANY SECRETARY'S CERTIFICATE

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 14-month period ended 29 February 2020, 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.

T Singh
Company Secretary

9 April 2020

INDEPENDENT AUDITOR'S REPORT

To the shareholder of Mercantile Bank Limited

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

OPINION

We have audited the financial statements of Mercantile Bank Limited (the Company) set out on pages 9 to 63, which comprise the statement of financial position as at 29 February 2020, and the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the 14-month period then ended, and the notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the financial statements present fairly, in all material respects, the financial position of Mercantile Bank Limited as at 29 February 2020, and its financial performance and cash flows for the 14-month period then ended in accordance with International Financial Reporting Standards (IFRS) and the requirements of the Companies Act of South Africa.

BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (ISA). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with sections 290 and 291 of the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (Revised January 2018)*, parts 1 and 3 of the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (Revised November 2018)* (together the IRBA Codes) and other independence requirements applicable to performing audits of financial statements in South Africa. We have fulfilled our other ethical responsibilities, as applicable, in accordance with the IRBA Codes and in accordance with other ethical requirements applicable to performing audits in South Africa. The IRBA Codes are consistent with the corresponding sections of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* and the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* respectively. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

OTHER INFORMATION

The Directors are responsible for the other information. The other information comprises the Directors' Responsibility Statement, the Company Secretary's certificate, the Audit Committee Report and the Directors' Report as required by the Companies Act of South Africa and the supplementary information as disclosed on page 64. The other information does not include the Company's financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

RESPONSIBILITIES OF THE DIRECTORS FOR THE FINANCIAL STATEMENTS

The Directors are responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards 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 misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISA, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In terms of the Independent Regulatory Board for Auditors (IRBA) Rule published in Government Gazette Number 39475 dated 4 December 2015, we report that Deloitte & Touche has been the auditor of Mercantile Bank Limited for 18 years.

Deloitte & Touche

Deloitte & Touche
Registered Auditor
Per: Diana Jorge
Partner

9 April 2020

National Executive: *LL Bam Chief Executive Officer, *TMM Jordan Deputy Chief Executive Officer; Clients & Industries, *MJ Jarvis Chief Operating Officer, *AF Mackie Audit & Assurance, *N Singh Risk Advisory, *DP Ndlovu Tax & Legal, *MR Verster Consulting, *JK Mazzocco People & Purpose, MG Dicks Risk Independence & Legal, *KL Hodson Financial Advisory, *B Nyembe Responsible Business & Public Policy, *TJ Brown Chairman of the Board

**Partner and Registered Auditor*

A full list of partners and directors is available on request.

B-BBEE rating: Level 1 contribution in terms of the DTI Generic Scorecard as per the amended Codes of Good Practice.

Associate of Deloitte Africa, a Member of Deloitte Tohmatsu Limited.

AUDIT COMMITTEE REPORT

for the 14-month period ended 29 February 2020

The Audit Committee is pleased to present its report for the 2020 financial period. This report has been prepared based on the requirements of the Companies Act, the Banks Act, King IV and other applicable regulatory requirements.

The Audit Committee duties include its statutory duties in terms of section 94(7) of the Companies Act, section 64 of the Banks Act, to the extent applicable, as well as additional duties assigned to it by the Board. The Audit Committee is a committee of the Mercantile Board and has assumed the responsibilities of an audit committee in respect of all subsidiaries of Mercantile, with the exception of the securitisation vehicle, Compass Securitisation (RF) Limited, which has a separate audit committee. The role of the Audit Committee is fundamental in ensuring that trust and integrity are maintained over corporate reporting, entrenched by the efficiency of internal controls, the effectiveness of the Internal Audit function, the independence of the External Auditor, and optimised through a combined assurance model. The Audit Committee's main objective is to assist the Board in fulfilling its oversight responsibilities, and in particular, in evaluating the adequacy and efficiency of accounting policies, internal controls and financial and corporate reporting processes. In addition, the Audit Committee assesses the effectiveness of the internal audit activity and the independence and effectiveness of the External Auditor.

TERMS OF REFERENCE

The Audit Committee is both a statutory and a Board Committee. Its powers and terms of reference are derived from the Companies Act and are formalised in its charter, which is reviewed annually and approved by the Board. The Audit Committee has executed its duties during the past financial period in accordance with its charter and the Companies Act.

COMPOSITION

The Audit Committee comprises three independent Non-Executive Directors. As at 29 February 2020, the members were:

- JP Verster *(Chairman)*;
- JD McKenzie; and
- K Makwane.

JP Verster and JD McKenzie were appointed to the Audit Committee on 29 November 2019. L Hyne and DR Motsepe resigned from the Audit Committee effective 29 November 2019. TH Njikizana served as Chairman of the Audit Committee until 5 February 2020. On 5 February 2020, K Makwane was appointed as a member of the Audit Committee and JP Verster was elected as the Chairman.

The CEO, Financial Director, other Executive Directors, heads of Risk, Internal Audit, Compliance Management and Treasury, as well as the External Auditor are permanent attendees to the committee meetings. The External and Internal Auditors have unrestricted access to the Audit Committee Chairman or any other member of the committee, including closed sessions without management, on any matter that they regard as relevant to the fulfilment of the committee's responsibilities. The Audit Committee Chairman meets with the External and Internal Auditors separately between Audit Committee meetings.

The Audit Committee's responsibility to oversee financial reporting requires that all members have an understanding of financial statements and IFRS; an ability to assess the general application of IFRS in connection with accounting for estimates, accruals and reserves; experience in preparing, auditing, analysing or evaluating financial statements that present a breadth and level of complexity of account issues generally comparable to what can reasonably be expected to arise in the financial statements, or experience actively supervising those engaged in such activities; an understanding of internal control over financial reporting and an understanding of the Audit Committee's function. At least one-third of the members of the Audit Committee, at any time, shall have academic qualifications or experience in economics, law, corporate governance, finance, accounting, commerce, industry, public affairs or human resources management. In addition, all Audit Committee members should meet predetermined skills, competency and experience requirements. The Audit Committee is free to consult with specialists or consultants to assist it with the performance of its functions, subject to a Board-approved process, and all Audit Committee members must remain current with developments affecting the required skill set.

MEETINGS

The Audit Committee held seven 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 period under review, the Audit Committee:

- 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 and the auditor's scope and terms of engagement, ensuring the fees agreed do not impinge on the auditor's ability to perform adequate procedures as disclosed in note 29 to the financial statements;
- Believes the appointment of Deloitte & Touche complies with the relevant provisions of the Banks Act, the Companies Act and King IV;
- 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, or 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 Audit Committee 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.

For the sake of completeness, it is noted that Internal Audit provided a written assessment of the effectiveness of the system of internal controls and risk management to the Audit Committee, who reported on these matters to the Board. It was the duty of the Audit Committee to agree a risk-based audit programme with Internal Audit.

The head of Internal Audit functionally reported to the Audit Committee, had unrestricted access to the Audit Committee 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 Audit Committee believes that significant internal financial controls are effective.

REGULATORY COMPLIANCE

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

- Reviewed and recommended the Compliance charter for approval; and
- Evaluated the effectiveness and performance of the Compliance function.

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

EXTERNAL AUDIT

Deloitte & Touche was appointed as the Company's External Auditor in 1998 and the Company has embedded the policy of rotating the audit partner every five years, which is aligned to the Companies Act. There have been significant changes in the management of the Company during the External Auditor's tenure, which has mitigated the attendant risk of familiarity between the External Auditor and management. The adoption of the mandatory audit firm rotation will be considered as and when required by regulation.

Based on processes followed and assurances received, the Audit Committee is satisfied that both Deloitte & Touche and the audit partner, D Jorge, are independent of the Company. The Audit Committee confirms that no reportable irregularities were identified and reported by the External Auditor (in terms of the Auditing Professions Act, No. 26 of 2005).

EXTERNAL AUDITOR'S SERVICES: NON-AUDIT SERVICES

The Company will not contract its External Auditor for non-audit services where such an engagement compromises their independence and, in particular, the following areas are specifically excluded from services that may be procured from the External Auditor:

- Bookkeeping or other services related to accounting records or financial statements;
- Financial information systems design and implementation;
- Appraisal or valuation services, fairness opinions or contribution-in-kind reports for financial reporting purposes;
- Actuarial services;
- Internal Audit outsourcing and/or co-sourcing;
- Performance of management functions;
- Staff recruitment agents;
- Broker-dealer, investment adviser or investment banking services; and
- Legal services.

The following is a summary of the policy adopted by the Audit Committee to ensure proper governance and approval of the use of the External Auditor to provide non-audit services.

The Company will not contract its auditor on services prohibited in terms of section 90(2) of the Companies Act, and under the Code of Professional Conduct mentioned in the Auditing Profession Act, as amended from time to time. To ensure that such is complied with:

- The External Auditor confirms in writing, prior to providing a service for non-audit services, that such does not impair their independence and that they may provide such service;
- The CEO may approve non-auditing services projects up to R250 000;
- The Audit Committee approves non-auditing services projects exceeding R250 000;
- The cumulative total of non-audit services fees paid to the External Auditor may not exceed 25% of the audit fee for that year. Where the engagement of services would take the cumulative total of non-audit service fees paid to the External Auditor over 25% of the audit fee for that year, the engagement must be approved by the Audit Committee in advance of the engagement commencing;
- Management includes a report on non-audit services provided by the External Auditor for notification at the Audit Committee meetings; and
- Services rendered by other audit firms are not subject to the above and the CEO can approve such from time to time in accordance with the Company's general limits of authorities.

COMBINED ASSURANCE

The Audit Committee is of the view that the arrangements in place for the combined assurance model are working toward achieving the objective of a more effective, integrated approach across the disciplines of risk management, compliance and audit (and other assurance providers, as applicable). The journey of combined assurance will continuously evolve as the process matures within the organisation.

FINANCE FUNCTION

The Audit Committee received regular reports from the Financial Director regarding the financial performance of the Company; the tracking and monitoring of key performance indicators; details of budgets, forecasts, long-term plans and capital expenditures; financial reporting controls and processes; and the adequacy and reliability of management information used during the financial reporting process. The Audit Committee believes that the Financial Director, MEL Teixeira, who is responsible for the Finance function, 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 followed and assurances obtained, we believe that the accounting practices are effective.

FINANCIAL STATEMENTS

The Audit Committee reviewed and discussed the financial statements, reporting process and financial information included in the financial statements after considering recommendations from the Social, Ethics and Transformation Committee, the Remuneration Committee, the Risk and Capital Management Committee and the Directors' Affairs Committee.

The Audit Committee remains satisfied with the overall control environment, including those supporting the financial statements for 2020, as confirmed by Internal Audit.

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

On behalf of the Audit Committee:

JP Verster
Chairman of the Audit Committee

9 April 2020

DIRECTORS' REPORT

for the 14-month period ended 29 February 2020

The Directors have pleasure in presenting their report, which forms part of the audited financial statements of the Company for the 14-month period ended 29 February 2020.

NATURE OF THE BUSINESS

The Company is a registered bank incorporated in the Republic of South Africa and provides its clients with a full spectrum of domestic and international banking and financial services to niche markets in business, commercial and alliance banking.

HOLDING COMPANY

As at 6 November 2019, the holding company of Mercantile was Mercantile Bank Holdings Limited and the ultimate holding company was CGD, a company registered in Portugal. On 7 November 2019, Capitec Bank, a company incorporated in the Republic of South Africa, acquired the entire issued share capital of Mercantile Bank Holdings Limited. The Prudential Authority granted Capitec Bank approval to acquire 100% of the shareholding in Mercantile Bank Holdings Limited, as a subsidiary of Capitec Bank, and to transfer 100% of the assets and liabilities of Mercantile to Capitec Bank, within a period of 24 months, following the acquisition of Mercantile Bank Holdings Limited by Capitec Bank. Post-acquisition, all the assets and liabilities of Mercantile Bank Holdings Limited were transferred to Capitec Bank and the process to transfer the assets and liabilities of Mercantile has commenced and will be finalised by no later than October 2021. The Prudential Authority and the Financial Sector Conduct Authority gave their permission on 12 February 2020 to deregister Mercantile Bank Holdings Limited as the Bank's controlling company. The now-dormant company was placed under deregistration on 31 March 2020.

FINANCIAL RESULTS

To align Mercantile's reporting period with that of Capitec Bank, the entity changed the end of its reporting period from 31 December to the last day of February. Amounts presented for the 2020 reporting period are for a 14-month period. Comparative figures are for a 12-month period. Consequently, comparative amounts for the statement of comprehensive income, statement of changes in equity, statement of cash flows and related notes are not entirely comparable. Details of the financial results are set out on pages 9 to 64 and, in the opinion of the Directors, require no further comment.

SHARE CAPITAL

There were no changes to the authorised and issued share capital of the Company during the current and previous financial periods. The authorised and issued share capital of the Company is detailed in note 22 to the financial statements.

DIRECTORS, COMPANY SECRETARY AND REGISTERED ADDRESSES

The Directors of the Company during the 14-month period were as follows:

Name	Date of appointment	Date of resignation
SL Botha*	29 November 2019	
JD McKenzie*	29 November 2019	
JP Verster*	29 November 2019	
GM Fourie#	29 November 2019	
AP du Plessis#	29 November 2019	
K Makwane*	5 February 2020	
CA Otto*	5 February 2020	
PJ Mouton*	5 February 2020	
DP Meintjes*	5 February 2020	
MS d P le Roux*	14 February 2020	
NS Mashiya#	14 February 2020	
KR Kumbier# *(CEO)*	1 June 2010	
MEL Teixeira# *(Financial Director)*	15 June 2018	
GP de Kock°	23 November 2000	5 February 2020
RS Caliço@*	1 July 2014	7 November 2019
L Hyne°	1 June 2003	29 November 2019
AT Ikalafeng°	16 November 2004	29 November 2019
TH Njikizana°^	6 November 2008	5 February 2020
DR Motsepe°	1 October 2014	29 November 2019

*@Portuguese ^Zimbabwean *Non-Executive #Executive*
°Independent Non-Executive

T Singh is the Company Secretary.

The registered addresses of the Company are:

Postal

PO Box 782699, Sandton 2146.

Physical

1st Floor, Mercantile Bank, 142 West Street, Sandown 2196.

DIVIDENDS

No dividend was declared in respect of the 14-month period ended 29 February 2020 (December 2018: R49.886 million, paid in 2019).

SPECIAL RESOLUTIONS

Two special resolutions were adopted during the reporting period. The first was at the 2019 Annual General Meeting held on 29 April 2019 to approve the fees and remuneration respectively payable to Non-Executive Directors and Executive Directors. A further special resolution was passed on 11 November 2019 to enable the Company to provide financial assistance to employees for the subscription of securities within the Group.

EVENTS AFTER THE REPORTING PERIOD

Details of events after the reporting period may be found in note 33 to the financial statements.

ACCOUNTING POLICIES

for the 14-month period ended 29 February 2020

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

1. BASIS OF PRESENTATION

The Company's financial statements are prepared in accordance with IFRS adopted by the International Accounting Standards Board, the South African Institute of Chartered Accountants' Financial Reporting Guides as issued by the Accounting Practices Committee, Financial Reporting Pronouncements as issued by the Financial Reporting Standards Council and the Companies Act.

The Company changed the end of its reporting period from 31 December to the last day of February. Amounts presented for the 2020 reporting period are for a 14-month period. Comparative figures are for a 12-month period. Consequently, comparative amounts for the statement of comprehensive income, statement of changes in equity, statement of cash flows and related notes are not entirely comparable.

In the current period, the Company has applied the below mandatory amendments to IFRS issued by the International Accounting Standards Board that are effective for an accounting period that begins on or after 1 January 2019.

With the exception of IFRS 16, all other IFRS that became effective in the current reporting period have had no material impact on the Company.

2. RECOGNITION OF ASSETS AND LIABILITIES

2.1 ASSETS

The Company recognises an asset 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 a liability 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

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

2.4 CONTINGENT LIABILITIES

A contingent liability is disclosed where the Company 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 an obligation in terms of which it is merely possible that an outflow of resources will be required to settle the obligation, or the amount of an obligation cannot be measured with sufficient reliability.

3. FINANCIAL INSTRUMENTS

A financial asset or financial liability is recognised in the Company's statement of financial position when the Company has become a party to the contractual provisions of that financial instrument. Regular purchases or sales of financial assets are recognised using settlement date accounting. On initial recognition, financial instruments are recognised at fair value and, in the case of a financial instrument not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial instruments are included.

3.1 DERIVATIVE FINANCIAL INSTRUMENTS

The Company uses the following derivative financial instruments to service client needs, and to reduce its underlying financial risks and/or to enhance returns:

- Forward exchange contracts;
- Foreign currency swaps; and
- Unlisted equity instruments.

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

A derivative's notional principal amount 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

Business model assessment

We determine our business models at the level that best reflects how we manage portfolios of financial assets to achieve our business objectives. Judgement is used in determining our business models, which is supported by relevant, objective evidence including:

- How the economic activities of our businesses generate benefits, for example, through trading revenue, enhancing yields or hedging funding or other costs, and how such economic activities are evaluated and reported to key management personnel; and
- The significant risks affecting the performance of our businesses, for example, market risk, credit risk or other risks as described in the Risk management section, and the activities undertaken to manage those risks.

Our business models fall into two categories, which are indicative of the key strategies used to generate returns:

- Held-to-collect contractual cash flows: the objective of this business model is to hold loans and securities to collect contractual principal and interest cash flows. Sales are incidental to this objective and are expected to be insignificant or infrequent.
- Other fair value business models: these business models are not held-to-collect and primarily represent business models where assets are held-for-trading or managed on a fair value basis.

