FIRSTRAND
Banking Group

Supplementary information

for the year ended 30 June 2003

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Additional financial information

Advances

R million	2003 Post-AC133	2003 Pre-AC133	2002 Actual	% change pre-AC133 on Actual
Gross advances				
Total advances	**193 526**	**194 568**	180 235	8.0
Less: Contractual interest suspended	**(613)**	**(613)**	(725)	(15.4)
Gross advances	**192 913**	**193 955**	179 510	8.0
Less: Impairments	**(3 302)**	**(4 437)**	(4 365)	1.7
Net advances	**189 611**	**189 518**	175 145	8.2
Rand and non-Rand denominated advances.				
All non-Rand denominated advances (USD)	**4 416**	**4 514**	3 630	24.4
At exchange rate applicable (R: USD)	**7.56**	**7.56**	10.31	(26.7)
Non-Rand denominated advances (R)	**33 383**	**34 128**	37 425	(8.8)
Rand denominated advances	**159 530**	**159 827**	142 085	12.5
Gross advances	**192 913**	**193 955**	179 510	8.0
Geographical split				
SA banking operations	**164 220**	**164 408**	150 248	9.4
International banking operations	**9 606**	**9 606**	11 733	(18.1)
US Corporate debt (CDO advances)	**6 620**	**7 366**	9 599	(23.3)
African banking operations	**7 340**	**7 340**	6 275	17.0
SA non-banking operations	**5 127**	**5 235**	1 655	>100.0
Gross advances	**192 913**	**193 955**	179 510	8.0
Product split				
Overdrafts and managed accounts	**41 261**	**41 261**	34 397	20.0
Card loans	**4 613**	**4 613**	3 942	17.0
Instalment finance	**25 726**	**25 726**	21 592	19.1
Lease payments receivable	**11 799**	**11 799**	9 514	24.0
HomeLoans	**53 257**	**53 257**	48 568	9.7
US Corporate debt	**6 620**	**7 366**	9 599	(23.3)
Other advances	**49 637**	**49 933**	51 898	(3.8)
Gross advances	**192 913**	**193 955**	179 510	8.0

Pre-AC133

Advances up 8.2% on:

- Strong growth in the FNB HomeLoans and WesBank books
- Slower than expected run-off in the NBS and Saambou books
- Decline in advances to corporates
- Decline in Rand value of Dollar denominated advances

Rand denominated advances have grown by 12.5%.

US Dollar denominated advances grew by 24.4% in real terms, but shrunk by 8.8% in Rand terms.

African subsidiaries continued their strong growth trend.

Post-AC133

Decrease in carrying value of advances with the application of fair value accounting to available for sale and trading assets.

Non-performing loans and impairment of advances

Non-performing loans

Movement in non-performing loans.

R million	2003 Post-AC133	2003 Pre-AC133	2002 Actual	% change pre-AC133 on Actual
Non-performing loans	**4 620**	**4 620**	5 305	(12.9)
Add: Present value adjustment[1]	**360**	**–**	–	–
Less: Recoverable amount	**(92)**	**(92)**	(1 014)	(91.0)
Net credit exposure	**4 888**	**4 529**	4 291	5.5
Less: Security	**(1 579)**	**(1 579)**	(1 266)	24.7
Less: Contractual interest suspended	**(613)**	**(613)**	(725)	(15.4)
Residual risk	**2 696**	**2 336**	2 300	1.6
Specific impairments[1]	**2 696**	**2 336**	2 300	1.6
Portfolio impairments[2]	**606**	**–**	–	–
General provision[2]	**–**	**2 101**	2 065	1.7
Total impairments	**3 302**	**4 437**	4 365	1.7
Fair value impairments	**378**	**–**	–	–
General risk reserve[2]	**1 117**	**–**	–	–
Total impairments and reserves	**4 797**	**4 437**	4 365	1.7
Total advances	**193 526**	**194 568**	180 235	8.0
Less: Contractual interest suspended	**(613)**	**(613)**	(725)	(15.4)
Gross advances	**192 913**	**193 955**	179 510	8.0
Less: Impairments	**(3 302)**	**(4 437)**	(4 365)	1.7
Net advances	**189 611**	**189 518**	175 145	8.2
General provision analysis				
Opening balance	**2 065**	**2 065**	1 346	53.4
Less: Exchange adjustments	**–**	**(102)**	65	(>100.0)
New and increased provisions	**138**	**138**	436	(68.3)
Acquisitions	**–**	**–**	218	(100.0)
Transfer to General Risk Reserve				
– opening balance	**(2 065)**	**–**	–	–
– current period	**(138)**	**–**	–	–
	–	**2 101**	2 065	1.7

1. AC133 requires an estimation of the time to recovery of the recoverable amount. The AC133 impairment calculation methodology takes the period to recovery into account in determining the amount of the impairment. The impairment calculation is a discounted cash flow method, which was not previously the case. The combination of the above results in an increase in specific impairments. Further details on these changes are set out in the section "Changes in accounting policy" on pages 14 to 16 of this booklet.

