risk and capital management report

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OVERVIEW

FirstRand Limited (FirstRand or the Group) believes that effective risk, capital and performance management are of primary importance to its success and is a key component of the delivery of sustainable returns to its shareholders. It is, therefore, deeply embedded in the Group's tactical and strategic decision making. The Group aligns its risk management approach to its strategy.

The Group defines risk widely – as any factor that, if not adequately assessed, monitored and managed, may prevent it from achieving its business objectives or result in adverse outcomes, including damage to its reputation.

Risk taking is an essential part of the Group's business and FirstRand explicitly recognises risk identification, assessment, monitoring and management as core competencies and important differentiators in the competitive environment in which it operates. Through its portfolio of leading franchises namely, FNB, RMB, WesBank and Ashburton Investments, FirstRand aims to be appropriately represented in all significant profit pools across all chosen markets and risk-taking activities. This entails building revenue streams that are diverse and create long-term value within acceptable earnings volatility parameters.

MANAGING THE RISK PROFILE

The Group believes a strong balance sheet and resilient earnings are key to growth, particularly when entering periods of uncertainty. The Group's focus areas to manage its risk profile and optimise its portfolio are:

Earnings resilience and balance sheet strength

- Strong earnings resilience through diversification, growth in client franchise, appropriate risk appetite and positive operating margins.
- Quality of returns with a focus on ROA (not gearing) and discipline in deployment of capital.
- Maintain balance sheet strength through:
  - appropriate action in new business origination;
  - managing non-performing loans and coverage ratios;
  - growing the deposit franchise and improving liquidity profile; and
  - maintaining a strong capital position.

Refer to the *deputy CEO's report* for a detailed discussion on the Group's strategies to ensure resilience in earnings, growth and returns and maintain balance sheet strength.

Current board-approved adjusted targets and actual capital ratios are summarised in the following table.

Capital adequacy position

%	CET1	Tier 1	Total
Regulatory minimum*	5.5	7.0	10.0
Target	10.0 – 11.0	>12.0	>14.0
Actual	**13.9**	**14.8**	**16.7**

** Excludes the bank-specific individual capital requirement.*

Risk governance

- Balancing the Group's overall risk capacity with a bottom-up and consolidated view of the planned risk profile for each business, in line with the board risk appetite principles.
- Strong risk governance with multiple points of control applied consistently throughout the organisation.

TOP AND EMERGING RISKS

- While there are signs of an improvement in South Africa's external imbalances, the country continues to run a large current account deficit. This imbalance reflects the economy's dependence on foreign capital inflows to fund growth and renders the economy vulnerable to any global or domestic economic developments that could affect foreign capital inflows.
- The normalisation of monetary policy in the US could also result in a slowdown in capital flows to South Africa, which will result in more currency weakness, higher inflation and lower economic growth.
- Factors that may impact the economy include potential power blackouts, an economic slump in China and/or a European economic fallout.
- Consumers' disposable income continues to be under pressure due to rising unemployment, tighter credit conditions, inflation (particularly linked to fuel and food) and additional tariffs (including e-tolls and electricity increases). Private investment spending will also slow as confidence wanes and profitability falls.
- Economic growth is affected by unrest in the labour market. A prolonged period of strike action across different sectors of the economy could negatively impact potential GDP growth and the long-term growth potential of the country.

- A changing and tougher regulatory landscape requires the Group to deal with a raft of new regulatory requirements. This includes recent and proposed changes relating to anti-money laundering, treating customers fairly, protection of personal information and Basel III. This is further exacerbated by new and complex international requirements such as the Foreign Account Tax Compliance Act and Office of Foreign Asset Control Sanctions, which do not form part of South African law, but which banks have to comply with in order to maintain correspondent banking relationships and secure funding.
- Cybercrime and potential money laundering threats continue to increase globally.

RECENT AND FUTURE REGULATORY CHANGES

The large volume of new regulatory and supervisory standards and requirements issued by international standard-setting bodies such as the Basel Committee on Banking Supervision (BCBS) requires ongoing review of South Africa's banking legislation and regulatory requirements in order to ensure that it aligns appropriately with international standards. Recent amendments to the Banks Act and the *Regulations relating to Banks* (the Regulations) included the implementation of the Basel III regulations with effect from 1 January 2013 and the Banks Amendment Act 22 of 2013, which came into effect on 10 December 2013.

Twin peaks

An important development in respect of the regulatory framework was a document issued for public comment in February 2013 by the Financial Regulatory Reform Steering Committee. This provides information on a wide-ranging set of reforms and proposals relating to, amongst others, the implementation of a twin peaks model of financial regulation in South Africa; details of which were initially published during February 2011 in a policy document, *A safer financial sector to serve South Africa better*. In this regard, four policy priorities were identified in order to reform the financial sector, including:

- financial stability;
- consumer protection and market conduct;
- expanding access of financial services through inclusion; and
- combating financial crime.

National Treasury indicated that the achievement of these objectives necessitates a change in the South African regulatory landscape from both a structural and a policy perspective which will include the introduction of a twin peaks approach to financial sector regulation. A twin peaks approach will primarily be aimed at the enhancement of systemic stability, improving market conduct regulation, sound micro- and macroprudential regulation and the strengthening of the operational independence, governance and accountability of regulators.

Financial regulatory reforms will be implemented in two phases, along with the development of necessary legislation to enable the relevant regulators to deliver on revised mandates. The draft Financial Sector Regulation Bill, 2013, the first of a series of bills to be published in order to achieve the financial regulatory objectives of the twin peaks model of financial regulation in South Africa, was published in December 2013. The design and implementation of a twin peaks model of financial regulation is a complex undertaking that requires substantial consultation and the Group will, as a key stakeholder, continue to foster close interaction and cooperation with the authorities and other stakeholders.

Below is a high-level overview of strategic, operational and functional outcomes resulting from execution of strategy, and related risk management focus areas.

Outcomes	Risk management focus areas
Capital management	
• Guidance issued by the South African Reserve Bank (SARB) covered the loss absorbency requirements for capital instruments, including Additional Tier 1 (AT1) and Tier 2 instruments. The add-on for domestic systemically important banks (D-SIB) was finalised in the current financial year but remains confidential. • Consultative papers released by BCBS on various topics are at different stages of testing, finalisation and implementation. There is increased focus on the leverage ratio framework, with additional disclosure requirements from 1 January 2015.	• Maintain strong capital levels, with particular focus on the quality of capital and optimise the Group's risk-weighted assets (RWA) and capital mix during the transitional period of Basel III implementation. • Continue to focus on optimal capital mix following guidance from the SARB on the loss absorbency requirements for capital instruments, as well as capacity for new issuance in the capital markets. • Continued participation in the SARB quantitative impact studies to assess the impact of Basel III developments on capital adequacy and leverage.
Credit risk	
• The Group's total gross advances increased 14% year-on-year with growth in corporate and commercial advances particularly robust at 17%. Retail advances growth of 11% was achieved within the Group's risk appetite framework. • With respect to FNB's retail advances, residential mortgages grew 5% in line with property prices. Card increased 13% on the back of new customer acquisition. Personal loans declined 3% year-on-year, reflecting adjustments in credit appetite in that segment, especially at the bottom end of the market. • FNB commercial advances growth of 18% was driven by new client acquisition in the business segment, resulting in 31% growth in business banking advances, with continuing growth in commercial property finance, agriculture and overdraft product sets. • RMB investment banking core advances growth (excluding repos) was driven by strong deal flow from the rest of Africa, especially in sectors such as oil and gas, telecoms and resources, and drawdowns relating to infrastructure development in South Africa, in particular renewable energy. • WesBank's advances growth reflects strong growth in new business volumes with 58% (in GBP terms) from MotoNovo, 10% from corporate and 21% from personal loans, whilst growth in new business volumes moderated to 6% in SA motor retail reflecting the more constrained economic environment and significant year-on-year slowdown in new vehicle sales. • Total NPLs continued to trend downwards and decreased 6% year-on-year. Retail NPLs declined 1% mainly as a result of the continued improvement in the residential mortgage portfolio offset by the 7% increase in the personal loans portfolio. The workout of certain non-performing accounts led to the significant improvement of 18% in corporate and commercial NPLs at June 2014.	*Retail credit portfolio* • Continued focus on limiting credit extension in the unsecured portfolios to existing retail transactional customers. • Ongoing refinement of credit scorecards and affordability risk management practices aligned to risk appetite and deteriorating macroeconomic context. • Focus on extending credit to lower-risk customers and investment in collection capabilities. *Commercial credit portfolio* • Focus on relationship banking with non-banked lending limited to where pricing is appropriate for increased risk. • Further develop commercial lending skills and product offerings, especially across the rest of Africa and India. • Strengthen risk management and legal recoveries capacity to cater for expected increase in NPLs as credit cycle emerges. *Corporate credit portfolio* • Available capacity for portfolio growth to be allocated to strategic growth areas and clients. • Continue to strengthen risk management in recognition of the challenging operating environment.

Outcomes	Risk management focus areas
Credit risk	
• The credit loss ratio of 0.84% remains below the long-run expected range of 100 to 110 bps. • Portfolio overlays at a franchise level increased 40% year-on-year. This reflects the Group's view that the negative retail credit cycle will continue to emerge, already reflected in the higher levels of arrears being experienced in the VAF, WesBank personal loans and card books. In addition, portfolio overlays increased on the back of deteriorating macroeconomic indicators, resulting in the creation of an additional R450 million of central portfolio overlays. • The overall credit picture remains in line with expectations and all of the Group's portfolios are tracking as anticipated, reflecting decisions taken as early as 2011 to exit origination in high-risk segments, particularly in personal loans.	
Counterparty credit risk	
• Successful implementation of global derivative regulatory reform requirements and a new, upgraded legal agreements database. • Improvement in analytics and reporting of derivative exposures, fair value adjustments and funding.	• Extend counterparty credit risk process to business in the rest of Africa. • Improve platform and process for security collateral. • Further improve exposure modelling.
Market risk in the trading book	
• Overall diversified levels of market risk remained relatively unchanged. • More focused market risk analysis and reporting in line with the Group's new risk appetite framework and governance structure.	• Upgrading the Group's central risk engine in order to improve the current operating environment and cater for anticipated regulatory changes.
Equity investment risk	
• New investments were added to the portfolio with significant realisation during the year. • Considerable growth in the unrealised value of the portfolio as earnings in the underlying investments continued to grow and strong cash generation allowed for degearing. • Ashburton Investments developed and launched five new funds in line with its strategy to provide global investors with traditional and alternative investment products.	• Growing the debt financing portfolio in relation to the equity financing portfolio in RMB resources. This is in line with RMB's decision to reduce volatility in the business, through limiting the exposure to new equity investments. • Ashburton Investments will continue to develop and launch new products and focus on improving its distribution capability.
Interest rate risk in the banking book	
• During the year, the average repo rate increased by 19 bps, resulting in a positive endowment impact as the SARB started to increase rates.	• The endowment book (capital and non-maturing deposits) is positioned to benefit from rising interest rates. • Continue to monitor developments relating to and quantify impact of a possible BCBS proposed Pillar 1 charge for interest rate risk in the banking book, currently in discussion phase.

Outcomes	Risk management focus areas
Foreign exchange and translation risk in the banking book	
• Continued to strengthen principles regarding the management of foreign exchange positions and funding to the Group's foreign entities. • Monitored net open forward positions in foreign exchange (NOFP) limits in each of the Group's foreign entities.	• Management of foreign exchange exposures on the balance sheets of the Group's foreign entities. • Continually assess and review the Group's foreign exchange exposures and enhance the quality and frequency of reporting.
Funding and liquidity risk	
• The Liquidity coverage ratio (LCR) was fully adopted by the SARB with the inclusion of a committed liquidity facility and will be phased in from 2015 to 2019. The minimum LCR requirement will be 60% at 1 January 2015, with 10% incremental step-ups each year to 100% on 1 January 2019. • During the year under review the deposit franchise grew 18% which resulted in a reduction in the Bank's reliance on institutional funding. Capital markets issuance increased 36% and the term profile of institutional funding was further lengthened to 27 months.	• Continue to focus on the Basel III liquidity regime with emphasis on both funding and market liquidity risk management. • Further optimise a risk-adjusted diversified funding profile in line with Basel III requirements relating to the LCR and continue to focus on growing the deposit franchise through innovative products and improve the risk profile of institutional funding. • In order to include the committed liquidity facility in the Bank's available liquidity resources, work is required to appropriately structure and prepare the Bank's assets to access this facility. FirstRand is in the process of applying to the SARB for a committed liquidity facility.
Operational risk	
• Improved quality of operational risk management information across the Group. • Created a single platform with an integrated view of the Group's operational risk profile based on the risk tool outputs. • Improved understanding of risks and controls in main business processes. • Reviewed operational risk appetite at Group and franchise levels and defined operational risk appetite at segment level. • Increased use of external data in scenario analysis to increase objectivity in the process. • Updated mandatory key risk indicators (KRIs) to cover significant Group-wide risks and improve the predictive capability of KRIs. • Implemented formal tracking and reporting of progress on critical projects/initiatives to address key operational risk themes across the Group.	• Embed operational risk appetite in business decision making at segment and business unit levels. • Continued refinement of the process-based risk and control identification and assessment through comprehensive coverage of, *inter alia*, critical handover points, information governance, regulatory, legal and IT risks. • Refine the scenario analysis process by appropriate linkages to key risk drivers and risk mitigation plans. • Refine KRIs to be more predictive of risk and align with operational risk appetite settings. • Embed the tracking of Group-wide mandatory KRIs (including IT risk). • Update advanced measurement approach capital modelling methodology and software. • Implement Basel principles for risk data aggregation and risk reporting.

Outcomes	Risk management focus areas
Regulatory risk	
- During the year under review, the SARB levied fines totalling R125 million on South Africa's four largest banks in relation to FICA regulations. FirstRand received a fine of R30 million relating to customer verification and record keeping. Required governance improvements in anti-money laundering reporting processes were also identified. The nature and extent of the SARB findings did not indicate any abuse of FirstRand's banking platforms by money launderers and the identified issues of non-compliance have not directly or indirectly led to any customer being financially prejudiced. - The proposed implementation of a twin peaks model of financial regulation in South Africa. - The Banks Amendment Act 22 of 2013, effective 10 December 2013, serves to, *inter alia,* amend banking legislation in line with requirements of the BCBS. - The draft Financial Sector Regulation Bill, 2013, was published in December 2013.	- FirstRand has, over the past five years, made significant investments in systems, processes and resources to ensure the correct capturing of customer information and the appropriate identification of suspicious transactions, and remains fully committed to addressing any ongoing weaknesses. - Continued support for regulatory objectives, improvements in risk management and governance practices, and cooperation with regulatory authorities and other stakeholders. - Continue to make significant investments in people, systems and processes to manage the risks emanating from a number of new local and international regulatory requirements.

BASEL PILLAR 3 DISCLOSURE

Regulation 43 of the revised Regulations of the Banks Act, 1990 (Act No. 94 of 1990), requires that a bank shall disclose in its annual financial statements and other disclosures to the public, reliable, relevant and timely qualitative and quantitative information that enables users of that information to make an accurate assessment of the bank's financial condition, including its capital adequacy, financial performance, business activities, risk profile and risk management practice. This disclosure requirement is commonly known as Pillar 3 of the Basel Accord. This is FirstRand's Basel Pillar 3 disclosure and complies with the risk disclosure requirements of regulation 43 of the *Regulations relating to Banks, (Regulations)*. The Basel III additional capital disclosure templates (as required per SARB Directive 8 and 20B) can be found on the Group's website, www.firstrand.co.za/investorcentre/pages/capitaldisclosures.aspx.

The *deputy CEO's report* and the *CFO's report* on pages 14 to 50 provide a high-level overview of the Group's financial condition, performance and risk profile for the year ended 30 June 2014.

FirstRand Limited is the listed holding company and regulated bank-controlling company. The wholly-owned subsidiaries of FirstRand are:

- FirstRand Bank Limited (the Bank or FRB);
- FirstRand EMA Holdings Proprietary Limited (FREMA);
- FirstRand Investment Holdings Proprietary Limited (FRIHL); and
- Ashburton Investments Holdings Limited (Ashburton Investments).

FRB and FREMA include the Group's regulated banking operations. Ashburton Investments is the Group's investment management business and all other activities are included under FRIHL. A simplified group structure can be found on page 491 of this report.

Some differences exist between the practices, approaches, processes and policies of the Bank and its fellow wholly-owned subsidiaries and these are highlighted by reference to the appropriate entity, where necessary. This report has been internally verified by the Group's governance processes in line with the Group's public disclosure policy. All information in this report is unaudited unless otherwise indicated.

SARB APPROACHES TO CALCULATION OF RWA

The following approaches are adopted by the Group for the calculation of RWA.

Risk type	FRB domestic operations	SARB approval date	Remaining FirstRand subsidiaries and FRB foreign operations	FRIHL entities
Credit risk	Advanced internal ratings-based (AIRB) approach	January 2008	Standardised approach	Standardised approach
Counterparty credit risk	Standardised method	May 2012	Current exposure method	Current exposure method
Market risk	Internal model approach	July 2007	Standardised approach	Standardised approach
Equity investment risk	Market-based approach: Simple risk-weighted method	June 2011	Market-based approach: Simple risk-weighted method	Market-based approach: Simple risk-weighted method
Operational risk*	Advanced measurement approach (AMA)	January 2009	The standardised approach (TSA)	Basic indicator approach (BIA), TSA, AMA
Other assets	Standardised approach	January 2008	Standardised approach	Standardised approach

* *All entities on the AMA and TSA for operational risk were included in the approval for use of AMA and TSA from January 2009; some entities were moved to FRIHL with a subsequent legal entity restructure. All other entities in FRIHL remain on the BIA approach.*

BASIS OF CONSOLIDATION

Consolidation of all entities for accounting purposes is in accordance with IFRS and for regulatory purposes in accordance with the requirements of the Regulations. There are some differences in the manner in which entities are consolidated for accounting and regulatory purposes. The following table provides the basis on which the different types of entities are treated for regulatory purposes.

Regulatory consolidation treatment

Shareholding	Banking, security firm or financial entity	Insurance entity	Commercial entity
Between 10% and 20%	▸ refer to threshold rules*.	Refer to threshold rules*	Internal rating-based approach risk weight up to maximum of 1250%.
Between 20% and 50%	Legal or *de facto* support: ▸ proportionately consolidate. No other significant shareholder: ▸ refer to threshold rules*.	Refer to threshold rules*	Individual investment greater than 15% of CET1, AT1, Tier 2: ▸ risk weight at 1250%. Individual investment up to 15% of CET1, AT1 and Tier 2: ▸ risk weight at no less than 100%.
Greater than 50%	Entity conducting trading activities/other bank, security firm or financial entity: ▸ consolidate.	Refer to threshold rules*	

* *As per regulation 38(5) of the Regulations.*

DEFINITIONS

The Group is exposed to a number of risks that are inherent in its operations. Identifying, assessing, pricing and managing these risks appropriately are core competencies of the individual business areas. Individual risk types are commonly grouped into three broad categories, namely strategic and business risks, financial risks and operational risks.

Risk category reference	Risk components	Definition
Strategic and business risks	Includes strategic risk, business risk, volume and margin risk, reputational risk, and environmental and social risks	Strategic risk is the risk to current or prospective earnings arising from inappropriate business decisions or the improper implementation of such decisions.
		Business risk is the risk to earnings and capital from potential changes in the business environment, client behaviour and technological progress. Business risk is often associated with volume and margin risk, and relates to the Group's ability to generate sufficient levels of revenue to offset its costs.
		Reputational risk is the risk of reputational damage due to compliance failures, pending litigations, underperformance or negative media coverage.
		Environmental and social risks focus on the environmental and social issues which impact the Group's ability to successfully and sustainably implement business strategy.
Financial risks	Credit risk	The risk of loss due to the non-performance of a counterparty in respect of any financial or other obligation. For fair value portfolios, the definition of credit risk is expanded to include the risk of losses through fair value changes arising from changes in credit spreads. Credit risk also includes credit default risk, pre-settlement risk, country risk, concentration risk and securitisation risk.
	Securitisations	Securitisation is the structured process whereby loans and other receivables are packaged, underwritten and sold in the form of asset-backed securities.
	Counterparty credit risk	The risk of a counterparty to a contract, transaction or agreement defaulting prior to the final settlement of the transaction's cash flows.
	Market risk in the trading book	The risk of adverse revaluation of any financial instrument as a consequence of changes in market prices or rates.
	Interest rate risk in the banking book	The sensitivity of a bank's financial position and earnings to unexpected, adverse movements in interest rates.

Risk category reference	Risk components	Definition
Financial risks	Equity investment risk	The risk of an adverse change in the fair value of an investment in a company, fund or any other financial instrument, whether listed, unlisted or bespoke.
	Foreign exchange and translation risk in the banking book	Foreign exchange risk is the risk of losses occurring or a foreign investment's value changing due to movements in foreign exchange rates. A bank is exposed to currency risk in its net open foreign currency positions and foreign investments.
		Translation risk is the risk associated with banks that deal in foreign currencies or hold foreign assets. The greater the proportion of asset, liability and equity classes denominated in a foreign currency, the greater the translation risk.
	Funding and liquidity risk	Funding liquidity risk is the risk that a bank will not be able to meet current and future cash flow and collateral requirements (expected and unexpected) without negatively affecting its reputation, daily operations and/or financial position.
		Market liquidity risk is the risk that market disruptions or lack of market liquidity will cause the bank to be unable (or able, but with difficulty) to trade in specific markets without affecting market prices significantly.
Operational risks	Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It includes fraud and criminal activity (internal and external), project risk, legal risk, business continuity, information and IT risk, process and human resources risk. Strategic, business and reputational risks are excluded from the definition.
	Regulatory risk	The risk of statutory or regulatory sanction and material financial loss or reputational damage as a result of failure to comply with any applicable laws, regulations or supervisory requirements.

RISK APPETITE

The Group's risk appetite frames all organisational decision making and is fully integrated with FirstRand's strategic objectives. The risk/reward framework, which includes the risk appetite statement below, aims to ensure that the Group maintains an appropriate balance between risk and reward. Business and strategic decisions and the setting of risk appetite are aligned to risk appetite targets to ensure they are met during a normal cyclical downturn. Therefore, at a business unit level, strategy and execution are managed through the availability and price of financial resources, earnings volatility limits and required hurdle rates.

Risk appetite statement

FirstRand's **risk appetite** is the aggregate level and type of risks the Group is willing and able to accept within its overall **risk capacity**, and is captured by a number of qualitative principles and quantitative measures.

The aim is to ensure that the Group maintains an appropriate balance between risk and reward. Risk appetite limits and targets are set to ensure the Group achieves its overall strategic objectives, namely to:

- deliver long-term franchise value;
- deliver superior and sustainable economic returns to shareholders within acceptable levels of volatility; and
- maintain balance sheet strength.

The Group's strategic objectives and financial targets frame its risk appetite in the context of risk and reward and contextualise the level of reward the Group expects to deliver to its stakeholders under normal and stressed conditions for the direct and consequential risk it assumes in the normal course of business.

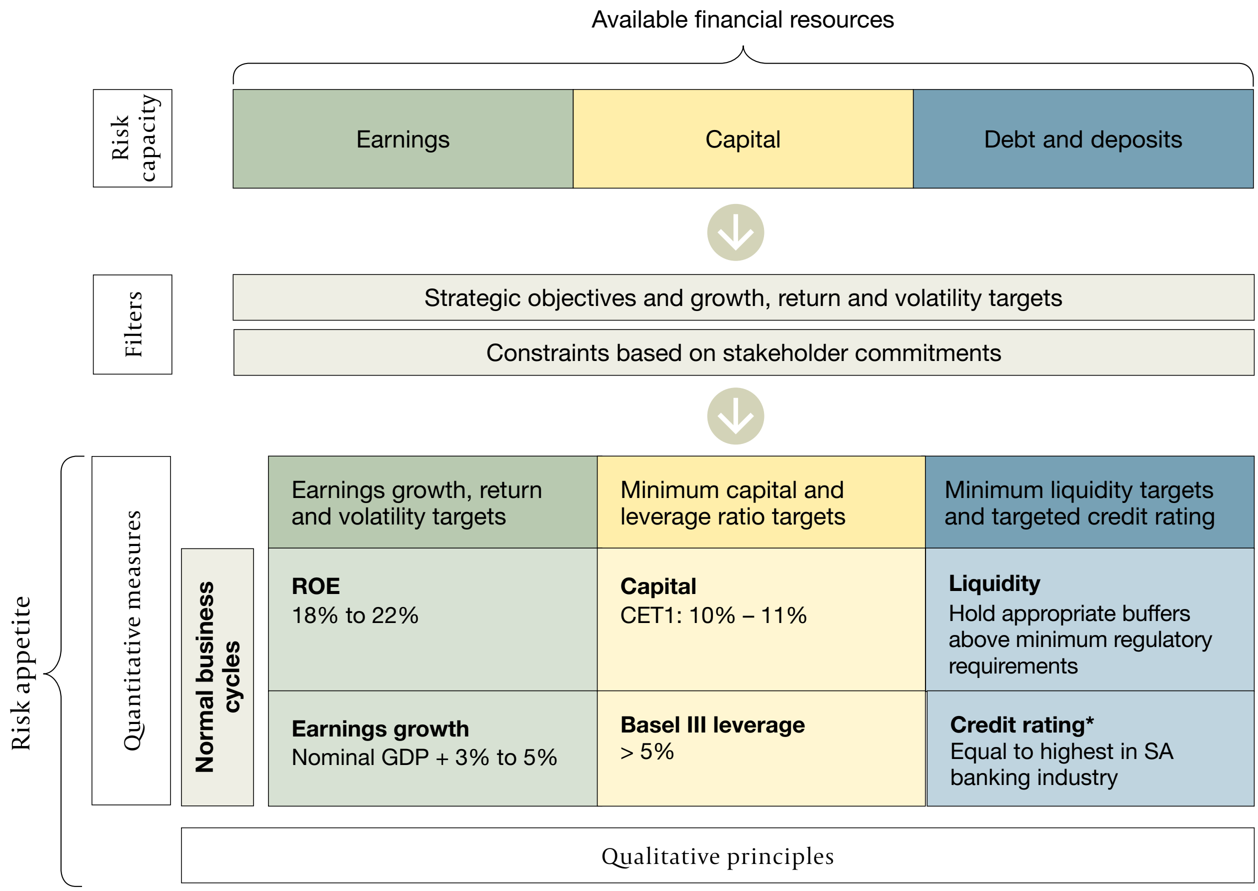
Risk capacity represents the absolute maximum level of risk the Group can technically assume given its current available financial resources, i.e. earnings, capital, debt and deposits. The Group views earnings as the primary defence against adverse outcomes. Risk capacity provides a reference for risk appetite and is not intended to be reached under any circumstances.

Risk appetite articulates what proportion of Group's financial resources should be utilised in the execution of its strategy and is determined through consideration of a number of filters, including:

- overall strategic objectives;
- growth, volatility and return targets; and
- meeting the Group's commitments to all stakeholders including regulators, depositors, debt holders and shareholders.

Risk appetite is captured through both quantitative measures and qualitative principles, which include set objectives for the level of earnings volatility and minimum levels of capital and liquidity to be maintained during defined time horizons in normal and stressed environments within a defined level of confidence.

Process for determining risk appetite



* *Refers to a rating agency's measure of a bank's intrinsic creditworthiness before considering external factors, e.g. affiliate or government support. The three major rating agencies use different terminology for this concept – Standard & Poor's, standalone credit profile; Fitch Ratings, viability rating; and Moody's, baseline credit assessment.*

The qualitative principles include:

- always act with a fiduciary mindset;
- comply with prudential regulatory requirements;
- comply with the spirit and intention of accounting and regulatory requirements;
- build and maintain a strong balance sheet which reflects conservatism and prudence across all disciplines;
- no risk taking without a deep understanding thereof;
- comply with internal targets in various defined states to the required confidence interval;
- no business models with excessive gearing through either on- or off-balance sheet leverage;
- limit concentrations in risky asset classes or sectors;
- ensure the Group's sources of income remain appropriately diversified across business lines, products, markets and regions;
- manage the business on a through-the-cycle basis to ensure sustainability;
- identify, measure, understand and manage the impact of downturn and stress conditions;
- strive for operational excellence and responsible business conduct; and
- avoid reputational damage.

Application of the risk/reward framework

Risk appetite, targets and limits are used to monitor Group's risk/reward profile on an ongoing basis. The risk/reward profile should be measured point-in-time and forward looking. Risk appetite should influence the business plans of each of the businesses and inform the risk taking activities and strategies set in each business.

The Group cascades overall appetite into targets and limits at risk type and franchise and subsequent activity level, and these represent the constraints Group imposes to ensure its commitments are attainable.