Solely payments of principal and interest assessment

Instruments held within a held-to-collect contractual cash flows business model are assessed to evaluate if their contractual cash flows are comprised of solely payments of principal and interest. Solely payments of principal and interest assessment payments are those which would typically be expected from basic lending arrangements. Principal amounts include par repayments from lending and financing arrangements and interest primarily relates to basic lending returns, including compensation for credit risk and the time value of money associated with the principal amount outstanding over a period of time. Interest can also include other basic lending risks and costs (for example, liquidity risk, servicing or administrative costs) associated with holding the financial asset for a period of time and a profit margin.

Where the contractual terms introduce exposure to risk or variability of cash flows that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

Financial assets at amortised cost

The Company has classified loans, trade receivables, negotiable securities and cash at banks as financial assets at amortised cost. Amortised cost is determined using the effective interest rate method. The effective interest rate is the rate that discounts expected 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. When calculating the effective interest rate, the Company estimates cash flows considering all contractual terms of the financial instrument.

Financial assets at fair value through profit or loss

A financial asset shall be measured at fair value through profit or loss unless it is measured at amortised cost or at fair value through other comprehensive income. Financial assets are measured at fair value through profit or loss primarily to eliminate or significantly reduce an accounting mismatch. The Company seeks to demonstrate that, by applying the fair value option which measures fair value gains and losses in profit or loss, it significantly reduces measurement inconsistency that would otherwise arise from measuring such designated financial assets at amortised cost.

Financial assets at fair value through other comprehensive income

Financial assets that are held for collection of contractual cash flows, where the assets' cash flows solely represent payments of principal and interest, and that are not designated at amortised cost or at fair value through profit or loss, are measured at fair value through other comprehensive income. The Company may make an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at fair value through profit or loss to present subsequent changes in fair value in other comprehensive income.

Movements in the carrying amount are taken through other comprehensive income, except for impairment gains or losses, interest revenue, foreign exchange gains and losses on the instruments, and amortised cost, which are recognised in profit or loss.

When the financial asset is derecognised, the cumulative gain or loss previously recognised in other comprehensive income may subsequently be reclassified within equity. Interest income on these financial assets is measured using the effective interest rate method. The Company has classified other investments as financial assets at fair value through other comprehensive income.

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.

Negotiable securities

Negotiable securities consist of government stock and treasury bills. These financial assets have been designated as loans and receivables and are measured at amortised cost subject to impairment.

Loans and advances

Loans and advances principally comprise amounts advanced to third parties in terms of certain products; namely current accounts, mortgage loans, credit card facilities, instalment sales and leases, structured loans and term loans. These financial assets are measured at amortised cost subject to impairment.

Investment in debt securities

Investment in debt securities consists of investments in promissory notes and are measured at fair value through profit or loss.

Other accounts receivable

Other accounts receivable comprises items in transit, structured loans, accrued income, prepayments, and deposits that meet the definition of financial assets and other receivables. These assets have been designated as loans and receivables and are measured at amortised cost.

Other investments

Other investments consist of unlisted equity investments. 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 otherwise disposed of. At that time, the cumulative gains or losses previously recognised in other comprehensive income may subsequently be reclassified within equity.

3.3 FINANCIAL LIABILITIES

The Company's financial liabilities include deposits, long-term funding, debt securities, and other accounts payable consisting of accruals, product-related credits and sundry creditors. These financial liabilities are measured at amortised cost. Derivative instruments are measured at fair value through profit or loss. The resultant gains and losses are included in profit or loss.

3.4 FAIR VALUE ESTIMATION

The fair value of publicly traded derivatives, securities and investments is based on quoted market prices at the reporting date. In the case of an asset held by the Company, the exit 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-publicly traded financial instruments, the Company uses a variety of valuation methods that take into consideration input assumptions, which are based, as far as possible, on objective market information and risks existing at each reporting date. Quoted market prices, or dealer quotes for the same or similar instruments, are used for selected securities, long-term investments and long-term debt. Other valuation techniques, such as earnings multiples, option pricing models, discounted cash flows, replacement cost, and net asset values of underlying investee entities, are used to determine fair values.

3.5 AMORTISED COST

Amortised cost is determined using the effective interest rate 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, less ECL.

3.6 IMPAIRMENT

Key principles of the accounting policy for impairment of financial assets are listed below:

- The Company assesses whether a financial asset has significantly increased credit risk since initial recognition to determine whether to use a 12-month expected loss approach or a lifetime expected loss approach to calculate its impairment provision.
- At each reporting date, the Company assesses whether there has been a SICR for financial assets since initial recognition, by comparing the credit risk of default occurring over the expected life between the reporting date and the date of initial recognition. In determining whether credit risk has increased significantly since initial recognition, the Company uses its internal credit risk grading system, external risk ratings, and expert judgement forecast information to assess deterioration in the credit quality of a financial asset.
- The Company assesses whether the credit risk on a financial asset has increased significantly on an individual or collective basis. For the purposes of a collective evaluation of impairment, financial assets are grouped based on shared credit risk characteristics, taking into account instrument type, credit risk ratings, date of initial recognition, remaining term to maturity, industry, geographical location of the borrower and other relevant factors. Assets migrate through the following three credit stages, based on the change in credit quality since initial recognition:
  - **Stage 1:** 12–month ECL

    Includes financial assets that have not had a SICR since initial recognition or that have low credit risk at the reporting date. ECL are calculated and recognised based on their probability of default over 12 months. Interest is recognised on the full amount due.
  - **Stage 2:** Lifetime ECL – not credit impaired

    Includes financial assets that have had a SICR since initial recognition, unless they have low credit risk at the reporting date, but that do not have objective evidence of impairment. ECL are calculated and recognised based on their lifetime probability of default. Interest is recognised on the full amount due.
  - **Stage 3:** Lifetime ECL – credit impaired

    Includes financial assets that have objective evidence of impairment at the reporting date. ECL are calculated and recognised based on their lifetime probability of default. Interest is only recognised insofar as it is expected to be recovered i.e. on the net carrying value (value of the exposure less calculated ECL).

The amount of ECL is measured as the probability-weighted present value of all cash shortfalls over the expected life of the financial asset discounted at its original effective interest rate. The Company considers its historical loss experience and adjusts this for current observable data. In addition, the Company uses reasonable and supportable expert judgement on future economic conditions, including estimating the amount of an ECL.

3.7 MODIFICATION

The Company sometimes renegotiates or otherwise modifies the contractual cash flows of loans to clients. When this happens, the Company assesses whether or not the new terms are substantially different to the original terms. If the terms are substantially different, the Company derecognises the original financial asset and recognises a ‘new’ asset at fair value and recalculates the effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a SICR has occurred. However, the Company also assesses whether the new financial asset recognised is deemed to be credit impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition and the Company recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate (or a credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets).

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such exchange or modification is treated as a derecognition of the original liability and recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in profit or loss.

3.8 DERECOGNITION

A financial instrument, or a portion of a financial instrument, will be derecognised and a gain or loss recognised when the Company's contractual rights expire, financial assets are transferred or financial liabilities are extinguished. On derecognition of a financial asset or liability, the difference between the consideration and the carrying amount on the settlement date, is included in finance charges and fair value movements for the period. On derecognition of equity instruments designated at fair value through other comprehensive income, the cumulative fair value gains/(losses) recognised in other comprehensive income are not subsequently recycled to profit or loss.

4. FOREIGN CURRENCY TRANSACTIONS

Transactions in foreign currencies are converted to the functional currency at the prevailing exchange rate on the transaction date. Monetary assets, liabilities and commitments in foreign currencies are translated to the functional currency using the rate of exchange at the reporting date. Gains and losses on foreign exchange are recognised in profit or loss.

5. SUBSIDIARIES

Investments in subsidiaries are measured at cost. Investments in subsidiaries are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

6. 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 expected costs to sell.

7. PROPERTY AND EQUIPMENT

All equipment is stated at historical cost, less any subsequent accumulated depreciation and impairment. 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 or loss as incurred.

Depreciation on equipment is calculated using the straight-line method. Leasehold improvements are depreciated over the period of the lease, or over such lesser period, as is considered appropriate.

The residual values and useful lives of equipment are reviewed and adjusted, if appropriate, at each reporting date.

Depreciation of an asset begins when it is available for use and ceases at the earlier of the dates that the asset is classified as held-for-sale or derecognised. The estimated useful lives of 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

Gains and losses on the disposal of property and equipment are recognised in profit or loss and are determined by deducting from the proceeds the net carrying amounts.

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The carrying amount is written down 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.

8. INTANGIBLE ASSETS

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

Computer software and licences, that are recognised as intangible assets, are amortised on a straight-line basis over a period of three to five years but, where appropriate, to a maximum of 10 years. These intangible assets are carried at historical cost less accumulated amortisation and/or impairment.

An intangible asset is derecognised on disposal, or when future economic benefits are no longer expected from its use or disposal. Gains and losses on the disposal of intangible assets are determined by deducting from the proceeds the net carrying amounts and are recognised in profit or loss.

At the end of each reporting period, the Company reviews the carrying amounts of intangible assets to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount of the asset is estimated to determine the extent of the impairment.

Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The carrying amount is written down 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.

9. TAX

Income tax expense represents the sum of current and deferred tax.

9.1 CURRENT TAX

Current tax is determined based on taxable profits for the period. Taxable profit may differ from accounting profit as it may exclude or include items of income or expense that are taxable or deductible in other periods, and it would further exclude 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.

9.2 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 of such items, and is determined 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 sufficient taxable temporary differences or taxable profits will be available against which those deductible temporary differences may be used. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from initial recognition of goodwill or from 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 timing of 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 use 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 it will be used.

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

9.3 CURRENT AND DEFERRED TAX

Current and deferred tax are recognised in profit or loss, except when they relate to items recognised in other comprehensive income or directly in equity, in which case the tax is recognised in the same statements as the related item.

10. INSTALMENT SALES AND LEASES

10.1 THE COMPANY AS THE LESSEE

Prior to 1 January 2019, the leases entered into by the Company were primarily operating leases classified under IAS 17. The total payments made under operating leases are recognised in profit or loss on a straight-line basis over the term 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 a penalty is recognised as an expense in the period in which termination takes place.

10.2 THE COMPANY AS THE LESSOR

Leases and instalment sale agreements are regarded as financing transactions with rentals and instalments receivable, less unearned finance charges 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.

11. RIGHT-OF-USE ASSET AND LEASE LIABILITY

As at 1 January 2019, the Company recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost (which is equal to the lease liability adjusted for previously recognised prepaid or accrued lease payments relating to that lease) and increased by initial direct cost incurred, and the amount of any provision recognised where the Company is contractually required to dismantle, remove or restore the leased asset. The Company applies the cost model subsequent to the initial measurement of right-of-use assets. The right-of-use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

The estimated useful lives of right-of-use assets are determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The lease liability is initially measured at the present value of the remaining lease payments on the commencement date, discounted using the interest rate implicit in the lease, if that rate can be readily determined. If that rate cannot be determined, the lessee uses the lessee's incremental borrowing rate. The incremental borrowing rate will be used on a portfolio basis, as a specific rate for a single lease asset does not materially differ from the rate obtained on a portfolio basis. The rate is based on the average yield on deposits at the date of inception. Inputs considered include the risk-free rate, three-month JIBAR and Bank-specific considerations. The lease liability is subsequently increased by interest cost on the lease liability and decreased by lease payments made.

Lease payments included in the measurement of the lease liability comprise the following: fixed payments; variable lease payments that depend on an index or a rate; amounts payable under a residual value guarantee; and the exercise price under a purchase option that the Company is certain to exercise.

In addition, the Company applied the following exemptions on transition that are permitted under the standard:

- The exemption to not recognise right-of-use assets and liabilities for leases with a remaining lease term of less than 12 months;
- Accounted for all low value assets on a straight-line basis over the lease term;
- Relied on previous assessments on whether leases are onerous as an alternative to performing an impairment review. There were no material onerous leases on 1 January 2019;
- Used a single discount rate for a portfolio of leases with reasonably similar characteristics;
- Excluded initial direct costs for the measurement of the right-of-use asset at the date of initial application;
- Applied the practical expedient to apply IFRS 16 only to contracts that were previously identified as leases. Therefore, the definition of a lease under IFRS 16 has been applied only to contracts entered into or changed on or after 1 January 2019; and
- Used hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

12. INTEREST INCOME AND INTEREST EXPENSE

Interest income and expense for all financial instruments, except those measured or designated at fair value through profit or loss, are recognised as interest income and interest expense in profit or loss using the effective interest method. Interest on financial instruments measured at fair value through profit or loss is included within the fair value movement during the period.

The effective interest rate is the rate that exactly discounts estimated future cash flows of the financial instrument through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. The future cash flows are estimated taking into account all the contractual terms of the instrument.

For financial assets at fair value through profit or loss, transaction costs are recognised in profit or loss at initial recognition.

The interest income or interest expense is calculated by applying the effective interest rate to the gross carrying amount of non-credit-impaired financial assets (i.e. at the amortised cost of the financial asset before adjusting for any ECL allowance) or to the amortised cost of financial liabilities.

For credit-impaired financial assets, the interest income is calculated by applying the effective interest rate to the amortised cost of the credit-impaired financial assets (i.e. the gross carrying amount less the allowance for ECL). For financial assets originated or purchased credit impaired, the effective interest rate reflects the ECL in determining the future cash flows expected to be received from the financial asset.

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 a defined contribution fund that is 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 or 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 current service cost of providing post-retirement medical benefits is recognised in profit or loss. The interest cost and the effect of settlements on the liability, are recognised in profit or loss and any remeasurement of the defined benefit liability (which include actuarial gains and losses) is recognised in other comprehensive income. The post-retirement liability recognised in the statement of financial position reflects the full value of the plan deficit.

16. KEY ASSUMPTIONS AND ESTIMATES APPLIED BY MANAGEMENT

The Company makes assumptions and estimates that affect the reported amounts of assets and liabilities. Assumptions and estimates 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 ECL ON LOANS AND ADVANCES

The extent of the ECL allowance for financial assets measured at amortised cost is calculated using complex models and significant assumptions about future economic conditions and credit behaviour.

Further significant judgements are necessary in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for SICR:

  ECL is measured as an allowance equal to a 12-month ECL for Stage 1 assets or a lifetime ECL for Stage 2 or Stage 3 assets. An asset moves to Stage 2 when its credit risk has increased significantly since initial recognition, and to Stage 3 when it becomes non-performing, which includes accounts in business rescue, debt review, liquidation and sequestration;
- Choosing appropriate models and assumptions for the measurement of ECL:

  Judgement is applied in identifying the most appropriate model for each type of asset, as well as for determining the assumptions used in these models, including assumptions that relate to key drivers of credit risk; and
- Establishing the number and relative weightings of forward-looking scenarios.

Currently, the Company does not make use of specific macro-economic forward-looking scenarios due to the lack of adequate correlation in the performance of its loans and advances relative to macro-economic indicators or an index of these indicators. A management overlay is applied for specific types of exposures based on expert collaborative opinions and assessments.

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 the extent practical, models use only observable data. Management is, however, required to make estimates in areas such as credit risk, volatilities and correlations. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

16.3 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.