2. The present value calculation applied in AC133 requires that all future cash flows, including future interest payments, be taken into account in the creation of credit risk impairments. To the extent that the risk pricing methodology of an enterprise is appropriate and the current expectations of recoverable cash flows are consistent with the initial expectations, then the risk premium inherent in future interest flows should compensate for the risk inherent in the underlying capital amount relating to expected future losses. The specific provision is supplemented where market conditions change and as a result an entity's expectation of future cash flows change and it is not possible to reprice sufficiently quickly to compensate for the change in risk. As a result, the previous general provision, which pre-AC133 took account of the inherent risk in the book without taking the risk premium charged into account, is no longer permitted under AC133. To the extent that the Banking Group is of the opinion that there are losses inherent in the performing portfolio of advances, which will only be identified in the future, or that insufficient data exists to reliably determine whether such losses exist, a portfolio impairment has been created. In line with standard industry practice, an impaired capital reserve has been created in terms of the requirements of the South African Reserve Bank ("SARB") reporting.

Impairments of advances

Total impairment levels, the current period transfer of the general provision to the general risk reserve in equity, and the resultant total impairment levels on a post-AC133 basis.

%	2003 Post-AC133	2003 Pre-AC133	2002 Actual
Non-performing loans as a percentage of gross advances	**2.4**	**2.4**	3.0
Specific impairments as a percentage of non-performing loans	**58.5**	**51.3**	43.4
Specific impairments as a percentage of gross advances	**1.4**	**1.2**	1.3
General provision as a percentage of gross advances	**–**	**1.1**	1.2
Portfolio impairments	**0.3**	**–**	–
Fair value impairments	**0.2**	**–**	–
General Risk Reserve	**0.6**	**–**	–
Total impairments as a percentage of gross advances	**2.5**	**2.3**	2.5
Total impairments as a percentage of non-performing loans	**102.9**	**96.0**	82.3
Total impairments as a percentage of residual risk	**176.9**	**187.1**	189.8

Income statement charge

In accordance with the requirements of AC133, numerous changes have been made to the way banks calculate impairments for bad debts. In general, these changes will lead to a reduction in the bad debt charge reflected in the income statement, although the annual charge will also become more volatile.

The table below sets out more details with regard to difference in the current period charge:

	Post-AC133	Pre-AC133
Specific impairments for bad debts	1 229	1 229
Time value of money adjustment against recoverable amounts	116	–
Adjustments for change in recognition of bad debts	64	–
Total specific impairments for bad debts	1 409	1 229
Portfolio impairments for bad debts	69	–
General provisions for bad debts	–	138
Total bad debt charge for the current period	1 478	1 367

Pre-AC133

Non-performing loans declined by 12.9%, predominantly as a result of:

- Improved corporate performance with the successful workout of certain large exposures
- Decline in non-performing US corporates and
- General improvement in retail advances

Non-security recoverables declined with the decrease in corporate non-performing loans.

Additional write-offs in respect of the following negatively impacted on current bad debts:

- R107 million in respect of card loans
- R130 million in respect of micro loans

Provisions remain conservative.

Post-AC133

Decrease in total impairments attributed to:

- Increase to specific impairments due to the implementation of present value methods
- Increase due to the introduction of portfolio impairments
- Decrease due to the reversal of general provisions
- Re-allocation of portion of old general provision to fair value provision for US corporate exposures

Increase in specific impairments for changes in recognition mandated by the introduction of AC133.

Non-interest revenue

R million	2003 Post-AC133	2003 Pre-AC133	2002 Actual	% change pre-AC133 on Actual
Non-interest revenue drivers				
Transactional income	**5 735**	**5 735**	5 132	11.7
Trading income	**1 583**	**1 447**	1 772	(18.3)
Investment income	**118**	**118**	494	(76.1)
Other income	**219**	**218**	373	(41.6)
Total non-interest income	**7 655**	**7 518**	7 771	(3.3)
Translation (losses)/gains	**(532)**	**(605)**	548	(>100.0)
Non-interest income	**7 123**	**6 913**	8 319	(16.9)
Transactional income				
Banking fee and commission income	**5 116**	**5 116**	4 168	22.7
Knowledge-based fee and commission income	**303**	**303**	734	(58.7)
Non-banking fee and commission income	**316**	**316**	230	37.4
Transactional income	**5 735**	**5 735**	5 132	11.7
Trading income				
Foreign exchange trading	**731**	**731**	1 024	(28.6)
Treasury trading operations	**852**	**716**	748	(4.3)
Trading income	**1 583**	**1 447**	1 772	(18.3)
Other income includes the performance of Ansbacher (UK), which incurred trading losses on its exposure to US Corporate and emerging market debt portfolios.				
Foreign exchange trading				
Domestic-based currency trading	**772**	**772**	943	(18.1)
Foreign-based currency trading	**(41)**	**(41)**	81	(>100.0)
Foreign exchange trading	**731**	**731**	1 024	(28.6)
Investment income				
(Loss) on realisation of investment banking assets	**(1)**	**(1)**	(14)	(92.9)
Dividends received	**214**	**215**	437	(50.8)
Income from associated companies	**494**	**484**	368	31.5
Investment income	**707**	**698**	791	(11.8)
Unrealised loss on assets held against employee liabilities	**(95)**	**(95)**	71	(>100.0)
Gross investment income	**612**	**602**	862	(30.2)
Share of income from associated companies disclosed separately	**(494)**	**(484)**	(368)	31.5
Net investment income disclosed	**118**	**118**	494	(76.1)

Other income

Other income includes property rentals, insurance brokerage and profit or losses on sale of plant and equipment.