Management of risk is the responsibility of everybody across all levels of the organisation, supported through the three lines of control framework of risk management.

The risk/reward framework provides for a structured approach to define risk appetite, targets and limits that apply to each key resource as well as the level of risk that can be assumed in this context. The framework provides guidance on how financial resources, including risk-taking capacity, should be allocated. Although different commitments are made to various stakeholders, these are monitored collectively. Quantitative targets and limits are augmented by a number of qualitative principles that serve to provide guidelines on boundaries for risk taking activities.

Stress testing and scenario planning are used to assess whether the desired profile can be delivered and whether the business stays within the constraints it has set for itself. The scenarios are based on changing macroeconomic variables, plausible event risks and regulatory and competitive changes.

The Group employs a comprehensive, consistent and integrated approach to stress testing and scenario planning. The impact of risk scenarios on the business is evaluated and the need for adjustment to origination is considered and appropriate actions are taken. More severe scenarios are run less frequently but are critical to inform buffers, capital and liquidity planning, validate existing quantitative risk models and to understand required management action.

RISK GOVERNANCE

The Group believes that effective risk management is supported by effective governance structures, robust policy frameworks and a risk-focused culture. Strong governance structures and policy frameworks foster the embedding of risk considerations in business processes and ensure that consistent standards exist across the Group. In line with the Group's corporate governance framework, the board retains ultimate responsibility for providing strategic direction, setting risk appetite and ensuring that risks are adequately identified, measured, monitored, managed and reported on.

RISK GOVERNANCE FRAMEWORK

The Group's business performance and risk management framework (BPRMF) describes the Group's approach to risk management. Effective risk management requires multiple points of control or safeguards that should be consistently applied at various levels throughout the organisation. There are three lines of control across the Group's operations, which are recognised in the BPRMF:

- first line – risk ownership;
- second line – risk control; and
- third line – independent assurance.

In the first line (risk ownership), risk taking is inherent in the individual businesses' activities. Management carries the primary responsibility for risks in its business, in particular, identifying and managing risk appropriately. Business owners, the board and exco are supported in these responsibilities by Group Treasury in FCC.

In the second line (risk control), business heads are supported by deployed divisional and segment risk management functions that are involved in all business decisions and are represented at an executive level across franchises. Franchise heads of risk have a direct reporting line to the Group chief risk officer and the relevant franchise CEO. Franchise and segment risk managers are responsible for risk identification, measurement and control. Divisional and segment risk management activities are overseen by the independent, central risk control functions in FCC, namely enterprise risk management (ERM) and regulatory risk management (RRM). ERM and RRM are represented on FirstRand's exco by the Group's chief risk officer and the head of regulatory risk management, respectively. These central risk control functions provide independent oversight and monitoring across the Group on behalf of the board and relevant committees.

In the third line, Group Internal Audit (GIA) in FCC and external advisors provide independent and objective assurance on the adequacy and effectiveness of governance, risk management practices and control across the Group to the board, audit committee and regulators. GIA is headed by the chief audit executive and reports to the board through the audit committee chairman. The chief audit executive has direct, unrestricted access to the Group CEO, executives, franchises and all business unit functions, records, property and personnel.

GIA conducts work in accordance with international internal audit standards and practices, and its activities are considered annually by the external auditors.

The table below lists the responsibilities of the different business areas in the operating franchises and FCC in the lines of risk control.

Responsibilities in the lines of risk control

FIRST LINE

HEADS OF BUSINESS

- act in accordance with mandates approved by the board or its delegated authority;
- identify, quantify and monitor key risks to business under normal and stress conditions;
- implement strategy within approved risk appetite parameters;
- design business processes to appropriately manage risk;
- ensure that board-approved risk policies, frameworks, standards, processes, methodologies and risk tools are implemented;
- specify and implement early warning measures, associated reporting, management and escalation processes through governance structures;
- implement risk mitigation and response strategies;
- implement timeous corrective actions and loss control measures as required; and
- ensure staff understand and implement responsibilities for risk management.

GROUP TREASURY

- provides an integrated approach to financial resource management;
- optimises the Group's portfolio to deliver sustainable returns within an acceptable level of risk;
- performs scenario analysis and stress testing;
- manages the Group's liquidity, funding, interest rate risk and market risk in the banking book and foreign exchange mismatch;
- performs capital management and planning; and
- advises senior management on potential capital actions, dividend strategy and other capital management developments.

SECOND LINE

DEPLOYED RISK MANAGEMENT

- supports management in identifying and quantifying key risks;
- ensures that board-approved risk policies, frameworks, standards, methodologies and tools are adhered to;
- approves design of business risk processes to ensure appropriate risk management;
- identifies process flaws and risk management issues and initiates and monitors corrective action;
- ensures timeous risk management and loss containment activities; and
- compiles, analyses and escalates risk reports on performance, risk exposures and corrective actions, through governance structures in appropriate format and frequency.

ENTERPRISE RISK MANAGEMENT

- maintains the BPRMF and its ancillary risk frameworks, policies, standards and risk governance structures;
- develops and communicates risk management strategy and challenges risk profiles;
- monitors adequate and effective implementation of risk management processes;
- reports risk exposures and performance to management and governance structures;
- supports management with risk aspects of business decisions;
- ensures appropriate risk management skills and culture;
- performs risk measurement validation; and
- manages regulatory relationships from a risk perspective.

REGULATORY RISK MANAGEMENT

- monitors that business practices, policies, frameworks and approaches are consistent with applicable laws and regulations.

THIRD LINE

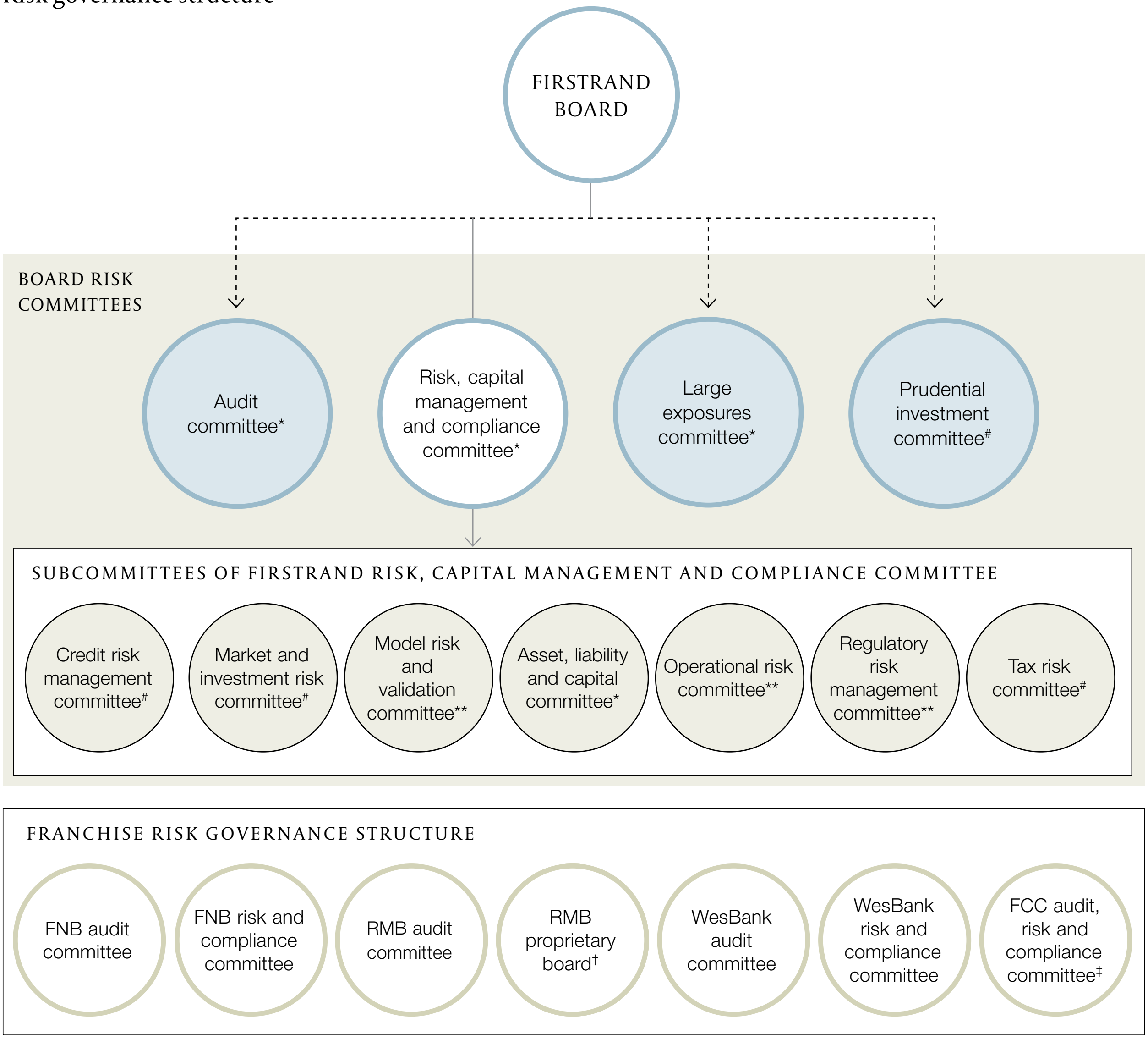
GROUP INTERNAL AUDIT

- monitors risk management infrastructure and practices;
- reviews the reliability and integrity of financial and operational information;
- reviews the significant systems established by management to ensure compliance with laws and regulations;
- reviews safeguarding and existence of assets;
- assesses whether resources are acquired economically and used efficiently and effectively;
- reviews operations or programmes for consistency with established goals and objectives;
- evaluates and assesses significant changes in functions, systems, services, processes, operations and controls; and
- provides an assessment of the adequacy and effectiveness of the system of internal controls (including financial controls) and risk management to the audit committee.

RISK GOVERNANCE STRUCTURE

The risk management structure is set out in the Group's BPRMF. As a policy of both the board and exco, it delineates the roles and responsibilities of key stakeholders in business, support and control functions across the various franchises and the Group. The following diagram illustrates how the risk committees fit into the board committee structure. Other board committees, with clearly defined responsibilities, exist and are described in the *corporate governance* section of this report. One of these is the strategic executive committee, which ensures alignment of franchise strategies, sets risk appetite and is responsible for optimal deployment of the Group's financial and non-financial resources.

Risk governance structure



* Chairperson is an independent non-executive board member.
** Chairperson is an external member.
\# Chairperson is a member of senior executive management. The credit risk management committee has non-executive board representation.
† The RMB proprietary board is the risk and regulatory committee for RMB.
‡ Ashburton Investments' audit, risk and compliance committee reported into FCC audit, risk and compliance committee during the year under review.

The primary board committee overseeing risk matters across the Group is the FirstRand risk, capital management and compliance (RCC) committee. It has delegated responsibility for a number of specialist topics to various subcommittees. The RCC committee submits its reports and findings to the board and highlights control issues to the audit committee.

Additional risk, audit and compliance committees exist in each franchise; the governance structures of which align closely with that of the Group, as illustrated in the previous chart. The Group board committees comprise of members of franchise advisory boards, audit and risk committees to ensure a common understanding of the challenges businesses face and how these are addressed across the Group. The franchise audit, risk and compliance committees, as illustrated in the previous diagram, support the board risk committees and the subcommittees of the RCC committee in the third line of control across the Group.

The responsibilities of the board risk committees and the subcommittees of the RCC committee are included in the following tables. Further detail on the roles and responsibilities of the RCC committee and its subcommittees relating to each particular risk type is provided in the major risk sections of this report.

Responsibilities of the board risk committees

Committee	Responsibility
Audit committee	‣ assists the board with its duties relating to the safeguarding of assets, operation of adequate systems and controls, assessment of going concern status and ensuring that relevant compliance and risk management processes are in place; ‣ ensures that a combined assurance model is applied to provide a coordinated approach to all assurance activities (by management, internal and external assurance providers); ‣ oversees and reviews work performed by the external auditors and internal audit function; and ‣ oversees financial risks and internal financial controls including the integrity, accuracy and completeness of the integrated report, which are provided to shareholders and other stakeholders.
Risk, capital management and compliance committee	‣ approves risk management policies, frameworks, strategies and processes; ‣ monitors containment of risk exposures within the risk appetite framework; ‣ reports assessment of the adequacy and effectiveness of risk appetite, risk management, ICAAP and compliance processes to the board; ‣ monitors the implementation of risk management strategy, risk appetite limits and effectiveness of risk management; ‣ initiates and monitors corrective action, where appropriate; ‣ monitors that the Group takes appropriate action to manage its regulatory and supervisory risks and complies with applicable laws, rules, codes and standards; ‣ approves regulatory capital models, risk and capital targets, limits and thresholds; and ‣ monitors capital adequacy and ensures that a sound capital management process exists.
Large exposures committee (LEC)	‣ approves credit applications or renewals in excess of 10% of the Group's qualifying capital and reserves; and ‣ delegates the mandate for approval of group and individual facilities to the FirstRand wholesale credit approval committee, commercial credit approval committee and the FirstRand retail credit policy, risk appetite and mandate approval committee (subcommittees of LEC), as appropriate.
Prudential investment committee (PIC)	‣ provides oversight to ensure that investment risk and transactions are carefully assessed prior to approval; and ‣ ensures investment exposures comply with FirstRand's prudential investment guidelines.

Responsibilities of the subcommittees of the RCC committee

Committee	Responsibility
Credit risk management committee	- approves credit risk management and risk appetite policies as well as forward looking credit risk indicators developed by the retail, commercial and corporate portfolios; - independent analysis, evaluation and ongoing oversight of credit portfolio quality and performance relative to credit risk appetite thresholds; - monitors quality of the in-force business, business origination, and underlying assets in the securitisation process; - monitors scenario and sensitivity analysis, stress tests, credit economic capital utilisation, credit pricing and credit concentrations; - ensures uniform interpretation of credit regulatory requirements and acceptable standards of credit reporting; - monitors corrective actions in terms of non-adherence to the credit risk management framework based on reports by GIA and reports to the RCC committee; and - reviews credit economic conditions outlook as described in the Group's house view and ensures that business units align credit origination strategies accordingly.
Market and investment risk committee	- approves market and investment risk management policies, standards and processes; - monitors the effectiveness of market and investment risk management processes; - monitors the market and investment risk profile; and - approves market and investment risk-related limits.
Model risk and validation committee	- approves or recommends for approval by the RCC committee, all material aspects of model validation work including credit ratings and estimations, internal models for market risk and advanced measurement operational risk models for the regulatory capital calculations.
Asset, liability and capital committee (ALCCO)	- approves and monitors effectiveness of management policies, assumptions, limits and processes for liquidity and funding risk, capital and market risk in the banking book (interest rate risk and foreign exchange and translation risk); - monitors the management of funding of the Group's balance sheet; - provides governance and oversight of the level and composition of capital, and considers the supply and demand of capital across the Group; - approves buffers over regulatory capital and monitors capital adequacy ratios; and - approves frameworks and policies relating to internal funds transfer pricing for the Group.
Operational risk committee	- provides governance, oversight and coordination of relevant operational risk management practices and initiates corrective action, where required; - monitors the Group and franchise operational risk profiles against operational risk appetite; - mandates the FirstRand operational risk management committee to approve operational risk-related methodologies, processes, guidelines and relevant documentation; - reviews and recommends the Group's operational risk appetite for approval by RCC committee; - approves the operational risk management framework and all its subpolicies/frameworks used in the management of the different operational risk classes including fraud risk, legal risk, business resilience, information governance, information technology and physical security;

Committee	Responsibility
Operational risk committee continued	monitors the formal reports of the ORC subcommittees on the effectiveness of specific operational risk classes; ensures the maintenance of an independent and appropriately skilled operational risk management function; monitors the adequate and effective implementation of the operational risk management framework across the Group and key corrective actions; and reports on material operational risk items to the RCC committee.
Regulatory risk management committee	approves regulatory risk management principles, frameworks, plans, policies and standards; and monitors the effectiveness of regulatory risk management across the Group and initiates corrective action where required.
Tax risk committee	sets tax strategy and tax risk appetite; approves the tax management frameworks and policies; and monitors tax risk assessments and profiles, compliance tax risks, corrective actions and escalation to the RCC committee, where required.

Combined assurance

Formal enterprise-wide governance structures for enhancing the practice of combined assurance at Group and franchise levels are overseen by the audit committee. The primary objective of the Group and assurance forums is for the assurance providers to work together with management to deliver appropriate assurance cost effectively. The assurance providers in this model include GIA, senior management, ERM, RRM and external auditors. The combined outcome of independent oversight, validation and audit tasks performed by the assurance providers ensure a high standard across methodological, operational and process components of the Group's risk and capital management.

Combined assurance results in a more efficient assurance process through the elimination of duplication, more focused risk-based assurance against key control areas and heightened awareness of emerging issues resulting in the implementation of appropriate preventative and corrective action plans.

Regular risk reporting and challenge of current practices

As part of the reporting, challenge, debate and control process, ERM drives the implementation of more sophisticated risk assessment methodologies through the design of appropriate policies and processes, including the deployment of skilled risk management personnel in each of the franchises.

ERM, together with GIA, ensures that all pertinent risk information is accurately captured, evaluated and escalated appropriately and timeously. This enables the board and its designated committees to retain effective control over the Group's risk position at all times.

RISK CULTURE

The Group and its stakeholders recognise that effective risk management requires the maintenance of a proper risk culture, in addition to appropriate risk governance structures, policy frameworks and effective risk and capital methodologies.

ERM, in conjunction with the Group's ethics office, collaborate closely to identify and manage risk culture.

The Group believes its risk culture is influenced by the interaction of the following:

- competent and ethical leadership in setting strategy, risk appetite and a positive attitude towards appropriate risk practices;
- robust risk governance structures to ensure risk policy frameworks are visible and implemented, and that appropriate committee memberships and structures exist;
- best practice risk and capital methodologies for the appropriate identification, measurement, monitoring, management and reporting of risk and allocation of capital;
- accurate assessment of the broader organisational culture which determines business ethics practices, and supports or detracts from risk goals; and
- a people risk profile that provides a balance between skills and ethical values and the appropriate allocation of resources and accountability for performance.

The Group has established four parameters as the dominant drivers impacting the risk rating of its culture, outlined in the following table.

Risk culture parameters

Parameters	Activities
Leadership living good values	- ensure that leaders set the appropriate tone in terms of responsible business conduct.
Setting risk goals	- ensure risk management goals are set and properly communicated throughout the organisation; and - ensure that ethics and accountability to risk management parameters are considered as important as efficiency, innovation and profit.
Providing resources	- ensure risk management goals are attainable by adequately resourcing risk management functions; and - apply fit and proper tests for key risk roles.
Aligning measurement and rewards	- ensure risk metrics are incorporated into measurements and the way business rewards performance.

RISK AND CAPITAL METHODOLOGIES

Best practice risk and capital management methodologies have been developed in and for the relevant business areas. The detailed sections covering each major risk type provide in-depth descriptions of the approaches, methodologies, models and processes used in the identification and management of each major risk. Each section also describes:

- the applicable governance and policy framework;
- an analysis of the relevant portfolios;
- the risk profile with respect to the type of risk under consideration; and
- the capital requirement.

STRATEGIC AND BUSINESS RISK

INTRODUCTION AND OBJECTIVES

Any business runs the risk of choosing an inappropriate strategy or failing to execute its strategy appropriately. The Group's objective is to minimise this risk in the normal course of business.

Business risk is considered in the strategic planning process and as a part of regular and pervasive stress testing and scenario analyses carried out across the Group. The objective is to develop and maintain a portfolio that delivers sustainable earnings and minimises the chance of adverse outcomes.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

The development and execution of business level strategy is the responsibility of the strategic executive committee and the individual business areas, subject to approval by the board. This includes the approval of any subsequent material changes to strategic plans, budgets, acquisitions, significant equity investments and new strategic alliances.

Business unit and Group executive management, as well as Group Treasury and ERM review the external environment, industry trends, potential emerging risk factors, competitor actions and regulatory changes as part of strategic planning. Through this review, as well as regular scenario planning and stress-testing exercises, the risk to earnings and the level of potential business risks faced are assessed. Reports on the results of these exercises are discussed at various business, risk and board committees and are ultimately taken into account in the setting of risk appetite and potential revisions to existing strategic plans.

ASSESSMENT AND MANAGEMENT

Strategic risk is not readily quantifiable and is not a risk that an organisation can or should hold a protective capital buffer against. The risk to earnings on the other hand can be assessed and this forms an explicit part of the Group's risk processes.

Volume and margin risk

Volume and margin risk is considered part of strategic planning and is regularly assessed through the Group's management and governance processes and ICAAP. Volume and margin risk could result in a situation where the operating income of the Group is insufficient to absorb the variability in income and operating costs.

Reputational risk

As a financial services provider, the Group's business is one inherently built on trust and close relationships with its clients. Reputational risk can arise from environmental, social and governance issues or as a consequence of financial or operational risk events.

The Group's reputation is built on the way in which it conducts business and it protects its reputation by managing and controlling these risks across its operations. It seeks to avoid large risk concentrations by establishing a risk profile that is balanced within and across risk types. In this respect, potential reputational risks are also taken into account as part of stress-testing exercises. The Group aims to establish a risk and earnings profile within the constraints of its risk appetite and seeks to limit potential stress losses from credit, market, liquidity or operational risks that may otherwise introduce an undesirable degree of volatility in its financial results and adversely affect its reputation.

ENVIRONMENTAL AND SOCIAL RISK MANAGEMENT

Equator Principles and environmental and social risk analysis (ESRA)

FirstRand has formally integrated environmental and social risk management processes into its credit risk governance process, which is supported by enterprise-wide social and ethics committee structures. These processes include the following key measures:

- defining requirements for environmental and social risk assessment, and monitoring approved transactions;
- developing and communicating environmental and social performance standards that clients will be expected to meet within an acceptable time frame; and
- defining environmental and social roles and responsibilities for both FirstRand and its clients.

FirstRand became an Equator Principles (EP) finance institution in July 2009. Within FirstRand, the application of EP forms part of ESRA and is a specific framework for determining, assessing and managing environmental and social risk in affected transactions.

During 2012/2013, the EP Association and its member financial institutions conducted a strategic review and increased the scope of transactions to which EP applies. This new revised standard (EP III) has been implemented at FirstRand effective December 2013 for all products in the new scope of EP, which includes the types of transactions set out in the following table.

ESRA transaction type

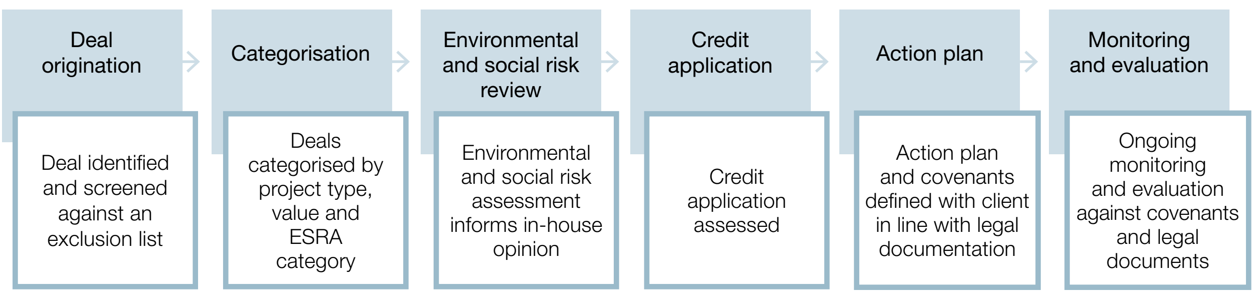
Transaction type	Threshold amount after which an ESRA review is triggered
Project finance transactions	Total project capital costs at or above US$10 million: EP review. All category A (high risk) and B (medium risk) transactions with a total project capital cost of less than US$10 million: in-house ESRA review.
Project finance advisory	Total project capital costs at or above US$10 million: EP review.
Corporate loans	No threshold applied, all corporate loans: in-house ESRA review.
Corporate loans – project related	Total aggregate loan amount is at least US$100 million of which the member banks' individual commitment (before syndication or sell down) is at least US$50 million and loan tenor is at least two years: EP review.
Bridge loans (subject to EP)	Bridge loans with a tenor of less than two years that are intended to be refinanced by project finance (at or above US$10 million): EP review.
Equity investment deals	No threshold applied, all equity investment deals: in-house ESRA review.
Affected commercial loans (inclusive of property finance)	No threshold applied, all property finance or property securitised loans: in-house ESRA review. Commercial loans (non-property related) – total facility amount above R7.5 million: in-house ESRA review.

ESRA review process

Specialist resources in the franchises serve as technical advisors to franchise senior management and employees involved with credit transactions and provide assessment, review, consultation and specialist advice on lending transactions.

Each of the Group's operating franchises have formalised credit and compliance processes for the implementation of ESRA, with oversight provided by franchise social and ethics committees, risk and compliance officers, and credit committees throughout the Group. The ESRA process is incorporated in the FirstRand credit risk management framework as an aspect of transaction risk management, and in the FirstRand environmental sustainability risk framework (a subframework of the regulatory risk management framework) as an aspect of environmental and social risk management. At a Group level, oversight is also provided by RRM and franchise social and ethics committees. The ESRA review process is illustrated in the following chart.

ESRA review process



In the event that a transaction is identified as being a high environmental or social risk, or an exception to the defined process, the transactor, franchise chief risk officers and franchise heads of credit are informed through a formalised escalation process. Transaction approval is provided by franchise chief risk officers and heads of credit and reported to the relevant quarterly franchise social and ethics committees by the chief risk officer for discussion and noting.

FirstRand has formal governance processes for managing environmental and social risks affecting the Group's ability to successfully implement business strategy. These processes involve the integration of environmental and social information into the relevant sections of risk reports at Group and franchise level. Tolerances and mitigating actions are defined at Group and franchise level, and progress in respect of these is tracked through existing risk reporting structures. Provision is made for the escalation of significant environmental and social issues to the board via the executive, RCC and audit committees.

2014 EP performance

The Group measures EP performance in line with the International Finance Corporation (IFC) performance standards as either Category A (high risk), Category B (medium risk) or Category C (low to no risk), per the definitions set out in the table.

Definition of EP performance categories

IFC/equator category	Risks/impacts
Category A (high risk)	Projects with potential significant adverse social or environmental impacts that are diverse, irreversible or unprecedented. Issues relating to these risks may lead to work stoppages, legal authorisations being withdrawn and reputational damage. Examples could include projects involving the physical displacement of the natural environment or communities.
Category B (medium risk)	Projects with potential limited adverse social or environmental impacts that are few in number, generally site specific, largely reversible and readily addressed through mitigation measures. Issues relating to these risks may lead to fines, penalties or legal non-compliance and reputational damage. Examples could include increased use of energy or increased atmospheric emissions.
Category C (low risk)	Projects with minimal or no social or environmental impacts.

During the financial year the new automated categorisation tool was implemented in the franchises, which will improve the accuracy of future reporting of ESRA transactions. Additional disclosure to comply with the EP III reporting requirements are included in this report.

EP transactions

The projects reported are the structured EP-defined deals, which were reviewed by in-house environmental and social risk specialists. These specialists provide technical advice to divisional senior management and employees involved with credit transactions and provide assessment, review, consultation and specialist advice on lending transactions.

All category A and B transactions were subjected to independent EP review to establish environmental and social risks of the project and have reached financial close during the reporting period. Financial close is assumed when all conditions precedent to initial drawing of the debt have been satisfied or waived. EP reporting is externally assured for public disclosure by an independent third party as per the requirements set out by the EP Association.

Analysis of EP transactions

The number of EP transactions screened per industry categories and regions is provided in the following tables.

EP project finance loans

	2014				2013*			
Transactions per category**	**Total**	**A high risk**	**B medium risk**	**C low risk**	**Total**	**A high risk**	**B medium risk**	**C low risk**
By sector								
Mining		**2**	**–**	**–**		3	–	–
Infrastructure		**–**	**–**	**1**		–	–	2
Power		**–**	**1**	**–**		–	–	–
Renewable energy		**–**	**2**	**–**		–	4	–
Retail		**–**	**–**	**8**		–	–	12
By region								
Americas		**–**	**–**	**–**		2	–	–
Middle East and Africa		**2**	**3**	**9**		1	4	14
By country designation								
Designated#		**–**	**–**	**–**		2	–	–
Non-designated		**2**	**3**	**9**		1	4	14
Independent review†								
Yes		**2**	**3**	**–**		3	4	–
No		**–**	**–**	**9**		–	–	14
By EP category								
Total number of EP transactions	**14**	**2**	**3**	**9**	21	3	4	14

* *The 2013 financial year data were restated in order to reflect transactions that reached financial close during the 2013 period in line with changes in the reporting requirements of EP III.*

** *No transactions in the oil and gas category or Europe, Asia and Oceania regions reached financial close during 2013 and 2014.*

A designated country is a high income country as per the Organisation for Economic Cooperation and Development (OECD) country list.