17. RECENT ACCOUNTING DEVELOPMENTS

There are a number of new and revised standards in issue that are not yet effective, and that the Company has no plans to early adopt. The following standards could be applicable to the business of the Company and might have an impact on future financial statements. The impact of initial application of the following standards and interpretations is not expected to be significant to the Company:

Standard	Standard title and detail	Effective date
Conceptual Framework	The Conceptual Framework for Financial Reporting	Annual periods beginning on or after 1 January 2020
IAS 1	**Presentation of Financial Statements** Classification of liabilities as current or non-current Narrow-scope amendments to clarify how to classify debt and other liabilities as current or non-current	Annual periods beginning on or after 1 January 2022
IAS 1	**Presentation of Financial Statements** Definition of material	Annual periods beginning on or after 1 January 2020
IAS 8	**Accounting Policies, Changes in Accounting Estimates and Erros** Amendments regarding the definition of material	Annual periods beginning on or after 1 January 2020
IAS 28	**Investments in Associates and Joint Ventures** Amendments regarding the sale of contribution of assets between an investor and its associate or joint venture	Deferred indefinitely
IFRS 10	**Consolidated Financial Statements** Amendments regarding the sale or contribution of assets between an investor and its associate or joint venture	Deferred indefinitely

STATEMENT OF FINANCIAL POSITION

as at 29 February 2020

	Note	2020 R'000	2018 R'000
ASSETS			
Cash and cash equivalents	3	**4 124 242**	3 123 604
Derivative financial instruments	4	**31 727**	17 903
Negotiable securities	5	**877 383**	790 810
Loans and advances	6	**9 260 444**	9 322 697
Other investments	7	**1 139**	8 016
Other accounts receivable	8	**406 650**	492 078
Non-current assets held-for-sale	9	**17 169**	22 500
Interest in subsidiaries	10	**172 755**	109 271
Investment in debt securities	11	**155 761**	151 629
Property and equipment	12	**34 427**	47 847
Right-of-use asset	13	**54 084**	–
Intangible assets	14	**82 936**	128 394
Deferred tax assets	15	**49 347**	42 961
Current tax receivable	16	**4 672**	–
Total assets		**15 272 736**	14 257 710
LIABILITIES AND EQUITY			
Liabilities		**12 663 919**	11 810 836
Other accounts payable	17	**344 076**	419 125
Current tax payable	16	**–**	5 726
Provisions and other liabilities	18	**73 502**	136 381
Derivative financial instruments	4	**30 005**	15 437
Lease liability	13	**58 515**	–
Deposits	20	**12 157 821**	10 491 287
Long-term funding	21	**–**	742 880
Shareholder's equity		**2 608 817**	2 446 874
Share capital and share premium	22	**1 483 300**	1 483 300
Employee benefits reserve		**(5 224)**	(5 632)
Other reserves		**422**	5 758
Retained earnings		**1 130 319**	963 448
Total liabilities and equity		**15 272 736**	14 257 710

STATEMENT OF COMPREHENSIVE INCOME

for the 14-month period ended 29 February 2020

	Note	2020 R'000	2018 R'000
Interest income	24	**1 499 307**	1 167 202
Interest expense	25	**(820 423)**	(615 799)
Net interest income		**678 884**	551 403
Net charge for credit losses	6.4	**(155 057)**	(21 765)
Net interest income after credit losses		**523 827**	529 638
Net non-interest income		**447 527**	355 605
Non-interest income	26	**1 082 790**	769 914
Fee and commission expenditure	27	**(635 263)**	(414 309)
Other trading-related expenditure	28	**(37 333)**	–
Operating income		**934 021**	885 243
Operating expenditure	29	**(633 836)**	(554 533)
Profit before tax		**300 185**	330 710
Tax	30	**(83 428)**	(92 432)
Profit after tax		**216 757**	238 278
Other comprehensive income			
Items that will not be reclassified to profit or loss:			
Remeasurement to fair value of other investments		**(6 877)**	672
Remeasurement of defined benefit obligation	19	**567**	815
Deferred tax thereon	15	**1 382**	(380)
Other comprehensive income net of tax		**(4 928)**	1 107
Total comprehensive income		**211 829**	239 385
Profit after tax attributable to equity holder of the Company		**216 757**	238 278
Total comprehensive income attributable to equity holder of the Company		**211 829**	239 385

STATEMENT OF CHANGES IN EQUITY

for the 14-month period ended 29 February 2020

	Share capital R'000	Share premium R'000	Employee benefits reserve R'000	Other reserves R'000	Retained earnings R'000	Total R'000
Balance as at 1 January 2018	124 969	1 358 331	(6 218)	5 237	767 628	2 249 947
Net movement for the year	–	–	586	521	195 820	196 927
Total comprehensive income for the year	–	–	586	521	238 278	239 385
Profit after tax	–	–	–	–	238 278	238 278
Other comprehensive income	–	–	815	672	–	1 487
Tax relating to other comprehensive income	–	–	(229)	(151)	–	(380)
Dividend paid	–	–	–	–	(42 458)	(42 458)
Balance as at 31 December 2018	**124 969**	**1 358 331**	**(5 632)**	**5 758**	**963 448**	**2 446 874**
Net movement for the period	**–**	**–**	**408**	**(5 336)**	**166 871**	**161 943**
Total comprehensive income for the period	**–**	**–**	**408**	**(5 336)**	**216 757**	**211 829**
Profit after tax	**–**	**–**	**–**	**–**	**216 757**	**216 757**
Other comprehensive income	**–**	**–**	**567**	**(6 877)**	**–**	**(6 310)**
Tax relating to other comprehensive income	**–**	**–**	**(159)**	**1 541**	**–**	**1 382**
Dividend paid	**–**	**–**	**–**	**–**	**(49 886)**	**(49 886)**
Balance as at 29 February 2020	**124 969**	**1 358 331**	**(5 224)**	**422**	**1 130 319**	**2 608 817**

STATEMENT OF CASH FLOWS

for the 14-month period ended 29 February 2020

	Note	2020 R'000	2018 R'000
Cash flows from operating activities			
Cash receipts from clients	31.1	**2 585 059**	1 910 864
Cash paid to clients, suppliers and employees	31.2	**(2 052 995)**	(1 495 290)
Cash generated from operations	31.3	**532 064**	415 574
Tax (paid)	31.4	**(98 830)**	(109 300)
Net (increase) in income-earning assets	31.5	**(181 595)**	(212 086)
Net increase in deposits and other accounts	31.6	**1 672 631**	1 241 664
Net cash inflow from operating activities		**1 924 270**	1 335 852
Cash flows from investing activities			
Purchase of intangible assets	14	**(21 740)**	(28 601)
Purchase of property and equipment	12	**(8 158)**	(14 873)
Proceeds on disposal of property and equipment		**18**	9
Dividends paid		**(49 886)**	(42 458)
Investment in debt securities	11	**–**	(47 409)
(Increase) in interest in subsidiaries		**(63 484)**	(69 028)
Net cash (outflow) from investing activities		**(143 250)**	(202 360)
Cash flows from financing activities			
Net (decrease)/increase in long-term funding	21	**(742 880)**	279 827
Proceeds from long-term borrowings		**–**	740 010
Repayment of long-term borrowings		**(742 880)**	(459 477)
(Gain) on exchange rate movements		**–**	(706)
Payment of lease liability		**(37 502)**	–
Net cash (outflow)/inflow from financing activities		**(780 382)**	279 827
Net cash inflow for the period		**1 000 638**	1 413 319
Cash and cash equivalents at the beginning of the period		**3 123 604**	1 710 285
Cash and cash equivalents at the end of the period	3	**4 124 242**	3 123 604

NOTES TO THE FINANCIAL STATEMENTS

for the 14-month period ended 29 February 2020

1. CHANGE IN ACCOUNTING POLICY

The Company has adopted IFRS 16 as issued by the International Accounting Standards Board with a transition date of 1 January 2019, which resulted in changes in accounting policies applied in preparing the financial statements. The Company did not early adopt any parts of IFRS 16 in previous years.

The core principle of this standard is that the lessee and the lessor should recognise all rights and obligations arising from leasing arrangements on the balance sheet. The reclassifications and adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 January 2019. In terms of this approach, comparative information is not restated and the right-of-use asset at the date of initial application for leases previously classified as operating leases (IAS 17) is equal to the lease liability, adjusted for previously recognised prepaid or accrued lease payments relating to the leases. The weighted average incremental borrowing rate applied to lease liabilities recognised in the statement of financial position as at 1 January 2019 is 5.7%.

Effect on the statement of financial position	R'000
ASSETS	91 025
Reconciled as follows:	
Recognition of right-of-use asset	91 025
Opening balance in terms of IFRS 16 on 1 January 2019	91 025
LIABILITIES	(91 025)
Reconciled as follows:	
Recognition of lease liability	(91 025)
Opening balance in terms of IFRS 16 on 1 January 2019	(91 025)

2. CATEGORIES AND FAIR VALUES OF FINANCIAL INSTRUMENTS

2.1 CATEGORY ANALYSIS OF FINANCIAL INSTRUMENTS

	2020		2018		
	Fair value R'000	Carrying amount R'000	Fair value R'000	Carrying amount R'000	Hierarchy of valuation technique
ASSETS					
Amortised cost	**14 669 976**	**14 668 719**	13 727 782	13 729 201	
Loans and advances					
Current accounts	**2 082 927**	**2 082 927**	2 187 905	2 187 905	Level 3
Credit cards	**45 592**	**45 592**	41 800	41 800	Level 3
Mortgage loans	**5 328 926**	**5 328 926**	4 952 970	4 952 970	Level 3
Instalment sales and leases	**681 682**	**681 682**	901 854	901 854	Level 3
Structured loans	**37 792**	**37 792**	134 126	134 126	Level 3
Medium-term loans	**1 083 525**	**1 083 525**	1 104 042	1 104 042	Level 3
Negotiable securities					
Government stock	**–**	**–**	25 292	25 800	Level 2
Treasury bills	**878 640**	**877 383**	764 111	765 022	Level 2
Cash and cash equivalents	**4 124 242**	**4 124 242**	3 123 604	3 123 604	*
Other accounts receivable	**406 650**	**406 650**	492 078	492 078	*
Fair value through profit or loss	**187 488**	**187 488**	169 532	169 532	
Derivative financial instruments	**31 727**	**31 727**	17 903	17 903	Level 2
Investment in debt securities	**155 761**	**155 761**	151 629	151 629	Level 3
Fair value through other comprehensive income					
Other investments	**1 139**	**1 139**	8 016	8 016	Level 3
	14 858 603	**14 857 346**	13 905 330	13 906 749	
LIABILITIES					
Fair value through profit or loss					
Derivative financial instruments	**30 005**	**30 005**	15 437	15 437	Level 2
Amortised cost	**12 501 897**	**12 501 897**	11 653 292	11 653 292	
Long-term funding	**–**	**–**	742 880	742 880	Level 3
Deposits	**12 157 821**	**12 157 821**	10 491 287	10 491 287	Level 3
Other accounts payable	**344 076**	**344 076**	419 125	419 125	*
	12 531 902	**12 531 902**	11 668 729	11 668 729	

** The fair value of these assets closely approximates their carrying amount due to the short-term or on-demand repayment terms.*

2. CATEGORIES AND FAIR VALUES OF FINANCIAL INSTRUMENTS continued

2.2 VALUATION TECHNIQUES AND ASSUMPTIONS APPLIED FOR THE PURPOSE OF MEASURING FAIR VALUE

- Cash and cash equivalents have short terms to maturity and are carried at amortised cost. For this reason, the carrying amounts at the reporting date approximate the fair value.
- Treasury bills are carried at amortised cost. Fair value is determined using average yields 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 and thus the values reported approximate the fair value.
- The fair value of derivatives and securities is determined using observable Reuters forward points at the reporting date.
- The fair value of other financial assets and financial liabilities, excluding derivatives, is determined in accordance with generally accepted pricing models, based on discounted cash flow analysis, using prices from observable current market transactions and adjusted by relevant market pricing.
- The fair value of other investments that 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.
- Investment in debt securities is carried at fair value through profit or loss. Fair value is based on contractual cash flows which bear variable rates of interest adjusted for increased credit risk.

2.3 FAIR VALUE MEASUREMENTS AS REQUIRED BY IFRS 13

Financial instruments that are measured at fair value subsequent to initial recognition 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).

2.4 RECONCILIATION OF LEVEL 3 FAIR VALUE MEASUREMENTS OF FINANCIAL ASSETS

	2020 R'000	2018 R'000
Fair value through other comprehensive income		
Other investments – unlisted equities		
Balance at the beginning of the period	**8 016**	6 923
Additions	**–**	421
(Losses)/Gains on remeasurement to fair value in other comprehensive income	**(6 877)**	672
Balance at the end of the period	**1 139**	8 016
Fair value through profit or loss		
Investment in debt securities		
Balance at the beginning of the period	**151 220**	104 220
Additions	**–**	47 000
Interest accrued	**4 541**	409
Balance at the end of the period	**155 761**	151 220

3. CASH AND CASH EQUIVALENTS

	2020 R'000	2018 R'000
Cash on hand	**24 806**	29 981
Mandatory balances with the Central Bank	**246 581**	309 252
Money market funds	**–**	1 565 038
Rand-denominated domestic bank balances	**2 801 569**	414 047
Foreign currency-denominated bank balances	**1 051 447**	805 411
Less: ECL on performing cash and cash equivalents (Stage 1)	**(161)**	(125)
	4 124 242	3 123 604

4. DERIVATIVE FINANCIAL INSTRUMENTS

	Notional principal of assets R'000	Fair value of assets R'000	Notional principal of liabilities R'000	Fair value of liabilities R'000
2020				
Mandatorily measured at fair value through profit or loss				
Forward exchange contracts	**167 394**	**7 689**	**575 722**	**30 005**
Foreign currency swap contracts	**365 434**	**24 038**	**–**	**–**
	532 828	**31 727**	**575 722**	**30 005**
2018				
Mandatorily measured at fair value through profit or loss				
Forward exchange contracts	343 030	6 097	554 064	14 049
Foreign currency swap contracts*	429 071	11 806	129 679	1 388
	772 101	17 903	683 744	15 437

	2020 R'000	2018 R'000
Maximum exposure to credit risk*	**31 727**	17 903
Cash collateral held as security*	**38 040**	47 958

** Additional disclosure in respect of the prior year has been included.*

5. NEGOTIABLE SECURITIES

	2020 R'000	2018 R'000
Amortised cost		
Treasury bills	**877 407**	765 022
Government stock	**–**	25 800
Less: ECL on performing negotiable securities (Stage 1)	**(24)**	(12)
	877 383	790 810
Maturity analysis		
Maturing within one month	**89 925**	149 668
Maturing after one month but within six months	**323 358**	587 053
Maturing after six months but within 12 months	**464 100**	28 300
Maturing after one year but within five years	**–**	25 789
	877 383	790 810

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

6. LOANS AND ADVANCES

6.1 PRODUCT ANALYSIS

	2020 R'000	2018 R'000
Amortised cost		
Current accounts	**2 129 084**	2 236 794
Credit cards	**49 184**	44 022
Mortgage loans	**5 406 641**	4 991 393
Instalment sales and leases	**692 710**	913 193
Structured loans	**37 792**	134 126
Medium-term loans	**1 192 167**	1 179 997
Gross loans and advances	**9 507 578**	9 499 525
Less: ECL on performing loans and advances (Stage 1)	**(62 871)**	(67 660)
ECL on underperforming loans and advances (Stage 2)	**(38 436)**	(19 713)
ECL on non-performing loans and advances (Stage 3)	**(145 827)**	(89 455)
Net loans and advances	**9 260 444**	9 322 697

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

6.2 MATURITY ANALYSIS

	2020 R'000	2018 R'000
Repayable on demand and maturing within one month	**2 113 210**	2 296 598
Maturing after one month but within six months	**120 294**	147 351
Maturing after six months but within 12 months	**75 272**	78 575
Maturing after 12 months	**7 198 802**	6 977 001
	9 507 578	9 499 525

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

6.3 DETAILED PRODUCT ANALYSIS OF LOANS AND ADVANCES

	Gross amount R'000	ECL Stage 1 R'000	ECL Stage 2 R'000	ECL Stage 3 R'000	Net balance R'000
2020					
Current accounts	**2 129 084**	**(19 565)**	**(8 854)**	**(22 434)**	**2 078 231**
Credit cards	**49 184**	**(455)**	**(18)**	**(3 119)**	**45 592**
Mortgage loans	**5 406 641**	**(7 867)**	**(15 779)**	**(61 489)**	**5 321 506**
Instalment sales and leases	**692 710**	**(1 534)**	**(3 018)**	**(8 500)**	**679 658**
Structured loans	**37 792**	**–**	**–**	**–**	**37 792**
Medium-term loans	**1 192 167**	**(33 450)**	**(10 767)**	**(50 285)**	**1 097 665**
	9 507 578	**(62 871)**	**(38 436)**	**(145 827)**	**9 260 444**
2018					
Current accounts	2 236 794	(29 274)	(2 567)	(17 048)	2 187 905
Credit cards	44 022	(391)	(56)	(1 775)	41 800
Mortgage loans	4 991 393	(6 198)	(5 788)	(26 437)	4 952 970
Instalment sales and leases	913 193	(3 371)	(2 107)	(5 861)	901 854
Structured loans	134 126	–	–	–	134 126
Medium-term loans	1 179 997	(28 426)	(9 195)	(38 334)	1 104 042
	9 499 525	(67 660)	(19 713)	(89 455)	9 322 697

6. LOANS AND ADVANCES continued

6.3 DETAILED PRODUCT ANALYSIS OF LOANS AND ADVANCES continued

6.3.1 Off-balance sheet ECL included in product analysis

	ECL			
	Stage 1 R'000	Stage 2 R'000	Stage 3 R'000	Total R'000
2020				
Current accounts	**6 557**	**123**	**69**	**6 749**
Credit cards	**104**	**–**	**8**	**112**
Mortgage loans	**1 095**	**21**	**126**	**1 242**
Instalment sales and leases	**14**	**–**	**–**	**14**
Structured loans	**–**	**–**	**–**	**–**
Medium-term loans	**224**	**–**	**–**	**224**
	7 994	**144**	**203**	**8 341**
2018				
Current accounts	9 656	117	189	9 962
Credit cards	94	1	120	215
Mortgage loans	2 021	–	36	2 057
Instalment sales and leases	67	–	–	67
Structured loans	–	–	–	–
Medium-term loans	1 784	65	12	1 861
	13 622	183	357	14 162

Refer to note 23.1 for gross contingent liabilities and commitments to which these ECLs relate.

6.3.2 Detailed analysis of leases (rental assets) included in instalment sales and leases

	2020 R'000	2018 R'000
Gross investment in lease receivables		
Less than one year	**–**	74 223
One to five years	**–**	129 937
More than five years	**–**	–
Gross investment in lease receivables	**–**	204 160
Unearned finance income	**–**	(40 220)
Net investment in lease receivables	**–**	163 940
Net lease receivable		
Less than one year	**–**	60 473
One to five years	**–**	103 467
More than five years	**–**	–
Net investment in lease receivables	**–**	163 940
Less: ECL	**–**	(4 389)
Net lease receivable	**–**	159 551

During 2020, the Bank disposed of its rental asset loan book to Mercantile Rental Finance Proprietary Limited.