Pre-AC133

Transactional income

Banking fee and commission income growth of 22.7% driven by:

- Increased retail client numbers, transaction volumes and some price increases
- Broadened product offerings to corporate customers and volume increases

Knowledge-based income lower on softer equity markets resulting in lower mergers and acquisitions activity.

Trading income

Negatively impacted on by:

- Less volatility in markets reducing transaction volumes
- Lower spreads

Investment income

Decline of 11.8% in investment income affected by:

- Lower dividends received on investments due to first time equity accounting of certain international associated companies in the year under review
- Strong performance from associated companies
- Few realisations due to weak equity markets

Negative return on assets held against employee liabilities given adverse equity markets and long-term positioning of assets.

Post-AC133

Increase in treasury trading operations due to fair value adjustments on non-qualifying hedges.

Share of income of associated companies

R million	2003 Post-AC133	2003 Pre-AC133	2002 Actual	% change pre-AC133 on Actual
McCarthy Retail	**78**	**78**	72	8.3
Less: Provision	**(78)**	**(78)**	(72)	8.3
Relyant Retail Limited	**14**	**14**	0	100.0
Toyota Finance	**4**	**4**	(3)	>100.0
Zeda Car Leasing	**21**	**21**	9	>100.0
OUTsurance	**86**	**86**	27	>100.0
FirstLink's associated companies	**38**	**38**	(1)	>100.0
RMB Private Equity associated companies	**244**	**234**	313	(25.2)
FirstRand International associated companies	**65**	**65**	0	>100.0
Other	**23**	**23**	23	0.0
Share of income of associated companies	**494**	**484**	368	31.5

Pre-AC133

Increase of 31.5% affected by:

- Strong results from OUTsurance, specifically on the personal lines business
- Reduced contributions from the Private Equity associated companies because of a significant profit on disposal which was included in the prior year
- The return to profitability of the Banking Group's insurance broking operations
- The first time equity accounting of international associated companies in FirstRand International

Operating expenditure

R million	2003 Post-AC133	2003 Pre-AC133	2002 Actual	% change pre-AC133 on Actual
Staff expenditure	**4 911**	**4 911**	4 412	11.3
Depreciation	**612**	**612**	436	40.4
Goodwill	**9**	**9**	9	–
Amortisation of other intangible assets	**68**	**68**	67	1.5
Advertising and marketing	**413**	**413**	295	40.0
Maintenance	**607**	**607**	563	7.8
Other expenditure	**2 917**	**2 917**	2 596	12.4
Total non-interest expenditure	**9 537**	**9 537**	8 378	13.8

Pre-AC133

Staff cost increase affected by above inflation increases in local operations.

Accelerated depreciation on certain property assets.

Increased spending on advertising and marketing focussed on media exposure and product launches.

Business segment performance
All the results reflected in this section are on a pre-AC133 basis.

The divisional performances of the Banking Group, before tax, can be analysed as follows:

Net income before taxation – R million[1]	June 2003	June 2002	% change
Retail segment	**3 327**	2 548	31.8
FNB Retail	**1 890**	1 291[2]	46.4
WesBank	**716**	676	5.9
FNB Africa	**574**	511	12.3
OUTsurance and FirstLink	**147**	70[3]	>100.0
Corporate segment	**1 793**	1 480	21.1
Rand Merchant Bank	**1 071**	910	17.7
FNB Corporate	**722**	570	26.7
Wealth segment	**(47)**	63	(>100.0)
RMB Private Bank	**38**	21	81.0
FNB Trust Services	**27**	31	(12.9)
Ansbacher (UK)	**(112)**	11	(>100.0)
Capital centre	**758**	382[2, 3]	98.4
	5 831	4 473	30.4
Exceptional translation (loss)/gain	**(605)**	548	(>100.0)
Income before tax	**5 226**	5 021	4.1

1. *All business units operate on a fully-funded basis. As a result, the numbers above do not include investment return on capital.*
2. *These figures have been restated to reflect a transfer of R32 million profit from Capital Centre to Retail bank in respect of the acquisitions made in the previous financial year.*
3. *Interest calculated on capital allocated to the Capital Centre has been reallocated to the appropriate short-term insurance centres.*

Retail segment
FNB Retail

R million	June 2003	June 2002	% change
Retail bank	**1 282**	996	28.7
FNB HomeLoans	**555**	326	70.2
eBucks.com	**53**	(31)	>100.0
FNB Retail	**1 890**	1 291	46.4

Retail bank

FNB Retail achieved excellent results, benefiting from satisfactory year-on-year growth of 9.6% in advances and 6.8% in deposits. Strong organic advances growth of 20.1% in card loans and 52.3% (off a low base of R2.26 billion) in personal loans was achieved.

Deposit growth benefited from particularly strong demand for investment related products such as money market, notice and fixed deposits, as investors pursued safer investment strategies. This was further enhanced by a better than expected retention rate of maturing deposits on the acquired Saambou deposit book. Deposit margins improved from 3.3% in the prior year to 3.6% in the year under review.

Non-interest revenue increased by 13.9%, primarily as a result of growth in customers and per-customer transactional volumes, and the resultant increase in related fees charged.