† *An independent review is not required for category C projects. EP provides details on what is required for each category and product type.*

Project-related corporate loans

The Group is required to disclose project-related corporate loans that reached financial close from year ending 30 June 2014, with comparative information from 30 June 2015. The information will include the detailed breakdown of project-related corporate loans per category split by sector, region, country designation, independent review and total transactions. Whilst there are project-related corporate loans that were initiated during the 2014 financial year, none of these reached financial close. Performance data of project-related corporate loans, that have reached financial close, will be disclosed from 2015 onwards.

EP project finance advisory transactions

	2014				2013*			
Transactions per category**	**Total**	**A high risk**	**B medium risk**	**C low risk**	**Total**	**A high risk**	**B medium risk**	**C low risk**
By sector								
Mining		**1**	**–**	**–**		2	–	–
Infrastructure		**–**	**1**	**–**		–	–	–
Power		**–**	**–**	**–**		–	1	–
Renewable energy		**–**	**1**	**–**		–	4	–
By region								
Middle East and Africa		**1**	**2**	**–**		2	5	–
Total by EP category	**3**	**1**	**2**	**–**	7	2	5	–

* *The 2013 financial year data were restated in order to reflect transactions that reached financial close during the 2013 period in line with changes in the reporting requirements of EP III.*

** *No project finance advisory transactions reached financial close in the oil, gas and retail sectors, and Americas, Europe, Asia and Oceania regions during 2013 and 2014.*

ESRA process going forward

The Group is currently in the sixth year of implementation of ESRA processes. Continued focus will be given to awareness training, effective application and continued improvement of the ESRA process. In the new financial year, areas of focus will include the expansion of the ESRA process into the Group's subsidiaries in the rest of Africa. Rollout of this process is expected to take place over a three-year period.

CAPITAL MANAGEMENT

INTRODUCTION AND OBJECTIVES

The overall capital management objective is to maintain sound capital ratios and a strong credit rating to ensure confidence in the solvency and quality of capital in the Group during calm and turbulent periods in the economy and financial markets. Capitalisation ratios within the Group's risk appetite and appropriate to safeguarding operations and interests of stakeholders are, therefore, maintained.

The optimal level and composition of capital is determined after taking into account business units' organic growth plans – provided financial targets are met. In addition, other factors taken into consideration are:

- targeted capital ratios;
- future business plans;
- issuance of capital instruments;
- stress testing scenarios;
- appropriate buffers in excess of minimum requirements;
- rating agencies' considerations;
- investor expectations (including debt holders);
- economic capital requirements;
- proposed regulatory changes; and
- the board's risk appetite.

Allocating resources effectively, including capital and risk capacity, in terms of the risk appetite targets and in a manner that maximises value for shareholders is a core competence and key focus area. Sound capital management practices, therefore, form an important component of overall business strategy.

Effectiveness of capital allocation decisions and efficiency of the capital structure are important determinants of the ability to generate returns for shareholders. The Group seeks to hold limited excesses above the capital required to support its medium-term growth plans (including appropriate buffers for stresses and volatility) and future regulatory changes.

The total capital plan includes a dividend policy, which is set to ensure sustainable dividend cover based on sustainable normalised earnings. The plan also takes into account volatile earnings brought on by fair value accounting, anticipated earnings yield on capital employed, organic growth requirements and a safety margin for unexpected fluctuations in business plans.

CAPITAL ADEQUACY AND PLANNING

Year under review

The capital planning process ensures that the total capital adequacy and CET1 ratios remain within approved ranges or above target levels across economic and business cycles. The Group is appropriately capitalised under a range of normal and severe scenarios (including stress events) and taking into account ongoing regulatory developments and expansion initiatives in the rest of Africa.

The Group operated above its targeted capitalisation range throughout the year under review, reporting a total capital adequacy ratio of 16.7% and a CET1 ratio of 13.9% at 30 June 2014. The add-on for domestic systemically important banks (D-SIB) was finalised during the current financial year, however, remains confidential. The Group's internal target levels have been revised in order to take into account end-state regulatory minimum requirements, including the capital conservation buffer, and also after considering various stakeholder constraints.

The board-approved adjusted targets and actual capital ratios at 30 June 2014 are summarised in the table below.

Capital adequacy position

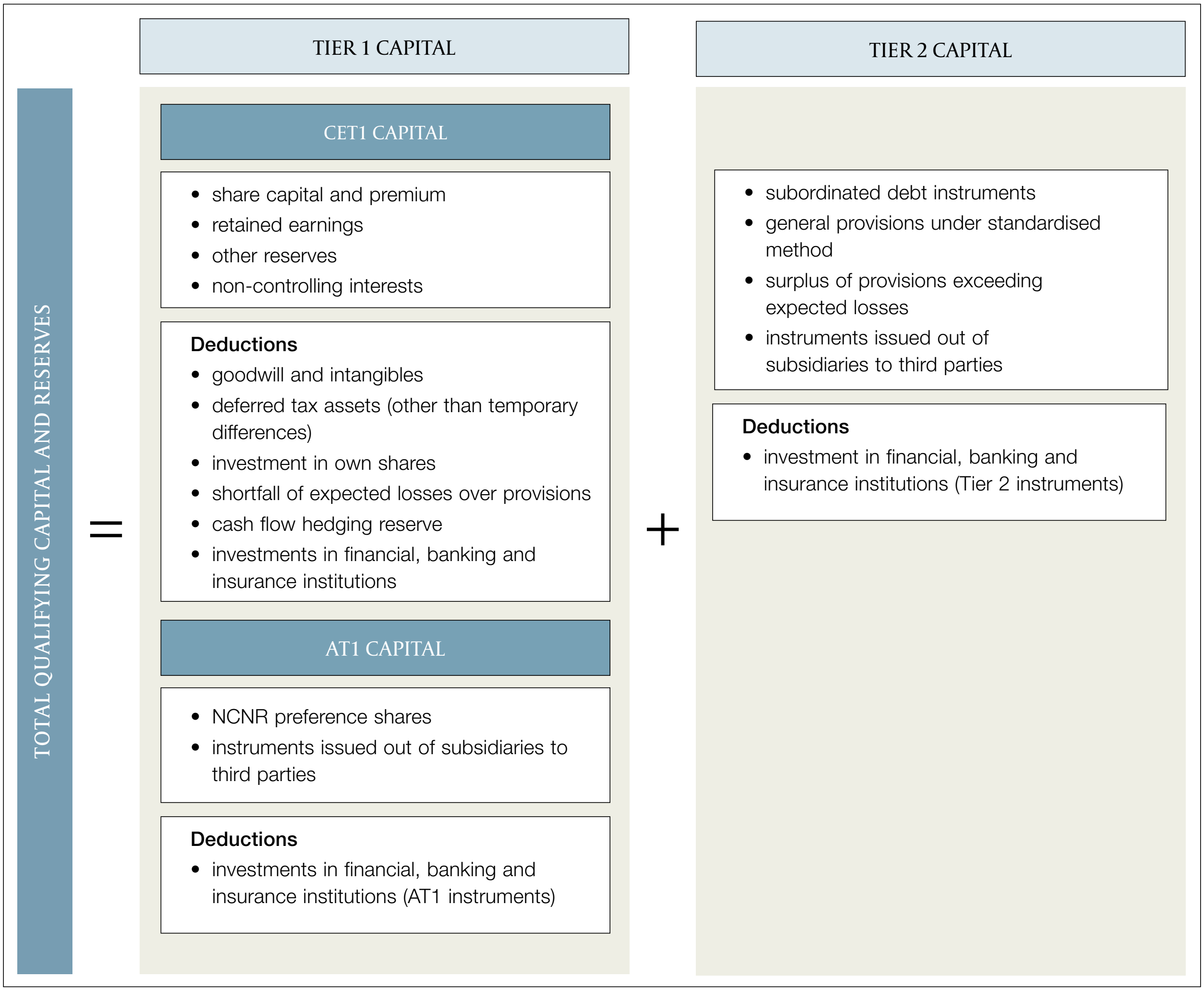
%	CET1	Tier 1	Total
Regulatory minimum*	5.5	7.0	10.0
Target	10.0 – 11.0	>12.0	>14.0
Actual	**13.9**	**14.8**	**16.7**

* *Excludes the bank-specific individual capital requirement.*

Basel III

Regulatory capital supply includes CET1, Tier 1 and Tier 2 qualifying capital and reserves. The following diagram illustrates the main elements:

Qualifying capital components



The BCBS has issued a number of consultative documents over the past year. These papers cover various topics and are at different stages of testing, finalisation and implementation.

The Group continues to participate in the BCBS's quantitative impact studies to assess the effect of Basel III and monitor the impact of leverage for the industry. The BCBS issued the final leverage framework in January 2014, with final calibrations and adjustments expected by 2017. The ratio is expected to transition to a Pillar 1 requirement by 2018. The leverage ratio is calculated by dividing Tier 1 capital by total exposures (on- and off-balance sheet) as defined. The Group's current leverage ratio comfortably exceeds the existing SARB minimum requirement of 4%.

Internal capital adequacy assessment process

ICAAP is key to the Group's risk and capital management processes as it is an integral tool in meeting the capital management objectives of the Group. ICAAP allows and facilitates:

- the link between business strategy, risk introduced and capital required to support the strategy;
- the establishment of frameworks, policies and procedures for the effective management of material risks;
- the embedding of a responsible risk culture at all levels in the organisation;
- the effective allocation and management of capital in the organisation;
- the development of recognised stress tests to provide useful information which serve as early warnings/triggers, so that contingency plans can be implemented;
- the determination of the capital management strategy and how the Group will manage its capital during business as usual and periods of stress; and
- the capital plan.

The board-approved capital plan is reviewed annually as part of the Group's ICAAP, with the stress-testing framework an extension of the process. ICAAP assists in the allocation of capital in proportion to risks inherent in the respective businesses with reference to normal economic circumstances and times of potential stress, which may lead to the realisation of risks not previously considered. These processes are under continuous review and refinement, and continue to inform the targeted buffer over the minimum capital requirement.

The Group aims to back all economic risk with CET1 capital adjusted for volatile reserves (foreign currency translation and availale-for-sale reserves) and remains well capitalised in the current environment.

Capital adequacy

Supply of capital

The following table summarises the qualifying capital for the Group.

Composition of qualifying capital

	FirstRand	
R million	**2014**	**2013***
CET1 capital	**79 344**	71 869
Tier 1 capital	**84 647**	77 212
Total qualifying capital and reserves**	**95 368**	84 690

* *Comparatives have not been restated for IFRS changes.*

** *Share capital, share premium and retained earnings included in total qualifying capital and reserves have been audited.*

CET1 capital benefited from strong internal capital generation through earnings. All profits were appropriated at 30 June 2014.

Existing non-compliant Basel III NCNR preference shares and Tier 2 instruments were grandfathered by an additional 10% in January 2014. Given SARB guidance on the loss absorbency requirements for capital instruments, the Group continues to focus on the most optimal capital mix and pricing. During the year under review, the Group issued R3.8 billion Basel III-compliant Tier 2 instruments. For more detail on these instruments refer to the main features template discussed below.

Demand for capital

The table below shows the breakdown of the RWA per risk type as per current SARB regulations.

RWA and capital requirements

	FirstRand				
	2014				2013
	RWA				
R million	Advanced approach	Standardised approach	Total	Capital requirement*	RWA
Credit risk	**319 368**	**78 792**	**398 160**	**39 816**	358 133
– Corporate, banks and sovereigns	**140 257**	**22 433**	**162 690**	**16 269**	138 931
– Small and medium enterprises (SMEs)	**41 835**	**20 011**	**61 846**	**6 185**	54 242
– Residential mortgages	**48 203**	**5 534**	**53 737**	**5 374**	53 226
– Qualifying revolving retail	**20 030**	**220**	**20 250**	**2 025**	18 581
– Other retail	**67 130**	**14 790**	**81 920**	**8 192**	69 767
– Securitisation exposure	**1 913**	**–**	**1 913**	**191**	4 642
– Other	**–**	**15 804**	**15 804**	**1 580**	18 744
Counterparty credit risk**	**1 127**	**190**	**1 317**	**132**	2 548
Total credit risk	**320 495**	**78 982**	**399 477**	**39 948**	360 681
Operational risk#	**73 398**	**20 215**	**93 613**	**9 361**	83 219
Market risk	**11 577**	**1 541**	**13 118**	**1 312**	9 785
Equity investment risk	**34 128**	**–**	**34 128**	**3 413**	38 190
Other assets†	**–**	**32 110**	**32 110**	**3 211**	28 085
Total RWA	**439 598**	**132 848**	**572 446**	**57 245**	519 960

* *Capital requirement calculated at 10.0% of RWA.*
** *Excludes default risk.*
\# *Exposures subject to the basic indicator approach are included under the standardised approach.*
† *Includes the investment in financial, banking and insurance entities and deferred tax assets risk weighted at 250%.*

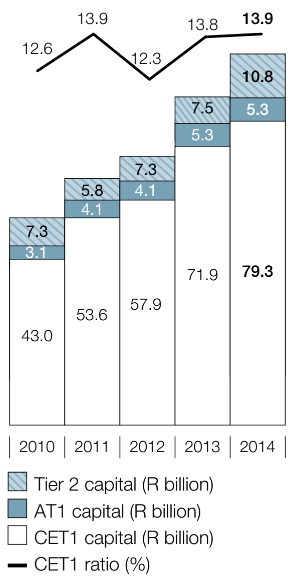
Overall movement in RWA can be attributed to the following:

- credit risk increased due to volume growth, partly offset by model recalibrations;
- operational risk increased due to:
  - recalibration of risk scenarios;
  - increase in gross income for entities on the standardised approach; and
  - the SARB add-on for the difference between the capital calculated on the AMA approach and the standardised approach;
- market risk increased due to the implementation of a higher capital multiplier resulting in an increase in general market risk; and
- equity investment risk decreased mainly due to the change in IFRS reporting for post-employment assets and realisations of equity investments.

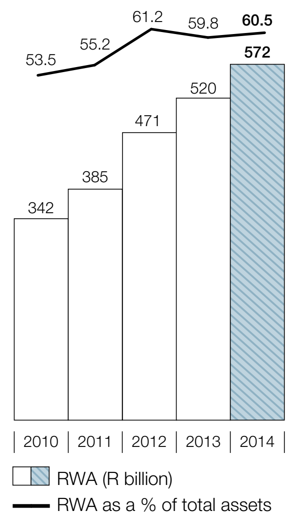
Historical overview of capital adequacy

The graphs below show the historical overview of RWA and capital adequacy of FirstRand.

Capital adequacy



RWA history



Refer to www.firstrand.co.za/investorcentre/pages/capitaldisclosures.aspx for further detail on the following:

- composition of capital;
- main features of capital instruments; and
- reconciliation of audited financial statements to regulatory capital and reserves.

The abovementioned disclosure templates comply with the requirements of SARB Directive 8 of 2013, which forms part of the annual Pillar 3 disclosure for the year ended 30 June 2014.

Scan with your smart device's QR code reader to access additional capital disclosures on the Group's website.

Capital adequacy position for FirstRand, its subsidiaries and foreign branches

The registered banking subsidiaries of FirstRand must comply with SARB regulations and those of the respective in-country regulators, with primary focus placed on Tier 1 capital and total capital adequacy ratios. Based on the outcome of detailed stress testing, each entity targets a capital level in excess of the regulatory minimum. Adequate controls and processes are in place to ensure that each entity is adequately capitalised to meet local regulatory requirements. Capital generated by subsidiaries/branches in excess of targeted levels is returned to FirstRand, usually in the form of dividends/return of profits. During the year under review, no restrictions were experienced on the repayment of such dividends or profits to the Group.

The capital adequacy positions of FirstRand, its subsidiaries and foreign branches are set out below.

RWA and capital adequacy positions of FirstRand, its subsidiaries and foreign branches

	For the year ended 30 June			
	2014			2013
	RWA R million	Tier 1 %	Total capital adequacy %	Total capital adequacy %
Basel III				
FirstRand	**572 446**	**14.8**	**16.7**	16.3
FirstRand Bank South Africa	**423 257**	**14.2**	**16.1**	14.9
FirstRand Bank London	**22 413**	**10.2**	**19.0**	11.3
FirstRand Bank India	**1 803**	**31.0**	**31.8**	36.0
RMB Australia	**9 199**	**14.1**	**14.1**	11.5
Basel I/II*				
FNB Namibia**	**18 034**	**13.8**	**17.1**	16.2
FNB Botswana	**14 286**	**15.9**	**18.3**	17.4
FNB Swaziland	**2 333**	**21.2**	**22.3**	28.1
FNB Lesotho	**647**	**14.0**	**17.7**	18.1
FNB Mozambique**,#	**3 058**	**7.8**	**8.2**	12.7
FNB Zambia	**3 023**	**26.5**	**31.9**	26.6
FNB Tanzania	**324**	**>100**	**>100**	26.7
RMB Nigeria	**417**	**>100**	**>100**	>100

* *Based on local rules.*
** *Currently operating under Basel II regulations.*
\# *Capital ratios do not reflect recapitalisation due to outstanding notarisation. Total capital adequacy including recapitalisation is 15.8%.*

CREDIT RISK

INTRODUCTION AND OBJECTIVES

The goal of credit risk management is to maximise the Group's risk-adjusted return, i.e. NIACC, within acceptable levels of earnings volatility by maintaining credit risk exposure within acceptable parameters.

Credit risk is one of the core risks assumed as part of achieving the Group's business objectives. It is the most significant risk type in terms of regulatory and economic capital requirements. Credit risk management objectives are two-fold:

- **Risk control:** Appropriate limits are placed on the assumption of credit risk and steps are taken to ensure the accuracy of credit risk assessments and reports. Deployed and central credit risk management teams fulfil this task.
- **Management:** Credit risk is taken within the constraints of the risk appetite framework. The credit portfolio is managed at an aggregate level to optimise the exposure to this risk. Business units and deployed risk functions, overseen by the Group credit risk management function in ERM and relevant board committees, fulfil this role.

Credit risk management across the Group is split into three distinct portfolios: retail, commercial and corporate. These portfolios are aligned to customer profiles. As advances are split across operating franchises, default risk is allocated to the income-receiving portfolio.

Based on the Group's risk appetite for credit risk, as measured on a ROE, NIACC and volatility of earnings basis, credit risk management principles include appropriate capital holdings and pricing for risk on an individual and portfolio basis. The scope of credit risk identification and management practices across the Group, therefore, spans the credit value chain, including credit origination strategy, risk appetite, risk quantification and measurement and collection and recovery of delinquent accounts.

Credit risk is managed through comprehensive policies and processes that ensure adequate identification, measurement, monitoring, control and reporting of credit risk exposure. The objective is to ensure a sound credit risk management environment with appropriate credit granting, administration, measurement and monitoring through the implementation of adequate risk management controls.

Retail credit

FNB's secured retail products include mortgage finance with property as security for the loan and pension-backed loans, where lending is secured by a portion of the client's pension fund to purchase or improve a property. WesBank's secured retail credit exposure arises mainly from instalment sale agreements for motor vehicle financing.

Unsecured products in both FNB and WesBank include:

- personal loans ranging from small short-term loans to larger loans;
- revolving loans, overdrafts, temporary loans and device loans linked mainly to transactional accounts of FNB-banked clients; and
- credit cards with revolving credit limits and either straight or budget period repayment facilities.

Commercial credit

The commercial credit portfolio strategy is focused on tailoring credit products for commercial customers. FNB (primary relationship owner) and WesBank both provide products, which include:

- revolving overdraft facilities linked to transactional demand deposit accounts;
- traditional VAF and fleet petrol cards;
- dealer funding solutions to selected vehicle dealerships secured by trade stock;
- guarantees and letters of credit to assist in the facilitation of transactions;
- forward exchange contracts and interest rate swaps;
- secured term loans;
- property finance includes owner-occupied and multi-tenanted properties as well as finance for residential developments secured by the properties;
- leveraged finance provides specialised business financing to fund, amongst others, business acquisitions, management buy-outs, management buy-ins, BEE transactions and balance sheet restructuring; and
- working capital facilities secured against debtors books and selective invoice discounting.

Corporate credit

Corporate credit products include the following offered by RMB to large corporate multi-banked customers:

- all-inclusive financing packages for investment banking clients;
- funding of corporate businesses, government and parastatals through debt capital market instruments;
- structured asset finance for client funding requirements in local and cross-border strategic jurisdictions in the rest of Africa;
- structuring, raising and underwriting of equity capital and structured equity solutions;
- infrastructure and project finance;
- leveraged finance;
- real estate investment banking;

- guarantees and letters of credit to assist in the facilitation of transactions;
- working capital and general banking facilities; and
- resource finance.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

The Group has a comprehensive credit governance committee structure with the responsibility to approve, monitor and oversee credit risk management and exposures of the Group. Additional management committees within the business assist in strengthening credit risk management.

The RCC committee and franchise excos regularly receive and review reports on the adequacy and robustness of credit risk identification, management and control processes, as well as on the current and projected credit risk profile across the Group. The credit risk management governance structures, related roles and responsibilities as well as lines of accountability are set out in the credit risk management framework. Approved by the RCC committee and FirstRand credit risk management committee (a subcommittee of the RCC committee), the credit risk management framework is board-approved policy and a subframework of the BPRMF, as discussed in the *risk governance* section.

The large exposure committee (a board committee) and the FirstRand credit risk management committee support the RCC committee in its tasks. The model risk and validation committee, also a subcommittee of the RCC committee, supports the RCC committee specifically on risk capital models. For a description of the role and responsibilities of these committees refer to the *risk governance* section.

The Group credit risk management function

The Group credit risk management function in ERM provides independent oversight of the credit risk management practices of the Group's operating franchises to ensure effective and holistic credit risk management process. It is responsible for the credit risk management framework and related policies and monitors the implementation of credit risk-related frameworks. In addition, its responsibilities include:

- reporting an independent view of the Group's credit risk profile and potential areas of concern via the risk committees to the board;
- challenging the risk profile, providing advice or guidance on credit risk management matters as requested, setting standards for credit risk reporting and providing additional reporting where required;
- maintaining and overseeing the Group's credit governance structures and credit measurement process;
- performing independent validations of regulatory capital credit rating systems;
- acting as key contact to the SARB on credit risk matters, including credit BA returns;
- ensuring completeness of credit risk identification;
- implementing credit risk methodologies and capabilities across the Group; and
- facilitating and managing credit risk appetite processes across the Group.

The Group credit risk management function is supported by credit risk functions within the franchises, which are managed by portfolio heads (retail, commercial and corporate).

Specific credit responsibilities lie with each credit portfolio head, including:

- accountability to the Group's governance forums and liaison with regulators;
- maintaining high competency levels/skills in each credit function;
- alignment of credit origination strategy and appetite;
- implementation and assessment of credit governance frameworks and policy compliance;
- streamlining and consolidation of functions, systems and mandates; and
- calculating volatility profile for aggregate portfolios.

ASSESSMENT AND MANAGEMENT

Calculation of internal ratings and rating process

The assessment of credit risk across the Group relies on internally-developed quantitative models for regulatory purposes under the Regulations, as well as addressing business needs.

Credit risk models are widely employed in the assessment of capital requirements, pricing, impairment calculations and stress testing of the credit portfolio. All of these models are built on a number of client and facility rating models, in line with SARB AIRB approach requirements and the Group's model building frameworks. The credit risk approaches across the Group are shown in the following table.

Basel approach	FirstRand Bank SA	Remaining FirstRand subsidiaries
AIRB	✓	
Standardised approach		✓

Even though the remaining subsidiaries do not have regulatory approval to use the AIRB approach, the same or similar models are applied for the internal assessment of credit risk on the standardised approach. The models are used for internal assessment of the following three primary credit risk components discussed in the following sections:

- probability of default (PD);
- exposure at default (EAD); and
- loss given default (LGD).

Management of the credit portfolio is reliant on these three credit risk measures. PD, EAD and LGD are inputs into the portfolio and Group-level credit risk assessment where the measures are combined with estimates of correlations between individual counterparties, industries and portfolios to reflect diversification benefits across the portfolio.

Probability of default

PD is defined as the probability of a counterparty defaulting on any of its obligations over the next 12 months and is a measure of the counterparty's ability and willingness to repay facilities granted. A default, in this context, is defined along two dimensions:

- time-driven: the counterparty is in arrears for more than 90 days or three instalments; and
- event-driven: there is reason to believe that the exposure will not be recovered in full and has been classified as such.

This definition of default is consistently applied across all credit portfolios as well as in the recognition of NPLs for accounting purposes.

The Group employs a granular, 100-point master rating scale, which has been mapped to the continuum of default probabilities, as illustrated in the following table.

Mapping of FirstRand (FR) grades to rating agency scales

FR rating	Midpoint PD	International scale mapping*
FR 1 – 14	0.06%	AAA, AA, A
FR 15 – 25	0.29%	BBB
FR 26 – 32	0.77%	BB+, BB
FR 33 – 39	1.44%	BB-
FR 40 – 53	2.52%	B+
FR 54 – 83	6.18%	B
FR 84 – 90	13.68%	B-
FR 91 – 99	59.11%	Below B-
FR 100	100%	D (defaulted)

* *Indicative mapping to the international rating scales of Standard & Poor's. These mappings are reviewed and updated on a regular basis.*

FR 1 is the lowest PD and FR 100 the highest. External ratings have also been mapped to the master rating scale for reporting purposes. In line with international best practice, the Group distinguishes between the two measures of PD, both used for the management of exposure to credit risk:

- Through-the-cycle (TTC) PD measures reflect long-term, average default expectations over the course of the economic cycle. TTC PDs are inputs in economic and regulatory capital calculations.
- Point-in-time (PIT) PD measures reflect default expectations in the current economic environment and thus tend to be more volatile than TTC PDs. PIT PDs are used in credit portfolio management, including risk appetite and portfolio monitoring.

Exposure at default

The EAD of a particular facility is defined as the expected exposure to a counterparty through a facility should the counterparty default over the next 12 months. It reflects commitments made and facilities granted that have not been paid out and that may be drawn over the period under consideration (i.e. off-balance sheet exposures). It is also a measure of potential future exposure on derivative positions.

Tailored to the respective portfolios and products employed, a number of EAD models are in use across the Group. These have been developed internally and are calibrated to historical default experience.

Loss given default

LGD is the third major credit risk component estimated on the basis of internal models. It is defined as the economic loss on a particular facility upon default of the counterparty. It is expressed as a percentage of exposure outstanding at the time of default. In most portfolios, LGD is dependent on:

- type, quality and level of subordination;
- value of collateral held compared to the size of overall exposure; and
- effectiveness of the recovery process and timing of cash flows received during the workout or restructuring process.

A number of models are used to assess LGDs across various portfolios. These models were developed internally and the outputs are calibrated to reflect both the internal loss experience, where available, and external benchmarks, where appropriate.

Typically, a distinction is made between the long-run expected LGDs (long-run LGDs) and LGDs reflective of downturn conditions. The latter is a more conservative assessment of risk, which incorporates a degree of interdependence between PD and LGD that can be found in a number of portfolios i.e. instances where deteriorating collateral values are also indicative of higher default risk. The more conservative measure of LGD is used in the calculation of regulatory capital estimates.

Expected loss (EL)

EL, the product of the primary risk measures PD, EAD and LGD, is a forward-looking measure of portfolio or transaction risk. It is used for a variety of purposes along with other risk measures. EL is not directly comparable to impairment levels, as EL calculations are based on the regulatory parameters TTC PD and downturn LGD, and impairment calculations are driven by IFRS requirements.

Slotting approach

Specialised lending relates mainly to project and commodity finance. In terms of the slotting approach, the exposure is rated after assessing the risks and mitigations applied to reduce/eliminate risk and mapped to one of four supervisory categories. This will apply where the Group finances an entity created to finance and/or operate physical assets where the primary source of repayment of the obligation is the income generated by the assets, i.e. specialised lending specifically in project and commodity finance.

Rating process

The Group employs a consistent rating process differentiated by the type of counterparty and the type of model employed for rating purposes. For example, retail portfolios are segmented into homogeneous pools in an automated process. Based on the internal product level data, PDs are then estimated (and continuously updated) for each pool. The following table summarises the processes and approaches employed and provides an overview of the types of exposures within each of the portfolios.