6. LOANS AND ADVANCES continued

6.4 ECL BY PRODUCT

	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
2020							
Balance at the beginning of the period	**(176 827)**	**(48 889)**	**(2 222)**	**(38 422)**	**(11 339)**	**–**	**(75 955)**
Movements for the period							
Credit losses written off*	**98 933**	**42 830**	**652**	**13 759**	**10 067**	**–**	**31 625**
Net impairments (raised)	**(169 240)**	**(44 794)**	**(2 022)**	**(60 472)**	**(11 780)**	**–**	**(50 172)**
Balance at the end of the period	**(247 134)**	**(50 853)**	**(3 592)**	**(85 135)**	**(13 052)**	**–**	**(94 502)**
2018							
Balance at the beginning of the year	(253 548)	(87 029)	(2 045)	(67 874)	(6 104)	–	(90 496)
Movements for the period							
Credit losses written off	105 703	27 784	950	51 734	2 778	–	22 457
Net impairments (raised)/ released	(28 982)	10 356	(1 127)	(22 282)	(8 013)	–	(7 916)
Balance at the end of the period	(176 827)	(48 889)	(2 222)	(38 422)	(11 339)	–	(75 955)

* *Loans written off are generally subject to continued collection efforts for a period of time following write-off. The contractual amount outstanding on loans written off that are subject to enforcement activity is R41.5 million (2018: R6.5 million).*

	2020 R'000	2018 R'000
Net charge for credit losses in the statement of comprehensive income		
Net impairments raised	**(169 240)**	(28 982)
Interest adjustment on impaired advances	**18 361**	6 975
Amounts written off directly to comprehensive income	**(6 420)**	–
Recoveries in respect of amounts previously written off	**2 242**	242
	(155 057)	(21 765)

6. LOANS AND ADVANCES continued

6.5 ECL BY STAGE

	ECL			
	Stage 1 R'000	Stage 2 R'000	Stage 3 R'000	Total R'000
2020				
Balance at the beginning of the period	**(67 660)**	**(19 713)**	**(89 455)**	**(176 828)**
Transfers^				
Transfer to Stage 1	**(53)**	**454**	**5 929**	**6 330**
Transfer to Stage 2	**433**	**(7 939)**	**–**	**(7 507)**
Transfer to Stage 3	**459**	**484**	**(53 173)**	**(52 230)**
Movements for the period	**(3 829)**	**(8 540)**	**(133 621)**	**(145 990)**
Credit losses written off	**–**	**–**	**98 933**	**98 933**
New financial assets originated or purchased	**(11 286)**	**(3 473)**	**(1 936)**	**(16 695)**
Financial assets that have been derecognised	**19 065**	**291**	**32 457**	**51 814**
Change in model assumptions and methodology	**–**	**–**	**(4 961)**	**(4 961)**
Balance at the end of the period	**(62 871)**	**(38 436)**	**(145 827)**	**(247 133)**
2018				
Balance at the beginning of the year	(82 157)	(13 698)	(157 693)	(253 548)
Transfers^				
Transfer to Stage 1	(4 738)	4 524	214	–
Transfer to Stage 2	222	(222)	–	–
Transfer to Stage 3	318	127	(445)	–
Movements for the year	24 325	(12 926)	(73 773)	(62 374)
Credit losses written off	–	–	105 703	105 703
New financial assets originated or purchased	(10 405)	(3 353)	(2 556)	(16 314)
Financial assets that have been derecognised	4 775	5 835	39 095	49 705
Balance at the end of the year	(67 660)	(19 713)	(89 455)	(176 828)

^ *Transfers of ECL occur when the credit stage of an account at the end of the financial period differs from that at the beginning of the period. In this case, the opening balance of that account's ECL is disclosed as a reduction of ECL in its original credit stage and an increase in ECL in its new credit stage. In the prior year disclosure, the movements which arose as a direct result of the change in credit stage fell within the 'movements for the period' line. In the current period disclosure, the movements in ECL following changes in credit stages are reflected in the 'Transfers' line itself.*

Disclosure relating to the qualitative drivers of changes in ECL have been included under the risk management and control section.

6. LOANS AND ADVANCES continued

6.6 PRODUCT ANALYSIS OF PERFORMING LOANS AND ADVANCES

	Gross amount R'000	ECL Stage 1 R'000	ECL Stage 2 R'000	Net balance R'000
2020				
Current accounts	**2 072 020**	**(19 565)**	**(8 854)**	**2 043 601**
Credit cards	**43 699**	**(455)**	**(18)**	**43 226**
Mortgage loans	**5 094 819**	**(7 867)**	**(15 779)**	**5 071 173**
Instalment sales and leases	**660 737**	**(1 534)**	**(3 018)**	**656 185**
Structured loans	**37 792**	**–**	**–**	**37 792**
Medium-term loans	**1 067 462**	**(33 450)**	**(10 767)**	**1 023 245**
	8 976 529	**(62 871)**	**(38 436)**	**8 875 222**
2018				
Current accounts	2 203 374	(29 274)	(2 567)	2 171 533
Credit cards	41 011	(391)	(56)	40 564
Mortgage loans	4 786 074	(6 198)	(5 788)	4 774 088
Instalment sales and leases	900 746	(3 371)	(2 107)	895 268
Structured loans	134 126	–	–	134 126
Medium-term loans	1 071 213	(28 426)	(9 195)	1 033 592
	9 136 544	(67 660)	(19 713)	9 049 171

6.7 PRODUCT ANALYSIS OF PERFORMING LOANS AND ADVANCES (EXCLUDING LOANS AND ADVANCES WITH RENEGOTIATED TERMS)

	2020 R'000	2018 R'000
Current accounts	**1 985 956**	2 203 374
Credit cards	**43 699**	41 011
Mortgage loans	**4 928 195**	4 651 706
Instalment sales and leases	**656 037**	890 648
Structured loans	**37 792**	134 126
Medium-term loans	**1 027 328**	1 033 807
	8 679 007	8 954 672

6.8 PRODUCT ANALYSIS OF LOANS AND ADVANCES WITH RENEGOTIATED TERMS THAT WOULD OTHERWISE BE PAST DUE OR IMPAIRED

	2020 R'000	2018 R'000
Current accounts	**86 064**	–
Credit cards	**–**	–
Mortgage loans	**166 624**	134 368
Instalment sales and leases	**4 700**	10 098
Structured loans	**–**	–
Medium-term loans	**40 134**	37 406
	297 522	181 872

6. LOANS AND ADVANCES continued

6.9 PRODUCT AGE ANALYSIS OF LOANS AND ADVANCES THAT ARE PAST DUE BUT NOT INDIVIDUALLY IMPAIRED

	Past due for 1 – 30 days R'000	Past due for 31 – 60 days R'000	Past due for 61 – 90 days R'000	Total gross amount R'000	Fair value of collateral and other credit enhancements R'000
2020					
Current accounts	–	–	–	–	–
Credit cards	–	–	–	–	–
Mortgage loans	**46 468**	**30 008**	**4 947**	**81 423**	**105 944**
Instalment sales and leases	**8 914**	**2 711**	**168**	**11 793**	**11 037**
Structured loans	–	–	–	–	–
Medium-term loans	**2 903**	**1 379**	**698**	**4 980**	**1 298**
	58 285	**34 098**	**5 813**	**98 196**	**118 279**
2018					
Current accounts	–	–	–	–	–
Credit cards	–	–	–	–	–
Mortgage loans	88 453	22 955	16 658	128 066	183 972
Instalment sales and leases	2 853	389	–	3 242	4 328
Structured loans	–	–	–	–	–
Medium-term loans	3 601	738	748	5 087	2 114
	94 907	24 082	17 406	136 395	190 414

6.10 PRODUCT ANALYSIS OF LOANS AND ADVANCES THAT ARE INDIVIDUALLY IMPAIRED

	Gross amount R'000	ECL Stage 3 R'000	Net balance R'000	Fair value of collateral and other credit enhancements R'000
2020				
Current accounts	**57 064**	**(22 434)**	**34 630**	**47 615**
Credit cards	**5 485**	**(3 119)**	**2 366**	–
Mortgage loans	**311 822**	**(61 489)**	**250 333**	**299 993**
Instalment sales and leases	**31 973**	**(8 500)**	**23 473**	**26 711**
Structured loans	–	–	–	–
Medium-term loans	**124 705**	**(50 285)**	**74 420**	**80 873**
	531 049	**(145 827)**	**385 222**	**455 192**
2018				
Current accounts	33 420	(17 048)	16 372	53 951
Credit cards	3 011	(1 775)	1 236	–
Mortgage loans	205 319	(26 437)	178 882	254 392
Instalment sales and leases	12 447	(5 861)	6 586	39 983
Structured loans	–	–	–	–
Medium-term loans	108 784	(38 334)	70 450	53 858
	362 981	(89 455)	273 526	402 184

6. LOANS AND ADVANCES continued

6.11 CREDIT QUALITY OF GROSS LOANS AND ADVANCES

	Stage 1 R'000	Stage 2 R'000	Stage 3 R'000	Total R'000
2020				
On-balance sheet exposure (refer to note 6)				
Low	**7 776 893**	**35 115**	**91 644**	**7 903 652**
Medium	**146 035**	**33 091**	**94 513**	**273 639**
High	**608 576**	**376 819**	**344 892**	**1 330 287**
	8 531 504	**445 025**	**531 049**	**9 507 578**
Off-balance sheet exposure (refer to note 23.1)				
Low	698 825	2 064	–	700 889
Medium	17 441	–	–	17 441
High	218 753	5 591	–	224 344
	935 019	7 655	–	942 674

The internal credit rating risk buckets used to explain low risk, medium risk and high risk are subjectively determined by bucketing accounts by credit risk gradings and behavioural patterns. New loans may be granted to certain high-risk clients, depending on the credit-granting strategy and granting scorecards.

2018

No comparative information is disclosed for 2018.

6.12 COLLATERAL HELD AS SECURITY AND OTHER CREDIT ENHANCEMENTS

Fair value of collateral and other credit enhancements is determined by referencing the realisable value of security held.

All Bank clients are accorded a 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 of assets (specific and general)	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 professional valuation (certain segments up to 100%)
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 and in compliance with the applicable Court rules and directives.

A client 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 will be disposed of in accordance with the applicable legislation. In the case of insolvent and deceased estates, the duly appointed liquidator or trustee will dispose of all assets.

7. OTHER INVESTMENTS

	2020 R'000	2018 R'000
Fair value through other comprehensive income		
Unlisted equities	**1 139**	8 016
	1 139	8 016

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

8. OTHER ACCOUNTS RECEIVABLE

	2020 R'000	2018 R'000
Items in transit	**297 211**	414 350
Loan to fellow subsidiary (refer to note 32.1)	**111**	111
Loan to joint venture (refer to note 32.1)*	**3 715**	1 261
Prepayments and deposits	**18 118**	18 307
Structured loans accrued income*	**833**	7 209
Other receivables	**86 662**	50 840
	406 650	492 078

** Additional disclosure in respect of the prior year has been included.*

The Directors consider that the carrying amount of other accounts receivable approximates fair value.

The other accounts receivable are all current and not past due, therefore no age analysis has been prepared for past due but not impaired receivables.

Structured loans accrued income relates to the present value of future cash flows.

9. NON-CURRENT ASSETS HELD-FOR-SALE

	2020 R'000	2018 R'000
Properties in possession	**17 169**	22 500
	17 169	22 500

The Bank purchased this property out of a loan default during 2012. An offer to purchase, received in 2017, was subsequently cancelled in 2018 as certain suspensive conditions were not met. The property has been accounted for at the lower of the carrying amount and fair value, less costs to sell. Management remains committed to disposing of the property within 12 months.

10. INTEREST IN SUBSIDIARIES

	2020 R'000	2018 R'000
Unlisted		
Shares at cost	**107 195**	107 195
Portion 2 of Lot 8 Sandown Proprietary Limited	**98**	98
Mercantile Rental Finance Proprietary Limited	**107 097**	107 097
Loans to subsidiaries	**65 560**	2 076
Mercantile Payment Solutions Proprietary Limited (joint venture)	**–**	2 076
Portion 2 of Lot 8 Sandown Proprietary Limited	**65 560**	–
	172 755	109 271

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

The loan to Portion 2 of Lot 8 Sandown Proprietary Limited bears interest at prevailing market rates and has no fixed terms of repayment.

11. INVESTMENT IN DEBT SECURITIES

	2020 R'000	2018 R'000
Fair value through profit or loss		
Investment in Compass Securitisation (RF) Limited D notes	**155 761**	151 629
	155 761	151 629

The notes (R1 000 000 each) are subordinated, unsecured, compulsorily redeemable and asset-backed.

During 2017, the Bank invested in 'D' notes (promissory notes) to the value of R103 million in the Mercantile Rental Finance Proprietary Limited securitisation vehicle. The notes are secured, mature on 6 June 2020, and interest on the notes is linked to JIBAR. In December 2018, an additional R47 million in notes was taken up by the Bank. These notes are also linked to JIBAR with interest repayable quarterly and maturing on 6 December 2021.

12. PROPERTY AND EQUIPMENT

	Leasehold improvements R'000	Computer equipment R'000	Furniture and fittings R'000	Office equipment R'000	Motor vehicles R'000	Total R'000
2020						
Open market value or cost at the beginning of the period	**13 571**	**72 685**	**12 212**	**28 065**	**781**	**127 314**
Additions	**–**	**7 653**	**181**	**324**	**–**	**8 158**
Write-off of obsolete assets	**–**	**(1 505)**	**(48)**	**(620)**	**–**	**(2 173)**
Open market value or cost at the end of the period	**13 571**	**78 833**	**12 345**	**27 769**	**781**	**133 299**
Accumulated depreciation and impairment losses at the beginning of the period	**(5 436)**	**(45 660)**	**(4 984)**	**(22 693)**	**(694)**	**(79 467)**
Depreciation – disclosed in operating expenditure	**(2 164)**	**(4 710)**	**(1 410)**	**(3 490)**	**(67)**	**(11 841)**
Depreciation – disclosed in fee and commission expenditure	**–**	**(9 730)**	**–**	**–**	**–**	**(9 730)**
Write-off of obsolete assets	**–**	**1 500**	**46**	**620**	**–**	**2 166**
Accumulated depreciation and impairment losses at the end of the period	**(7 600)**	**(58 600)**	**(6 348)**	**(25 563)**	**(761)**	**(98 872)**
Net carrying amount at the end of the period	**5 971**	**20 233**	**5 997**	**2 206**	**20**	**34 427**
2018						
Open market value or cost at the beginning of the year	13 344	59 363	11 629	27 454	781	112 571
Additions	271	13 384	583	635	–	14 873
Write-off of obsolete assets	(44)	(62)	–	(24)	–	(130)
Open market value or cost at the end of the year	13 571	72 685	12 212	28 065	781	127 314
Accumulated depreciation and impairment losses at the beginning of the year	(3 630)	(36 213)	(3 816)	(18 944)	(578)	(63 181)
Depreciation – disclosed in operating expenditure	(1 847)	(2 935)	(1 168)	(3 770)	(116)	(9 836)
Depreciation – disclosed in fee and commission expenditure	–	(6 540)	–	–	–	(6 540)
Write-off of obsolete assets	41	28	–	21	–	90
Accumulated depreciation and impairment losses at the end of the year	(5 436)	(45 660)	(4 984)	(22 693)	(694)	(79 467)
Net carrying amount at the end of the year	8 135	27 025	7 228	5 372	87	47 847

13. RIGHT-OF-USE ASSET AND LEASE LIABILITY

	2020 R'000
RIGHT-OF-USE ASSET	
2020	
Open market value or cost at the beginning of the period	–
Recognition of right-of-use asset 1 January 2019	91 025
Additions	–
Open market value or cost at the end of the period	91 025
Accumulated depreciation and impairment losses at the beginning of the period	–
Depreciation – disclosed in operating expenditure	(36 941)
Disposals	–
Accumulated depreciation and impairment losses at the end of the period	(36 941)
Net carrying amount at the end of the period	54 084
2018	
No comparative information is available for 2018 as IFRS 16 was not applicable in the prior period.	
LEASE LIABILITY	
Present value of lease liability	58 515
Lease liabilities included in the statement of financial position as at 29 February 2020	
Current	29 478
Non-current	29 037
Total	58 515
Maturity analysis – contractual undiscounted cash flows	
Less than one year	32 202
One to five years	29 267
More than five years	–
Total undiscounted lease liabilities as at 29 February 2020	61 469
Amounts recognised in profit or loss	
Interest on lease liabilities	4 992
Expense relating to short-term leases	528
Amounts recognised in the statement of cash flows	
Total cash flow for leases	37 502

Real estate leases

The Bank typically entered into three- to five-year leases for its business centres/branches. The majority of these leases include an option to renew the lease for an additional period (of the same duration) after the end of the contract term.

2018

No comparative information is disclosed for 2018 as IFRS 16 was not applicable in the prior period.

14. INTANGIBLE ASSETS

	2020 R'000	2018 R'000
Computer software		
Cost at the beginning of the period	**433 415**	404 836
Additions	**21 740**	28 601
Transfer	**–**	(22)
Write-off of obsolete computer software	**(341)**	–
Cost at the end of the period	**454 814**	433 415
Accumulated amortisation and impairment losses at the beginning of the period	**(305 021)**	(251 573)
Amortisation	**(66 876)**	(53 470)
Transfer	**–**	22
Write-off of obsolete computer software	**19**	–
Accumulated amortisation and impairment losses at the end of the period	**(371 878)**	(305 021)
Net carrying amount at the end of the period	**82 936**	128 394

During 2020 and 2018, the Bank identified no events or circumstances that would indicate that the Bank's intangible assets may need to be impaired.