FNB HomeLoans

FNB HomeLoans had an exceptional year with a 70.2% increase in profits. Profit was considerably enhanced by the benefits of scale resulting from the leveraging of its infrastructure through the Saambou and NBS acquisitions in the previous financial year. Margins were better than anticipated. The cost to income ratio improved from 53.3% to 50.7%, through a combination of revenue increases and stringent cost management.

Business segment performance continued

FNB HomeLoans achieved record payouts in the year under review with growth in new business of 21.4% as a result of continued strength in the property market, resulting in record payouts in the current year. However, the expected run-off in the NBS and Saambou acquired books, restricted total advances growth to 2.3%.

Non-interest revenue increased by 98% to R55 million, with the core FNB book recording an increase of R31 million (55%), primarily as a result of the selling of insurance products to clients.

The higher interest rate environment had a negative impact on non-performing loans, resulting in a deterioration from 2.4% to 2.7% during the year.

eBucks.com

eBucks.com achieved a maiden profit for the year under review, ahead of original business targets. Registered members on the rewards programme increased by 52% to 582 000 at year-end. The total value of internet-banking transactions processed increased by 350% from the prior year to R46.8 billion.

WesBank

WesBank delivered satisfactory results in an adverse trading environment, including continued high interest rates and stagnant growth in vehicle sales.

WesBank achieved record new vehicle sales, breaking the R24 billion mark for the year, an increase of 19.2% in the year under review.

The Business division, with total new business growth of 27.4% and advances growth of 29.1%, benefited significantly from its collaboration with FNB Corporate. The newly acquired Barloworld book further contributed to the robust growth in total advances of 27.3% for WesBank.

Interest turn remains under pressure due to a higher cost of borrowing and increased competitive margin pressure.

Arrears, non-performing loans and bad debt levels have improved further in the period under review. This is due to continued attention to both credit extension and collection capabilities. Non-performing loans as a percentage of advances declined to 0.93% at 30 June 2003 (2002: 1.4%), an all time low and considerably below historic norms.

FNB Africa

R million	June 2003	June 2002	% change
FNB Namibia	**249**	235	6.0
FNB Botswana	**296**	252	17.5
FNB Swaziland	**29**	24	20.8
	574	511	12.3

FNB Namibia experienced a difficult year with fairly stagnant local economic growth. In spite of this, advances growth of 20.8% was achieved through a focus on the corporate market. Bad debts were negatively impacted by the prolonged high interest rate environment. During the course of the current financial year, FNB Namibia paid a special dividend of R190 million. This had the effect of reducing its endowment effect on capital and consequently negatively impacted interest margins. Return on equity improved to 39.8% (2002: 26.3%), with the cost to income ratio contained at 46.3% (2002: 44.0%).

FNB Botswana had a successful year, achieving profit before tax growth of 15.4% in local currency terms. An additional provision against the Botswana WesBank book of P14 million to bring the provisioning in line with Banking Group policy, negatively impacted on performance. FNB Botswana achieved return on equity figures of 42.1% and improved its cost to income ratio to 39.3% (2002: 40.4%).

FNB Swaziland had an exceptional year despite difficult economic and political conditions in the country. The growth in profit before tax was driven mainly by a 29% increase in net interest revenue and a 23% increase in non-interest revenue.

FNB Swaziland improved its cost to income ratio to 60.0% (2002: 64.2%).

Short-term Insurance

R million	June 2003	June 2002	% change
OUTsurance (46%)	**85**	47	80.9
FirstLink	**62**	23	>100.0
	147	70	>100.0

OUTsurance achieved a 70.7% increase in gross premiums written, resulting in the R1 billion mark been exceeded for the first time. This performance was achieved despite stagnant growth in vehicle sales in the first six months of the calendar year due to the continued high interest rate environment.

OUTsurance achieved an impressive increase in retail client numbers. Expenses as a percentage of net premium earned excluding the OUTbonus, decreased from 28% to less than 20%. During March 2003, OUTsurance started providing cover for small and medium businesses.

The loss ratio (claims divided by premiums) was contained to below 60%, well below the industry average of 70%.

FirstLink achieved 82% growth in revenue from the commercial segment while benefiting from client retention rates significantly above industry norms in both the commercial and personal lines business.

Corporate segment

Rand Merchant Bank

RMB achieved very good results in the year under review, increasing profit by 17.7%. The Equities Trading, Special Projects and Private Equity divisions performed particularly well in challenging markets.

Special Projects division continues to be the highest profit contributor in RMB. Special Projects International benefited from an exceptional performance in respect of their International debt portfolios. Special Projects International continued to experience difficult trading conditions in the US Corporate debt markets, although not to the extent of the previous financial year, with unrealised mark-to-market losses on the portfolio reducing significantly. The Banking Group continues to maintain conservative provisions against these portfolios.

The Private Equity division achieved excellent results in spite of very limited realisation opportunities. The unrealised value of their book continues to grow and was R699 million at 30 June 2003, after the revaluation of certain available for sale and trading assets in terms of AC133.

RMB's trading desks managed to achieve very satisfactory results in a difficult trading environment, benefiting from an improvement in market conditions in the latter half of the financial year. The Equities trading division, and specifically the agricultural trading operation, performed very well.

Corporate finance achieved satisfactory fee and commission income in an exceptionally quiet market.