Credit portfolio rating process

Portfolio and type of exposures	Description of rating system
Large corporate portfolios (Wholesale: RMB, WesBank corporate and FCC) Exposures to private sector counterparties including corporates and securities firms and public sector counterparties. A wide range of products give rise to credit exposure, including loan facilities, structured finance facilities, contingent products and derivative instruments.	The default definitions applied in the rating systems are aligned to the Regulations. **Rating process:** • rating assignment to corporate credit counterparties is based on a detailed individual assessment of the counterparty's creditworthiness; • this assessment is performed through a qualitative analysis of the business and financial risks of the counterparty and is supplemented by internally developed statistical rating models; • rating models were developed using internal and external data covering more than ten years. Qualitative analysis is based on the methodology followed by international rating agencies; • the rating assessment is reviewed by the wholesale credit committee or delegated subcommittee and the rating (and associated PD) is approved by these committees; • no overrides of the ratings or the PDs are possible after approval by these committees; and • LGD and EAD estimates are based on modelling of a combination of internal and suitably adjusted international data with the same committee process responsible for reviewing and approving these measures.
Low default portfolios: sovereign and bank exposures (Corporate: RMB and FCC) Exposures to sovereign and bank counterparties.	The default definitions applied in the rating systems are aligned to the Regulations. **Rating process:** • expert judgement models are used in combination with external rating agency ratings as well as structured peer group analyses which form a key input in the ratings process. The analysis is supplemented by internally developed statistical models; • the calibration of PD and LGD ratings is based on a mapping to external default data as well as credit spread market data; • the rating assessment is reviewed by the wholesale credit committee or delegated subcommittee and the rating (as well as the associated PD) is approved by these committees; and • no overrides of the ratings or the PDs are possible after approval by these committees.

Portfolio and type of exposures	Description of rating system
Specialised lending portfolios (Corporate: RMB, FNB commercial and wealth (RMB private bank and FNB private clients)) Exposures to private-sector counterparties for the financing of income-producing real estate.	The default definitions applied in the rating systems are aligned to the Regulations. **Rating process:** - rating system is based on hybrid models using a combination of statistical cash flow simulation models and qualitative scorecards calibrated to a combination of internal data and external benchmarks; - the rating assessment is reviewed by the wholesale credit committee, commercial credit committee or delegated subcommittee and the rating (as well as the associated PD) is approved by these committees; and - no overrides of the ratings or the PDs are possible after approval by these committees.
Commercial portfolio (SME corporate and SME retail counterparties in FNB commercial and WesBank) Exposures to SME clients. A wide range of products give rise to credit exposure, including loan facilities, contingent products and term lending products.	The default definitions applied in the rating systems are aligned to the Regulations. **SME retail rating process:** - the SME retail portfolio is segmented into homogeneous pools and subpools through an automated scoring process using statistical models that incorporate product type, customer behaviour and delinquency status; - PDs are estimated for each subpool based on internal product level history associated with the respective homogeneous pools and subpools; and - LGD and EAD estimates are applied on a portfolio level, estimated from internal historical default and recovery experience. **SME corporate rating process:** - PD: Counterparties are scored using Moody's RiskCalc™ in addition to other internal risk drivers, the output of which is calibrated to internal historical default data; - LGD: Recovery rates are largely determined by collateral type and these have been set with reference to internal historical loss data, external data (Fitch Ratings) and Basel guidelines; and - EAD: Portfolio level credit conversion factors are estimated on the basis of the Group's internal historical experience and benchmarked against international studies.
Residential mortgages (Retail portfolios in FNB HomeLoans, FNB housing finance, wealth (RMB private bank and FNB private clients) and mortgage exposures in the FNB smart segment) Exposures to individuals for the financing of residential properties.	The default definition applied in the rating systems is aligned to the Regulations. **Rating process and approach:** - retail portfolios are segmented into homogeneous pools and subpools through an automated scoring process using statistical models that incorporate product type, loan characteristics, customer behaviour, application data and delinquency status; - PDs are estimated for each subpool based on internal product level history associated with the respective homogeneous pools and subpools; - no overrides of the PDs are possible. The only potential override is not that of the PD, but rather of the automated decision to lend or not. Such overrides may be done on the basis of the credit manager's judgement in a structured process supported by valid business reasons; and - LGD and EAD estimates are based on subsegmentation with reference to the collateral or product type as well as associated analyses and modelling of historical internal loss data. **Additional notes on qualifying revolving retail exposures:** - these exposures are unsecured and, therefore, only the efficiency of recovery processes impacts on the level of LGD; and - EAD measurement plays a significant role in the assessment of risk due to the typically high level of undrawn facilities characteristic of these product types. EAD estimates are based on actual historic EAD, segmented appropriately (e.g. straight versus budget in the case of credit cards).
Qualifying revolving retail exposures (Retail portfolios in FNB card, FNB core banking solutions and wealth) Exposures to individuals providing a revolving limit through a credit card or overdraft facility.	
Other retail exposures (Retail portfolios in FNB loans, FNB smart segment, WesBank VAF and WesBank loans)	

Model validation

Rating models are recalibrated and independently validated on an annual basis to ensure validity, efficacy and accuracy. Rating models across portfolios incorporate an appropriate degree of conservatism, achieved through prudent choice of model parameters and inclusion in the calibration of downturn periods such as 2001 and 2007 to 2009.

Independent validation of rating systems is carried out by the Group credit risk management function in ERM. It is responsible for reviewing all rating systems and an annual comprehensive revalidation of all material rating systems. The model risk audit team in GIA carries out sample revalidations of the rating systems. The results of these reviews are reported to and approved by the model risk and validation committee and the RCC committee, depending on materiality. As part of this process, extensive documentation covering all steps of the model development lifecycle from inception through to validation is maintained, including:

- developmental evidence, detailing processes followed and data used to set parameters for the model. These documents are updated at least annually by the model development teams;
- independent validation reports, documenting the process followed during the annual validation exercise and results obtained from these analyses; and
- model build and development frameworks, which are reviewed and, where required, updated annually. These frameworks provide guidance, principles and minimum standards which the model development teams are required to adhere to.

Credit risk mitigation

Since taking and managing of credit risk is core to its business, the Group aims to optimise the amount of credit risk it takes to achieve its return objectives. Mitigation of credit risk is an important component of this process, beginning with the structuring and approval of facilities for only those clients and within those parameters that fall within risk appetite.

Although, in principle, credit assessment focuses on the counterparty's ability to repay the debt, credit mitigation instruments are used where appropriate to reduce the Group's lending risk, resulting in security against the majority of exposures. These include financial or other collateral, netting agreements, guarantees or credit derivatives. The collateral types are driven by portfolio, product or counterparty type:

- mortgage and instalment sale finance portfolios in FNB HomeLoans, FNB wealth and WesBank are secured by the underlying assets financed;
- personal loans, overdrafts and credit card exposures are generally unsecured or secured by guarantees and sureties;
- FNB commercial credit exposures are secured by the assets of the SME counterparties and commercial property finance deals are secured by the underlying property and associated cash flows;
- working capital facilities in RMB corporate banking are unsecured;
- structured facilities in RMB are secured as part of the structure through financial or other collateral, including guarantees, credit derivative instruments and assets; and
- credit risk in RMB is mitigated through the use of netting agreements and financial collateral.

The Group employs strict policies governing the valuation and management of collateral across all business areas. Collateral is managed internally to ensure that title is retained over collateral taken over the life of the transaction. Collateral is valued at the inception of the credit agreement and subsequently where necessary through physical inspection or index valuation methods. For corporate and commercial counterparties, collateral is reassessed during the annual review of the counterparty's creditworthiness to ensure that proper title is retained over collateral. For mortgage portfolios, collateral is revalued on an ongoing basis using an index model and physical inspection is performed in the event of default at the beginning of the recovery process.

The concentrations within credit risk mitigation types, such as property, are monitored and managed in the three credit portfolios. FNB HomeLoans, housing finance and wealth monitor exposure to a number of geographical areas, as well as within loan-to-value bands.

Collateral is taken into account for capital calculation purposes through the determination of LGD. Collateral reduces LGD, and LGD levels are determined through statistical modelling techniques based on historical experience of the recovery processes.

Monitoring of weak exposures

Credit exposures are actively monitored throughout the life of transactions. Portfolios are formally reviewed by portfolio committees either monthly or quarterly to assess levels of individual counterparty risk, portfolio risks and to act on any early warning indicators. The performance and financial condition of borrowers is monitored based on information from internal performances, credit bureaux, borrowers and publicly-available information. The frequency of monitoring and contact with the borrower is determined from the borrower's risk profile. Reports on the overall quality of the portfolio are monitored at a business unit level, portfolio level and in aggregate for the Group.

Use of credit risk measures

The credit risk measures are used extensively in the Group's credit risk processes including the following:

- credit approval;
- pricing;
- limit setting/risk appetite;
- reporting;
- provisioning;
- capital calculations and allocation;
- profitability analysis;
- stress testing;
- risk management and credit monitoring; and
- performance measurement.

The following table describes the use of credit risk concepts and measures across a number of key areas and business processes related to the management of the credit portfolio.

Use of credit measures in the credit lifecycle

	Corporate	Retail
Determination of portfolio and client acquisition strategy	assessment of overall portfolio credit risk determined by PD, EAD and LGD; and acquisition and overall strategy set in terms of appropriate limits and Group risk appetite.	same measures as for corporate; and credit models determine loss thresholds used in setting of credit risk appetite.
Determination of individual and portfolio limits	industry and geographical concentrations; ratings; risk-related limits on the composition of portfolio; and Group credit risk appetite.	same measures as for corporate; and modeled versus actual experience is evaluated in setting of risk appetite.
Profitability analysis and pricing decisions	PD, EAD and LGD used to determine pricing; and economic profit used for profitability.	same measures as for corporate.
Credit approval	consideration of application's ratings; credit risk appetite limits; and projected risk-adjusted return on economic capital (PD, EAD and LGD are key inputs in these measures).	automated based on application scorecards (scorecards are reflective of PD, EAD and LGD); and assessment of client's affordability.
Credit monitoring and risk management	risk assessment based on PD, EAD and LGD; counterparty FR grades updated based on risk assessment; and portfolio model apportions and additional capital to large transactions that will increase concentration risk.	same measures as for corporate; and monthly analysis of portfolio and risk movements used in portfolio management and credit strategy decisions.
Impairments	PD and LGD used in assessment of impairments and provisioning; and judgmental assessment to determine adequacy of provisions.	loss identification period PD, LGD and roll rates used for specific, portfolio and incurred but not reported provisions.
Regulatory and economic capital calculation	primary credit risk measures, PD, EAD and LGD, are the most important inputs.	primary credit risk measures, PD, EAD and LGD, are the most important inputs.
Reporting to senior management and board	portfolio reports discussed at franchise and business unit risk committee meetings; and quarterly portfolio reports submitted to credit risk management and RCC committees.	portfolio reports discussed at franchise and business unit risk committee meetings; and quarterly portfolio reports submitted to credit risk management and RCC committees.

CREDIT RISK PORTFOLIO

Credit strategy is managed as part of the broader financial resource management process and is aligned with the Group's macroeconomic outlook.

The Group's total gross advances increased 14% year-on-year with growth in corporate and commercial advances particularly robust at 18%. Retail advances growth of 11% was achieved within the Group's risk appetite framework.

Total NPLs continued to trend downwards and decreased 6% year-on-year. Retail NPLs declined 1% mainly as a result of the continued improvement in the residential mortgage portfolio offset by the 7% increase in the unsecured lending portfolio. The workout of certain non-performing accounts led to the significant improvement of 18% in corporate and commercial NPLs at June 2014. Total NPLs as a percentage of advances improved to 2.34% from 2.82% at June 2013.

NPL coverage is 34%. The decline in retail coverage to 33% from 35% is expected and attributable to the positive performance of the underlying portfolios in recent years due to proactive risk mitigating measures implemented by the Group since 2011. The increasing proportion of debt review accounts (on which a lower coverage ratio applies) continues to drive the VAF coverage ratio down. Corporate coverage increased significantly to 37% from 29% at June 2013 as a result of the enhancement of collateral information and ongoing actions to resolve certain non-performing accounts.

The credit loss ratio of 0.80% is an improvement on the prior year as specific impairment losses continued to reduce. The portfolio impairment loss ratio of 0.16% is in line with that of the prior year and incorporates increased portfolio overlays both in the franchises and at the centre.

Credit assets

The following table provides a breakdown of credit exposure (including off-balance sheet exposures) by type, segment and SARB approach. The figures are based on IFRS and differ from exposure figures used for regulatory capital calculation, which reflect the recognition of permissible adjustments such as netting of certain exposures.

Credit exposure by type, segment and SARB approach (audited)

		AIRB	Standardised approach subsidiaries		
R million	**2014**	**FirstRand Bank (SA)**	**Regulated bank entities within Africa**	**Other subsidiaries**	**2013***
On-balance sheet exposures					
Cash and short-term funds	**54 647**	**46 295**	**6 243**	**2 109**	42 639
– Money at call and short notice	**35 385**	**30 255**	**3 116**	**2 014**	26 005
– Balances with central banks	**19 262**	**16 040**	**3 127**	**95**	16 634
Gross advances	**696 311**	**607 946**	**43 081**	**45 284**	610 498
FNB	**299 267**	**258 823**	**40 202**	**242**	271 395
– FNB retail	**208 423**	**208 423**	**–**	**–**	195 841
– FNB commercial**	**50 642**	**50 400**	**–**	**242**	42 834
– FNB Africa	**40 202**	**–**	**40 202**	**-**	32 720
WesBank	**167 037**	**143 671**	**-**	**23 366**	142 158
RMB investment banking	**218 279**	**196 829**	**2 879**	**18 571**	186 314
RMB corporate banking	**6 441**	**6 301**	**-**	**140**	5 101
FCC	**5 287**	**2 322**	**-**	**2 965**	5 530
Derivatives	**39 038**	**38 548**	**99**	**391**	52 277
Debt investment securities (excluding non-recourse investments)	**83 014**	**75 087**	**7 535**	**392**	96 099
Accounts receivable	**8 159**	**4 015**	**1 191**	**2 953**	7 804
Reinsurance assets	**408**	**–**	**–**	**408**	394
Off-balance sheet exposures	**125 274**	**114 038**	**8 636**	**2 600**	122 748
– Guarantees	**33 114**	**30 287**	**2 923**	**(96)**	30 137
– Letters of credit#	**7 588**	**6 945**	**547**	**96**	9 195
– Irrevocable commitments	**78 785**	**70 892**	**4 918**	**2 975**	78 783
– Credit derivatives	**5 787**	**5 914**	**248**	**(375)**	4 633
Total	**1 006 851**	**885 929**	**66 785**	**54 137**	932 459

* *June 2013 balances have been restated to reflect IFRS changes.*
** *Includes public sector.*
# *Includes acceptances.*

Reconciliation of gross advances to net advances (audited)

R million	2014	2013
Gross advances after interest in suspense	**696 311**	610 498
Less: total impairment loss (refer to note 12 of the consolidated annual financial statements)	**(10 385)**	(9 433)
Net advances (refer consolidated statement of financial position)	**685 926**	601 065

Credit quality (audited)

Advances are considered past due in the following circumstances:

- loans with a specific expiry date (e.g. term loans and VAF) and consumer loans repayable by regular instalments (e.g. mortgage loans and personal loans) are treated as overdue where one full instalment is in arrears for one day or more and remains unpaid as at the reporting date; or
- loans payable on demand (e.g. overdrafts) are treated as overdue where a demand for repayment was served on the borrower, but repayment has not been made in accordance with the stipulated requirements.

In these instances, the full outstanding amount is considered overdue even if part is not yet due.

A past due analysis is performed for advances with specific expiry or instalment repayment dates. The analysis is not applicable to overdraft products or products where no specific due date is determined. The level of risk on these types of products is assessed and reported with reference to the counterparty ratings of the exposures. The following tables provide the age analysis of loans and advances for the Group.

Age analysis of advances (audited)

	2014					
	Neither past due nor impaired		**Past due but not impaired**			
R million/%	**Current**	**Re-negotiated but current**	**One full instalment past due**	**Two full instalments past due**	**Impaired**	**Total**
– FNB retail	**196 483**	**769**	**2 548**	**1 367**	**7 256**	**208 423**
– FNB commercial*	**49 148**	**88**	**54**	**31**	**1 321**	**50 642**
– FNB Africa	**37 598**	**16**	**1 367**	**412**	**809**	**40 202**
FNB	**283 229**	**873**	**3 969**	**1 810**	**9 386**	**299 267**
WesBank	**155 983**	**–**	**4 348**	**1 922**	**4 784**	**167 037**
RMB investment banking**	**216 569**	**–**	**100**	**571**	**1 039**	**218 279**
RMB corporate banking	**6 435**	**–**	**–**	**–**	**6**	**6 441**
FCC	**5 287**	**–**	**–**	**–**	**–**	**5 287**
Total	**667 503**	**873**	**8 417**	**4 303**	**15 215**	**696 311**
Percentage of total book	**95.9%**	**0.1%**	**1.2%**	**0.6%**	**2.2%**	**100.0%**

* *Includes public sector.*
** *Impaired advances for RMB investment banking are net of cumulative credit fair value adjustments on the non-performing book.*

Age analysis of advances (audited) (continued)

	2013*					
	Neither past due nor impaired		Past due but not impaired			
R million/%	Current	Re-negotiated but current	One full instalment past due	Two full instalments past due	Impaired	Total
– FNB retail	182 868	507	2 457	1 394	8 615	195 841
– FNB commercial**	41 260	101	29	15	1 429	42 834
– FNB Africa	30 922	82	688	351	677	32 720
FNB	255 050	690	3 174	1 760	10 721	271 395
WesBank	134 271	–	2 830	1 127	3 930	142 158
RMB investment banking#	184 025	–	112	800	1 377	186 314
RMB corporate banking	5 091	–	1	–	9	5 101
FCC	5 530	–	–	–	–	5 530
Total	583 967	690	6 117	3 687	16 037	610 498
Percentage of total book	95.7%	0.1%	1.0%	0.6%	2.6%	100.0%

* *Balances have been restated to reflect IFRS changes.*
** *Includes public sector.*
\# *Impaired advances for RMB investment banking are net of cumulative credit fair value adjustments on the non-performing book.*

Renegotiated advances

Renegotiated but current financial assets would be past due or impaired were it not for renegotiation and are separately classified as neither past due nor impaired assets. Renegotiated but current advances include advances where, due to a deterioration in the counterparty's financial condition, the Group grants a concession whereby the original terms and conditions of the facility are amended and the counterparty is within the new terms of the advance. Renegotiated but current advances are advances which have not been classified as defaulted.

Advances are only classified as renegotiated but current if the terms of the renegotiated contract have not yet expired and remain classified as such until the terms of the renegotiated contract expire. Adherence to the new terms and conditions for each product segment is closely monitored. Renegotiated but current advances exclude advances which are extended or renewed as part of the ordinary course of business on similar terms and conditions as the original advances.

Non-performing loans cannot be reclassified as renegotiated but current unless the arrears balance has been repaid. Renegotiated but current financial assets are considered as part of the collective evaluation of impairment where financial assets are grouped on the basis of similar credit risk characteristics.

As part of the risk management and recoveries approach, the Group enters into arrangements with clients where concessions are made on payment terms (e.g. a reduction in payments for a specified period, changes in the payment profile or debt counselling payment plans). There are formally defined eligibility criteria appropriate for individual products to determine when clients are eligible for such arrangements.

Retail accounts which have been renegotiated and classified as NPLs cannot be reclassified to performing until all arrears have been paid up as per the Group's policy. All credit agreements which are subject to debt review orders in terms of the National Credit Act of 2007 are classified as NPLs in accordance with the Group's impairment policy. These agreements remain classified as such until arrears measured in terms of the initial contract have been repaid. Specific impairment is calculated on this group of assets.

Past due but not impaired

Advances neither past due but not impaired in the tables above include accounts in arrears by one or two full repayments. For the year ended 30 June 2014 exposures to technical and partial arrears of R6.4 billion (June 2013: R5.4 billion) were classified as neither past due nor impaired in accordance with FirstRand impairment methodology, primarily driven by retail exposures.

The following tables provide the credit quality of advances in the in-force portfolio. Detailed information on the movements on an asset class level is provided in the *PD, EAD and LGD profiles* section.

Credit quality of performing advances (audited)

	2014							
		FNB						
R million	Total neither past due nor impaired*	Retail	Commercial**	FNB Africa	WesBank	RMB investment banking	RMB corporate banking	FCC
FR 1 – 25	**177 066**	**42 763**	**3 314**	**5 563**	**2 983**	**118 613**	**1 697**	**2 133**
FR 26 – 91#	**481 675**	**147 285**	**45 419**	**31 769**	**151 958**	**97 374**	**4 737**	**3 133**
Above FR 92#	**9 635**	**7 204**	**503**	**282**	**1 042**	**582**	**1**	**21**
Total	**668 376**	**197 252**	**49 236**	**37 614**	**155 983**	**216 569**	**6 435**	**5 287**

* *Includes renegotiated but current advances.*
** *Includes public sector.*
\# *The mapping of the FR rating scale to the international rating scale was realigned during the 2014 financial year. The impact is a misalignment in the top range affecting advances which fall into FR 91 and is considered to be insignificant. The rating buckets for financial reporting will be aligned in the next financial year.*

	2013							
		FNB						
R million	Total neither past due nor impaired*	Retail	Commercial**	FNB Africa	WesBank	RMB investment banking	RMB corporate banking	FCC
FR 1 – 25	151 332	42 919	2 037	5 631	3 609	92 675	3 388	1 073
FR 26 – 91	422 075	132 552	38 620	25 027	130 008	89 804	1 703	4 361
Above FR 92	11 250	7 904	704	346	654	1 546	–	96
Total	584 657	183 375	41 361	31 004	134 271	184 025	5 091	5 530

* *Includes renegotiated but current advances.*
** *Includes public sector.*

The following tables provide an overview of the credit quality of other financial assets that are neither past due nor impaired.

Credit quality of other financial assets (excluding advances) neither past due nor impaired (audited)

	2014				
R million	**Debt investment securities***	**Derivatives**	**Cash and short-term funds**	**Reinsurance assets**	**Total**
AAA to BBB	**74 229**	**31 054**	**52 300**	**408**	**157 991**
BB+ to B-	**7 958**	**7 929**	**1 940**	**–**	**17 827**
CCC	**459**	**45**	**209**	**–**	**713**
Unrated	**368**	**10**	**198**	**–**	**576**
Total	**83 014**	**39 038**	**54 647**	**408**	**177 107**

* *Excludes non-recourse investments.*

	2013				
R million	**Debt investment securities***	**Derivatives**	**Cash and short-term funds**	**Reinsurance assets**	**Total**
AAA to BBB	89 062	34 154	40 945	394	164 555
BB+ to B-	6 443	18 078	1 417	–	25 938
CCC	517	36	207	–	760
Unrated	77	9	70	–	156
Total	96 099	52 277	42 639	394	191 409

* *Excludes non-recourse investments.*

Impairment of financial assets and NPLs

Adequacy of impairments is assessed through the ongoing review of the quality of credit exposures. Although credit management and workout processes are similar for amortised cost advances and fair value advances, impairments for these differ.

Refer to the policy for impairment of financial assets in the accounting policies and advances note in the consolidated annual financial statements for the analysis of the movement in the impairment of advances and NPLs.

For amortised cost advances, impairments are recognised through the creation of an impairment reserve and an impairment charge in the income statement. For fair value advances, the credit valuation adjustment is charged to the income statement through trading income and recognised as a change to the carrying value of the asset.

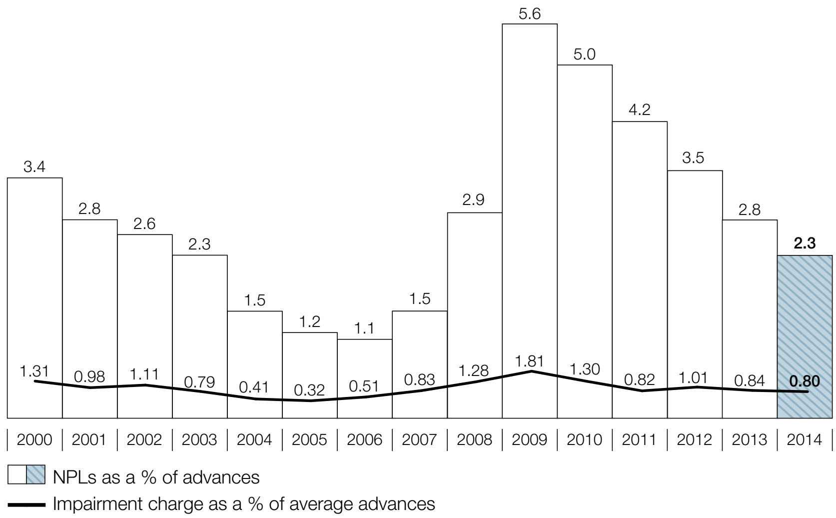
Specific impairments are created for non-performing loans where there is objective evidence that an incurred loss event will have an adverse impact on the estimated future cash flows from the asset. Potential recoveries from guarantees and collateral are incorporated into the calculation of impairment figures.

All assets not individually impaired, as described, are included in portfolios with similar credit characteristics (homogeneous pools) and collectively assessed. Portfolio impairments are created with reference to these performing advances based on historical patterns of losses in each part of the performing book. Points of consideration for this analysis are the level of arrears, arrears roll rates, PIT PDs, LGDs and the economic environment. Loans considered uncollectable are written off against the reserve for loan impairments. Subsequent recoveries against these facilities decrease the credit impairment charge in the income statement in the year of recovery.

The following chart shows a history of NPLs and impairments.

Total NPLs and impairments

%



* *Impairment charges are reflected before insurance proceeds where applicable. The impairment charge is calculated on an IFRS basis.*

Fair value sensitivity of corporate advances due to credit risk

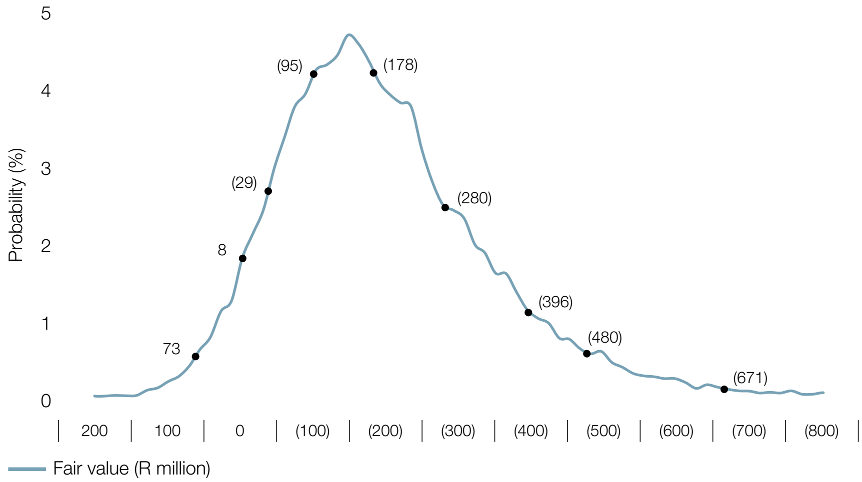
The investment banking division in RMB recognises a significant portion of corporate advances at fair value through profit or loss. The fair value adjustments directly impact the income statement and the value of advances. For risk management purposes, a migration matrix is used to estimate the fair value impact of changes in credit risk. The matrix contains probabilities of downgrading or upgrading to another rating bucket.

The main benefits of using the migration matrix to estimate the fair value impact of credit risk are:

- more realistic downgrades as better rating grades are less likely to be downgraded compared to riskier rating grades;
- migration matrices which take into account higher volatility of riskier rating grades;
- rating migration can be positive or negative;
- rating migration is not restricted by one notch only and, in extreme cases, includes default risk; and
- migration matrices can be based on different economic conditions (for example, long term, or downturn).

The following graph sets out the fair value impact based on actual observed rating migrations from Standard & Poor's over the long term. Based on this scenario the average fair value impact is a loss of approximately R178 million. The fair value at the 75th percentile (i.e. there is a probability of 25% of exceeding this value) of the distribution is a loss of approximately R280 million.

Distribution: Fair value impact – long- term scenario



Management of concentration risk

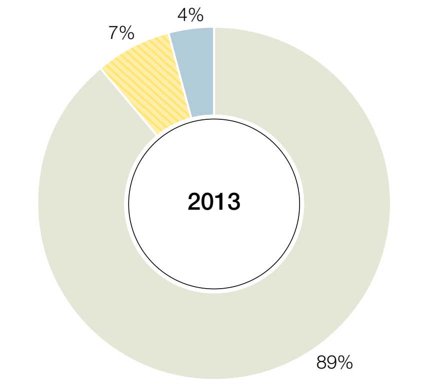
Credit concentration risk is the risk of loss to the Group arising from an excessive concentration of exposure to a single counterparty, industry, market, product, financial instrument or type of security, country or region, or maturity. This concentration typically exists when a number of counterparties are engaged in similar activities and have similar characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions.