15. DEFERRED TAX ASSETS

	2020 R'000	2018 R'000
Balance at the beginning of the period	**42 961**	15 088
Current year charge		
Per the statement of comprehensive income	**5 004**	16 483
IFRS 9 transitional adjustment	**–**	11 770
Other comprehensive income	**1 382**	(380)
Balance at the end of the period	**49 347**	42 961
Tax effects of temporary differences between tax and book value for:		
Intangible assets	**(5 209)**	(15 673)
Provisions and other liabilities	**25 756**	25 799
Impairments on loans and advances	**26 191**	21 839
Leased assets	**2 395**	769
Revaluations	**(121)**	(1 662)
Current assets	**335**	11 889
Total deferred tax assets	**49 347**	42 961

16. CURRENT TAX RECEIVABLE/PAYABLE

	2020 R'000	2018 R'000
South African Revenue Service		
Current tax receivable	**4 672**	–
Current tax payable	–	5 726

17. OTHER ACCOUNTS PAYABLE

	2020 R'000	2018 R'000
Accruals	**43 788**	35 462
Product-related credits	**287 814**	368 162
Sundry creditors	**12 474**	15 501
	344 076	419 125

18. PROVISIONS AND OTHER LIABILITIES

	Deferred bonus scheme R'000	Staff incentives R'000	Audit fees R'000	Post-retirement medical benefits R'000	Leave pay R'000	Other risks R'000	Total R'000
As at 1 January 2018	40 914	37 417	4 276	19 034	14 962	304	116 907
Provision raised	41 007	40 177	10 571	2 220	14 478	2 069	110 522
Reversal of provision	–	–	–	–	–	(505)	(505)
Charged to provision	(25 984)	(34 960)	(10 199)	(3 162)	(14 963)	(1 275)	(90 543)
As at 31 December 2018	**55 937**	**42 634**	**4 648**	**18 092**	**14 477**	**593**	**136 381**
Provision raised	**35 152**	**41 180**	**9 630**	**2 734**	**20 788**	**1 197**	**110 681**
Reversal of provision	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Charged to provision	**(87 026)**	**(45 859)**	**(13 974)**	**(3 592)**	**(21 897)**	**(1 212)**	**(173 560)**
As at 29 February 2020	**4 063**	**37 955**	**304**	**17 234**	**13 368**	**578**	**73 502**

POST-RETIREMENT MEDICAL BENEFITS

Refer to note 19 for detailed disclosure of this provision.

LEAVE PAY

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

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.

19. POST-RETIREMENT MEDICAL BENEFITS

The Bank operates a post-retirement medical scheme. Independent actuaries value this scheme annually (the last valuation was carried out as at 29 February 2020). It is the actuary's opinion that the plan is in a sound financial position.

	2020 R'000	2018 R'000
The amounts recognised in the statement of financial position are as follows (refer to note 18)		
Present value of total service liabilities	**17 234**	18 092
Liability in the statement of financial position	**17 234**	18 092
The amounts recognised in the statement of comprehensive income are as follows:		
Net interest cost (refer to note 25)	**1 604**	1 731
Staff cost (refer to note 29)	**(1 895)**	(1 858)
Current service cost	**6**	7
Benefits paid	**(1 901)**	(1 865)
Total included in comprehensive income	**(291)**	(127)
The amounts recognised in the statement of other comprehensive income are as follows:		
Remeasurement of defined benefit obligation	**(567)**	(815)
Total included in other comprehensive income	**(567)**	(815)
Reconciliation of the movement in the present value of total service liabilities:		
Balance at the beginning of the period	**18 092**	19 034
Current service cost	**6**	7
Interest costs	**1 604**	1 731
Remeasurement of defined benefit obligation	**(567)**	(815)
Employer benefit payments	**(1 901)**	(1 865)
Balance at the end of the period	**17 234**	18 092
The principal actuarial assumptions used were as follows:		
Discount rate	**9.1%**	9.4%
Rate of medical inflation	**6.6%**	7.7%
Salary inflation	**6.1%**	7.2%

The effect of a 1% increase/decrease in the assumed rate of medical inflation would result in an increase in the liability in the amount of R1.589 million (2018: R1.736 million) or a decrease of R1.381 million (2018: R1.502 million), respectively.

20. DEPOSITS

	2020 R'000	2018 R'000
Call deposits and current accounts	**7 427 242**	6 026 192
Savings accounts	**194 078**	186 515
Term and notice deposits	**3 652 977**	3 628 721
Foreign currency-denominated deposits	**883 524**	649 859
Total deposits	**12 157 821**	10 491 287
Maturity analysis		
Repayable on demand and maturing within one month	**9 184 657**	7 472 807
Maturing after one month but within six months	**1 286 814**	1 386 567
Maturing after six months but within 12 months	**126 118**	328 392
Maturing after 12 months	**1 560 232**	1 303 521
Total deposits	**12 157 821**	10 491 287

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

21. LONG-TERM FUNDING

	2020 R'000	2018 R'000
International Finance Corporation (IFC)		
Short-term portion payable in the next 12 months	–	–
Portion payable after 12 months but within five years	–	742 880
Total long-term funding	–	742 880
Long-term funding before non-cash movements	–	743 586
(Gain) on exchange rate movement	–	(706)
Total long-term funding	–	742 880

In 2018, a R740 million IFC facility was drawn-down, with quarterly interest repayments linked to JIBAR and semi-annual capital repayments due from 15 March 2020 to 15 March 2025. In February 2020, this IFC loan was fully repaid in line with an option for early settlement (refer to note 28).

22. SHARE CAPITAL AND SHARE PREMIUM

	Number of issued ordinary shares	Share capital R'000	Share premium R'000	Total R'000
22.1 ISSUED				
As at 29 February 2020 and 31 December 2018	**62 484 352**	**124 969**	**1 358 331**	**1 483 300**

22.2 AUTHORISED

The total authorised number of ordinary shares is 62 630 000 shares (2018: 62 630 000 shares) with a par value of R2.00 per share.

22.3 UNISSUED

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

22.4 RIGHTS, PREFERENCES AND RESTRICTIONS OF SHARES

Unless otherwise stated in the Company's memorandum of incorporation, a share affords every holder of such share the right to certain dividends when declared, return of capital on the winding up of the Company, and the right to attend and vote at meetings of shareholders.

23. CONTINGENT LIABILITIES AND COMMITMENTS

23.1 GUARANTEES, LETTERS OF CREDIT AND COMMITTED UNDRAWN FACILITIES

	2020 R'000	2018 R'000
Guarantees	**636 618**	1 003 723
Lending-related	**664**	692
Mortgage	**63 498**	213 611
Performance	**572 456**	789 420
Letters of credit	**2 674**	8 213
Committed undrawn facilities	**303 382**	279 882
	942 674	1 291 818

Refer to note 6.3.1 for the off-balance sheet ECL which relates to guarantees, letters of credit and committed undrawn facilities.

Committed undrawn facilities only include irrevocable facilities and do not include unutilised overdraft facilities as the Bank has a right to revoke these without notice.

	2020 R'000	2018 R'000
23.2 COMMITMENTS IN TERMS OF OPERATING LEASES		
The total minimum future lease payments in terms of operating leases are as follows:		
Property rentals		
Due within one year	–	30 776
Due between one and five years	–	60 229
	–	91 005
After-tax effect on operating leases	–	65 524

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

Following the implementation of IFRS16 from 1 January 2019, the disclosure relating to operating lease payments due is no longer required.

24. INTEREST INCOME

	2020 R'000	2018 R'000
Loans to subsidiaries and fellow subsidiaries	**41 476**	54 764
Amortised cost	**1 429 034**	1 094 991
Cash and cash equivalents	**226 015**	100 242
Negotiable securities	**73 766**	67 036
Loans and advances	**1 129 253**	927 713
Fair value through profit or loss		
Investment in debt securities	**28 797**	17 447
	1 499 307	1 167 202

25. INTEREST EXPENSE

	2020 R'000	2018 R'000
Deposits	**729 946**	539 473
Long-term funding	**83 881**	74 593
Net interest on defined benefit obligation	**1 604**	1 731
Interest on lease liabilities	**4 992**	–
Other	**–**	2
	820 423	615 799

26. NON-INTEREST INCOME

	2020 R'000	2018 R'000
Fee and commission income		
Loans and receivables and transactional income	**664 907**	506 713
Trading income		
Fair value through profit or loss		
Foreign currency	**417 883**	263 201
	1 082 790	769 914

27. FEE AND COMMISSION EXPENDITURE

	2020 R'000	2018 R'000
Relating to non-interest income earned from:		
Fees and commissions	**336 804**	233 288
Foreign currency	**298 459**	181 021
	635 263	414 309

28. OTHER TRADING-RELATED EXPENDITURE

	2020 R'000	2018 R'000
Impairment on property in possession (refer to note 9)	**6 145**	–
Early settlement fees on International Finance Corporation loan (refer to note 21)	**31 188**	–
	37 333	–

29. OPERATING EXPENDITURE

	2020 R'000	2018 R'000
Amortisation (refer to note 14)	**66 876**	53 470
Auditor's remuneration		
Audit fees – Current period	**9 630**	10 521
Fees for other services – Tax advisory fees	**196**	210
– Other	**10**	(5)
	9 836	10 726
Depreciation (refer to note 12)	**8 265**	9 836
Depreciation on right-of-use asset (refer to note 13)	**36 941**	–
Directors' remuneration (refer to note 32.4)		
Executive Directors' remuneration	**17 956**	17 031
Non-Executive Directors' fees	**4 889**	4 718
	22 845	21 749
Indirect tax		
Non-claimable value added tax	**17 088**	15 184
Skills development levy	**3 636**	2 535
	20 724	17 719
(Profit) on sale of intangible assets and property and equipment	**(18)**	(9)
Marketing	**2 855**	10 007
Operating leases for premises and related costs	**6 266**	35 338
Other operating costs	**84 869**	44 989
Professional fees		
Consulting	**2 836**	2 000
Legal and collection	**4 161**	3 131
Computer consulting and services	**75 484**	56 796
	82 481	61 927
Staff costs		
Salaries and short-term incentives	**293 584**	242 751
Post-retirement medical benefits (refer to notes 18 and 19)	**(1 895)**	(1 858)
Deferred bonus schemes (including amounts relating to Executive Directors)	**11 163**	41 007
Other (including amounts relating to Executive Directors)	**25 985**	6 881
	328 837	288 781
Total operating expenditure	**633 836**	554 533
Number of persons employed by the Company at the end of the period	**520**	472

30. TAX

	2020 R'000	2018 R'000
South African normal tax	**88 432**	108 915
Current period	**89 790**	108 332
Prior year	**(1 358)**	583
Deferred tax	**(5 004)**	(16 483)
Current period	**(5 754)**	(15 282)
Prior year	**750**	(1 201)
Total tax	**83 428**	92 432
Direct tax		
South African normal tax	**88 432**	108 915
South African tax rate reconciliation		
South African standard tax rate (%)	**28.00**	28.00
Expenses not deductible for tax purposes (%)	**0.03**	0.02
Expenses deductible for tax purposes (%)	**(0.09)**	–
Capital gain inclusion on unrealised portion not taxable (%)	**–**	0.02
Overprovision prior year (%)	**(0.15)**	(0.09)
Effective tax rate (%)	**27.79**	27.95

31. NOTES TO STATEMENT OF CASH FLOWS

	2020 R'000	2018 R'000
31.1 CASH RECEIPTS FROM CLIENTS		
Interest income	**1 499 307**	1 167 202
Non-interest income	**1 082 790**	769 914
Adjusted for: Revaluation of fair value financial instruments	**720**	(26 494)
Recoveries in respect of amounts previously written off	**2 242**	242
	2 585 059	1 910 864
31.2 CASH PAID TO CLIENTS, SUPPLIERS AND EMPLOYEES		
Interest expense	**(820 423)**	(615 799)
Operating expenditure and fee and commission expenditure	**(1 306 432)**	(968 842)
Adjusted for: Amortisation	**66 876**	53 470
Depreciation	**21 572**	16 376
Depreciation: IFRS 16	**36 941**	–
Write-off of obsolete property and equipment	**7**	40
Other trading-related expenditure	**11 361**	–
(Profit) on sale of intangible assets and property and equipment	**(18)**	(9)
Deferred bonus schemes expense	**11 163**	41 007
(Decrease) in provisions and other liabilities	**(74 042)**	(21 533)
	(2 052 995)	(1 495 290)

31. NOTES TO STATEMENT OF CASH FLOWS continued

	2020 R'000	2018 R'000
31.3 RECONCILIATION OF PROFIT BEFORE TAX TO CASH GENERATED FROM OPERATIONS		
Profit before tax	**300 185**	330 710
Profit before tax adjusted for:		
Revaluation of fair value financial instruments	**720**	(26 494)
Net impairments raised	**157 299**	22 007
Amortisation	**66 876**	53 470
Depreciation	**21 572**	16 376
Depreciation: IFRS 16	**36 941**	–
Other trading-related expenditure	**11 361**	–
Write-off of obsolete property and equipment	**7**	40
(Profit) on sale of intangible assets and property and equipment	**(18)**	(9)
Deferred bonus schemes expense	**11 163**	41 007
(Decrease) in provisions and other liabilities	**(74 042)**	(21 533)
Cash generated from operations	**532 064**	415 574
31.4 TAX		
Amounts (underpaid) at the beginning of the period	**(5 726)**	(6 111)
Statement of comprehensive income (charge)	**(88 432)**	(108 915)
Less: Amounts (overpaid)/underpaid at the end of the period	**(4 672)**	5 726
Total tax (paid)	**(98 0830)**	(109 300)
31.5 NET MOVEMENT IN INCOME-EARNING ASSETS		
(Increase)/Decrease in negotiable securities	**(86 573)**	113 340
(Increase) in loans and advances	**(95 022)**	(325 426)
Net (increase) in income-earning assets	**(181 595)**	(212 086)
31.6 NET MOVEMENT IN DEPOSITS AND OTHER ACCOUNTS		
Increase in deposits	**1 666 534**	1 149 426
Decrease in other accounts receivable	**79 398**	161 597
(Decrease) in other accounts payable	**(73 301)**	(69 359)
Net increase in deposits and other accounts	**1 672 631**	1 241 664

32. RELATED PARTY INFORMATION

32.1 BALANCES WITH THE HOLDING COMPANY, DIRECT AND FELLOW SUBSIDIARIES AND JOINT VENTURE

	2020 R'000	2018 R'000
Loans to subsidiaries		
Portion 2 of Lot 8 Sandown Proprietary Limited	**65 560**	–
Mercantile Rental Finance Proprietary Limited	**485 392**	364 967
	550 952	364 967
The loan to Mercantile Rental Finance Proprietary Limited is included in loans and advances and has been assessed for impairment.		
Loans to fellow subsidiary and joint venture (including other accounts receivable disclosed in note 8)		
Mercantile Insurance Brokers Proprietary Limited	**111**	111
Mercantile Payment Solutions Proprietary Limited	**3 715**	3 377
	3 826	3 488
Investment in debt securities		
Compass Securitisation (RF) Limited	**155 761**	151 629
Interbank placement with the current holding company		
Capitec Bank Limited	**2 112 613**	–
Deposits from the prior holding company, subsidiary, fellow subsidiary and joint venture		
Mercantile Bank Holdings Limited	**–**	3 821
Portion 2 of Lot 8 Sandown Proprietary Limited	**5 158**	69 462
The Mercantile Bank Foundation (NPC)	**–**	41
Mercantile Insurance Brokers Proprietary Limited	**635**	485
Mercantile Payment Solutions Proprietary Limited	**200**	–
	5 993	73 809

32. RELATED PARTY INFORMATION continued

32.2 TRANSACTIONS WITH THE HOLDING COMPANY, DIRECT AND FELLOW SUBSIDIARIES AND JOINT VENTURES

	2020 R'000	2018 R'000
Interest received from:		
Capitec Bank Limited	**14 888**	–
Mercantile Rental Finance Proprietary Limited	**41 223**	37 317
Portion 2 of Lot 8 Sandown Proprietary Limited	**253**	–
Compass Securitisation (RF) Limited	**28 797**	17 447
Interest paid to:		
Portion 2 of Lot 8 Sandown Proprietary Limited	**3 080**	2 540
Non-interest income earned from:		
Mercantile Rental Finance Proprietary Limited	**1 196**	484
Mercantile Payment Solutions Proprietary Limited	**142 657**	98 213
Dividends paid to:		
Mercantile Bank Holdings Limited	**49 886**	42 458
Donations paid to:		
The Mercantile Bank Foundation (NPC)	**–**	1 158
Operating expenditure paid to:		
Portion 2 of Lot 8 Sandown Proprietary Limited	**31 633**	25 056
Purchase of rental finance assets from:		
Mercantile Rental Finance Proprietary Limited	**100 000**	199 915
Sale of rental finance assets to:		
Mercantile Rental Finance Proprietary Limited	**185 479**	–

32.3 BALANCES BETWEEN THE PRIOR ULTIMATE SHAREHOLDER AND THE BANK

	Nature of account	2020 R'000	2018 R'000
Legal entity			
CGD – Lisbon (Branch of CGD)	Nostro accounts	**166 410**	173 509
Total assets		**166 410**	173 509
CGD – Lisbon (Branch of CGD)	Vostro accounts	**(3 077)**	(6 498)
Banco Comercial e de Investimentos – Mozambique (BCI) (Subsidiary of CGD)	Call and notice deposits	**(647)**	(820)
Banco Caixa Geral Totta SA (BCGA) (Subsidiary of CGD)	Call deposit	**(4 591)**	(10 144)
Total liabilities		**(8 315)**	(17 462)
Net assets		**158 095**	156 047
Transactions between the prior ultimate shareholder and the Bank:			
Interest paid by the Bank to BCI		**246**	13 674
Interest paid by the Bank to BCGA		**122**	85
Interest paid by the Bank to BNU		**–**	5 448
Interest received by the Bank from CGD – Lisbon		**301**	219
Fees received by the Bank from BCGA		**67**	99