FNB Corporate

FNB Corporate achieved excellent results despite poor demand for credit in the large corporate market, increasing profit before tax by 26.7% to R722 million. Despite the higher interest rate environment, non-performing loans as a percentage of gross advances decreased by 50% to a level of R724 million as a result of continued focus on retail concentrations and other advances and further streamlining of the general credit process.

Deposit margins and volumes improved significantly in the higher interest rate environment, resulting in a strong interest turn from the liability side of the balance sheet. Total advances growth remained under pressure, however, satisfactory advances growth of 19% was achieved in the medium corporate market.

Non-interest revenue of grew by 12.9%, primarily as a result of significant increase in electronic banking volumes and through market share growth.

The asset finance collaboration with WesBank was extremely successful, with new business of R2.3 billion written during the year, 83% up from the previous year.

Costs were well controlled, with the cost to income ratio improving from 59.2% to 56.2%.

RMB Private Bank

RMB Private Bank achieved exceptional results during the current year, with profit before taxation increasing by 81.0%. This was achieved by a combination of strong asset and liability growth, an improved margin environment and significant growth in clients, as well as client business volumes.

FNB Trust Services had a disappointing year with year-on-year profits decreasing by 12.9%. This was primarily due to reduced fees on lower will values due to the depressed equities markets.

Ansbacher (UK)

The Ansbacher (UK) Group delivered very disappointing results for the year to 30 June 2003. The low international interest rate environment squeezed margins on customer deposits. Poor overall stock market performance negatively impacted on the Ansbacher Group's investment advisory services. The international debt portfolios were particularly disappointing in difficult markets. The tightening of the regulatory environment in the United States of America ("US") forced a reduction in the size of and new business flows to the Caribbean operations.

On 21 July 2003, the FirstRand Group announced that certain of the businesses of the Ansbacher Group had become increasingly non-core and that FirstRand Limited was evaluating various possibilities for these businesses. These possibilities include disposing of its interest in the Ansbacher Group as a whole or in part.

Irish Litigation

In September 1999, Inspectors were appointed under the Irish Companies Act to investigate certain business which had commenced in 1971 involving Guinness & Mahon (Ireland) Limited, Guinness Mahon Cayman Trust Limited ("GMCT") and its Irish related business. The Ansbacher Group acquired GMCT (subsequently renamed Ansbacher (Cayman) Limited) in 1988 by which time the Irish related business had been substantially reduced and represented a small proportion of its overall business.

The report of the inspectors was published on 6 July 2002 and concluded that there was some evidence to suggest that the Irish related business might have breached, amongst other things, certain sections of Irish tax law. The Irish Revenue authorities have written to Ansbacher (Cayman) Limited and as a consequence the company and its advisers have entered into a process of engagement with them. Based on independent professional advice received, the directors are of the opinion that there is no reliable basis on which a liability for tax, if any, may be estimated. It is, however, recognised that the Irish Revenue authorities may take a contrary view. Given the uncertainty surrounding the scope and applicability of the company to taxes, the directors are of the view that no taxation or other provision is required.

The Irish Minister of Justice has made a substantive application to obtain reimbursement of the costs of the enquiry of approximately Eur 3.6 million against Ansbacher (Cayman) Limited and has made application to include six other parties in this regard. A preliminary application will be heard on 16 December 2003. Ansbacher (Cayman) Limited has a number of compelling arguments against the points raised in the application and therefore no provision for those costs is considered necessary.

Capital centre

Although the Banking Group capital centre reflected an increase in income of 98.4% relative to the prior period, these results are strongly influenced by the following:

- Exceptional bad debt provisions in the prior year against the debt and preference share exposures in McCarthy and other retail exposures and
- Considerable benefit derived from the endowment effect on capital as a result of the high interest rate environment.

Historically low international interest rates partially offset the high domestic rates during the current period.

International operations

Net income before taxation:

R million	2003 Post-AC133	2003 Pre-AC133	2002 Actual	% change pre-AC133 on Actual
FNB Namibia	**254**	**249**	235	6.0
FNB Botswana	**320**	**296**	252	17.5
FNB Swaziland	**32**	**29**	24	20.8
African subsidiaries	**606**	**574**	511	12.3
FirstRand International[1]	**210**	**193**	367	(47.4)
Ansbacher (UK)[1]	**(112)**	**(112)**	11	(>100.0)
Other	**89**	**106**	52	103.1
Total international earnings	**793**	**761**	941	(19.1)

1. Ansbacher (UK) was disclosed as part of FirstRand International in the 2002 annual report. FirstRand International was disclosed as R378 million.