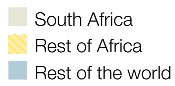
Concentration risk is managed based on the nature of the credit concentration within each portfolio. The Group's overall credit portfolio is well diversified. Diversification is achieved through setting maximum exposure guidelines to individual counterparties. The Group constantly reviews its concentration levels and sets maximum exposure guidelines to these. Excesses are reported to the RCC committee.

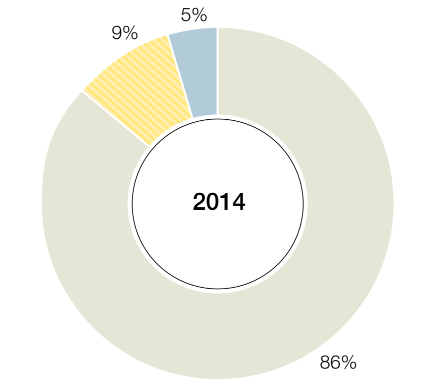
Geographic and industry concentration risk

Geographically, most of the Group's exposures are in South Africa. The following charts provide the geographical and industry split of gross advances after deduction of interest in suspense.

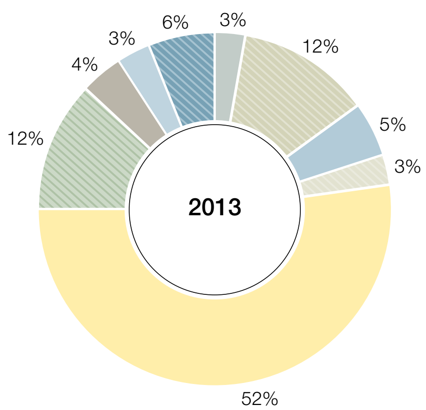
Geographical split by exposure (audited)

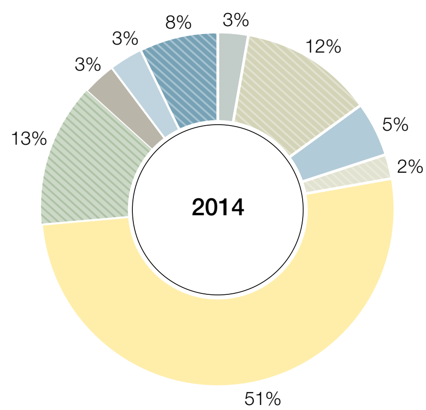






Industry split by exposure (audited)





The Group seeks to establish a balanced portfolio profile and closely monitors credit concentrations. The following tables provide a breakdown of credit exposure across geographical areas.

Concentration of significant exposure (audited)

	2014								
R million	**South Africa**	**Other Africa**	**United Kingdom**	**Other Europe**	**North America**	**South America**	**Austra-lasia**	**Asia**	**Total**
Advances	**597 147**	**62 273**	**28 314**	**4 316**	**1 223**	**161**	**1 165**	**1 712**	**696 311**
Derivatives	**21 721**	**287**	**14 263**	**1 961**	**707**	**–**	**1**	**98**	**39 038**
Debt investment securities*	**67 372**	**7 591**	**656**	**68**	**2 126**	**–**	**–**	**5 201**	**83 014**
Guarantees, acceptances and letters of credit**	**31 307**	**7 017**	**77**	**337**	**630**	**–**	**40**	**1 294**	**40 702**
Irrevocable commitments**	**67 489**	**9 252**	**805**	**584**	**61**	**–**	**–**	**594**	**78 785**

** Excludes non-recourse investments.*
*** Significant off-balance sheet exposures. Refer to the note on contingencies and commitments in the notes to the annual financial statements.*

	2013*								
R million	**South Africa**	**Other Africa**	**United Kingdom**	**Other Europe**	**North America**	**South America**	**Austra-lasia**	**Asia**	**Total**
Advances	541 337	45 644	15 949	3 374	1 024	372	1 357	1 441	610 498
Derivatives	29 865	298	18 673	2 194	833	7	–	407	52 277
Debt investment securities**	73 583	6 491	624	–	10 002	–	–	5 399	96 099
Guarantees, acceptances and letters of credit#	27 981	7 666	82	150	7	–	14	3 432	39 332
Irrevocable commitments#	68 411	7 312	1 485	517	530	124	–	404	78 783

* *Balances have been restated to reflect IFRS changes.*
** *Excludes non-recourse investments.*
\# *Significant off-balance sheet exposures. Refer to the note on contingencies and commitments in the notes to the financial statements.*

Average advances per major risk portfolios

R million	2014	2013*
Retail	**357 973**	321 541
FNB Africa	**36 605**	29 276
Wholesale	**206 821**	175 091
Commercial	**46 168**	39 780

* *June 2013 balances have been restated to reflect IFRS changes.*

The average amount of gross credit exposure during the reporting period is calculated on a monthly average basis.

Segmental analysis of advances

The following table provides a breakdown of credit exposures by the Group segments (audited).

	2014				
R million/%	**Advances**	**NPLs**	**NPLs as a % of advances**	**Total impairment charge**	**Impairments as % of average advances**
FNB	299 267	9 386	3.14	2 413	0.85
– FNB retail	208 423	7 256	3.48	1 818	0.90
– Residential mortgages	170 677	5 625	3.30	158	0.09
– Card	14 634	341	2.33	88	0.64
– Personal loans	12 516	729	5.82	980	7.72
– Other retail	10 596	561	5.29	592	6.76
– FNB commercial*	50 642	1 321	2.61	333	0.71
– FNB Africa	40 202	809	2.01	262	0.72
WesBank	167 037	4 784	2.86	2 081	1.35
– WesBank asset-backed finance	157 883	4 125	2.61	1 479	1.01
– WesBank retail	96 445	3 409	3.53	1 209	1.32
– WesBank corporate	38 763	633	1.63	135	0.37
– WesBank international	22 675	83	0.37	135	0.75
– WesBank loans	9 154	659	7.20	602	7.32
RMB investment banking	218 279	2 105	0.96	177	0.09
RMB corporate banking	6 441	6	0.09	32	0.55
FCC	5 287	–	–	549	0.08
Subtotal	696 311	16 281	2.34	5 252	0.80
Special impairments**	–	–	–	–	–
Total	696 311	16 281	2.34	5 252	0.80

* *Includes public sector.*

** *Special impairment in 2013 related to FNB commercial R215 million and RMB corporate banking R15 million.*

2013				
Advances	NPLs	NPLs as a % of advances	Total impairment charge	Impairments as % of average advances
271 395	10 721	3.95	2 838	1.10
195 841	8 615	4.40	2 330	1.22
163 046	6 911	4.24	507	0.32
13 001	302	2.32	23	0.19
12 885	943	7.32	1 402	11.39
6 909	459	6.64	398	7.47
42 834	1 429	3.34	318	0.81
32 720	677	2.07	190	0.65
142 158	3 930	2.76	1 649	1.26
134 858	3 486	2.58	1 219	0.98
87 309	2 461	2.82	945	1.18
34 293	975	2.84	177	0.53
13 256	50	0.38	97	0.86
7 300	444	6.08	430	6.48
186 314	2 571	1.38	61	0.03
5 101	9	0.18	29	0.75
5 530	–	–	–	–
610 498	17 231	2.82	4 577	0.80
–	–	–	230	0.04
610 498	17 231	2.82	4 807	0.84

REGULATORY DISCLOSURE

Credit rating systems and processes used for SARB approaches

The Group uses the AIRB approach for exposures of the Bank SA and the standardised approach for all other legal entities and offshore branches in the Group for regulatory capital purposes. Due to the relatively smaller size of the subsidiaries and the scarcity of relevant data, the Group plans to continue using the standardised approach for the foreseeable future for the majority of these portfolios.

For portfolios using the standardised approach, ratings from Standard & Poor's are used. External ratings are not available for all jurisdictions and for certain parts of the portfolio. The Group uses its internally-developed mapping between FR grade and S&P grades (refer to the table mapping of FirstRand (FR) grades to rating agency scales on page 181).

The following table provides the breakdown of exposures rated through the standardised approach by risk bucket. The risk-weights used are those prescribed in the Regulations and will differ primarily with asset class and credit rating. From June 2014 all exposures rated through the standardised approach are reported in this table and not only the African subsidiaries exposures as was previously the case.

Credit risk exposure rated through the standardised approach by risk bucket*

Risk bucket	Exposure (R million)
0%	**3 597**
10%	**21**
20%	**8 508**
35%	**13 893**
50%	**5 397**
75%	**24 656**
100%	**45 384**
Specific impairments	**940**
Total	**102 396**

* *No exposure amount is deducted from the Group's capital or reserve funds.*

Protected exposures

The table below includes the exposures for the standardised approach portfolios in the African subsidiaries, namely Botswana, Lesotho, Namibia, Swaziland, Tanzania and Zambia. The exposures are split according to retail, commercial and wholesale portfolios, as appropriate. The table also includes the amount of protection obtained through eligible financial collateral. Eligible financial collateral used is as specified in the Regulations for both standardised and AIRB approaches including guarantees or credit-derivative instruments after the effect of haircuts.

Standardised approach protected exposures per asset class

	2014*		
R million	**Exposure before credit risk mitigation**	**Eligible collateral****	**Exposure after credit risk mitigation**
Retail	**27 170**	**362**	**26 808**
Commercial and wholesale	**29 750**	**265**	**29 485**
Total	**56 920**	**627**	**56 293**

* *Protected exposures for standardised approach portfolios are new disclosure included from June 2014. Comparative information will be provided from June 2015 onwards.*

** *Eligible collateral includes cash, certificates of deposit, gold, debt securities, equities, undertakings for collective investments in transferable securities, mutual funds, financial receivables, guarantees and credit-derivative instruments.*

PD, EAD and LGD profiles

A summary of credit risk parameters as reported for regulatory capital purposes is shown in the following tables for each significant AIRB asset class. The parameters reflect through-the-cycle PDs and downturn LGDs. The Group uses EAD-weighted PDs based on the FirstRand master rating scale which are then mapped to Basel rating buckets (1 – 25) for regulatory reporting purposes.

The tables provide a summary of the risk-weight and EAD distribution by prescribed counterparty risk bands (Basel risk buckets). The EAD-weighted downturn LGD, EAD-weighted PD and average risk weight for the performing and total book are also shown as well as comparatives for the prior year.

Year-on-year trends are impacted by risk migration in the existing book (reflecting changes in the economic environment), quality of new business originated and any model recalibrations implemented during the course of the year. The risk profile reflects the Group's credit origination strategy, which focuses on targeting segments that provide an appropriate risk/return profile.

The risk weight per Basel risk bucket table must be read together with the EAD% distribution per Basel risk bucket table as the significant overall movements year-on-year are explained by the change in low volumes within individual rating buckets. The sovereign asset class includes public sector entities, local government and municipalities and sovereign exposures (including central government and central bank exposures) and specialised lending includes high volatility commercial real estate, income-producing real estate, object finance, commodity finance and project finance. The increase in EAD% and nominal EAD for the 1-5 bucket of banks and securities firms reflects funding provided to the London branch from the South African balance sheet. This is due to a change in the regulatory returns in which London branch exposures are now reflected as part of FRB SA.

Bank's risk profile per asset class: risk-weight per Basel risk bucket

	Risk weight									
%	**Total FRB**		**Corporate**		**Sovereign**		**Specialised lending**		**Banks and securities firms**	
Basel PD risk buckets	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
1 – 5	**3.0**	3.1	**0.1**	10.0	**3.8**	3.1	**5.2**	–	**0.7**	3.6
6 – 10	**22.7**	21.0	**27.2**	27.6	**26.5**	23.4	**16.8**	18.2	**16.1**	14.2
11 – 15	**37.5**	36.5	**60.0**	59.5	**53.1**	56.6	**41.0**	43.1	**51.5**	46.3
16 – 20	**52.3**	51.3	**101.7**	98.3	**74.6**	52.1	**94.6**	98.3	**100.7**	113.0
21 – 25	**110.1**	126.0	**157.1**	277.5	**354.3**	355.4	**235.9**	175.5	**142.1**	139.6
NPLs	**69.0**	59.4	**0.9**	6.2	**5.8**	–	**–**	–	**–**	–

	Risk weight									
%	**SME corporate**		**SME retail**		**Retail mortgages**		**Retail revolving**		**Other retail**	
Basel PD risk buckets	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
1 – 5	**4.1**	2.3	**5.8**	–	**1.2**	–	**1.7**	–	**1.5**	11.2
6 – 10	**1.9**	25.4	**13.1**	15.8	**5.1**	4.9	**5.7**	14.6	**22.1**	45.1
11 – 15	**48.0**	44.2	**34.5**	31.5	**15.3**	14.9	**23.1**	31.4	**29.7**	28.2
16 – 20	**63.9**	63.2	**40.3**	43.6	**36.6**	36.2	**61.7**	70.0	**47.0**	45.1
21 – 25	**116.9**	103.3	**73.7**	67.2	**77.6**	80.8	**157.4**	147.6	**107.1**	117.1
NPLs	**13.6**	173.0	**244.5**	134.7	**14.8**	23.2	**12.1**	76.4	**133.4**	105.8

Bank's risk profile per asset class: EAD% distribution per Basel risk bucket

%	EAD									
	Total FRB		Corporate		Sovereign		Specialised lending		Banks and securities firms	
Basel PD risk buckets	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013
1 – 5	**9.3**	9.3	**–**	0.4	**80.3**	83.1	**0.3**	0.1	**28.8**	3.9
6 – 10	**16.3**	16.0	**38.2**	33.8	**16.5**	13.5	**17.1**	14.8	**51.1**	67.7
11 – 15	**38.4**	36.9	**49.8**	53.3	**2.2**	2.3	**64.1**	54.7	**15.3**	22.6
16 – 20	**30.0**	31.2	**11.0**	10.3	**0.8**	0.6	**13.5**	23.0	**3.7**	4.9
21 – 25	**4.1**	4.5	**0.9**	2.0	**0.2**	0.2	**1.0**	2.2	**1.0**	0.9
NPLs	**1.8**	2.1	**0.2**	0.1	**–**	0.4	**4.0**	5.2	**–**	–

%	EAD									
	SME corporate		SME retail		Retail mortgages		Retail revolving		Other retail	
Basel PD risk buckets	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013
1 – 5	**0.2**	2.0	**2.5**	–	**0.6**	–	**2.1**	–	**–**	–
6 – 10	**–**	0.8	**6.3**	13.7	**0.6**	2.2	**8.8**	20.8	**–**	–
11 – 15	**55.7**	56.0	**34.6**	24.8	**53.8**	53.6	**36.0**	32.5	**13.9**	7.3
16 – 20	**39.3**	37.7	**48.7**	54.3	**38.6**	36.5	**43.6**	34.9	**69.0**	76.6
21 – 25	**3.3**	3.5	**5.4**	4.3	**3.8**	4.5	**7.8**	9.8	**13.0**	12.4
NPLs	**1.4**	2.0	**2.6**	2.8	**2.6**	3.2	**1.7**	2.1	**4.1**	3.7

Bank's risk profile per asset class: Nominal EAD per Basel risk bucket

	Nominal EAD									
R million	**Total FRB**		**Corporate**		**Sovereign**		**Specialised lending**		**Banks and securities firms**	
Basel PD risk buckets	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
1 – 5	**74 409**	67 222	**14**	621	**52 907**	64 718	**142**	41	**18 165**	1 833
6 – 10	**130 132**	111 135	**71 707**	51 741	**10 836**	10 489	**8 108**	5 709	**32 205**	31 518
11 – 15	**305 533**	267 689	**93 524**	81 772	**1 427**	1 782	**30 305**	21 087	**9 640**	10 500
16 – 20	**239 110**	226 451	**20 656**	15 818	**538**	448	**6 362**	8 848	**2 343**	2 280
21 – 25	**32 487**	32 860	**1 620**	3 124	**153**	157	**494**	848	**630**	406
NPLs	**14 275**	15 073	**405**	199	**–**	317	**1 873**	1 994	**–**	–
Total	**795 946**	720 430	**187 926**	153 275	**65 861**	77 911	**47 284**	38 527	**62 983**	46 537

	Nominal EAD									
R million	**SME corporate**		**SME retail**		**Retail mortgages**		**Retail revolving**		**Other retail**	
Basel PD risk buckets	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
1 – 5	**111**	9	**980**	–	**1 211**	–	**853**	–	**26**	–
6 – 10	**1**	314	**2 463**	–	**1 174**	4 226	**3 637**	7 108	**1**	30
11 – 15	**24 936**	23 392	**13 523**	8 797	**100 707**	101 273	**14 933**	11 121	**16 538**	7 965
16 – 20	**17 622**	15 753	**19 055**	19 297	**72 206**	68 918	**18 091**	11 952	**82 237**	83 137
21 – 25	**1 496**	1 469	**2 106**	1 544	**7 210**	8 543	**3 246**	3 341	**15 532**	13 428
NPLs	**624**	821	**1 013**	1 011	**4 784**	6 036	**720**	721	**4 856**	3 974
Total	**44 790**	41 758	**39 140**	30 649	**187 292**	188 996	**41 480**	34 243	**119 190**	108 534

Bank's PD%, LGD%, EL/EAD and RWA/EAD ratio per asset class

%	Total FRB 2014	Total FRB 2013	Corporate 2014	Corporate 2013	Sovereign 2014	Sovereign 2013	Specialised lending 2014	Specialised lending 2013	Banks and securities firms 2014	Banks and securities firms 2013
Average performing PD	**2.4**	2.5	**0.9**	1.2	**0.2**	0.1	**1.2**	1.8	**0.4**	0.5
Average performing LGD	**28.9**	28.3	**34.6**	34.5	**29.4**	28.4	**22.9**	23.2	**28.2**	30.2
Performing EL/EAD	**0.8**	0.8	**0.3**	0.5	**0.1**	0.1	**0.4**	0.7	**0.1**	0.2
Performing RWA/EAD	**39.3**	39.9	**52.9**	57.5	**10.0**	8.0	**46.2**	55.1	**21.5**	26.9
Average total book PD	**4.1**	4.5	**1.1**	1.3	**0.2**	0.5	**5.1**	6.9	**0.4**	0.5
Average total book LGD	**29.1**	28.7	**34.6**	34.5	**29.4**	28.4	**23.7**	25.0	**28.2**	30.2
Total book EL/EAD	**1.5**	1.6	**0.4**	0.6	**0.1**	0.1	**2.3**	3.1	**0.1**	0.2
Total book RWA/EAD	**39.8**	41.2	**52.8**	57.4	**10.0**	8.0	**44.4**	52.4	**21.5**	26.9

%	SME corporate 2014	SME corporate 2013	SME retail 2014	SME retail 2013	Retail mortgages 2014	Retail mortgages 2013	Retail revolving 2014	Retail revolving 2013	Other retail 2014	Other retail 2013
Average performing PD	**2.3**	2.5	**3.0**	2.9	**2.8**	2.9	**3.8**	4.1	**6.1**	6.0
Average performing LGD	**27.0**	26.5	**32.0**	30.7	**13.8**	13.9	**65.5**	65.2	**33.3**	32.8
Performing EL/EAD	**0.6**	0.6	**1.0**	0.8	**0.4**	0.4	**2.5**	2.7	**2.5**	2.5
Performing RWA/EAD	**56.6**	53.9	**37.5**	37.7	**26.0**	26.2	**48.9**	53.2	**52.6**	53.1
Average total book PD	**3.6**	4.4	**5.5**	5.7	**5.3**	6.0	**5.5**	6.2	**9.9**	9.4
Average total book LGD	**27.2**	27.4	**32.6**	31.0	**13.9**	14.2	**65.5**	65.3	**33.9**	33.6
Total book EL/EAD	**1.6**	1.7	**1.9**	2.0	**1.0**	1.2	**3.7**	4.1	**4.1**	4.2
Total book RWA/EAD	**56.0**	56.3	**42.8**	40.4	**25.7**	26.0	**48.3**	54.6	**55.9**	54.4

Bank's nominal credit extended, drawn exposure and EAD per asset class

R million	Total FRB 2014	Total FRB 2013	Corporate 2014	Corporate 2013	Sovereign 2014	Sovereign 2013	Specialised lending 2014	Specialised lending 2013	Banks and securities firms 2014	Banks and securities firms 2013
Total book credit extended	**1 016 183**	919 707	**236 559**	205 107	**72 449**	83 334	**47 704**	39 252	**180 870**	155 387
Total book drawn exposure	**691 762**	601 736	**151 431**	118 854	**62 698**	72 680	**46 397**	37 524	**55 274**	29 123
Total book nominal EAD	**795 946**	720 430	**187 926**	153 275	**65 861**	77 911	**47 284**	38 527	**62 983**	46 537

R million	SME corporate 2014	SME corporate 2013	SME retail 2014	SME retail 2013	Retail mortgages 2014	Retail mortgages 2013	Retail revolving 2014	Retail revolving 2013	Other retail 2014	Other retail 2013
Total book credit extended	**52 456**	49 445	**42 594**	36 735	**200 502**	195 405	**56 850**	46 262	**119 689**	108 780
Total book drawn exposure	**37 333**	35 338	**32 611**	28 174	**162 651**	153 618	**24 491**	19 278	**118 086**	107 147
Total book nominal EAD	**44 790**	41 758	**39 140**	30 649	**187 292**	188 996	**41 480**	34 243	**119 190**	108 534

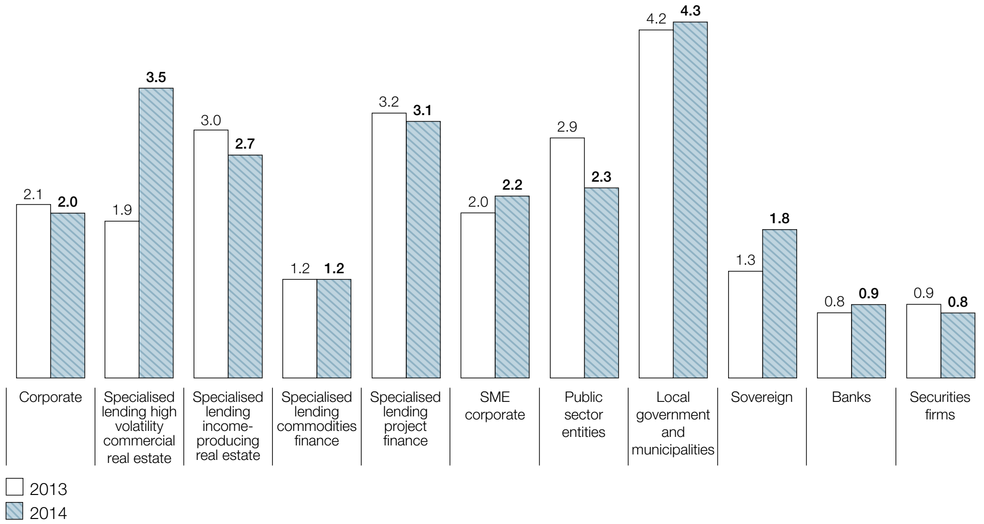
Maturity breakdown

Maturity is defined as the average time at which a bank will receive its contractual payments (cash flows), calculated for each account or exposure weighted by the size of each of the cash flows.

Maturity is used as an input in the AIRB regulatory capital calculation for wholesale portfolios. These are aggregated on an asset class basis for review and reporting purposes. The longer the maturity of a deal, the greater the uncertainty, and all else being equal, the larger the regulatory capital requirement will be. The following chart provides a maturity breakdown of AIRB asset classes within the wholesale credit portfolio.

Maturity breakdown per wholesale AIRB asset class

Maturity in years



Actual versus expected loss analysis

To provide a meaningful assessment of the effectiveness of internal ratings-based models, expected loss is compared against actual losses during the calendar year. This is performed for all significant AIRB asset classes.

Expected loss here refers to regulatory expected loss. This provides a one-year forward looking view, based on information available at the beginning of the year, i.e. 1 July 2013. Risk parameters include:

- PDs, which are calibrated to long-run default experience to avoid regulatory models being skewed to a specific part of the credit cycle;
- LGDs, which are calibrated to select downturn periods to reflect depressed asset prices during economic downturns; and
- EADs.

Actual losses during the period consist of the level of specific impairments at the start of the financial year (1 July 2013) and the net specific impairment charge recorded through the income statement for the year as determined by IFRS. It excludes the effect of post write-off recoveries, which would reduce the actual loss number. The calculation is based on the assumption that specific provisions raised are a fair estimate of what final losses on defaulted exposures would be, although the length of the workout period creates uncertainty in this assumption.

The measure of actual losses includes specific impairments raised for exposures which defaulted during the year, but which did not exist at 1 July 2013. These exposures are not reflected in the expected loss value described. As a result, significant volumes of new business can distort the analysis by inflating the actual loss figure.

The following table provides a comparison of actual loss to regulatory expected loss for each significant AIRB asset class. PDs used for regulatory capital purposes are based on long-run experience and are expected to underestimate actual defaults at the top of the credit cycle and overestimate actual defaults at the bottom of the credit cycle, under normal circumstances.

It should also be noted that the regulatory expected loss shown is based on the expected loss derived from the regulatory capital models that were applied at 30 June 2013. This comparison is supplemented with more detailed analyses on the following page, comparing actual and expected outcomes for each risk parameter (PD, LGD and EAD) over the year under review.

Actual versus expected loss per portfolio segment

	2014		2013		2012	
R million*	**Expected loss**	**Actual loss**	**Expected loss**	**Actual loss**	**Expected loss**	**Actual loss**
Corporate (corporate, banks and sovereign)**	**1 977**	**59**	1 621	70	1 499	313
SMEs (SME corporate and SME retail)#	**1 125**	**998**	1 146	989	1 507	1 094
Residential mortgages#	**2 422**	**1 913**	2 674	2 470	2 793	2 961
Qualifying revolving retail#	**1 434**	**1 512**	1 126	973	1 179	808
Other retail†	**1 981**	**2 336**	1 718	2 413	904	1 990
WesBank†	**3 076**	**3 825**	2 780	3 236	3 160	3 371
Total	**12 015**	**10 643**	11 065	10 151	11 042	10 537

* *The composition used above differs slightly from that used in the remainder of this section, due to impairment charges being on a business unit level as opposed to AIRB asset class level.*

** *Expected losses for the corporate portfolio are much higher than the actual losses due to it being a low default portfolio. As a result, the models use conservative data inputs.*

Actual losses are below expected losses which is expected given the current point in the economic cycle and that expected loss parameters are based on long run and downturn conditions.

† *Actual losses exceed expected losses for the Other retail and WesBank portfolios. Other retail and WesBank experienced high levels of new business written during the year. The related impairment is not reflected in the expected losses which are based on accounts that are in-force at the start of the year. However, these new accounts contribute to the actual losses as a result of additional provisions raised.*

For the analysis below, estimated values are based on regulatory capital models applied at 30 June 2013. For PDs, this is applied to the total performing book at 30 June 2013. For LGDs and EADs, it is applied to all facilities that defaulted over the subsequent 12 months.

Actual values are based on actual outcomes over the 12-month period July 2013 to June 2014. Due to the length of the workout period, there is uncertainty in the measure provided for actual LGDs as facilities that default during the year would only have had between one and twelve months to recover to date – depending on when the default event occurred.

The estimated EAD to actual EAD ratio is derived as the ratio of expected nominal exposure at default (for all accounts that defaulted during the 12-month period July 2013 to June 2014) to the actual nominal exposure at default for the same accounts.