32. RELATED PARTY INFORMATION continued

32.4 DIRECTOR AND DIRECTOR-RELATED ACTIVITIES

Directors' remuneration

	Directors' fees R'000	Salary R'000	Role-based allowance R'000	Fringe benefits R'000	Retirement funds and medical aid contri-butions R'000	Perfor-mance bonus# R'000	Total R'000
2020							
Non-Executive Directors							
RS Caliço^ (resigned 7 November 2019)	–	–	–	–	–	–	–
GP de Kock (resigned 29 February 2020)	**1 398**	–	–	–	–	–	**1 398**
L Hyne (resigned 29 November 2019)	**846**	–	–	–	–	–	**846**
AT Ikalafeng (resigned 29 November 2019)	**716**	–	–	–	–	–	**716**
DR Motsepe (resigned 29 November 2019)	**806**	–	–	–	–	–	**806**
TH Njikizana (resigned 29 February 2020)	**1 123**	–	–	–	–	–	**1 123**
SL Botha* (appointed 29 November 2019)	–	–	–	–	–	–	–
JD McKenzie* (appointed 29 November 2019)	–	–	–	–	–	–	–
JP Verster* (appointed 29 November 2019)	–	–	–	–	–	–	–
K Makwane* (appointed 5 February 2020)	–	–	–	–	–	–	–
CA Otto* (appointed 5 February 2020)	–	–	–	–	–	–	–
PJ Mouton* (appointed 5 February 2020)	–	–	–	–	–	–	–
DP Meintjes* (appointed 5 February 2020)	–	–	–	–	–	–	–
MS d P le Roux* (appointed 14 February 2020)	–	–	–	–	–	–	–
NS Mashiya* (appointed 14 February 2020)	–	–	–	–	–	–	–
Executive Directors							
KR Kumbier	–	**5 182**	**2 680**	–	**887**	**4 312**	**13 061**
MEL Teixeira	–	**2 955**	–	–	**440**	**1 500**	**4 895**
AP du Plessis* (appointed 29 November 2019)	–	–	–	–	–	–	–
GM Fourie* (appointed 29 November 2019)	–	–	–	–	–	–	–
	4 889	**8 137**	**2 680**	–	**1 327**	**5 812**	**22 845**

The value of the CEO's performance bonus is for the financial period under report but, in line with a Guidance Note issued by the Prudential Authority on 6 April 2020, the amount will be paid at a future date yet to be determined. The value of the Financial Director's performance bonus is for the financial period under report but payment will be made in the subsequent financial year.

^ *Employees of CGD, the former holding company, are not paid a fee for holding a directorship on the board of that company's subsidiaries. Accordingly, Mr Caliço did not receive a fee for his role as a Non-Executive Director on the Mercantile Board.*

* *Directors of Capitec Bank, the incumbent holding company, are not paid a fee for holding a directorship on the board of a subsidiary.*

32. RELATED PARTY INFORMATION continued

32.4 DIRECTOR AND DIRECTOR-RELATED ACTIVITIES continued

Directors' remuneration continued

	Directors' fees R'000	Salary R'000	Role-based allowance R'000	Fringe benefits R'000	Retirement funds and medical aid contri-butions R'000	Perfor-mance bonus# R'000	Total R'000
2018							
Non-Executive Directors							
RS Caliço (appointed 18 June 2018)^	–	–	–	–	–	–	–
GP de Kock	1 282	–	–	–	–	–	1 282
L Hyne	880	–	–	–	–	–	880
AT Ikalafeng	745	–	–	–	–	–	745
DR Motsepe	838	–	–	–	–	–	838
TH Njikizana	973	–	–	–	–	–	973
Executive Directors							
RS Caliço (resigned 16 June 2018)	–	1 570	–	296	–	–	1 866
KR Kumbier	–	4 052	3 034	–	693	4 791	12 570
MEL Teixeira (appointed 15 June 2018)	–	1 402	–	–	197	996	2 595
	4 718	7 024	3 034	296	890	5 812	21 749

Value of performance bonus earned for the financial year under report but payment has been deferred to the subsequent year(s).

^ *Employees of CGD, the former holding company, are not paid a fee for holding a directorship on the board of that company's subsidiaries. Accordingly, Mr Caliço did not receive a fee for his role as a Non-Executive Director on the Mercantile Board.*

	2020 R'000	2018 R'000
Balances with/(from) key management personnel (Board of Directors)		
Loans and advances	**2**	25
Committed undrawn facilities	**5 265**	5 402
Deposits	**(19 755)**	(8 093)
Amounts paid by CGD to RS Caliço	**–**	439

32. RELATED PARTY INFORMATION continued

32.4 DIRECTOR AND DIRECTOR-RELATED ACTIVITIES continued

Service agreements

KR Kumbier, CEO

Mr Kumbier was employed by Mercantile as Executive Director: Finance and Business on 1 June 2010. He was subsequently appointed Deputy CEO (effective 1 April 2012) and, thereafter, as CEO from 1 April 2013. On 7 November 2019, control of Mercantile was transferred to Capitec Bank. Mr Kumbier's service agreement provided *inter alia* that, should CGD enter into a transaction that has the effect that it relinquishes its control of Mercantile Bank Holdings Limited, he will be entitled to terminate his employment with Mercantile Bank Holdings Limited and Mercantile within 30 business days from the date of approval of the transaction. In terms of the change in control clause, were Mr Kumbier to terminate his employment, he would be paid a package equivalent to 12 months of his remuneration, which payment would be in addition to any amounts owing to Mr Kumbier in respect of his notice pay. Mr Kumbier informed the Board of his intention to exercise the clause and terminate his employment. Capitec Bank requested Mr Kumbier to stay on as CEO and agreed to buy him out of the clause for an amount of R12.4 million, which was the equivalent value of the exit clause. Mr Kumbier's service agreement was subsequently revised on 11 November 2019 to align with the remuneration and benefits of the Capitec Bank Group Executives.

The Remuneration Committee's annual bonus decision for Mr Kumbier considered performance during the period against Bank and individual performance measures. The Remuneration Committee noted performance against key financial and non-financial measures contained in the balanced scorecard and the strong personal contribution made by Mr Kumbier, particularly in the sale of the Bank and in building and embedding a strong leadership team. In addition, the former shareholder, CGD, awarded Mr Kumbier a R3.9 million retention bonus that would be payable if he remained at Mercantile during the sale process.

Mercantile's senior management team was permitted to participate in the Capitec Bank Employee Share Purchase Scheme (ESPS). Essentially, in terms of the scheme rules, Mercantile shall subsidise the amount allocated by an employee to purchase Capitec Bank Holdings shares through the ESPS by contributing a taxable cash amount equal to 20% of the cash amount invested by the employee. The aggregate cash amount is then used to purchase Capitec Bank Holdings shares through the ESPS. Mr Kumbier has participated in the ESPS since its introduction in November 2019 and the Bank's 20% taxable contribution on his investment was R1.2 million.

MEL Teixeira, Financial Director

Ms Teixeira joined Mercantile in January 2006 and was promoted to Chief Financial Officer in April 2013. On 15 June 2018, Ms Teixeira was appointed Financial Director of the Bank. In terms of her service agreement, Ms Teixeira has agreed to perform such duties, functions and services as are assigned to her from time to time by the Board of Directors and which are consistent and commensurate with her position as Financial Director.

32. RELATED PARTY INFORMATION continued

32.4 DIRECTOR AND DIRECTOR-RELATED ACTIVITIES continued

Ms Teixeira has participated in Mercantile's long-term incentive scheme (cash-settled scheme) since its inception. The following table sets out the details of the awards that vested during the current reporting period and the balance of unvested awards:

	Number of awards granted	% vesting of awards granted	Number of vested awards	Proxy price cents	Cash settled R'000	Number of unvested awards	Vesting year of unvested awards
Awards granted in March 2016	2 000 000	175.0	3 500 000	87.6	3 067	–	–
Awards granted in March 2017#	2 000 000	89.2	1 783 770	95.2	1 698	98 148	2020
Awards granted in March 2018#	1 900 000	49.8	946 326	95.2	901	726 574	2021
Awards granted in March 2019#	2 000 000	7.1	142 130	95.2	135	1 431 481	2021

As a result of the transfer of control of Mercantile to Capitec Bank, unvested awards were vested pro rata *on the date of change of control based on the time lapsed from initial date of granting to that date. The balance of unvested awards will vest according to the original timelines and the value at each vesting date will be calculated based on the increase in the Bank's net asset value against the date of change of control and performance against budget for the relevant financial period.*

Mercantile's senior management team was permitted to participate in the Capitec Bank Employee Share Purchase Scheme (ESPS). Essentially, in terms of the scheme rules, Mercantile shall subsidise the amount allocated by an employee to purchase Capitec Bank Holdings shares through the ESPS by contributing a taxable cash amount equal to 20% of the cash amount invested by the employee. The aggregate cash amount is then used to purchase Capitec Bank Holdings shares through the ESPS. Ms Teixeira has participated in the ESPS since its introduction in November 2019 and the Bank's 20% taxable contribution on her investment was R300k.

RS Caliço, Deputy CEO

Mr Caliço was seconded by the former shareholder, CGD, to Mercantile in July 2014 as an Executive Director and was appointed Deputy CEO of the Bank from July 2015. Mr Caliço stepped down as Deputy CEO on 16 June 2018 and served Mercantile as a Non-Executive Director from 18 June 2018 until his resignation from the Mercantile Board of Directors, effective 7 November 2019.

Amounts earned by Directors for directorial services to other Group companies and not included in the Company's statement of comprehensive income

	Services to Capitec Bank 2020 R'000
Non-Executive Directors	
SL Botha (appointed 29 November 2019)	**719**
JD McKenzie (appointed 29 November 2019)	**446**
JP Verster (appointed 29 November 2019)	**316**
K Makwane (appointed 5 February 2020)	**71**
CA Otto (appointed 5 February 2020)	**83**
PJ Mouton (appointed 5 February 2020)	**60**
DP Meintjes (appointed 5 February 2020)	**61**
MS d P le Roux (appointed 14 February 2020)	**43**
Executive Directors	
AP du Plessis (appointed 29 November 2019)	**3 505**
GM Fourie (appointed 29 November 2019)	**4 494**
NS Mashiya (appointed 14 February 2020)	**540**
	10 338

Comparatives for 2018 are not presented as the Directors were appointed to the Mercantile Board during the current reporting period.

33. EVENTS AFTER THE REPORTING PERIOD

COVID-19 PANDEMIC

From the beginning of 2020, the global economy has been adversely affected by the outbreak of COVID-19. This pandemic could result in a global economic downturn that will have an adverse impact on sovereign governments, with expectations of suppressed fiscal revenues, increases in health expenditure, and reduced international trade likely to negatively affect government revenues and GDP. Consequently, unemployment and adjustments in fiscal and monetary policies to respond to the crisis will impact economies.

While it seems likely at this point that the travel and tourism, entertainment, automotive, oil and gas, and health industries will be most affected due to disruptions in supply and demand, Mercantile has no concentrated focus on any of these and holds a well-diversified loan portfolio book spread evenly across retail and wholesale, manufacturing, financial services and real estate.

From a credit perspective, the Bank shall rapidly identify affected clients to understand how they can be supported. The Bank is conducting high-level stress testing on its loan assets to assess requisite levels of preparedness and the potential magnitude of any negative impact. As the pandemic evolves, there is an expectation of repayment delays and/or requests to extend loan repayments due to adverse impacts on borrower cash flows. As a bank, Mercantile will consider these requests and systems and processes have been implemented to assess requests as they arise.

It is anticipated that the COVID-19 pandemic might negatively impact the Bank's profitability for the year ending 28 February 2021, particularly in respect of interest and non-interest income, ECL and operating expenses. While the Bank has implemented the necessary measures to mitigate the risks associated with this pandemic, it is not able to quantify the pandemic's future financial impact on its business.

It is also noteworthy that the Bank holds a 208% Liquidity Coverage Ratio, which is well above the prudential minimum of 100% (and the revised minimum of 80%, per the Prudential Authority directive issued on 6 April 2020). Further, the Prudential Authority has reduced the Systemic Risk Add-on (Pillar 2A) Capital requirement from 1% to 0%, which increases the Bank's capital buffer from R1.2 billion to R1.3 billion. The Bank may apply to the Prudential Authority for additional relief on the capital conservation buffer, if required.

OTHER EVENTS

Other than the above-mentioned considerations, no other material events occurred after the reporting period i.e. between the accounting date and the date of this report, that require adjustment to disclosures in the financial statements. However, it is noteworthy that, on 5 March 2020, Mercantile completed its acquisition of the remaining 50% shareholding in the Mercantile Payment Solutions Proprietary Limited joint venture. The cost of this acquisition and its related contribution to profits will reflect in the annual financial statements for the year ended 28 February 2021.

RISK MANAGEMENT AND CONTROL

RISK MANAGEMENT PHILOSOPHY

The Bank recognises that the business of banking and financial services is conducted within an environment of complex inter-related risks. Risk management is a key focus of the Bank and addresses a wide spectrum of risks that are continually evaluated. Related policies and procedures are reviewed and stress tested to adapt to changing circumstances. Risks inherent to existing activities are maintained within the approved risk tolerance levels, thereby optimising the risk-return parameters for the creation of sustainable growth and value for all stakeholders.

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 for concentration risk – 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 risk 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 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 and 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 the shareholder's funds.

A number of risk initiatives were implemented and others further entrenched during the period. These included, *inter alia:*

- Enhancements to the Risk Tolerance Framework as approved by the Board and incorporated into the Business Bank's ICAAP;
- Further progress was made with the alignment of processes to the requirements set out in RDARR;
- Business continuity management continues to be an area of focus;
- Enhancements to risk reporting, automation of selected regulatory reporting and the introduction of additional stress testing;
- Continual enhancement and expansion of the prudential management schedule, wherein risk-related ratios are monitored and reported monthly to the ALCO and the Board;
- Review of the application of the Principles for Sound Liquidity Risk Management and Supervision and applying conservative liquidity buffers;
- Enhanced liquidity evaluation, monitoring and management;
- Review of the application of the Principles for the Sound Management of Operational Risk;
- Various projects were undertaken during the current period by the Operational Risk team to improve efficiencies and mitigate risk; and
- Continuous improvement regarding cybersecurity and the implementation of artificial intelligence/machine learning technologies in the threat intelligence space. Completion of associated action plans is monitored by the Information Security Steering Committee.

ENTERPRISE-WIDE RISK MANAGEMENT

An Enterprise 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 on business activities and the related risks. The overall objective of enterprise risk management is to ensure an integrated and effective risk management framework where all risks are identified, quantified and managed 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, Senior Management, Risk, business line management, Finance and Control, Legal/Compliance, Treasury and Operations with support from IT. Independent oversight and validation by Internal Audit ensures a high standard of assurance across methodology, operational and process components of the Bank's risk and capital management processes.

RISK MANAGEMENT LIFE CYCLE AND PROCESS

All of the Bank's policies and procedure manuals are subject to ongoing review and are signed off at least annually 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 and 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 life cycle, defined as:

RISK IDENTIFICATION (AND COMPREHENSION)

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

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

Once risks have been identified, they need to be measured. Certain risks will 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 levels 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, the RCMC and the CREDCOM meet on a regular basis to collaborate on risk control and process review, to establish how much risk is acceptable and to decide how the Bank will remain 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, the RCMC and the 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 applicable 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 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 Risk Management Framework, which include:

Direct risks	Indirect risks
Credit risk	Strategic risk
Counterparty risk	Reputational 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 (including cyber) risk	Compliance risk
Investment risk	Market conduct 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 RCMC. Discretionary limits and authorities are, in turn and within laid-down parameters, delegated to line heads and line managers 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 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 risks are re-evaluated quarterly and any changes are approved by the RCMC. Business and operating units are integrally involved in the process of both risk identification and evaluation.

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 and 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 ALCO (which incorporates Capital Management), under the auspices of the RCMC, proactively evaluates and manages the capital requirements of the Bank, as determined by internal assessments and regulatory requirements. A comprehensive re-evaluation of the capital requirements under the ICAAP is regularly undertaken with consideration being given to all risks impacting 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 at least 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 and will remain a focus area during 2020 in line with RDARR requirements.

CREDIT RISK

Credit risk is the risk of suffering a financial loss should any of the Bank's clients or market counterparties fail to fulfil their contractual obligations to the Bank. Credit risk is a significant risk for the Bank and management carefully manages its exposure to credit risk. Credit risk management and control are centralised in a credit risk management team, which reports regularly to the Board of Directors.

The Bank offers a spread of banking products common to the banking industry. The core market focus is established small- to medium-sized businesses and commercial companies across a wide variety of industries, as well as private banking to respective entrepreneurs. Credit assessments are undertaken on consideration of a multitude of variables including company history and conduct, industry and experience, owner contribution and commitment, financial position and credit payment profiles, security available to mitigate risk and reputational considerations, among others.

Prospective deals and/or products, as well as requests for substantial increases in credit facilities, are considered at a daily credit consideration meeting. A formal and detailed application will then be submitted through the normal credit process if the Credit Consideration Committee considers the proposal desirable.