Pre-AC133

Profit growth of 12.3% in African operations affected by:

- Higher non-performing loans in Namibia due to prolonged high interest rate environment
- Lower endowment effect on FNB Namibia capital due to special dividend during the year
- Additional provision of Pula14 million at FNB Botswana
- Strong growth in Swaziland operation off a low base
- Effective cost containment in all operations

Decline in FirstRand International and Ansbacher (UK) resulted from:

- Curtailment of the Ansbacher Cayman operations due to an adverse US regulatory environment
- Reduced margins on client funds due to low international interest rate environment
- Losses in treasury trading operations in Ansbacher (UK)
- Negative impact of adverse stock markets on investment advisory business of Ansbacher (UK)

Segmental information

	South African banking	South African non-banking	Other African banking	Interna-national	Sub-total	Currency translation losses	Total
Geographic							
Net interest income before impairment of advances	6 855	187	688	1 004	8 734	–	8 734
Impairment of advances	(1 005)	(52)	(50)	(260)	(1 367)	–	(1 367)
Net interest income after impairment of advances	**5 850**	**135**	**638**	**744**	**7 367**	**–**	**7 367**
Non-interest revenue	6 327	318	414	459	7 518	(605)	6 913
Net income from operations	**12 177**	**453**	**1 052**	**1 203**	**14 885**	**(605)**	**14 280**
Operating expenditure	(7 901)	(117)	(478)	(1 042)	(9 538)	–	(9 538)
Income from operations	**4 276**	**336**	**574**	**161**	**5 347**	**(605)**	**4 742**
Share of income of associated companies	36	422	–	26	484	–	484
Income before taxation	**4 312**	**758**	**574**	**187**	**5 831**	**(605)**	**5 226**
Indirect taxation	(292)	(41)	(12)	(1)	(346)	–	(346)
Income before direct taxation	**4 020**	**717**	**562**	**186**	**5 485**	**(605)**	**4 880**
Direct taxation	(1 050)	(68)	(60)	(8)	(1 186)	–	(1 186)
Income after taxation	**2 970**	**649**	**502**	**178**	**4 299**	**(605)**	**3 694**
Earnings attributable to outside shareholders	–	(112)	(125)	(40)	(277)	–	(277)
Earnings attributable to ordinary shareholders	**2 970**	**537**	**377**	**138**	**4 022**	**(605)**	**3 417**
Cost to income (%)	59.8	12.6	43.3	70.0	57.0		59.1
Diversity (%)	48.1	79.8	37.6	32.6	47.8		45.9

	Retail	Corporate	Wealth	Capital Centre	Sub-total	Currency translation losses	Total
Segment							
Net interest income before impairment of advances	5 943	955	365	1 471	8 734	–	8 734
Impairment of advances	(917)	(387)	(36)	(27)	(1 367)	–	(1 367)
Net interest income after impairment of advances	**5 026**	**568**	**329**	**1 444**	**7 367**	**–**	**7 367**
Non-interest revenue	4 387	2 882	530	(281)	7 518	(605)	6 913
Net income from operations	**9 413**	**3 450**	**859**	**1 163**	**14 885**	**(605)**	**14 280**
Operating expenditure	(6 230)	(1 956)	(906)	(446)	(9 538)	–	(9 538)
Income from operations	**3 183**	**1 494**	**(47)**	**717**	**5 347**	**(605)**	**4 742**
Share of income of associated companies	144	299	–	41	484	–	484
Income before taxation	**3 327**	**1 793**	**(47)**	**758**	**5 831**	**(605)**	**5 226**
Indirect taxation	(228)	(36)	(7)	(75)	(346)	–	(346)
Income before direct taxation	**3 099**	**1 757**	**(54)**	**683**	**5 485**	**(605)**	**4 880**
Direct taxation	(670)	(380)	12	(148)	(1 186)	–	(1 186)
Income after taxation	**2 429**	**1 377**	**(42)**	**535**	**4 299**	**(605)**	**3 694**
Earnings attributable to outside shareholders	(127)	(25)	–	(125)	(277)	–	(277)
Earnings attributable to ordinary shareholders	**2 302**	**1 352**	**(42)**	**410**	**4 022**	**(605)**	**3 417**
Goodwill	–	–	–	10	10	–	10
Loss on sale of fixed assets	–	–	–	36	36	–	36
Headline earnings	2 302	1 352	(42)	456	4 068	(605)	3 463
South African income	1 925	1 157	37	388	3 507	(605)	2 902
Other African income	377	45	–	–	422	–	422
International income	–	150	(79)	68	139	–	139
Return on equity (%)	38.5	31.3	(0.1)	–	25.8	–	21.9
Cost to income ratio (%)	59.5	47.3	101.2	–	57.0	–	59.1
Diversity ratio (%)	43.3	76.9	59.2	–	47.8	–	45.9

Segmental information continued

R million	Financial year 2003 Pre-AC133	Financial year 2003 First six months	Financial year 2003 Second six months	Financial year 2002 Pre-AC133	Financial year 2002 First six months	Financial year 2002 Second six months
Retail segment	**3 327**	**1 746**	**1 581**	2 548	1 248	1 276
FNB Retail	**1 890**	**1 051**	**839**	1 291	667	624
WesBank	**716**	**332**	**384**	676	303	373
FNB Africa	**574**	**306**	**268**	511	252	259
OUTsurance and FirstLink	**147**	**57**	**90**	70	26	44
Corporate segment	**1 793**	**656**	**1 137**	1 480	538	942
Rand Merchant Bank	**1 071**	**413**	**658**	910	284	626
FNB Corporate	**722**	**243**	**479**	570	254	316
Wealth segment	**(47)**	**(60)**	**13**	63	64	(1)
RMB Private Bank	**38**	**19**	**19**	21	6	15
FNB Trust Services	**27**	**12**	**13**	31	12	19
Ansbacher (UK)	**(112)**	**(91)**	**(21)**	11	46	(35)
Capital centre	**758**	**380**	**378**	382	128	254
	5 831	**2 722**	**3 109**	4 473	1 978	2 495
Exceptional translation (losses)/gain	**(605)**	**(362)**	**(243)**	548	714	(166)
Income before taxation	**5 226**	**2 360**	**2 866**	5 021	2 692	2 329