Risk parameters used to determine regulatory expected loss

	2014				
	PD		**LGD**		**Estimated EAD to actual EAD ratio**
Asset class	**Estimated %**	**Actual %**	**Estimated %**	**Actual %**	**%**
Corporate, banks and sovereign*	**0.8**	**0.2**	**18.7**	**28.2**	**101.9**
Specialised lending – property finance	**2.3**	**0.5**	**16.9**	**2.0**	**133.7**
SME corporate	**2.4**	**1.2**	**26.6**	**20.9**	**111.3**
SME retail	**2.8**	**2.3**	**32.4**	**34.2**	**109.3**
Residential mortgages	**2.9**	**2.0**	**15.4**	**8.8**	**103.2**
Qualifying revolving retail	**4.4**	**2.8**	**65.2**	**71.8**	**106.8**
Other retail	**6.0**	**6.1**	**42.6**	**43.6**	**106.9**
Total	**2.6**	**1.9**	**24.9**	**26.0**	**106.3**

* *Corporate, banks and sovereign are shown as one asset class to align with the respective asset class in the actual versus expected loss table.*

	2013				
	PD		**LGD**		**Estimated EAD to actual EAD ratio**
Asset class	**Estimated %**	**Actual %**	**Estimated %**	**Actual %**	**%**
Corporate, banks and sovereign*	0.9	0.3	15.8	34.6	107.9
Specialised lending – property finance	2.1	1.2	31.0	3.3	102.7
SME corporate	2.3	1.3	29.3	28.4	109.9
SME retail	2.9	2.8	32.1	26.3	111.6
Residential mortgages	3.4	2.6	15.6	12.6	104.7
Qualifying revolving retail	3.6	2.6	67.6	63.3	91.9
Other retail	6.3	5.6	33.4	33.3	104.1
Total	2.7	2.0	22.2	28.5	106.0

* *Corporate, banks and sovereign are shown as one asset class to align with the respective asset class in the actual versus expected loss table.*

	2012				
	PD		LGD		Estimated EAD to actual EAD ratio
Asset class	**Estimated %**	**Actual %**	**Estimated %**	**Actual %**	**%**
Corporate, banks and sovereign*	0.7	0.1	37.3	10.9	194.5
Specialised lending – property finance	2.7	2.3	21.8	28.8	116.0
SME corporate	4.9	2.3	27.0	29.0	144.3
SME retail	3.2	3.0	28.8	20.9	113.3
Residential mortgages	3.6	2.9	15.3	11.5	104.4
Qualifying revolving retail	3.0	2.5	72.4	68.5	98.9
Other retail	6.0	5.1	46.0	43.7	102.9
Total	2.7	2.0	30.6	27.5	108.0

* *Corporate, banks and sovereign are shown as one asset class to align with the actual versus expected loss table.*

The corporate, banks and sovereign regulatory capital models remain conservative as these are low default portfolios with actual default rates remaining lower than expected default rates.

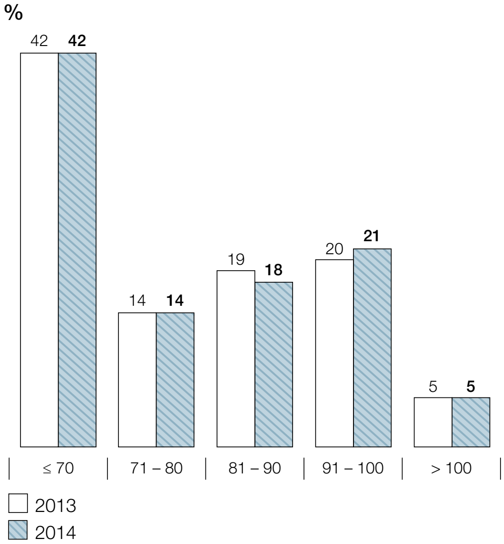
Differences between the actual and expected LGDs for corporates, banks and sovereigns as well as specialised lending (property finance) are due to low default volumes where the loss experience on individual defaults can dominate the result. The difference in the outputs as compared to prior years are primarily as a result of the actual and expected LGD being based only on counterparties which have defaulted during the respective years. Differences in the loss characteristics of accounts which default over time can be significant, particularly in the wholesale and commercial portfolios where defaults are sparse.

The qualifying revolving retail asset class LGD models applied for regulatory capital at June 2013 underestimated LGDs and reflect the model in use at the time. FNB's strategy to grow core transactional accounts and improve cross-sell resulted in strong new business growth in consumer overdrafts which resulted higher actual losses and LGDs than had previously been experienced. An updated model is being developed and should predict LGDs for this asset class at a more appropriate level.

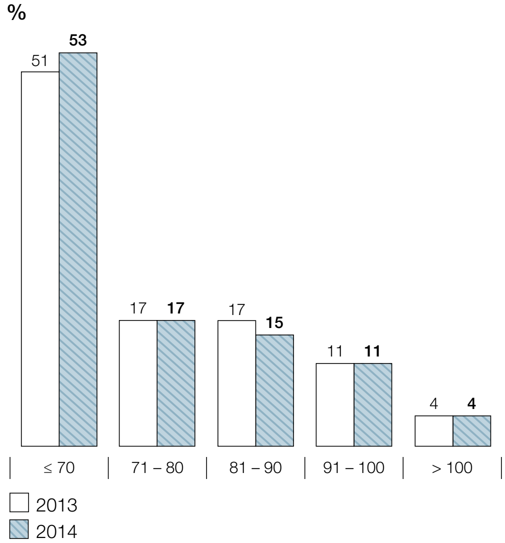
RISK ANALYSES

The graphs below provide the balance-to-value and age distributions of residential mortgage portfolios and show that the focus on loan-to-value ratios for new business resulted in an improvement in the balance-to-original value although the Group places more emphasis on counterparty creditworthiness as opposed to only on the underlying security. Pressures on property market values have negatively impacted the balance-to-market value distribution.

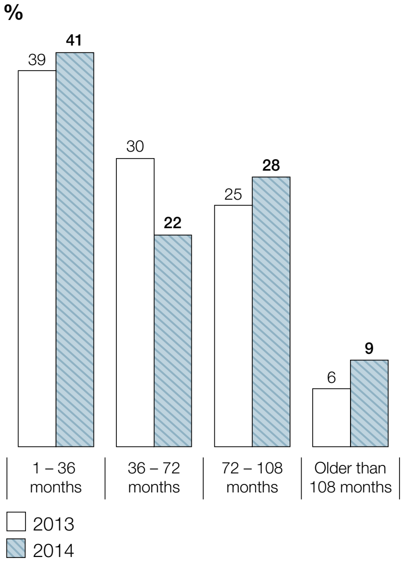
Residential mortgages balance-to-original value



Residential mortgages balance-to-market value

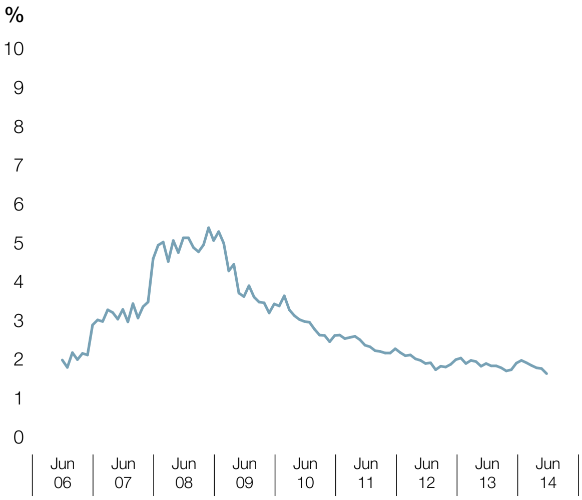


Residential mortgages age distribution



The graph below shows the arrears in the FNB HomeLoans portfolio. It includes loans where more than one full payment is in arrears expressed as a percentage of the total advances balance.

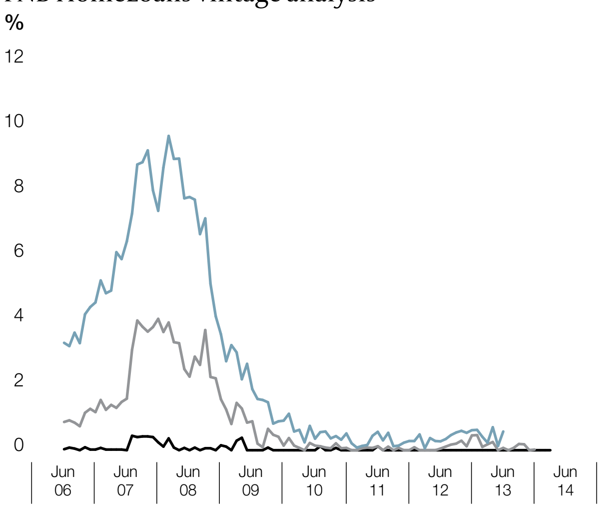
FNB HomeLoans arrears



The following graphs provide vintage analyses for certain retail portfolios. Vintage graphs show default experience three, six and twelve months after origination date and reflect the impact of origination strategies and the macroeconomic environment.

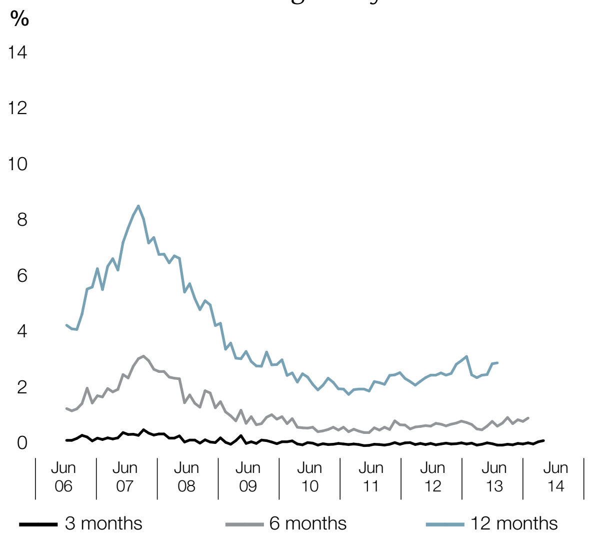
FNB HomeLoan vintages continue to perform at record lows even when considering the pre-2008 period. This can be attributed to risk mitigation actions taken across all residential mortgage portfolios.

FNB HomeLoans vintage analysis



The WesBank retail six and twelve month cumulative vintage analysis continues to show a noticeable improvement in the quality of business written since mid-2007. This is due to improved customer profiles and enhanced collection strategies.

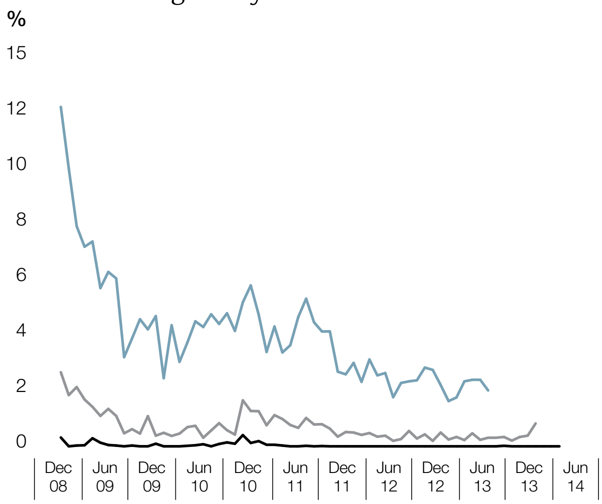
WesBank retail VAF vintage analysis



The uptick in VAF vintages is due, in part, to strong new business volumes in recent years. The emerging strain is driven by pressure on consumer disposable income as a result of rising inflation, higher debt costs and administered price increases on motor vehicles. The Group actively adjusts risk appetite and credit parameters to ensure that vintages continue to perform in line with expectations given where it is in the credit cycle.

The following chart shows that FNB card has experienced a marginal increase in NPLs, in line with expectations. Default rates remain at very low levels, even on a through-the-cycle basis. The expectation is that default rates have bottomed and moderate increases are expected off this level.

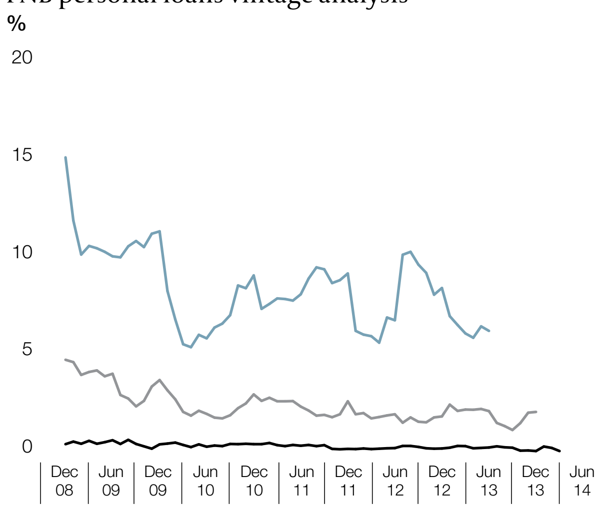
FNB card vintage analysis



The default experience of the FNB and WesBank personal loans portfolios is within risk appetite.

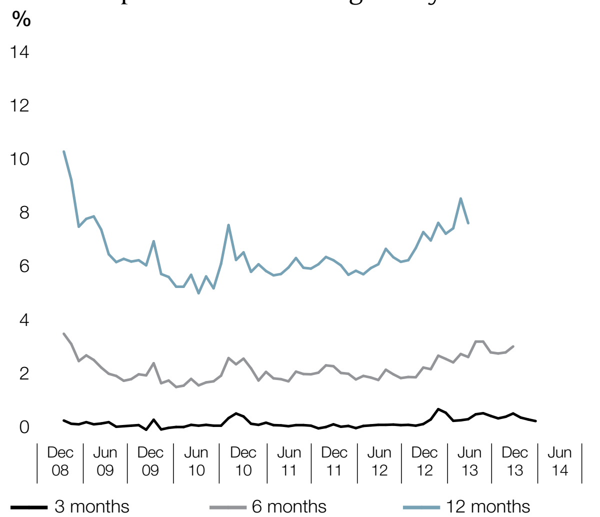
Vintages for personal loans are within thresholds and risk appetite. Continued actions are undertaken to ensure these portfolios remain within risk appetite. FNB loans vintages are performing at the lowest levels since December 2008. The positive risk outcome is the result of active management of credit risk appetite and parameters even as the risk levels within the unsecured lending market have heightened.

FNB personal loans vintage analysis



WesBank personal loans vintages have continued to show a marginal deterioration from 2010 levels. This is due to new joint ventures entered into where performance is expected to be somewhat worse in the initial stages. The introduction of a more conservative risk appetite in early 2014 is expected to improve performance back to 2012 levels and early signs are encouraging.

WesBank personal loans vintage analysis



RETAIL PROPERTIES IN POSSESSION

The Group took a decision to write off the carrying value of its South African properties in possession. At June 2014, 156 properties were part of the Group's portfolio (June 2013: 300). Eight properties relate to the FNB Africa portfolio and have been valued at R5.6 million.

SECURITISATIONS AND CONDUITS

INTRODUCTION AND OBJECTIVES

Securitisation is the process whereby interests in loans and other receivables are packaged, underwritten and sold in the form of asset-backed securities to capital market investors.

Asset securitisations enable the Group to access funding markets at debt ratings higher than its own corporate rating, which generally provides access to broader funding sources at more favourable rates. By removing the assets and supporting funding from the balance sheet, the Group is able to reduce some of the costs of on-balance sheet financing and manage potential asset-liability mismatches and credit concentrations.

The Group uses securitisation as a tool to achieve one or more of the following objectives:

- improve the Group's liquidity position through the diversification of funding sources;
- match the cash flow profile of assets and liabilities;
- reduce balance sheet credit risk exposure;
- reduce capital requirements; and
- manage credit concentration risk.

The table below provides an overview of the Group's role in securitisation and conduit structures.

Transaction	Originator	Sponsor	Servicer	Investor	Liquidity provider	Credit enhancement provider	Swap counter-party
Own securitisations							
Fresco 2	✓	✓	✓	✓		✓	
Nitro 4	✓	✓	✓	✓			✓
Turbo Finance 2	✓	✓	✓	✓			
Turbo Finance 3	✓	✓	✓	✓			
Turbo Finance 4	✓	✓	✓	✓			
Conduit structures							
iNdwa*		✓	✓		✓		✓
iVuzi*		✓	✓		✓	✓	✓
iNkotha**			✓				
iNguza**			✓				
Third party							
– Homes Obligor Mortgage Enhanced Securities					✓		
– Private Residential Mortgages 2					✓		
– Superdrive Investments				✓			
– Torque Securitisation					✓		

* *Conduits incorporated under regulations relating to securitisation scheme.*
** *Conduits incorporated under regulations relating to commercial paper.*

OVERSIGHT AND RISK MITIGATION

The Group's role in securitisation transactions, both Group originated and sponsored transactions, as well as third party securitisations, results in various financial and operational risks, including:

- liquidity and funding risk;
- interest rate risk;
- credit risk;
- currency risk;
- operational risk;
- reputational risk; and
- compliance risk.

For securitisations originated by the Group, exposures are managed from a credit perspective by the originating business units as if the securitisation had never occurred. Resultant risks from retained exposure and the overall origination and maintenance of the securitisation structures are managed as part of the day-to-day management of the various risk types. This includes risk mitigation and management actions depending on the risk limits and appetite per risk area. The performance of securitisations is monitored on an ongoing basis and reported to management and governance forums.

Some of the governance and management processes in place to monitor risks as a result of securitisation transactions are outlined below:

- proposed securitisations follow a rigorous internal approval process and are reviewed for approval by ALCCO, the RCC committee and the board;
- the performance of Group and third-party off-balance sheet transactions are discussed and monitored at a bimonthly meeting of Group Treasury's off-balance sheet forum, which includes representation from investor relations;
- changes to retained exposures (as result of ratings, reviews, note redemptions and credit losses) are reflected in the monthly BA 500 regulatory return; and
- transaction investor reports, alignment with special purpose vehicle financial reporting and the impact of underlying asset performance are reviewed on the quarterly BA501 regulatory return.

The Group does not employ credit risk mitigation techniques to hedge credit risk on retained securitisation tranches.

SECURITISATION ACCOUNTING POLICIES

From an accounting perspective, traditional securitisations are treated as sales transactions. At inception, the assets are sold to a special purpose vehicle (SPV) at carrying value and no gains or losses are recognised. For synthetic securitisations, the credit derivatives used in the transaction are recognised at fair value, with any fair value adjustments reported in profit or loss.

Securitisation entities are consolidated into FRIHL for financial reporting purposes. Any retained notes are accounted for as available-for-sale investment securities within the banking book. Liabilities as a result of securitisation vehicles are accounted for in line with Group accounting policies for liabilities, provisions and contingent liabilities.

The Group does not currently employ any form of warehousing prior to structuring a new securitisation transaction.

YEAR UNDER REVIEW

Issuance of Turbo Finance 4

In November 2013, the Group closed its fourth UK traditional auto loan securitisation, Turbo Finance 4 plc (Turbo Finance 4). Turbo Finance 4 is a revolving cash securitisation of fixed rate auto loans extended to obligors by MotoNovo Finance. The note issuance of GBP378.7 million is rated by both Fitch and Moody's.

The incorporation of a 12-month revolving period has enabled the Bank to extend the term of funding by an additional year. Despite the increase in the weighted average life of the transaction, the Class A note was issued 2 bps below the Turbo 3 Class A note. The performance of past and existing Turbo Finance transactions has helped to further improve rating assumptions used by the rating agencies, allowing for an additional reduction in the level of subordination required for the Aaa/AAA Class A notes (13% compared to 18% for Turbo 3 and 28% for Turbo 1).

The following table provides further detail regarding the notes.

Turbo Finance 4 notes issued

Tranche	Rating (Moody's/ Fitch)	Amount (GBP million)	Credit enhance-ment* (%)	Coupon
A	Aaa(sf)/AAA(sf)	328.9	13.14	1m Libor + 58
B	A1(sf)/A+(sf)	33.6	4.27	1m Libor + 115
C	Ba1(sf)/BBB(sf)	11.3	1.28	6%
D	NR/NR	4.9	0.00	20%
Total		378.7		

* *Calculated including the class D notes/cash component.*

The Bank was, however, required to retain GBP18 million of the Class B tranche. FirstRand, acting through its London branch, continues to act as servicer for the transaction. The transaction is compliant with Article 122a of the EU Capital Requirement Directive where the Bank chose to use the on-balance sheet retention method to meet the 5% retained interest requirements of Article 122a.

Maturity of Fresco 2

Launched in August 2007, Fresco 2 represented the Group's second synthetic securitisation of wholesale corporate credit exposures. Scheduled amortisation of Fresco 2 commenced in November 2012 and in August 2013, the transaction matured with final redemption of all outstanding notes.

During its lifetime, the Fresco 2 securitisation provided both funding and credit risk mitigation against the Group's wholesale credit exposures. The transaction performed in line with expectations.

Nitro Securitisation 4 Issuer Trust (Nitro 4) ratings affirmed

In July 2013, Moody's Investor Services affirmed the Baa2(sf)/A1.za(sf) and Ba2(sf)/Baa1.za(sf) ratings of the Class B and Class C notes, respectively. At the same time, the rating agency affirmed the A1(sf)/Aaa.za(sf) ratings on the outstanding Class A8 to A14 notes. The rating actions reflect the adequate level of credit enhancement, which protects against sovereign and counterparty risk.

Exposures intended to be securitised or resecuritised in the future

FirstRand uses securitisation primarily as a funding tool. The ability to securitise assets is dependent on the availability of assets to securitise, investor appetite for securitisation paper and comparison with alternative sources of funding. All assets on the Group's balance sheet are considered as exposures that could possibly be securitised within the market constraints mentioned above. The Group obtains SARB approval for the structure and limits imposed by the board on the size of assets that may be securitised.

Resecuritisation results from portfolio management actions and the size of the exposure is dependent on future market factors. This exposure is reported as part of the investor reporting process.

TRADITIONAL AND SYNTHETIC SECURITISATIONS

The following tables show the traditional and synthetic securitisations currently in issue and the rating distribution of any exposures retained. Whilst national scale ratings have been used in this table, global scale equivalent ratings are used for internal risk management purposes and regulatory capital reporting.

Securitisation transactions

R million	Asset type	Year initiated	Expected close	Rating agency
Traditional securitisations**				
Nitro 4	Retail: Auto loans	2007	2016	Moody's
Turbo Finance 2	Retail: Auto loans	2012	2015	Moody's and Fitch
Turbo Finance 3	Retail: Auto loans	2012	2015	Moody's and Fitch
Turbo Finance 4	Retail: Auto loans	2013	2021	Moody's and Fitch
Synthetic securitisations**				
Fresco 2	Corporate receivables	2007	2013	Fitch
Total				

* *Does not include cash reserves.*

** *Includes transactions structured by the Group and excludes third-party transactions.*

Rating distribution of retained and purchased securitisation exposures

R million	AAA (zaf)	AA (zaf)	AA- (zaf)	A+ (zaf)	A (zaf)	BBB+ (zaf)	BBB (zaf)	BB (zaf)	B+ (zaf)	Not rated	Total
Traditional											
At 30 June 2014	**1 463**	**–**	**–**	**247**	**–**	**–**	**235**	**–**	**–**	**1 380**	**3 325**
At 30 June 2013	98	–	–	81	–	–	–	–	–	1 300	1 479
Synthetic											
At 30 June 2014	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
At 30 June 2013	–	–	–	–	–	3 020	–	52	–	123	3 195
Third party											
At 30 June 2014	**504**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**504**
At 30 June 2013	503	–	–	–	–	–	–	–	–	–	503

	Assets outstanding*		Notes outstanding		Retained exposure	
Assets securitised	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
19 167	**10 066**	7 019	**10 895**	7 823	**3 325**	1 479
3 982	**576**	1 453	**717**	1 747	**268**	589
4 037	**1 067**	2 200	**1 189**	2 402	**488**	409
4 570	**1 907**	3 366	**2 108**	3 674	**574**	481
6 578	**6 516**	–	**6 881**	–	**1 995**	–
20 000	**–**	5 000	**–**	5 000	**–**	3 195
20 000		5 000	**–**	5 000	**–**	3 195
39 167	**10 066**	12 019	**10 895**	12 823	**3 325**	4 674

RESECURITISATIONS

A resecuritisation exposure is where the risk associated with an underlying pool of exposures is tranched and at least one of the underlying exposures is a securitisation exposure. Securitisation paper is, on occasion, acquired by the Group's asset-backed commercial paper conduits and managed as part of the underlying portfolio. This makes up a minimal portion of the total portfolio and is accounted for as a resecuritisation exposure for regulatory capital purposes.

Resecuritisation exposure

	2014		2013	
Programme*	**Resecuritisation exposure (R million)**	**% of total programme**	**Resecuritisation exposure (R million)**	**% of total programme**
iVuzi	**11.0**	**0.3**	47.5	1.1

* *Excludes distributions relating to iNguza underlying exposure as this is driven by note holders and does not impact third parties.*

CONDUIT PROGRAMMES

The Group has conduit programmes incorporated under both securitisation scheme and commercial paper regulations. The iNdwa and iVusi conduit programmes are incorporated under securitisation scheme regulations. These are debt capital market vehicles, which provide investment-grade corporate South African counterparties with an alternative source of funding to traditional bank funding or capital markets issuance under their own domestic medium-term debt programmes. It also provides institutional investors with highly-rated short-term alternative investments. The fixed income fund, iNkotha, is a call-loan bond fund, which offers overnight borrowers and lenders an alternative to traditional overnight bank borrowings or deposits.

The commercial paper programme, iNguza, issues bespoke notes to investors. These notes use the credit risk of separate and distinct transactions of a different underlying borrower or obligors. Note holders will have recourse only to the assets in relation to the underlying transaction and will not have recourse to any other assets. Risk relating to the underlying transactions is transferred directly to note holders and managed by them according to their risk appetite levels. Notes are listed on the JSE and may be traded through members of the JSE.

Both the fixed income fund and the commercial paper programme have been incorporated under commercial paper regulations.

All assets originated for the conduit programmes are rigorously evaluated as part of the Group's credit approval processes applicable to any other corporate exposure held by the Group.

The conduit programmes have proved resilient during difficult financial market conditions and experienced a tightening of credit spreads in line with the corporate debt market. Supply of assets and demand for notes issued by the conduits remains healthy, albeit within the constraints of newly introduced collective investment scheme regulations.

The following tables show the programmes currently in place, the ratings distribution of the underlying assets and the role played by the Group in each of these programmes. All of these capital market vehicles continue to perform in line with expectations.

Conduit programmes*

					Non-recourse investments		Credit enhancement provided	
R million	**Underlying assets**	**Year initiated**	**Rating agency**	**Programme size**	**2014**	**2013**	**2014**	**2013**
Securitisations**								
iNdwa	Corporate and structured finance term loans	2003	Fitch	15 000	4 420	5 160	–	–
iVuzi	Corporate and structured finance term loans	2007	Fitch	15 000	3 871	4 123	1 044	1 070
Total				30 000	8 291	9 283	1 044	1 070
Fixed income fund[#]								
iNkotha	Overnight corporate loans	2006	GCR[†]	10 000	2 937	2 957	–	–
Total				10 000	2 937	2 957	–	–
Commercial paper programme[#]								
iNguza	Corporate and structured finance term loans	2008	GCR[†]	15 000	9 482	10 964	–	–
Total				15 000	9 482	10 964	–	–

* *Conduit programmes are consolidated into FRIHL for financial reporting purposes.*
** *Conduits incorporated under regulations relating to securitisation scheme.*
# *Conduits incorporated under regulations relating to commercial paper.*
† *Global credit rating.*

Rating distribution of conduits*

R million	**F1+(zaf)**	**AAA(zaf)**	**AA+(zaf)**	**AA(zaf)**	**AA-(zaf)**	**A+(zaf)**	**A(zaf)**	**A-(zaf)**	**Total**
Securitisations									
At 30 June 2014	**–**	**674**	**1 054**	**2 744**	**250**	**1 247**	**1 533**	**789**	**8 291**
At 30 June 2013	–	–	820	2 841	1 777	1 945	1 284	616	9 283
Fixed income funds									
At 30 June 2014	**–**	**–**	**270**	**367**	**422**	**798**	**610**	**470**	**2 937**
At 30 June 2013	–	–	–	648	827	601	321	560	2 957

* *Excludes distributions relating to iNguza underlying exposure as this is driven by note holders and does not impact third parties.*

LIQUIDITY FACILITIES

The following table provides a summary of the liquidity facilities provided by the Group.

Liquidity facilities

R million	Transaction type	2014	2013
Own transactions		**4 463**	5 751
iNdwa	Conduit	**3 204**	3 866
iVuzi	Conduit	**1 159**	1 885
Third party transactions	Securitisations	**214**	1 522
Total		**4 577**	7 273

All liquidity facilities granted to the transactions in the table above rank senior in terms of payment priority in the event of a drawdown. Economic capital is allocated to the liquidity facility extended to iNdwa and iVuzi as if the underlying assets were held by the Group. The conduit programmes are consolidated into FRIHL for financial reporting purposes.

ADDITIONAL INFORMATION

Capital against securitisation exposures has been calculated on consideration of a hierarchy of approaches based on the Regulations. The supervisory formula is used for conduits and the ratings-based approach has been selected for remaining exposures. Capital calculated under both of these approaches is limited to the capital that would have been held had the assets remained on-balance sheet. The following table provides the securitisation exposures retained or purchased as well as associated capital requirements per risk band.