The Bank continues to adopt 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 automated on the Bank's workflow system. Levels of credit approval mandates are determined by the experience of the mandated individual, with dual or multiple sign-off on all material values. Mandates have also been accorded to frontline management within predetermined rules and parameters as approved by the RCMC, which approvals are evaluated and monitored by Credit on an ongoing basis.

The Bank's Credit Risk Strategy, which is contained within our Risk and Credit Risk policy manuals, is approved by the Bank's CREDCOM and ratified by the RCMC. Credit parameters and risk appetite levels are clearly defined and reflected in governing procedures and policies, which are reassessed from time to time to ensure relevance and competitiveness.

Dependent on the risk profile of the client across all portfolios or market segments, the risk inherent in the product offering and the track record and payment history of the client, varying types and levels of security are taken to mitigate credit-related risks. Unsecured lending is only considered for financially strong borrowers or for some facilities, such as overdrafts and credit cards within certain segments and portfolios.

The Bank does, however, have a small structured loan portfolio that includes an element of unsecured lending which is carefully managed within the agreed RCMC limits/parameters. The Bank is appropriately rewarded for the increased risk taken in this regard. This portfolio, however, currently carries minimal exposure.

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.

The Bank does not lend to foreign-registered companies but does provide banking to several locally registered companies that have foreign shareholding.

Monthly reporting to the ALCO includes reporting on large exposures. A portfolio analysis report is also prepared monthly and quarterly and presented to the RCMC analysing the performance and composure of the portfolio including client, geographic, segment and product concentration.

An ongoing weekly review is undertaken by the CREDCOM of all new and renewal proposals for lending in excess of R2 million (in aggregate). This meeting covers a wide variety of topics, including reporting on excess and arrear positions, security-related matters, possible changes in risk grades, the Bank's advances portfolio composure and performance, and any other relevant credit-related matters requiring specific mention or discussion. Adverse behavioural patterns, such as continual excesses above approved limits and arrears on loan facilities, are monitored closely by the Credit Department and are discussed at the weekly CREDCOM meeting with appropriate actions being taken.

Identified accounts with continued behavioural concerns and/or financial underperformance are monitored by way of monthly 'watch list' reporting. Monthly collection meetings are held and non-performing exposures are interrogated and monitored. To protect the Bank, prompt action is taken by senior internal stakeholders, including the CEO, on large defaults. This action has seen a good measure of historical success given our flat structure that drives agility.

Risk grading is applied for payment performance and account conduct and serves as the driver in a comprehensive impairment model for amortising debt and performance reviews for working capital facilities. The Bank's impairment and provisioning methodology is now aligned with the requirements of IFRS 9 as adopted in the previous financial period.

The following is highlighted for the period under review:

- A culture of learning and development continued through the period, with minimal staff attrition evident;
- The departmental structure, which is largely based on the market segments served, continued to prove beneficial with efforts ongoing to further identify risk and enhance client experience;
- Credit mandates were amended along with various other initiatives to build capacity and drive efficiencies, as well as to drive an improved client experience. These amendments were considered in line with the staff's technical competence and tenure within the role;
- The resilience of businesses to succeed and survive continues to be hampered by market conditions stemming in part from slow economic growth and the pressure on consumer spend. This has resulted in heightened monitoring and supervision of the portfolio, especially in terms of early warning management;
- Continued inroads have been made regarding the review of large exposure or high-risk security profiles and related risks, which is further bolstered by the Credit, Legal and Compliance area when monitoring covenants;
- Enhanced focus and continuous improvement of the Bank's workflow system deployed within the Credit Assessment areas, with enhancements ongoing; and
- The ongoing efforts regarding the automation of credit decision-making in the lower end of the Business Banking segment, where the deal values are low and the volumes high, will continue into 2020, with comprehensive analysis and testing expected to be amplified given current market conditions prior to eventual adoption and roll-out.

CREDIT RISK MEASUREMENT

Loans and advances (including loan commitments and guarantees)

The estimation of credit exposure for risk management purposes is complex and requires the use of models as the exposure varies with changes in market conditions, expected cash flows and time value of money. The assessment of credit risk of a portfolio of assets entails further estimations regarding the likelihood of defaults occurring in the associated loss ratios and of default correlations between counterparties. The Bank measures credit risk using PD, EAD and LGD.

CREDIT RISK GRADING

The Bank uses internal credit risk gradings that reflect its assessment of the PD of individual counterparties. The Bank's rating method comprises two main rating levels for instruments not in default (1 and 2) and three main default classes (3 to 5). The credit grades are calibrated such that the risk of default increases exponentially at each higher risk grade.

The following data is typically used to monitor the Bank's exposures:

- Payment record, including payment ratios and ageing analysis;
- Extent of utilisation of granted limit;
- Forbearances (both requested and granted);
- Changes in business, financial and economic conditions;
- Credit rating information supplied by external rating agencies (limited use thereof); and
- Information obtained by the periodic review of client files, including audited financial statements' review and market data, such as changes in the financial sector the client operates within, etc.

The table below lists the Bank's internal credit risk grades to external ratings:

Company's credit risk grade	Description
1	Low to fair risk
2	Increased credit risk
3	Monitoring
4	Doubtful
5	Impaired

SICR

The Bank monitors all financial assets, issued loan commitments and financial guarantee contracts that are subject to impairment requirements to assess whether there has been a SICR since initial recognition. If there has been a SICR, the Bank will measure the loss allowance based on lifetime rather than 12-month ECL.

The Bank considers a financial instrument to have experienced a SICR if the borrower is on the watch list and/or meets at least one of the following criteria:

- Significant adverse changes in business, financial and/or economic conditions in which the borrower operates;
- Actual or expected forbearance or restructuring;
- Actual or expected significant adverse change in operating results of the borrower;
- Significant change in collateral value which is expected to increase the risk of default; or
- Early signs of cash flow or liquidity problems such as delays in servicing of trade creditors and loans.

A backstop is applied and the financial instrument is considered to have experienced a SICR if the borrower is more than 30 days past due on contractual payments.

The Bank has not applied the low credit risk exemption for any financial instruments for the period ended 29 February 2020.

DEFINITION OF DEFAULT AND CREDIT-IMPAIRED ASSETS

Critical to the determination of ECL is the definition of default. The definition of default is used in measuring the amount of ECL and in the determination of whether the loss allowance is based on 12-month or lifetime ECL, as default is a component of the PD which affects the measurement of ECL.

The Bank defines a financial instrument as being in default, which is fully aligned with the definition of credit impaired, when it meets at least one of the following criteria:

QUANTITATIVE CRITERIA

The borrower is more than 90 days past due on its contractual payments.

QUALITATIVE CRITERIA

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. These are instances where, *inter alia:*

- The borrower is in long-term forbearance;
- The borrower is deceased and collectability is questionable or unknown;
- The borrower is insolvent;
- The borrower remains in unauthorised breach of financial covenant(s) that might have a negative impact on recoverability;
- An active market for the financial assets has disappeared because of financial difficulties;
- Concessions have been made by the lender relating to the borrower's financial difficulty or inability to meet contractual obligations (distressed restructure) and the borrower remains in breach of conceded terms; or
- It is becoming probable that the borrower may enter bankruptcy.

The criteria above have been applied to all financial instruments held by the Bank and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to the PD, EAD and LGD throughout the Bank's expected loss calculations.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a period of six consecutive months. This period of six months has been determined based on analysis that considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions and it is aligned with regulatory requirements.

ECL STAGE DETERMINATION

IFRS 9 outlines a three-stage model for impairment based on changes in credit quality since initial recognition as summarised below:

- A financial instrument that is not credit impaired on initial recognition is classified as Stage 1 and has its credit risk continuously measured by the Bank. Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months;
- If a SICR since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit impaired;
- If the financial instrument is credit impaired, the financial instrument is then moved to Stage 3; and
- Instruments in Stage 2 or 3 have their ECL measured based on ECL on a lifetime basis.

MEASURING ECL – EXPLANATION OF INPUTS, ASSUMPTIONS AND ESTIMATION TECHNIQUES

ECL is measured on either a 12-month (12M) or lifetime basis depending on whether a SICR has occurred since initial recognition or whether an asset is considered to be credit-impaired. A pervasive concept in measuring ECL, in accordance with IFRS 9, is that the measurement should consider forward-looking information. ECL is the discounted product of the PD, EAD and LGD defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation (as per Definition of default and credit-impaired above), either over the next 12 months (12M PD) or over the remaining lifetime (lifetime PD) of the obligation. The calculation is based on a hybrid Markov chain model.
- EAD is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest and expected drawdowns on committed facilities over the next 12 months (12M EAD) or over the remaining lifetime (lifetime EAD). The Bank's modelling approach for EAD reflects expected changes in the balance outstanding over the lifetime of the loan exposure that is permitted by the current contractual terms, such as amortisation profiles, changes in utilisation of undrawn commitments and credit mitigation actions taken before default.
- LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the Bank expects to receive, taking into account cash flows from any collateral. The LGD models for secured assets consider forecasts of future collateral valuation taking into account sale discounts, time to realisation of collateral, cross-collateralisation, seniority of claim, cost of realisation of collateral and cure rates (i.e. exit from non-performing status). LGD models for unsecured assets consider time of recovery, recovery rates and seniority of claims. The calculation is on a discounted cash flow basis, where the cash flows are discounted by the original effective interest rate of the loan.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure. These three components are multiplied and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted to the reporting date. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

The lifetime PD is developed by applying a maturity profile to the current 12-month PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and credit grade band. This is supported by historical analysis.

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type.

- For amortising products and bullet repayment loans, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis.

- For revolving products, the EAD is predicted by adding a credit conversion factor to the current drawn balance, which allows for the expected drawdown of the remaining limit by the time of default.

The 12-month and lifetime LGDs are determined based on factors that impact the recoveries made post-default.

- For secured products, this is primarily based on collateral type, projected collateral values and time to recovery.
- For unsecured products, LGDs are typically set at product level due to the limited differentiation in recoveries achieved across different borrowers.

Assumptions underlying the ECL calculation, such as how the maturity profile of the PDs change, etc., are monitored and reviewed periodically. There have been no significant changes in estimation techniques or significant assumptions made during the reporting period.

FORWARD-LOOKING INFORMATION INCORPORATED IN THE ECL MODELS

The Bank performed a statistical analysis of the correlation between the default rates and various macro-economic factors and indices thereof. A full statistical model concluded that it would not be appropriate to incorporate macro-economic forecasts into the determination of the ECL without incurring significant expenses due to the lack of adequate correlation in the performance of the Bank's loans and advances relative to macro-economic indicators or an index of these indicators. The Bank will continue to monitor these correlations and will incorporate forward-looking information into the ECL model once more information is included in the observation period to take cognisance of economic cycles and the relative impact they have on the performance of the Bank's loans and advances.

The current risk assessment framework includes stringent credit risk assessments that are performed during the lifetime of the exposures and it is believed that these will incorporate sufficient forward-looking assessment. Additional ECL are recognised by way of a management overlay after significant expert consultation with executive management and seasoned credit professionals.

In addition to the specific management overlay and in lieu of macro-economic forward-looking indicators, the following parameters were applied to the model and resulted in an additional impairment of R13 million:

- Increased time to recover for all collateral types;
- Increased PDs across the various product types; and
- Additional haircuts on residential and commercial properties (based on the values of the properties). These haircuts were applied to all collateral in the portfolio and not only on the non-performing portion of the book.

THE IMPACT OF COVID-19 ON MACRO-ECONOMIC VARIABLES

Management considered information available as at 29 February 2020 and the potential impact of COVID-19 and, in response, applied the following sensitivities:

- Increased PDs by an additional 5% for all exposures;
- Increased the estimated time to recover assumptions on specified collateralised assets;
- Re-evaluated anticipated recoveries on collateral currently under collection; and
- Identified specific industries where clients might more likely be affected to estimate the probabilities of these clients migrating to Stage 2 lifetime ECL.

CREDIT RISK EXPOSURE

MAXIMUM EXPOSURE TO CREDIT RISK – FINANCIAL INSTRUMENTS SUBJECT TO IMPAIRMENT

The following table provides an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amounts of the financial assets below also represent the Bank's maximum exposure to credit risk on each of these assets.

	Loans and advances R'000	Committed undrawn facilities R'000	Other R'000	Total R'000
2020				
Current accounts	**2 129 084**	**–**	**–**	**2 129 084**
Credit cards	**49 184**	**86 070**	**–**	**135 254**
Mortgage loans	**5 406 641**	**217 312**	**–**	**5 623 953**
Instalment sales and leases	**692 710**	**–**	**–**	**692 710**
Structured loans	**37 792**	**–**	**–**	**37 792**
Medium-term loans	**1 192 167**	**–**	**–**	**1 192 167**
Negotiable securities	**–**	**–**	**877 407**	**877 407**
Cash and cash equivalents	**–**	**–**	**4 124 403**	**4 124 403**
Guarantees	**–**	**–**	**636 618**	**636 618**
Letters of credit	**–**	**–**	**2 674**	**2 674**
	9 507 578	**303 382**	**5 641 102**	**15 452 062**

	Loans and advances R'000	Committed undrawn facilities R'000	Other R'000	Total R'000
2018				
Current accounts	2 236 794	–	–	2 236 794
Credit cards	44 022	94 475	–	138 497
Mortgage loans	4 991 393	185 407	–	5 176 800
Instalment sales and leases	913 193	–	–	913 193
Structured loans	134 126	–	–	134 126
Medium-term loans	1 179 997	–	–	1 179 997
Negotiable securities	–	–	790 822	790 810
Cash and cash equivalents	–	–	3 123 729	3 123 729
Guarantees	–	–	1 003 723	1 003 723
Letters of credit	–	–	8 213	8 213
	9 499 525	279 882	4 926 487	14 705 894

CREDIT QUALITY OF INVESTMENTS

The following table provides an analysis of the international long-term credit ratings of investments by Moody's Investors Service:

	Aaa to Aa3 R'000	A1 to A3 R'000	Baa1 to Baa3 R'000	Not rated R'000	ECL R'000	Total carrying amount R'000
2020						
Cash on hand	**–**	**–**	**24 806**	**–**	**–**	**24 806**
Bank balances[(1) (3)]	**741 140**	**142 182**	**2 969 694**	**–**	**(161)**	**3 852 855**
Central bank balances[(2)]	**–**	**–**	**246 581**	**–**	**–**	**246 581**
Treasury bills	**–**	**–**	**877 407**	**–**	**(24)**	**877 383**
Other receivables	**–**	**–**	**176 645**	**230 005**	**–**	**406 650**
Derivative assets	**–**	**–**	**–**	**31 727**	**–**	**31 727**
	741 140	**142 182**	**4 295 133**	**261 732**	**(185)**	**5 440 002**
2018*						
Cash on hand	–	–	29 981	–	–	29 981
Bank balances[(1) (3)]	572 661	104 354	542 443	–	(125)	1 219 333
Central bank balances[(2)]	–	–	309 252	–	–	309 252
Treasury bills	–	–	765 022	–	(12)	765 010
Government stock	–	–	25 800	–	–	25 800
Money market funds[(3)]	–	–	1 565 038	–	–	1 565 038
Other receivables	–	–	284 052	208 026	–	492 078
Derivative assets	–	–	–	17 903	–	17 903
	572 661	104 354	3 521 588	225 929	(137)	4 424 395

* *Additional disclosure in respect of the prior year has been included.*

(1) *The bank balances were with 26 institutions (2018: 27), with the maximum exposure to one institution being R2 113 million (2018:R467 million).*

(2) *All central bank balances are with the SARB and include the mandatory reserve deposit requirement.*

(3) *Where a financial institution does not have a Moody's Investors Service credit rating, the rating of the country in which the company is domiciled is used.*

COLLATERAL AND OTHER CREDIT ENHANCEMENTS

The Bank employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Bank has internal policies on the acceptability of specific classes of collateral or credit risk mitigation. The Bank prepares a valuation of the collateral obtained as part of the loan origination process and this assessment is reviewed periodically. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets, such as premises, inventory and accounts receivable; and
- Charges over financial instruments, such as debt securities.

Longer-term finance and lending to corporate entities are generally secured, while credit card facilities are generally unsecured. The Bank's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Bank since the prior period.

A portion of the Bank's financial assets, originated by the mortgage business, has sufficiently low loan-to-value ratios, which results in no loss allowance being recognised in accordance with the Bank's ECL model. The Bank closely monitors collateral held for financial assets considered to be credit impaired, as it becomes more likely that the Bank will take possession of collateral to mitigate potential credit losses. Financial assets that are credit impaired, and related collateral held to mitigate potential losses, are detailed in note 6.11 of the notes to the financial statements.

LOSS ALLOWANCE

The loss allowance recognised in the period could be impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3, due to financial instruments experiencing significant increases (or decreases) of credit risk, or becoming credit impaired in the period, and the consequent step up (or step down) between 12-month and lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, releases for financial instruments derecognised in the period and write-offs of allowances related to assets that were written off during the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions (not applicable during 2018); and
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis.

The changes in the loss allowance between the beginning and the end of the financial period due to these factors are detailed in note 6.5 to the financial statements.

MODIFICATION OF FINANCIAL ASSETS

The Bank sometimes modifies the terms of loans provided to clients due to commercial renegotiations or for distressed loans to ensure maximum recovery.

Such restructuring activities include extended payment term arrangements and payment holidays. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Restructuring is most commonly applied to term loans.