- FNB Retail
  - Significant increase in provisions and expenses in the second 6 months
  - Partially compensated for by an increase in margins
- OUTsurance
  - Benefited from a recovery in vehicle sales in second 6 months
  - Continued strong growth from OUTsurance with scale benefit enhancement
- Rand Merchant Bank
  - Traditionally better second 6 months trading performance
  - Improved performance of CDO performance in the second 6 months
- FNB Corporate
  - A bad debt write-off in first 6 months, substantially reversed in second 6 months
- Ansbacher (UK)
  - Trading losses in the first 6 months not repeated in the second 6 months
  - US regulatory environment continues to pressure the basic Ansbacher business case

Changes in accounting policy

AC133 – Financial instruments: Recognition and measurement

Introduction

The Banking Group adopted the new accounting statement on recognition and measurement of financial instruments (AC133) on 1 July 2002. The statement is the South African equivalent of IAS39, the International Financial Reporting Standard dealing with this issue.

The statement introduces fair value accounting to certain classes of financial assets and liabilities such as advances, derivative instruments and investments in debt and equity securities. The statement is not applicable to assets such as fixed assets or investments in subsidiaries and associated companies.

Depending on the asset classification used, fair value changes are reflected in income and expenditure or directly in equity. There are four primary asset categories:

- Originated assets, such as most of the Banking Group's normal advances, which are carried at amortised cost
- Held-to-maturity assets, such as certain government bonds, where the Banking Group has the intention to hold the asset until maturity, which are carried at amortised cost
- Trading assets, such as most equities trading portfolios where the intention is to trade with a short-term profit motive, which is fair valued with changes in fair value recorded in the income statement on a yearly basis and
- Available for sale assets, such as certain private equity investments where there is no trading intention, which are carried at fair value with unrealised fair value changes reflected in equity until realisation.

AC133 also allows for the designation of any financial instrument as "Held for trading", irrespective of the described categories above, with fair value changes on such assets reflected in the income statement on a yearly basis.

The Banking Group is required to designate financial instruments into these categories on initial recognition, and the designation is final, thereby effectively determining the future accounting treatment of the instrument on either an amortised cost or fair value basis.

AC133 is a prospective accounting statement and does not provide for the restatement of historical numbers. It has comprehensive transitional provisions, which affect opening equity balances.

General provisions

Prior to the implementation of AC133, the Banking Group, consistent with existing banking industry practice, calculated a general provision for bad debts based on a matrix model by applying the one-year historical default frequency to its advances book.

AC133 prescribes that a cash flow valuation methodology be used in calculating provisions in the future. This methodology requires that all future expected cash flows, including interest income be taken into account in this calculation.

AC133 is ambiguous in dealing with the transitional arrangements in respect of treatment of the adjustments to provisions, but not in respect of the methodology used in calculating the quantum of impairments. The South African Institute of Chartered Accountants issued an interpretation (ED168) on the correct transitional treatment on 4 September 2003, stating that the release of previous provisions should be treated on the same basis as other transitional adjustments relating to AC133 subject to certain requirements. The Banking Group complies with these requirements, and consequently, transferred the once-off release of the previous general provision for bad debts of R2 065 million to opening retained income.

The credit risk premium included in interest charged to clients offsets future losses to the extent that risk pricing has been correctly applied. The Banking Group's credit model includes risk pricing and consequently, to the extent that the Banking Group is of the opinion that the credit premium is not sufficient to compensate for future losses inherent in the performing advances portfolio, or that insufficient data exists to reliably determine whether such losses exist, a portfolio provision is created. In line with this methodology, a portfolio provision of R535 million was created at 1 July 2002.

The Banking Group created an impaired capital reserve of R1 530 million (R791 million after tax) at 1 July 2002 in compliance with the regulatory provisioning requirements set out in the regulations to the Banks Act.

Utilising the Banking Group's credit model, and in line with the methodology for raising a portfolio impairment discussed above, an impairment was created at year-end, predominantly against retail lending to the low-income market.

Subsequent to the release of interim results for the six-month period ended 31 December 2002, the Banking Group has raised additional impairments against its corporate and acquired home loans books. These impairments arose because of a lack of sufficiently robust historical data and are considered conservative.

Internal hedging transactions

Historically the Banking Group utilised internal transactions to hedge their risk exposure in respect of its banking operations with the central treasury operation of the Banking Group. Internal transactions were pooled in terms of certain common criteria and hedged out on a net aggregated basis with external parties in the market. These transactions qualified for hedge accounting treatment prior to the introduction of AC133.

AC133 contains very strict rules for the application of hedge accounting. As a result, the previous method of centralising all interest rate exposure with the central treasury does not qualify for hedge accounting in terms of these requirements.

This has had a far-reaching impact on the Banking Group's economic hedge structures. The Banking Group hedges the underlying interest rate risk inherent in its banking book using derivative instruments. In terms of AC133, these derivatives are valued at fair value while the underlying banking book is valued at amortised cost. As a consequence, a timing difference arises in the recognition of income.