Retained or purchased securitisation exposure and the associated regulatory capital charges

	Exposure		RWA		Capital*	
R million	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
Risk weighted bands						
≤10%	**3 464**	3 989	**671**	348	**67**	33
>10% ≤20%	**2 167**	750	**423**	93	**42**	9
>50% ≤100%	**30**	1 331	**23**	859	**2**	82
>100% ≤650%	**206**	–	**720**	–	**72**	–
1250%/deduction	**1 380**	1 423	**13 798**	14 968	**1 380**	1 422
Look through	**2 303**	6 027	**1 087**	2 962	**109**	281
Total	**9 550**	13 520	**16 722**	19 230	**1 672**	1 827

* *Capital is calculated at the SARB transitional minimum requirement of 10% for 2014 (9.5%: 2013) (excluding the bank-specific individual capital requirement) and includes a 6% capital scalar.*

The Group did not securitise any exposures that were impaired or past due at the time of securitisation.

COUNTERPARTY CREDIT RISK

INTRODUCTION AND OBJECTIVES

Counterparty credit risk measures a counterparty's ability to satisfy its obligations under a contract that has positive economic value to the bank at any point during the life of the contract. It differs from normal credit risk in that the economic value of the transaction is uncertain and dependent on market factors that are typically not under the control of the bank or the client.

Counterparty credit risk is taken mainly in the Group's trading and securities financing businesses. The objective of counterparty credit risk management is to ensure that this risk is appropriately measured, analysed and reported on, and is only taken within specified limits in line with the Group's risk appetite framework as mandated by the board.

During the year under review, the Group focused on improving the risk management of the portfolio while growing client market access responsibly. FirstRand is, and will continue to be, an active participant in processes to implement legislative and structural reforms in the local derivatives market. Changes to international regulations relating to derivative market reforms are regularly monitored.

The risk to bilateral over-the-counter (OTC) counterparties is reduced by restricting transactions to higher-rated counterparties and collateralising all mark-to-market movements in the majority of cases. The risk to clients in securities financing is reduced by improved margining and restricting exposure to higher quality underlying assets.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

RMB's credit department is responsible for the overall management of counterparty credit risk. It is supported by RMB's derivative counterparty risk department which is responsible for ensuring that market and credit risk methodologies are consistently applied in the quantification of risk.

Counterparty credit risk is managed on the basis of the principles, approaches, policies and processes set out in the credit risk management framework for wholesale credit exposures.

In this respect, counterparty credit risk governance aligns closely with the Group's credit risk governance framework, with mandates and responsibilities cascading from the board through the RCC committee to the respective credit committees and subcommittees as well as deployed and central risk management functions. Refer to the *risk governance* section, and organisational structure and governance in the *credit risk* section for more details.

The derivative counterparty risk committee supports the credit risk management committee and its subcommittees with analysis and quantification of counterparty credit risk for traded product exposures.

ASSESSMENT AND MANAGEMENT

Quantification of risk exposure

The measurement of counterparty credit risk aligns closely with credit risk measurement practices and is focused on establishing appropriate limits at a counterparty level and on ongoing portfolio risk management.

To this end, appropriate quantification methodologies of potential future exposure over the life of a product, even under distressed market conditions, are developed and approved at the relevant technical committees.

Individual counterparty risk limit applications are prepared using the approved risk quantification methodologies, and assessed and approved by the dedicated counterparty credit committee, which has appropriate executive and non-executive representation.

All counterparty credit risk limits are subject to annual review, while counterparty exposures are monitored by the respective risk functions on a daily basis. Overall counterparty risk limits are allocated across a number of products. Desk-level reports are used to ensure sufficient limit availability prior to executing additional trades with counterparties.

Business and risk management functions share the following responsibilities in this process:

- quantification of exposure and risk, as well as management of facility utilisation within approved credit limits;
- ongoing monitoring of counterparty creditworthiness to ensure early identification of high-risk exposures and predetermined facility reviews at certain intervals;
- collateral management;
- management of high-risk (watch list) exposures;
- collections and workout process management for defaulted assets; and
- counterparty credit risk reporting.

Limit breaches are dealt with in accordance with the approved excess mandate. Significant limit breaches necessitate reporting to the head of the business unit, head of risk for the affected business unit and derivative counterparty risk management function. Any remedial actions are agreed amongst these parties and failure to remedy such a breach is reported to the RMB proprietary board, ERM and RCC committee.

As part of the ongoing process of understanding the drivers of counterparty credit risk, regular analysis is carried out on OTC derivative and securities financing portfolios on a look-through basis. This portfolio review process seeks to identify concentrations, assess the impact of stress scenarios and to better understand the interaction of underlying market risk factors and credit exposure. The benefits gained include clearer insight into potential collateral, earnings and capital volatility, and potentially risky trading behaviour by counterparties.

Advanced monitoring of the creditworthiness of developed market counterparty banks is conducted through the real-time analysis of the spreads on listed securities that have been issued or referenced by these banks.

Counterparty credit risk mitigation

Where appropriate, various instruments are used to mitigate the potential exposure to certain counterparties. These include financial or other collateral in line with common credit risk practices, as well as netting agreements, guarantees and credit derivatives.

The Group uses International Swaps and Derivatives Association (ISDA) and International Securities Market Association agreements for the purpose of netting derivative transactions and repurchase transactions respectively. These master agreements as well as associated credit support annexes (CSA) set out internationally accepted valuation and default covenants, which are evaluated and applied on a daily basis, including daily margin calls based on approved CSA thresholds.

For regulatory purposes, net exposure figures are used in capital calculations, whilst for accounting purposes netting is only applied where a legal right to set off and the intention to settle on a netted basis exist.

Collateral to be provided in the event of a credit rating downgrade

In rare instances, FirstRand has signed ISDA agreements where both parties would be required to post additional collateral in the event of a rating downgrade. The additional collateral to be provided by the Group in the event of a credit rating downgrade is not material and would not adversely impact its financial position. ISDA agreements with these provisions are, however, being actively phased out.

When assessing the portfolio in aggregate, the collateral that would need to be provided in the event of a rating downgrade is subject to many factors, including market moves in the underlying traded instruments and netting of existing positions.

While these variables are not quantifiable, the following table, in addition to showing the effect of counterparty credit risk mitigation, provides a guide to the order of magnitude of the netted portfolio size and collateral placed with the Group. In aggregate, all of the positive mark-to-market values shown would need to reverse before the Group would be a net provider of collateral.

COUNTERPARTY CREDIT RISK PROFILE

The following table provides an overview of the counterparty credit risk arising from the Group's derivative and structured finance transactions.

Composition of counterparty credit exposure

R million	2014*	2013
Gross positive fair value	**97 902**	107 161
Netting benefits	**(11 661)**	(12 105)
Netted current credit exposures before mitigation	**86 241**	95 056
Collateral value	**(76 413)**	(82 268)
Netted potential future exposure	**11 764**	3 661
Exposure at default**	**24 571**	21 097

* *The increase in netted potential exposure in June 2014 was due to the inclusion of central counterparties for futures clearing operations not included in June 2013.*

** *Includes exposures calculated under both the standardised and current exposure method. The Bank implemented the standardised method in June 2012. EAD under the standardised method is quantified by scaling either the current credit exposure less collateral or the net potential future exposure by a factor of 1.4. The latter explains why the summation of the netted current exposure, collateral value and netted potential future exposure in the table above differs from the EAD computed.*

The Group employs credit derivatives primarily for the purposes of protecting its own positions and for hedging its credit portfolio, as indicated in the following tables.

Credit derivatives exposure

	2014			
R million	**Credit default swaps**	**Total return swaps**	**Other**	**Total**
Own credit portfolio				
– protection bought	**–**	**–**	**–**	**–**
– protection sold	**127**	**–**	**–**	**127**
Intermediation activities				
– protection bought	**3 555**	**–**	**–**	**3 555**
– protection sold	**5 787**	**–**	**–**	**5 787**

	2013			
R million	**Credit default swaps**	**Total return swaps**	**Other**	**Total**
Own credit portfolio				
– protection bought	–	–	–	–
– protection sold	2 145	–	–	2 145
Intermediation activities				
– protection bought	3 511	–	–	3 511
– protection sold	4 633	–	–	4 633

MARKET RISK IN THE TRADING BOOK

INTRODUCTION AND OBJECTIVES

The Group's market risk emanates mainly from the provision of hedging solutions for clients, market-making activities and term-lending products. Market risk in the trading book is taken and managed by RMB. The relevant businesses within RMB function as the centres of expertise with respect to all market risk-related activities and market risk is managed and contained within the Group's appetite.

Compared to the previous year, overall diversified levels of market risk have remained relatively unchanged. The performance of market risk-taking activities is measured as the higher of the Group's internal expected tail loss (ETL) measure (as a proxy for economic capital) and regulatory capital based on Value-at-Risk (VaR) plus stressed VaR.

Interest rate risk in the banking book is managed by Group Treasury and is disclosed as part of the *interest rate in the banking book* section of this report.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

In terms of the market risk framework, a subframework of the BPRMF, responsibility for determining market risk appetite vests with the board, which also retains independent oversight of market risk-related activities through the RCC committee and its market and investment risk subcommittee.

Separate governance forums, such as RMB's proprietary board, take responsibility for allocating these mandates further, whilst deployed and central risk management functions provide independent control and oversight of the overall market risk process.

ASSESSMENT AND MANAGEMENT

Quantification of risk exposures

Market risk exposures are primarily measured and managed using an ETL measure and ETL limits. The ETL measure used by RMB is a historical simulation measure assessing the average loss beyond a selected percentile. RMB's ETL is based on a confidence interval of 99% and applicable holding periods. Since ETL is adjusted for the trading liquidity of the portfolio, it is referred to as liquidity-adjusted ETL. Holding periods, ranging between 10 and 90 days, are used in the calculation and are based on an assessment of distressed liquidity of portfolios. Historical data sets are chosen to incorporate periods of market stress such as data from the 2008/2009 global financial crisis.

VaR calculations over holding periods of 1 day and 10 days are used as an additional tool in the assessment of market risk. Loss escalation procedures are used to highlight positions to be reviewed by management.

The Group's VaR number should be interpreted in light of the limitations of the methodology used, as follows:

- due to its nature, historical simulation VaR may not provide an accurate estimate of future market moves;
- the use of a 99% confidence level does not reflect the extent of potential losses beyond that percentile. The ETL is a better measure to quantify losses beyond that percentile (but still subject to similar limitations as stated for VaR);
- use of a 1-day time horizon is not a fair reflection of profit or loss for positions with low trading liquidity, which cannot be closed out or hedged within one day;
- as exposures and risk factors can change during daily trading, exposures and risk factors are not necessarily captured in the VaR calibration which uses end-of-day trading data; and
- where historical data is not available, time series data is approximated or backfilled using appropriate quantitative methodologies. Use of proxies is, however, limited.

These limitations mean that the Group cannot guarantee that losses will not exceed VaR.

Risk concentrations in the market risk environment are controlled by means of appropriate ETL sublimits for individual asset classes and the maximum allowable exposure for each business unit. In addition to the general market risk limits described above, limits covering obligor specific risk and event risk have been introduced and utilisation against these limits is monitored continuously, based on the regulatory building block approach.

Stress testing

Stress testing provides an indication of potential losses that could occur under extreme market conditions. The ETL assessment provides a view of risk exposures under stress conditions.

Additional stress testing, to supplement the ETL assessment, is conducted using historical market downturn scenarios and includes the use of what-if hypothetical and forward-looking simulations. The stress test calibrations are reviewed regularly to ensure that the results are indicative of the possible impact of severely distressed and event-driven market conditions. Stress and scenario analyses are regularly reported to and considered by the relevant governance bodies.

Earnings volatility

A key element of the Group's risk appetite framework is an assessment of potential earnings volatility that may arise from underlying activities. Earnings volatility for market risk is quantified by subjecting key market risk exposures to predetermined stress conditions, ranging from business-as-usual stress through severe stress and event risks.

In addition to assessing the maximum acceptable level of earnings volatility, stress testing is used to understand sources of earnings volatility and highlight unused capacity within the Group's risk appetite. Market risk earnings volatility is calculated and assessed on a quarterly basis.

Back testing

Back testing is performed in order to verify the predictive ability of the VaR model and ensure ongoing appropriateness. The regulatory standard for back testing is to measure daily profits and losses against daily VaR at the 99th percentile. The number of breaches over a period of 250 trading days is calculated, and, should the number exceed that which is considered appropriate, the model is recalibrated.

Regulatory and economic capital for market risk

The internal VaR model for general market risk was approved by the SARB for local trading units and is consistent with the methodologies stipulated in the Basel III framework. For all international legal entities, the standardised approach is used for regulatory market risk capital purposes.

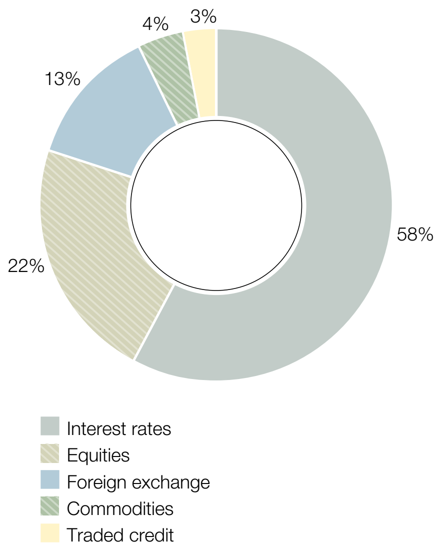
Economic capital for market risk is calculated using liquidity-adjusted ETL plus an assessment of specific risk.

MARKET RISK IN THE TRADING BOOK PROFILE

The following chart shows the distribution of exposures per asset class across the Group's trading activities at 30 June 2014 based on the VaR methodology. VaR equity exposure shown relates mainly to listed equity exposures in RMB Australia Holdings. These exposures are predominantly in the junior resources sector and are reflected on the RMB Australia Holdings balance sheet. The interest rate asset class represented the most significant exposure at year end. The main difference in asset class mix from the previous year relates to commodities, which at year end constituted a much smaller percentage of the total.

VaR exposure per asset class (audited)

%



VaR analysis by risk type

The following table reflects VaR over a 1-day holding period at a 99% confidence level. Results indicate that overall levels of market risk remained fairly unchanged between June 2013 and 2014. The most notable differences in risk when compared to the prior year relate to the interest rate and commodity components. Commodity exposures were significantly reduced during December 2013 and remained low for the remainder of the year. Overall interest rate risk increased as a result of interest rate derivative exposures on book, as well as the formation of a new trading desk created as part of the Group's derivative transformation initiative. Overall levels of diversification have remained relatively unchanged compared to the previous year.

1-day 99% VaR analysis by instrument (audited)

	2014				2013
R million	**Min***	**Max***	**Average**	**Period end**	**Period end**
Risk type					
Equities	**13.1**	**49.0**	**20.1**	**18.2**	13.9
Interest rates**	**17.0**	**57.9**	**34.6**	**49.6**	33.7
Foreign exchange	**5.9**	**45.6**	**12.1**	**11.2**	7.9
Commodities	**3.0**	**18.4**	**8.6**	**3.3**	19.6
Traded credit	**0.6**	**5.8**	**2.7**	**2.6**	2.9
Diversification effect	**–**	**–**	**–**	**(26.2)**	(22.8)
Diversified total	**36.6**	**98.3**	**57.2**	**58.7**	55.2

* *The maximum and minimum VaR figures for each asset class did not necessarily occur on the same day. Consequently, a diversification effect was omitted from the above table.*

** *Banking book exposures are managed by Group Treasury and are reported under the banking book interest rate risk section.*

The following table reflects 10-day VaR and stress VaR (sVaR) at the 99% confidence level at year end. The 10-day VaR calculation is performed using 10-day scenarios created from the past 260 trading days, whereas the 10-day sVaR is calculated using scenario data from the static stress period (2008/2009).

The overall results are commensurate with the 1-day VaR results above. When considering sVaR only, the abovementioned increase in interest rate risk and decrease in commodity risk is evident. Similarly, the same trends are noted with regards to VaR, except for the interest rate component, where the 10-day VaR has declined slightly from the prior year end. The apparent anomaly reflects the changing interest rate environment experienced during the past year, where 1-day scenarios reflect volatility to a greater extent than 10-day scenarios.

10-day 99% VaR and sVaR analysis by instrument

	2014		2013	
	Period end		**Period end**	
R million	**VaR**	**sVaR**	**VaR**	**sVaR**
Risk type				
Equities	**41.5**	**29.3**	40.4	14.9
Interest rates	**78.6**	**137.0**	98.0	84.5
Foreign exchange	**32.2**	**24.3**	37.5	35.5
Commodities	**6.9**	**12.9**	37.3	50.8
Traded credit	**4.6**	**5.5**	4.9	9.4
Diversification effect	**(39.0)**	**(57.5)**	(69.7)	(91.5)
Diversified total	**124.9**	**151.5**	148.4	103.6

Other risk measures

Other risk factors are considered in the assessment and management of market risk. These include interest rate and equity specific risk. Specific risk accurately measures idiosyncratic risk not captured by ETL and VaR measures for interest rate and equity risk, such as default risk, credit migration risk and event risk, and identifies concentrations in a portfolio. The following table includes specific risk capital for the year.

Specific risk capital*

R million	**2014**	**2013****
Interest rate specific risk	**99**	96
Equity specific risk	**85**	69
Total	**184**	165

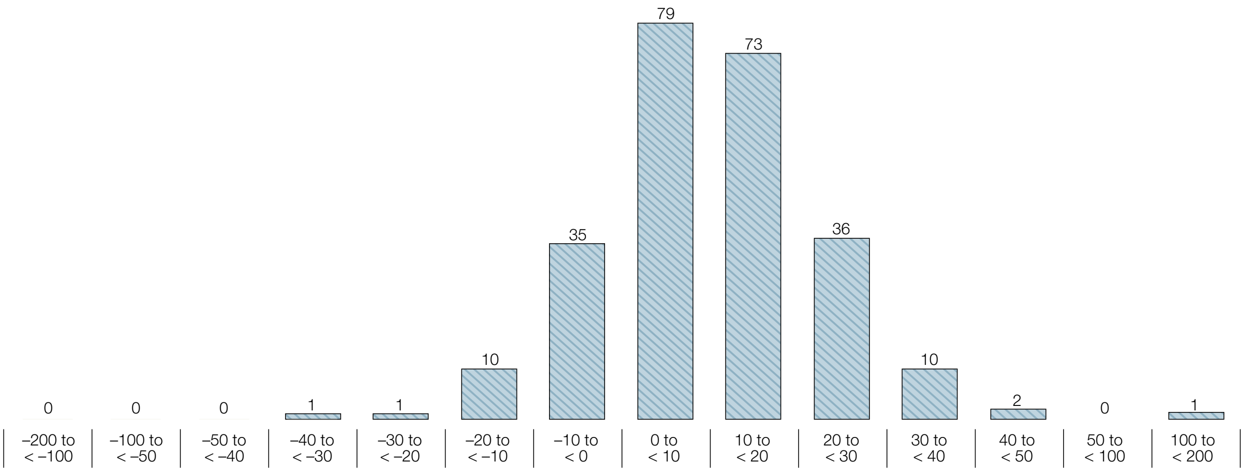
* *Capital calculated at the SARB transitional minimum requirement of 10% (excluding the bank-specific individual capital requirement).*
** *June 2013 numbers were restated to reflect the required regulatory capital charge for FirstRand.*

Distribution of daily trading earnings from trading units

The following histogram shows the daily revenue for the Group's local trading units for the year. The results are skewed towards profitability.

2014 distribution of daily earnings – frequency

Days in a period

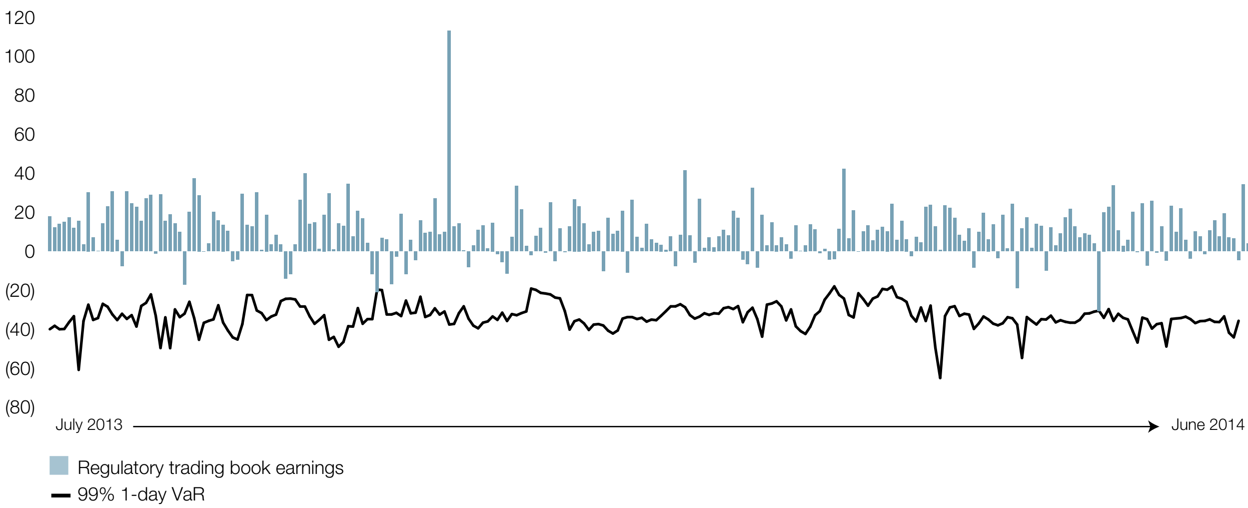


Back testing: daily regulatory trading book earnings and VaR

The Group tracks its daily local earnings profile as illustrated in the following chart. The earnings and 1-day VaR relate to the Group's internal VaR model. Exposures were contained within risk limits during the trading period.

Back testing: daily regulatory trading book earnings versus 1-day 99% VaR*

R million



* *Certain 1-day VaR numbers for the six-month period between July and December 2013 have been restated due to a data error. There was no impact on the back test and the error has since been rectified.*

Trading book earnings exceeded 1-day VaR on two occasions during the year under review. This indicates a reasonably accurate quantification of market risk provided by the Group's internal model.

International

RMB Australia Holdings and the Bank's India branch hold the highest exposure to market risk amongst the international operations. The same approach is employed for the measurement and management of market risk as in the domestic portfolio.

FRIHL – VaR analysis by risk type

The table reflects VaR over a 1-day holding period at a 99% confidence level for FRIHL. Market risk in FRIHL relates to the trading activities in RMB Australia Holdings Ltd and RMB Securities Trading (Pty) Ltd (RST), and represents a subset of the VaR analysis by asset class reflected above for the Group. Overall levels of risk remained largely unchanged on the prior year.

1-day 99% VaR analysis for FRIHL (audited)

	2014				2013
R million	**Min***	**Max***	**Average**	**Period end**	**Period end**
Diversified total	**10.6**	**28.8**	**14.7**	**13.3**	10.8

* *The maximum and minimum VaR figures for each asset class did not necessarily occur on the same day. Consequently, a diversification effect was omitted from the above table.*

Regulatory market risk for FRIHL is measured using the standardised approach. Commensurate with the slight increase in VaR observed above, market risk calibrated using the regulatory standardised approach has increased slightly since the previous year.

Market risk standardised approach for FRIHL*

R million	**2014**	**2013**
Specific risk	**42**	39
General risk	**51**	42

* *The above FRIHL regulatory market risk numbers comprise RST and RMB Resources.*

FNB Africa subsidiaries – standardised approach

Market risk for the African subsidiaries is measured using the standardised approach. In addition, the same ETL and VaR methodologies described above are used as supplementary measures.

Trading activities in the rest of Africa continued to grow over the past year and are expected to grow further as RMB expands its footprint and operations. During the year under review, market risk was contained within acceptable stress loss limits and was effectively managed in the African subsidiaries.

Market risk standardised approach for the African subsidiaries

	2014				2013
R million	**Min***	**Max***	**Average**	**Period end**	**Period end**
Risk type					
Interest rates	**3.4**	**14.8**	**8.9**	**7.4**	13.2
Foreign exchange	**5.0**	**45.5**	**33.0**	**16.0**	24.4
Total	**8.3**	**60.3**	**41.9**	**23.3**	37.6

* *The previous year end numbers were restated in line with regulatory capital reported for the June 2014 year end.*

INTEREST RATE RISK IN THE BANKING BOOK

INTRODUCTION AND OBJECTIVES

Interest rate risk in the banking book (IRRBB) originates from the differing repricing characteristics of balance sheet transactions, yield curve risk, basis risk and client optionality embedded in banking book products.

The endowment effect, which results from a large proportion of non- and low-rate liabilities that fund variable-rate assets, remains the primary driver of IRRBB and results in Group earnings being vulnerable to interest rate cuts, and would result in increased margins in a hiking cycle. The increase in the repo rate in the current financial year had a positive impact on the margin from the endowment book.

IRRBB is an inevitable risk associated with banking and can be an important source of profitability and shareholder value. Within FirstRand, IRRBB continues to be managed from an earnings approach, with the aim to protect and enhance the Bank's earnings and economic value within approved risk limit and appetite levels. The strategic hedge positions which were in place in the previous financial year have been allowed to roll off in the current financial year and the book is positioned to benefit from a hiking cycle. The endowment hedge portfolio is managed dynamically taking into account the continuously changing macroeconomic environment.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

The control and management of IRRBB is governed by the framework for the management of IRRBB, a subframework of the BPRMF. Ultimate responsibility for determining risk limits and appetite for the Group vests with the board. Independent oversight for monitoring is done through the RCC committee, who, in turn, has delegated the responsibility for IRRBB to Group ALCCO. ALCCO also maintains responsibility on behalf of the board for the allocation of sublimits and remedial action to be taken in the event of any limit breaches.

Individual ALCCOs exist in each of the African subsidiaries and international branches which monitor and manage in-country IRRBB. Material issues from individual ALCCOs are reported through to FirstRand ALCCO.

ASSESSMENT AND MANAGEMENT

FirstRand Bank South Africa

Interest rate risk originates from trading and non-trading/banking book activities. In the trading book, interest rate risk is primarily quantified and managed using ETL measures and limits. This is covered in *market risk in the trading book* section of this report.

Management and monitoring of the FirstRand domestic banking book is split between the RMB book and the remaining domestic banking book. RMB manages its banking book under the market risk framework; as such, risk is measured and monitored in conjunction with the trading book with management oversight provided by the market and investment risk committee. The RMB banking book interest rate risk exposure was R35.2 million on a 10-day ETL basis at 30 June 2014 (June 2013: R31.5 million). Refer to *market risk in the trading book* section. Any further reference relating to the banking book excludes the RMB book.

The remaining banking book consists predominantly of retail balances from FNB and WesBank, and the FCC balance sheet. This is managed centrally by Group Treasury with oversight from FCC risk management.

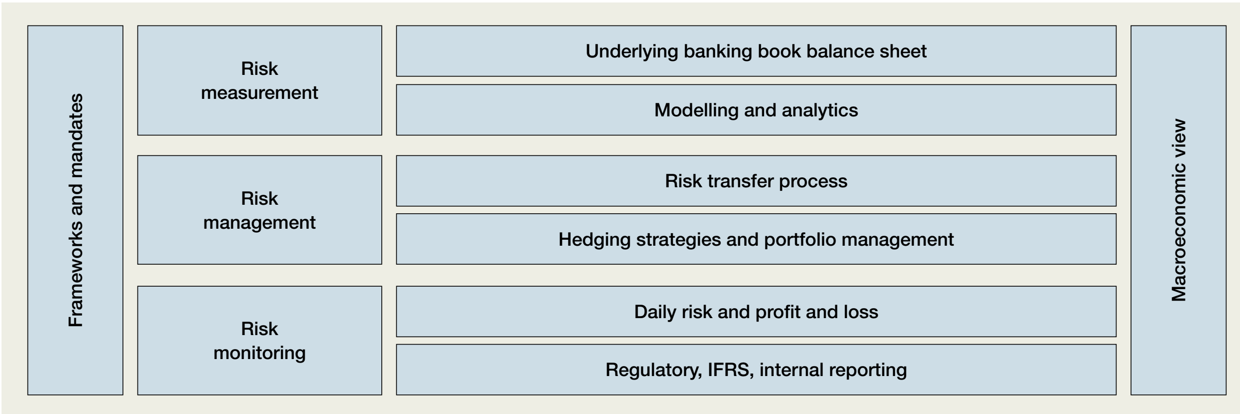
The internal funds transfer pricing (FTP) process is used to transfer interest rate risk from the franchises to Group Treasury. This process allows risk to be managed centrally and holistically in line with the Group's macroeconomic outlook. Management of the resultant risk position is achieved by balance sheet optimisation or through the use of derivative transactions. Derivative instruments used are mainly interest rate swaps, for which there is a liquid market. Where possible, hedge accounting is used to minimise accounting mismatches, thus ensuring that amounts deferred in equity are released to the income statement at the same time as movements attributable to the underlying hedged asset/liability. The interest rate risk from the fixed-rate book is managed to low levels with remaining risk stemming from timing and basis risk.