The risk of default of such assets after modification is assessed at the reporting date and compared with the risk under the original terms at initial recognition, when the modification is not substantial and does not result in derecognition of the original asset. The Bank may determine that the credit risk has significantly improved after restructuring so that the assets are moved from Stage 3 or Stage 2 (lifetime ECL) to Stage 1 (12-month ECL). This is only the case for assets that have performed in accordance with the new terms for six consecutive months or more.

WRITE-OFF POLICY

Loans and debt securities are written off when the Bank has no reasonable expectation of recovering the financial asset (either in its entirety or a portion thereof). This is the case when the Bank determines that the borrower does not have assets or sources of income that could generate enough cash flows to repay the amounts subject to the write-off. A write-off constitutes a derecognition event. The Bank may apply enforcement activities to financial assets written off. Recoveries resulting from the Bank's enforcement activities will result in a reduction of the impairments provision.

PRESENTATION OF ALLOWANCE FOR ECL IN THE STATEMENT OF FINANCIAL POSITION

Loss allowances for ECL are presented in the statement of financial position as follows:

- For financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets; and
- The Bank presents a combined loss allowance for both components where a financial instrument includes both a drawn and an undrawn component and the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component. The combined amount is presented as a deduction from the gross carrying amount of the drawn component.

OPERATIONAL RISK

Operational risk is defined as the risk of loss from inadequate or failed internal processes, people and systems or from external events. Operational risks faced by the Bank are extensive and include, among others, 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 reputation risk, as well as the risk of financial loss.

The aim of operational risk management is to enhance the level of risk maturity across the Bank by implementing and embedding risk-based control identification and assessments, challenging the *status quo* with regard to operational controls 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 upskilling 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;
- Review and amendment of appropriate risk mitigation actions in line with the Bank's risk appetite and tolerances as approved by the Board;
- Ongoing improvements to the disaster recovery and business continuity plans, including conducting a variety of simulation exercises in critical operational 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 programme;
- Ongoing review of the Bank-wide risk and 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;
- Embarking on a programme to comply with the requirements of BCBS 239 to ensure accurate, complete, consistent and timely risk information. The Board is fully supportive of this project and has committed human and financial resources;
- Limiting access to systems and enforcing strong password controls;
- Embedding combined assurance across the Bank to maximise risk management activities and minimise duplication of efforts; and
- Managing a comprehensive insurance programme to safeguard the Bank's financial and non-financial assets.

Disaster recovery and business continuity management facilities are outsourced to specialist service providers.

The Bank further benchmarks itself and stays abreast of developments with regard to operational risk by actively participating as a member of the BASA operational risk forum as well as of industry working groups tasked with investigating and making recommendations to BASA on topical issues.

The Bank subscribes to the Principles for the Sound Management of Operational Risk.

TECHNOLOGY RISK

Information security and sound IT controls are critical disciplines within banking businesses that require focus and attention in order to maintain processes and technologies in line with business risk appetite and the ever-changing threat landscape.

An IT governance and information security review was performed on the Business Bank by external consultants to determine gaps and maturity levels with regard to information security protocols. This review used the ISF SoGP 2018 as the best practice framework against which controls were assessed. Using this framework allows for a health check benchmark against the ISF SoGP 2018, as well as easy reporting in ISO 27002 and CoBit 5 views which was a specific Business Bank requirement.

The following key milestones were achieved during the period:

- Successful submission in respect of the SWIFT client security programme;
- Successfully completed multiple disaster recovery and business continuity tests;
- Improved the maturity of the risk management artefacts and refreshed risk management principles within technology;
- Deployed and implemented the certificate management programme, to effectively govern the on-boarding, renewal and resignation of certificates;
- Deployed rogue device monitoring to identify third-party or unauthorised assets on the Mercantile network;
- Implementation of the new backup technology stack to allow cost-effective backup and recovery processes;
- Reviewed the current hardware security module environment and re-established the key components. Worked on re-establishing the disaster recovery component for the hardware security module; and
- Successfully on-boarded the Head of Data Governance to start working on the data strategy for the Bank.

MARKET RISK

Market risk is characterised by the adverse correlation in market prices or rates relative to positions taken. It entails re-evaluating financial instruments in line with prevailing market prices or rates. Market risk can be quantified as the potential change in the value of the banking book, as a result of volatility to which the financial environment is susceptible, to between the present and a future point in time. The Board is responsible for determining market risk appetite and tolerance thresholds, per the Business Bank risk appetite framework, which are reviewed at least annually or depending on prevailing market conditions.

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 the RCMC will have to evaluate and approve such action. The Trading Committee will ensure that the Bank is sensibly positioned, taking into account agreed limits, policies, prevailing market conditions, available liquidity and the risk-reward trade-off, mainly in respect 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 event of a limit violation, the ALM forum records this and it is immediately corrected and reported to the ALCO.

The Bank does not perform a detailed sensitivity analysis on the potential impact of a change in exchange rates on a daily basis as the Bank does not currently have any proprietary trading positions. The impact of changes in foreign currency client positions is, however, modelled to take cognisance of credit risks associated with volatility in foreign currency exchange rates, with the purpose of covering adverse positions by calling for initial and variation margins. A detailed sensitivity analysis is performed for interest rate and liquidity risk (described on pages 59 to 63).

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. Controls are in place to monitor foreign exchange exposures on a real-time basis through the Bank's Treasury system. Various conservative prudential risk limits are in place and associated exposures relating thereto are reported to the ALCO, the RCMC and the Board on a regular basis.

FOREIGN CURRENCY RISK

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

The Bank has conservative net open foreign currency position limits that are well below the limits allowed by the SARB. For the period under review, the highest net open position recorded for any single day was R20.1 million (2018: R18.2 million). An adverse movement in the exchange rate of 10% would reduce the Bank's income by R2.0 million (2018: R1.8 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
2020					
Total foreign exchange assets	**783 550**	**151 262**	**97 505**	**47 377**	**1 079 694**
Total foreign exchange liabilities	**(696 110)**	**(97 790)**	**(57 301)**	**(32 501)**	**(883 702)**
Commitments to purchase foreign currency	**354 213**	**255 816**	**64 351**	**21 648**	**696 028**
Commitments to sell foreign currency	**(434 987)**	**(304 612)**	**(106 813)**	**(33 372)**	**(879 784)**
Year-end effective net open foreign currency positions	**6 666**	**4 676**	**(2 258)**	**3 152**	**12 236**
2018					
Total foreign exchange assets	606 246	110 126	69 526	26 055	811 953
Total foreign exchange liabilities	(483 600)	(91 035)	(51 018)	(24 983)	(650 636)
Commitments to purchase foreign currency	582 286	156 522	29 283	28 987	797 078
Commitments to sell foreign currency	(696 194)	(173 122)	(46 328)	(28 417)	(944 061)
Year-end effective net open foreign currency positions	8 738	2 491	1 463	1 642	14 334

INTEREST RATE RISK

Interest rate risk is the impact on net interest earnings and 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 clients. Interest margins may increase as a result of such changes, but may reduce or create losses in the event that unexpected adverse movements occur. The ALM forum monitors interest rate repricing on a daily basis and reports back to the ALCO, the RCMC and the Board.

The Bank is exposed to interest rate risk as it takes deposits from clients at both fixed and variable 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 the management of interest rate risk is to ensure a higher degree of interest rate margin stability and lower interest rate risk over an interest rate cycle. This is achieved by hedging material exposures and by not allowing any intentional proprietary interest rate positions. Under interest rate swap contracts, the Bank agrees to exchange the difference between fixed and variable 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 or receive 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 repricing characteristics of two floating rates, such as the South African prime rate and the three-month JIBAR.

To measure interest rate risk, the Bank aggregates interest rate-sensitive assets and liabilities into defined time bands, in accordance with the respective interest repricing 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 the RCMC on a regular basis.

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

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 or 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 regularly to the ALCO and the Board.

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 would increase by R8.6 million or decrease by R13.7 million, respectively (2018: increase/decrease by R11.5 million/R18.4 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 following summarises the Bank's exposure to interest rate risk. Assets and liabilities are included at carrying amounts, categorised by the earlier of contractual repricing or maturity dates and also indicate their effective interest rates at period-end. The repricing profile indicates that the Bank remains asset-sensitive, although to a lesser extent than previously, as interest-earning assets reprice sooner than interest-paying liabilities before and after derivative hedging activities. Thus, future net interest income remains vulnerable to a decrease in market interest rates.

	Up to 1 month R'000	1 to 3 months R'000	3 to 12 months R'000	1 to 5 years R'000	Non-interest-sensitive R'000	Total R'000	Effective interest rate %
2020							
ASSETS							
Cash and cash equivalents	2 783 407	–	–	–	1 340 835	4 124 242	5.2
Derivative financial instruments	–	–	–	–	31 727	31 727	–
Negotiable securities	89 925	147 670	639 788	–	–	877 383	7.5
Loans and advances	8 976 517	–	–	–	283 927	9 260 444	10.6
Other accounts receivable	–	–	–	–	406 650	406 650	–
Non-current assets held-for-sale	–	–	–	–	17 169	17 169	–
Other investments	–	–	–	–	1 139	1 139	–
Interest in subsidiaries	65 562		–	–	107 193	172 755	–
Investment in debt securities	–	155 761	–	–	–	155 761	16.5
Property and equipment	–	–	–	–	34 427	34 427	–
Right-of-use asset	–	–	–	–	54 084	54 084	–
Intangible assets	–	–	–	–	82 936	82 936	–
Current tax receivable	–	–	–	–	4 672	4 672	–
Deferred tax assets	–	–	–	–	49 347	49 347	–
Total assets	**11 915 411**	**303 431**	**639 788**	**–**	**2 414 106**	**15 272 736**	
EQUITY AND LIABILITIES							
Other accounts payable	–	–	–	–	344 076	344 076	–
Derivative financial instruments	–	–	–	–	30 005	30 005	–
Provisions and other liabilities	–	–	–	–	73 502	73 502	–
Deposits	9 164 450	118 383	317 266	102 497	2 455 225	12 157 821	5.6
Lease liability	–	–	–	–	58 515	58 515	–
Long-term funding	–	–	–	–	–	–	10.3
Total equity	–	–	–	–	2 608 817	2 608 817	–
Total equity and liabilities	**9 164 450**	**118 383**	**317 266**	**102 497**	**5 570 140**	**15 272 736**	
Financial position interest sensitivity gap	**2 750 961**	**185 048**	**322 522**	**(102 497)**		**3 156 034**	

	Up to 1 month R'000	1 to 3 months R'000	3 to 12 months R'000	1 to 5 years R'000	Non-interest-sensitive R'000	Total R'000	Effective interest rate %
2018							
ASSETS							
Cash and cash equivalents	2 029 505	–	–	–	1 094 099	3 123 604	5.6
Derivative financial instruments	–	–	–	–	17 903	17 903	–
Negotiable securities	149 668	341 074	274 279	25 801	(12)	790 810	9.4
Loans and advances	9 499 497	–	–	–	(176 800)	9 322 697	10.7
Other accounts receivable	–	–	–	–	492 078	492 078	–
Non-current assets held-for-sale	–	–	–	–	22 500	22 500	–
Other investments	–	–	–	–	8 016	8 016	–
Interest in subsidiaries	2 077		–	–	107 194	109 271	–
Investment in debt securities	–	151 629	–	–	–	151 629	16.6
Property and equipment	–	–	–	–	47 847	47 847	–
Intangible assets	–	–	–	–	128 394	128 394	–
Deferred tax assets	–	–	–	–	42 961	42 961	–
Total assets	11 680 747	492 703	274 279	25 801	1 784 180	14 257 710	
EQUITY AND LIABILITIES							
Other accounts payable	–	–	–	–	419 125	419 125	–
Derivative financial instruments	–	–	–	–	15 437	15 437	–
Current tax payable	–	–	–	–	5 726	5 726	–
Provisions and other liabilities	–	–	–	–	136 381	136 381	–
Deposits	7 666 331	237 036	519 699	62 268	2 005 953	10 491 287	5.7
Long-term funding	–	742 880	–	–	–	742 880	10.6
Total equity	–	–	–	–	2 446 874	2 446 874	–
Total equity and liabilities	7 666 331	979 916	519 699	62 268	5 029 496	14 257 710	
Financial position interest sensitivity gap	4 014 416	(487 213)	(245 420)	(36 467)		3 245 316	

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 defined 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 the RCMC on a regular basis. 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:

- Contractual maturity mismatches analysis;
- Monitoring of daily cash flow movements and requirements, including daily settlements and collateral management processes;
- Maintenance of increased levels of readily available, high-quality liquid assets (in excess of the statutory requirements), as well as strong financial position liquidity ratios;
- An assumptions-based sensitivity analysis to assess potential cash flows at risk;
- Graphical analysis of client deposits trend line;
- Management of concentration risk (undue reliance on any single counterparty or counterparty Business Bank, sector, market, product, instrument, currency and tenor);
- Maintenance of sources of funding for contingency funding needs;
- Monitoring of daily cash flow movements and requirements, including daily settlements and collateral management processes;
- Targeting of a diversified funding base to avoid undue concentrations by investor, market source and maturity;
- Creation and monitoring of prudential liquidity risk limits;
- Maintenance of an appropriate mix of term funding; and
- Redefinition of stress testing in line with prudential ratios and possible regulatory requirements in respect of 10-day liquid asset holdings (stressed to 30 days).

Overall, the Bank's key liquidity risk metrics, which have been formulated to achieve a prudent liquidity profile, were maintained at acceptable levels. Through 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 subscribes to the Bank of International Settlement's Principles for Sound Liquidity Risk Management and Supervision. Overall, the Bank's liquidity position remains strong.

Macro-economic conditions continue to impede growth in advances and deposits as the South African banking sector is characterised by certain structural features, such as a low discretionary propensity to save and a higher degree of contractual savings with institutions such as pension funds, provident funds and asset management services. The Bank was successful in raising commercial, retail and wholesale funding, while ensuring compliance with the Basel III liquidity requirements.

There were no significant changes to the way in which the Bank manages and measures liquidity risk. The Bank is adequately funded and able to meet all of its current and future obligations.

The following table summarises the 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	Mismatch R'000
2020			
Maturing up to one month	**6 758 559**	**9 616 521**	**(2 857 962)**
Maturing between one and three months	**175 057**	**1 112 244**	**(937 187)**
Maturing between three and six months	**435 744**	**205 268**	**230 476**
Maturing between six months and one year	**539 923**	**140 617**	**399 306**
Maturing after one year	**6 667 761**	**1 589 269**	**5 078 492**
Non-contractual	**695 692**	**–**	**695 692**
	15 272 736	**12 663 919**	**2 608 817**
2018			
Maturing up to one month	6 062 632	8 040 900	(1 978 268)
Maturing between one and three months	370 555	1 192 592	(822 037)
Maturing between three and six months	375 281	202 478	172 803
Maturing between six months and one year	106 887	328 467	(221 580)
Maturing after one year	7 160 220	2 046 399	5 113 821
Non-contractual	182 135	–	182 135
	14 257 710	11 810 836	2 446 874

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

	Up to 1 month R'000	1 to 3 months R'000	4 to 6 months R'000	7 to 12 months R'000	Over 1 year R'000
2020					
Deposits	**9 185 169**	**1 103 194**	**196 986**	**132 693**	**1 692 344**
Long-term funding	**–**	**–**	**–**	**–**	**–**
Derivative financial instruments	**11 656**	**11 646**	**6 550**	**154**	**–**
Other accounts payable	**344 076**	**–**	**–**	**–**	**–**
Lease liability	**2 909**	**5 555**	**8 157**	**15 581**	**29 267**
Guarantees, letters of credit and committed undrawn facilities	**942 674**	**–**	**–**	**–**	**–**
	10 486 484	**1 120 395**	**211 693**	**148 428**	**1 721 611**
2018					
Deposits	7 473 522	1 196 187	206 128	348 715	1 419 241
Long-term funding	–	–	–	–	1 020 382
Derivative financial instruments	6 860	6 265	2 236	76	–
Other accounts payable	419 125	–	–	–	–
Guarantees, letters of credit and committed undrawn facilities	1 291 818	–	–	–	–
Operating lease commitments	2 639	5 234	7 750	15 152	60 230
	9 193 964	1 207 686	216 114	363 943	2 499 853

CAPITAL MANAGEMENT

The Bank is subject to specific 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 ICAAP 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 signal. Despite the regulations allowing the Bank to consider different tiers of capital, the capital of the Bank consists almost entirely of Tier 1 capital. The Bank remains well capitalised 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 surplus capital held. The dividend policy remains insignificant in relation to earnings and 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 assuring itself that the Bank will fulfil the solvency and liquidity test immediately after completing the distribution.

The level of capital for the Bank is as follows:

	Unaudited 2020 R'000	Audited 2018 R'000
Risk-weighted assets – banking book		
Credit risk	**9 301 860**	9 917 993
Operational risk	**1 908 192**	1 648 930
Market risk	**14 500**	14 338
Equity	**1 139**	8 016
Other assets	**974 106**	1 024 274
	12 199 797	12 613 551
Net qualifying capital and reserves		
Tier 1 capital	**2 494 187**	2 254 121
Share capital and share premium	**1 483 300**	1 483 300
Retained earnings	**1 093 416**	883 415
Other reserves	**(4 802)**	127
Less: Deductions	**(77 727)**	(112 721)
Tier 2 capital	**101 468**	87 499
General allowance for ECL	**101 468**	87 499
	2 595 655	2 341 620
Capital adequacy ratio (%)	**21.3**	18.6
Tier 1 capital (%)	**20.5**	17.9
Tier 2 capital (%)	**0.8**	0.7

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