The impact of the timing difference on current period income is set out below:

R million	Post-AC133	Pre-AC133
Fair value hedge losses at 30 June 2002	(211)	–
Fair value hedge profits at 30 June 2003	187	–
Net release of hedge profits to the income statement	398	

In terms of impending changes to AC133, as set out in ED 166, this anomaly in the standard is likely to be corrected in future periods, and this profit is unlikely to re-occur.

The Banking Group, prior to 30 June 2003, externalised various of its previous internal hedging structures to be compliant with hedging requirements of AC133.

Impact of adoption of AC133 on opening equity

The table below provides disclosure of the adjustment required to opening equity of the Banking Group as a result of the implementation of AC133, together with accompanying commentary.

R million	Retained income	Re-valuation reserve	General risk reserve	Total
Closing balance at 30 June 2002	12 343	–	–	12 343
Present value adjustment for off-market loans[1]	(110)			(110)
Present value adjustment for specific loan impairments[2]	(311)			(311)
Non-qualifying interest rate hedges[3]	(211)			(211)
Release of general loan provisions[4]	2 065			2 065
Creation of a General Risk Reserve (impaired capital reserve)[5]	(1 530)	440	1 090	–
Creation of portfolio impairment	(535)			(535)
Revaluation of held for trading portfolios[6]	(21)			(21)
Revaluation of available for sale portfolios[7]	(671)			(671)
Transfer of available for sale portfolios	671	(671)		–
Taxation on above	196	23	(327)	(108)
Restated opening balance at 1 July 2002	11 886	(208)	763	12 441

1. AC133 requires that loans and advances should be recognised at inception at the fair value of the consideration given. Where off-market rates are applicable, then the fair value of the consideration is measured by present valuing the future cash flows using an applicable market interest rate. This gives rise to an "up front loss" on inception of such loans, which then gradually unwinds over the life of the transaction
2. A major change introduced by AC133 requires that the impairment of advances, on an individual or portfolio basis, must be calculated using a present value methodology, based on expected future cash flows of identified impaired advances or losses inherent in a portfolio of advances. This results in an increase in specific impairments previously provided to take account of the delay in collection of the recoverable amount.
3. AC133 sets onerous requirements before hedge accounting can be applied, including restrictions on the use of partial hedges, internal hedges and net hedging. While the Banking Group has complied with these requirements in certain circumstances, in other situations, where the cost of complying exceeds any tangible business benefit, the Banking Group has elected to reflect the hedges through the income statement.
4. The present value calculation applied in AC133 requires that all future cash flows, including future interest payments, be taken into account in the creation of credit risk impairments. To the extent that the risk pricing methodology of an enterprise is appropriate and the current expectations of recoverable cash flows are consistent with the initial expectations, then the risk premium inherent in future interest flows should compensate for the risk inherent in the underlying capital amount relating to expected future losses. The specific impairment is supplemented where market conditions change and as a result an entity's expectation of future cash flows change and it is not possible to re-price sufficiently quickly to compensate for the change in risk. This additional impairment is included in adjustment 2 above. As a result, the old general provision, which pre-AC133 took account of the inherent risk in the book without taking the risk premium charged into account, is no longer permitted under AC133. To the extent that the Banking Group is of the opinion that there are losses inherent in the performing portfolio of advances, which will only be identified in the future, or that insufficient data exist to reliably determine whether such losses exist, a portfolio provision has been created. In line with standard industry practice, an impaired capital reserve has been created in terms of the requirements of the SARB reporting (refer 5 below).
5. The general risk reserve is created to comply with the minimum provisioning levels required in terms of the SARB. The formulistic approach prescribed by the SARB, results in levels of provisioning which incorporate "unexpected losses" in a portfolio of advances. To the extent that general or specific impairments created relate to advances now held as "Available for sale", these impairments have been included in the Revaluation Reserve Column of the statement of changes in equity.
6. Investment banking assets previously held at cost, now designated at fair value. This category includes private equity investments, which are not associated companies or subsidiaries.
7. Adjustment relating to the measurement of available for sale financial assets to fair value or amortised cost, on 1 July 2002.

Impact on current income

R million	Net interest income	Bad debts	Other income	Other	Total
Unwind of present value adjustment in the current period	114				114
Increase in specific provision (Present value)		(116)			(116)
Increase in specific provision (Other)		(64)			(64)
Portfolio provision		(69)			(69)
General provision		138			138
Non-qualifying hedge profits			398		398
Mark-to-market vs accrual profits			(6)	11	5
Translation losses			73		73
Re-allocations	256		(256)		–
Effect on individual line items	370	(111)	209	11	479
Less tax impact on the above	(111)	33	(41)	(3)	(122)
Net impact on current period income	259	(78)	168	8	357

Impact on closing reserves

R million	Retained income	Other non-distributable reserves	Re-valuation reserve	General risk reserve	Total
Reserves before AC133	14 302	1 077	–	–	15 379
Opening adjustment	(458)		(208)	763	97
Current period income statement effect	357				357
Transfer to general risk reserve	(138)			138	–
Revaluation of available for sale portfolios			897		897
Currency reserve		(11)			(11)
Other		(16)			(16)
Revised closing reserves	14 063	1 050	689	901	16 703

Notes

Notes

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This information is available on
our website at www.firstrand.co.za

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