A number of measurement techniques are used to monitor IRRBB. These focus on the NII sensitivity/earnings risk and the overall impact on economic value of equity (EVE). A repricing gap is also generated to better understand the repricing characteristics of the balance sheet. In calculating the repricing gap, all banking book assets, liabilities and derivative instruments are placed in gap intervals based on their repricing characteristics.

Foreign operations

Management of foreign branches and subsidiaries is performed by in-country management teams with oversight provided by Group Treasury and FCC risk management. For subsidiaries, earnings sensitivity measures are used to monitor and manage interest rate risk in line with the Group's appetite. Where applicable, PV01 and ETL risk limits are also used for endowment hedges.

Interest rate risk management and assessment



SENSITIVITY ANALYSIS

A change in interest rates impacts both the earnings potential of the banking book (as underlying assets and liabilities reprice to new rates), as well as the economic/net asset value of an entity (as a result of a change in the fair value of any open risk portfolios used to manage the earnings risk). The role of management is to protect both the financial performance as a result of a change in earnings and to protect long-term economic value. To achieve this, both earnings sensitivity and EVE sensitivity measures are monitored and managed within appropriate risk limits and appetite levels, considering the macroeconomic environment and factors which could cause a change in rates.

Earnings sensitivity

Earnings models are run on a monthly basis to provide a measure of the NII sensitivity of the existing banking book balance sheet to shocks in interest rates. Underlying transactions are modelled on a contractual basis, assuming a constant balance sheet size and mix. No adjustments are made for prepayments in the underlying book, however, prepayment assumptions are factored into the calculation of hedges for fixed rate lending. Rollover assumptions are not applied to off-balance sheet positions.

The following tables show the 12-month NII sensitivity for a sustained, instantaneous parallel 200 bps downward and upward shock to interest rates. The increased sensitivity in June 2014 compared to June 2013 is attributable to endowment hedges that have rolled off. Given uncertainty in the rate environment in the previous financial year, the endowment book was positioned to provide protection against potential rate cuts. These hedges have been allowed to roll off given changes in the macroeconomic environment and the Group's net interest margin is positioned to benefit from rate hikes as a result of the endowment impact.

Assuming no change in the balance sheet and no management action in response to interest rate movements, an instantaneous, sustained parallel decrease in interest rates of 200 bps would result in a reduction in projected 12-month NII of R2 679 million. A similar increase in interest rates would result in an increase in projected 12-month NII of R2 578 million. The NII sensitivity analysis below excludes the banking books which are managed separately. The bulk of the sensitivity relates to the endowment book mismatch. The Group's average endowment book was R122 billion for the year. Total sensitivity to ZAR rate moves is measured in the Bank whilst African subsidiaries are measured in their home currency.

Projected NII sensitivity to interest rate movements (audited*)

	2014		
	Change in projected 12-month NII		
R million	**FirstRand Bank**	**FNB Africa**	**FirstRand**
Downward 200 bps	**(2 258)**	**(421)**	**(2 679)**
Upward 200 bps	**2 218**	**363**	**2 581**

	2013		
	Change in projected 12-month NII		
R million	**FirstRand Bank**	**FNB Africa**	**FirstRand**
Downward 200 bps	(789)	(260)	(1 049)
Upward 200 bps	676	258	934

* *The earnings modelling process and roll-over assumptions applied are not subject to the scope of reasonable assurance.*

Economic value of equity (EVE)

An EVE sensitivity measure is used to assess the impact on the total net asset value of the Group as a result of a shock to underlying rates. Unlike in the trading book where a change in rates will impact the fair value income and the reportable earnings of an entity when a rate change occurs, the realisation of a rate move in the banking book will impact the distributable and non-distributable reserves of the entity to varying degrees and is reflected in the NII margin more as an opportunity cost/benefit over the life of the underlying transactions. As a result, a purely forward looking EVE measure applied to the banking book, be it a 1 bps shock or a full stress shock, is monitored relative to total risk limit and appetite levels.

The table below highlights the sensitivity of the net asset value as a percentage of total capital. The EVE shock applied is based on regulatory guidelines and is a sustained, instantaneous parallel 200 bps downward and upward shock to interest rates. This is applied to risk portfolios managed by Group Treasury which, as a result of the risk transfer through the FTP process, captures relevant open risk positions in the banking book. This measure does not take into account the unrealised economic benefit embedded in the entity as a result of the banking book products which are not recognised at fair value. The change in the current period is attributable to the endowment hedge position in place in the previous financial year which was allowed to roll off in anticipation of a hiking cycle.

The table below reflects a point-in-time view which is dynamically managed and can change significantly in a short space of time. This disclosure differs from previous EVE sensitivity disclosure as it looks at the economic sensitivity of the banking book as a whole as opposed to only the sensitivity of products impacting the cash flow and available-for-sale reserves. The economic sensitivity analysis below excludes the banking books of RMB and the foreign operations, which are managed separately. The bulk of the sensitivity originates from the endowment hedges which decreased from the previous financial year.

Net asset value sensitivity to interest rate movements as a percentage of total Group capital (audited)

%	**2014**	**2013**
Downward 200 bps	**0.25**	1.45
Upward 200 bps	**(0.28)**	(1.42)

EQUITY INVESTMENT RISK

INTRODUCTION AND OBJECTIVES

Equity investment risk arises primarily from equity exposures from investment banking activities in RMB, e.g. exposures to equity risk arising from principal investments or structured lending. In addition, equity investment risk arises from strategic investments held by WesBank, FNB and FCC.

Ashburton Investments was launched in 2013, which has required the seeding of new traditional and alternative funds both locally and offshore, which exposes the Group to equity investment risk.

In addition, equity investment risk arises from strategic investments held by WesBank, FNB and FCC.

The Group actively monitors regulatory developments, including amendments to current regulations as a result of Basel III. This has resulted in changes to the risk weighting of certain classes of investments.

The overall quality of the investment portfolio remains acceptable and is within risk appetite. During the year under review, there were few equity realisations with several new equity investments undertaken as part of a portfolio rebuilding strategy.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

The responsibility for determining equity investment risk appetite vests with the board. The following structures have been established in order to assess and manage equity investment risk:

- the prudential investment committee (investment committee) chaired by the RMB chief investment officer and its delegated subcommittees are responsible for oversight of the approval of portfolio investment transactions in equity, quasi-equity or quasi-debt instruments;
- where the structure of the investments also incorporate significant components of senior debt, approval authority will rest with the respective credit committees and the large exposures committee, as appropriate;
- the biannual investment risk oversight committee assesses the quality, size and performance of the investment portfolio across RMB and reviews movements in light of risk appetite;
- the RMB CRO, in consultation with the Group CRO and with support from the deployed and central risk management functions, provides independent oversight and reporting of all investment activities in RMB to the RMB proprietary board, as well as the market and investment risk committee. FNB and WesBank executive management monitor and manage investments through the financial reporting process; and
- RCC and MIRC committees are responsible for the oversight of investment risk measurement and management across the Group.

In Ashburton Investments, new fund investments are approved by the investment forum before review and approval by its investment product development, investment distribution and executive committees. Also prior to seeding, capital and investment limits are provided by the capital management committee and the market and investment risk committee, respectively. Ashburton Investments is in the process of establishing its own capital management committee to monitor and report on these positions to the appropriate Group governance committees. Ashburton Investments' audit, risk and compliance committee reported into FCC audit, risk and compliance committee during the year under review.

ASSESSMENT AND MANAGEMENT

Management of exposures

The equity investment risk portfolio is managed through a rigorous evaluation and review process from inception to exit of a transaction. All investments are subject to a comprehensive due diligence, during which a thorough understanding of the target company's business, risks, challenges, competitors, management team and unique advantage or value proposition is developed.

For each transaction, an appropriate structure is put in place which aligns the interests of all parties involved through the use of incentives and constraints for management and the selling party. Where appropriate, the Group seeks to take a number of seats on the company's board and maintains close oversight through monitoring of operations.

The investment thesis, results of the due diligence process and investment structure are discussed at the investment committee before final approval is granted. In addition, normal semi-annual reviews are carried out for each investment and crucial parts of these reviews, such as valuation estimates, are independently peer reviewed.

Recording of exposures – accounting policies

IAS 39 requires equity investments to be classified as financial assets at fair value through profit and loss, or available-for-sale financial assets.

Consistent with the Group's accounting policies, the consolidated financial statements include the assets, liabilities and results of operations of all equity investments in which the Group has power over the relevant activities and the ability to use that power to affect the variable returns received from the entity.

Equity investments in associates and joint ventures are included in the consolidated financial statements using the equity accounting method. Associates are entities where the Group holds an equity interest of between 20% and 50%, or over which it has the ability to exercise significant influence, but does not control. Joint ventures are entities in which the Group has joint control over the relevant activities of the joint venture through a contractual agreement.

Measurement of risk exposures

Risk exposures are measured as potential loss under stress conditions. A series of standardised stress tests are used to assess potential losses under current market conditions, adverse market conditions, as well as severe stress/event risk. These stress tests are conducted at individual investment and portfolio levels.

The Group targets an investment portfolio profile that is diversified along a number of pertinent dimensions, such as geography, industry, investment stage and vintage (i.e. annual replacements of realisations).

Stress testing

Economic and regulatory capital calculations are complemented with regular stress tests of market values and underlying drivers of valuation e.g. company earnings, valuation multiples and assessments of stress resulting from portfolio concentrations.

Regulatory and economic capital

The SARB simple risk weighted method under the market-based approach, 300% (listed) or 400% (unlisted) is applied for the quantification of regulatory capital. Under the Regulations, the risk weight applied to investments in financial, banking and insurance institutions are subject to the aggregate and individual value of the Group's shareholding in these investments and also in relation to the Group's qualifying CET1 capital. The shareholdings in the investments are bucketed depending on the size of investment.

For economic capital purposes, an approach using market value shocks to the underlying investments is used to assess economic capital requirements for unlisted investments after taking any unrealised profits not taken to book into account.

Where price discovery is reliable, the risk of listed equity investments is measured based on a 90-day ETL calculated using RMB's internal market risk model. The ETL risk measure is supplemented by a measure of the specific (idiosyncratic) risk of the individual securities per the specific risk measurement methodology.

EQUITY INVESTMENT RISK PROFILE

Market prices in selected industries continued to present the Group with opportunities to build its private equity portfolio. Unrealised profits for the investment portfolio remained resilient. The private equity portfolio has been subject to a portfolio rebuilding initiative during the year.

Investment risk exposure and sensitivity of investment risk exposure

R million	2014	2013**
Listed investment risk exposure included in the equity investment risk ETL process	**516**	431
ETL on above equity investment risk exposures	**161**	194
Estimated sensitivity of remaining investment balances		
Sensitivity to 10% movement in market value on investment fair value*	**397**	729
Cumulative gains realised from sale of positions in the banking book during the period	**1 786**	550

* *Audited. The 10% sensitivity movement is calculated on the carrying value of investments excluding investments subject to the ETL process and the carrying value of investments in associates and joint ventures. The decline in the sensitivity value from 2013 to 2014 relates mainly to a change in accounting treatment of the employee liability insurance.*

** *June 2013 number was restated to reflect IFRS changes.*

The following table provides information relating to equity investment risk.

Investment valuations and associated regulatory capital requirements

R million	2014 Publicly quoted investments	2014 Privately held	2014 Total
Carrying value of investments*	**1 907**	**9 630**	**11 537**
Per risk bucket			
250%	**3**	**2 558**	**2 561**
300%	**1 904**	**–**	**1 904**
400%	**–**	**7 072**	**7 072**
Latent revaluation gains not recognised in the balance sheet**	**183**	**5 750**	**5 933**
Fair value#	**2 090**	**15 380**	**17 470**
Total unrealised gains recognised directly in balance sheet through equity instead of the income statement**	**259**	**45**	**304**
Capital requirement†	**586**	**2 952**	**3 538**

* *Financial, banking and insurance entities that meet Basel III classification criteria are subject to risk weighting at 250% whilst listed and unlisted investments are subject to 300% and 400% risk weighting respectively. This is additional disclosure from June 2014. Comparative information will be provided from June 2015.*

** *These unrealised gains or losses are not included in Tier 1 or Tier 2 capital.*

\# *The fair values of listed private equity investments were not considered to be materially different from the quoted market prices.*

† *Capital requirement calculated at 10% of RWA (excluding the bank-specific individual capital requirement), and includes capital on investments in financial entities. These investments are included as other assets in the RWA table in the capital section.*

R million	2013 Publicly quoted investments	2013 Privately held	2013 Total
Carrying value of investments*	2 521	9 262	11 783
Latent revaluation gains not recognised in the balance sheet**	–	5 411	5 411
Fair value#	2 521	14 673	17 194
Total unrealised gains recognised directly in balance sheet through equity instead of the income statement**	517	-	517
Capital requirement†	718	3 279	3 997

* *The carrying value includes investments in financial, banking and insurance entities, which from 1 January 2013 are subject to the Basel III 250% risk weighting.*

** *These unrealised gains or losses are not included in Tier 1 or Tier 2 capital. Numbers restated to reflect correct values as at 30 June 2013.*

\# *The fair values of listed private equity investments were not considered to be materially different from the quoted market prices.*

† *Capital requirement calculated at 9.5% of RWA (excluding the bank-specific individual capital requirement), and includes capital on investments in financial entities. These investments are included as other assets in the RWA table in the capital section.*

FOREIGN EXCHANGE AND TRANSLATION RISK IN THE BANKING BOOK

INTRODUCTION AND OBJECTIVES

Foreign exchange risk arises from on- and off-balance sheet positions whose valuation in rand is subject to currency movements. Key activities giving rise to these positions are foreign currency placements, lending and investing activities, raising of foreign currency funding and trading and client facilitation activities in foreign currencies. The objective of foreign exchange risk management is to ensure that currency mismatches are managed within the Group's risk appetite and to ensure governance and oversight.

Translation risk is the risk to the rand-based reported earnings from fluctuations in the exchange rate when applied to the value, earnings and assets of foreign operations. Translation risk is, at present, seen as an unavoidable risk which results from having offshore operations. The Group does not actively hedge this risk.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

Foreign exchange risk results from activities of all the franchises, but management and consolidation of all these positions occur in one of two business units. Client flow and foreign exchange trading, including daily currency mismatch, are consolidated under and executed by RMB global markets. Foreign currency funding, foreign assets as well as foreign currency exposure, liquidity and term mismatch are consolidated under and managed by Group Treasury.

Market risk, foreign exposure and mismatch limits are approved by the board and the primary governance body is the RCC committee. Trading risk and the NOFP are overseen by the market and investment risk committee, a subcommittee of the RCC committee and mismatch risk is governed through Group international ALCCO processes. In addition to the committee structures, business units charged with frontline management of these risks have deployed risk managers within their units who assess and report this risk on an ongoing basis.

ASSESSMENT AND MANAGEMENT

In addition to the regulatory prudential limit on foreign asset exposure (25% of local liabilities), the board has set internal limits on FirstRand's total foreign currency exposure, within the regulatory limit but allowing opportunity for expansion and growth. Internal limits are also set per franchise, taking into account existing foreign asset exposure and future growth plans. Internal limits and utilisation are continuously monitored and reviewed when necessary.

The Group's NOFP position is within the regulatory limit of USD848 million, with the actual exposure at a net negative USD4 million. Senior management implemented various levels of internal prudential limits, taking into account fluctuating exchange rates and the Group's capital position. These limits fall below the regulatory limit but are large enough to cater for the hedging, settlement and execution positions of business units. Group Treasury is the clearer of all currency positions in FirstRand and is, therefore, tasked with the responsibility for managing the Group's position within internal and prudential limits. Any breaches are reported through the risk management structures and corrective action is monitored by both the deployed risk managers and ERM.

FOREIGN EXCHANGE AND TRANSLATION RISK PROFILE

Over the past year, no significant foreign exchange positions have been run, apart from translation risk in strategic foreign investments. Mismatches have been contained well within regulatory limits at all times. The macro foreign asset exposure of the Group remained below both regulatory and board limits and there is significant headroom for expansion into foreign assets.

FUNDING AND LIQUIDITY RISK

INTRODUCTION AND OBJECTIVES

The Group strives to fund its activities in a sustainable, diversified, efficient and flexible manner, underpinned by strong counterparty relationships within prudential limits and exceeding minimum requirements. The objective is to maintain natural market share, but also to outperform at the margin, which will provide the Group with a natural liquidity buffer.

Given the liquidity risk introduced by its business activities, the Group's objective is to optimise its funding profile within structural and regulatory constraints to enable franchises to operate in an efficient and sustainable manner.

Compliance with the Basel III Liquidity Coverage Ratio (LCR) influences the Group's funding strategy, in particular as it seeks to restore the correct risk-adjusted pricing of deposits. The Group is actively building its deposit franchise through innovative and competitive products and pricing, while also improving the risk profile of its institutional funding.

At 30 June 2014, the Bank exceeded the 60% minimum LCR requirement (effective 1 January 2015), per the *pro forma* LCR issued by the BCBS and inclusive of the SARB communicated national discretion items.

The Group has maintained a robust liquidity position during the year under review, holding sufficient levels of available liquidity relative to the Group's appetite and prevailing market conditions. At 30 June 2014, the Bank's available sources of liquidity per the BCBS LCR amounted to R93 billion, with an additional R22 billion of management liquidity available.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

Liquidity risk management is governed by the liquidity risk management framework, which provides relevant standards in accordance with regulatory requirements and international best practice. As a subframework of the BPRMF, the liquidity risk management framework is approved by the board and sets out consistent and comprehensive standards, principles, policies and procedures to be implemented throughout the Group to effectively identify, measure, report and manage liquidity risk.

The board retains ultimate responsibility for the effective management of liquidity risk. The board has delegated its responsibility for the assessment and management of this risk to the RCC committee, which in turn delegated this task to Group ALCCO. Group ALCCO's primary responsibility is the assessment, control and management of both liquidity and interest rate risk for the Bank, its international branches as well as the subsidiaries in FREMA, either directly or indirectly, through providing guidance, management and oversight to the asset and liability management functions and ALCCOs in these entities.

Group Treasury is mandated to manage the funding and liquidity risk of the Group. Group Treasury is responsible for:

- recommending, implementing and reviewing the liquidity risk appetite, strategy and risk management processes of the Group; and
- managing and maintaining prudential liquidity limits across all entities in the Group.

Governance is provided by an independent risk team responsible for ensuring that the liquidity risk management framework is implemented appropriately.

The Group's liquidity position, exposures and auxiliary information are reported weekly to the funding and liquidity portfolio management committee and monthly to the funding executive committee. In addition, management aspects of the liquidity position are reported daily to Group Treasury. The liquidity risk management team provides regular reports to Group ALCCO.

Foreign entities

Foreign branches are part of the Bank, while subsidiaries are managed on a standalone basis with no implicit or explicit support. All subsidiaries are managed within in-country capital base and liquidity resources with focus on developing deposit franchises.

International branches and subsidiaries have in-country treasury functions responsible for the day-to-day management of these entities' funding and liquidity risk. Group Treasury provides:

- overall funding and liquidity risk management frameworks and mandates;
- dedicated resources to assist with technical expertise in asset/liability management and fundraising activities; and
- alignment to international best practice and latest regulatory developments.

Individual ALCCOs have been established in each of the subsidiaries in FREMA and manage liquidity risk in-country in line with the Group principles under delegated mandates from their respective boards. Reports from these committees are regularly presented to Group ALCCO and management and control of liquidity risk in the subsidiaries are based on guidance and principles that have been set out and approved by Group ALCCO.

From a liquidity risk perspective, international businesses report into the international ALCCO (a subcommittee of Group ALCCO), which meets quarterly to review and discuss region-specific liquidity and interest rate risk issues. Individual ALCCOs are held locally monthly and include representation from Group Treasury.

FirstRand has been granted a renewed dispensation by the Financial Services Authority (FSA) for a waiver on a Whole-firm Liquidity Modification application basis where the FSA considers local risk reporting and compliance of the parent bank sufficient to waive FSA requirements for FirstRand Bank (London branch). FSA reporting commenced in January 2011. As part of the liquidity risk management framework for London branch, the branch has access to the Bank of England's discount window facility for approved collateral.

FUNDING MANAGEMENT

The banking sector in South Africa is characterised by certain structural features, such as a low discretionary savings rate and a higher degree of contractual savings that are captured by institutions such as pension funds, provident funds and providers of asset management services. A portion of these contractual savings translate into institutional funding for banks which have higher liquidity risk than deposits raised through the deposit franchise. Recent observations suggest that South African corporates and the public sector also make use of financial intermediaries that provide bulking and maturity transformation services with their cyclical cash surpluses. Structural liquidity risk is, therefore, higher in South Africa than in most other markets. This risk is, however, to some extent mitigated by the following factors:

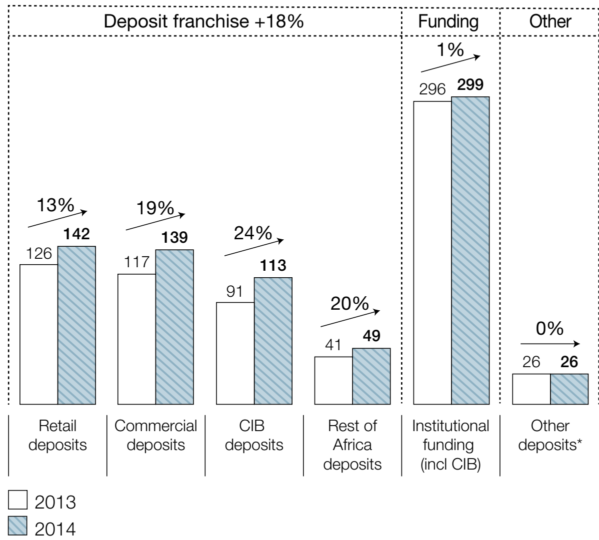
- the closed rand system where all rand transactions are cleared and settled in South Africa through registered banks and clearing institutions domiciled in South Africa;
- concentration of customer current accounts with the four largest banks;
- prudential exchange control framework in place in South Africa; and
- the low dependency of South African banks on foreign currency funding.

During the year under review, there has been increased liquidity demand by banks as a consequence of the money supply constraints introduced by LCR. In light of the structural features discussed above, focus is currently placed on achieving a risk-adjusted diversified funding profile which also complies with Basel III requirements.

The Group manages its funding structure by source, counterparty type, product, currency and market. The deposit franchise represents the most efficient source of funding and comprised 63% of domestic funding liabilities at 30 June 2014. During the year under review, the Group has continued to focus on growing its deposit franchise across all segments with increasing emphasis on savings products and term savings. Progress has been made in developing suitable products to attract a greater proportion of clients' available liquidity with improved risk-adjusted pricing. To fund operations, the Group accesses the domestic money markets daily and has, during the course of the year, accessed both domestic and foreign capital markets. The Group has frequently issued various capital and funding instruments within the domestic capital markets on an auction and reverse enquiry basis with strong support from investors.

The graph below provides a segmental analysis of the Group's funding base and illustrates the success of its deposit franchise focus.

Group funding by segment
R billion



* *Consists of liabilities relating to conduits and securitisations.*

Funds transfer pricing

The Group operates a funds transfer pricing framework which incorporates liquidity costs and benefits as well as regulatory friction costs into product pricing and performance measurement for all on- and off-balance sheet activities. Franchises are incentivised to:

- preserve and enhance funding stability;
- ensure that asset pricing is aligned to liquidity risk;
- reward liabilities in accordance with behavioural characteristics and maturity; and
- manage contingencies with respect to potential funding drawdowns.

Funding measurement and activity

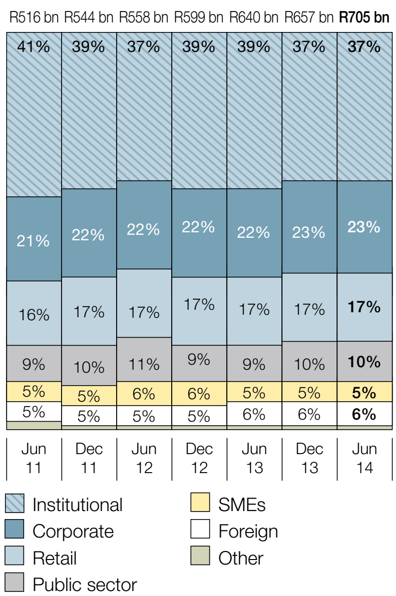
The Bank, FirstRand's wholly-owned subsidiary and debt issuer, generates a larger proportion of its funding from the deposit franchise in comparison to the South African aggregate, however, its funding profile also reflects the structural features described above. The table below provides an analysis of the Bank's funding sources.

Bank's funding sources*

	As at 30 June 2014			
% of funding liabilities	**Total**	**Short-term**	**Medium-term**	**Long-term**
Institutional funding	**37.0**	**12.2**	**8.2**	**16.6**
Deposit franchise	**63.0**	**47.8**	**6.5**	**8.7**
Corporate	**22.7**	**19.5**	**1.4**	**1.8**
Retail	**17.0**	**12.7**	**2.9**	**1.4**
SMEs	**5.2**	**4.6**	**0.4**	**0.2**
Governments and parastatals	**9.6**	**7.9**	**1.2**	**0.5**
Foreign	**6.1**	**3.0**	**0.4**	**2.7**
Other	**2.4**	**0.1**	**0.2**	**2.1**
Total	**100.0**	**60.0**	**14.7**	**25.3**

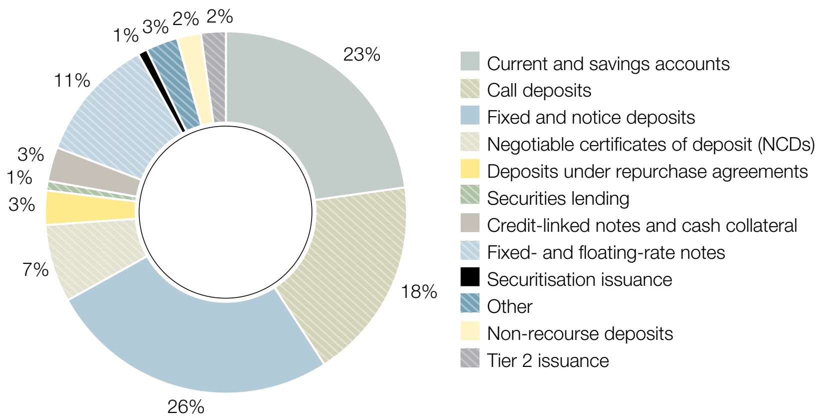
* *Reflects solo supervision, i.e. FRB excluding foreign branches.*

Bank's funding analysis by source



The following chart illustrates the Group's funding instruments by instrument type, including senior debt and securitisation.

Group's funding analysis by instrument type

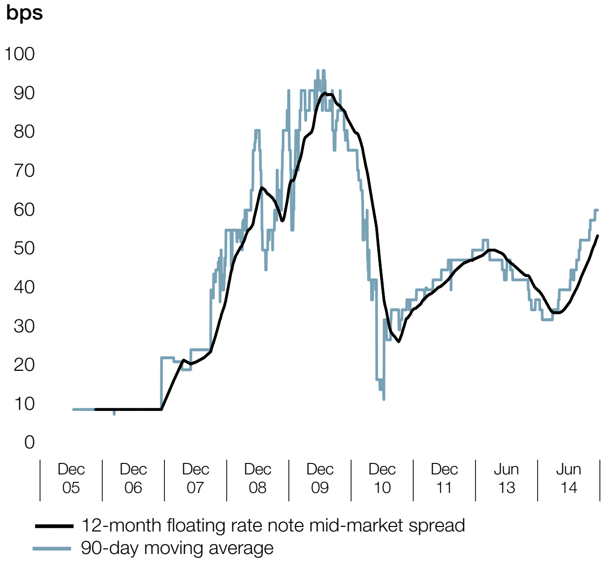


The Group's aim is to fund the balance sheet in the most efficient manner, taking into account the liquidity risk management framework, as well as regulatory and rating agency requirements.

To ensure maximum efficiency and flexibility in accessing funding opportunities, a range of debt programmes has been established. The Bank's strategy for domestic vanilla public issuance is to create actively-traded benchmarks, which facilitate secondary market liquidity in both domestic and offshore markets. The value of this strategy is that it assists in identifying cost-effective funding opportunities while ensuring a good understanding of market liquidity.

The following graph is a representation of the market cost of liquidity, which is measured as the spread paid on NCDs relative to the prevailing swap curve for that tenor. The liquidity spread graph is based on the most actively-issued money market instrument by banks, namely 12-month NCDs. During the year under review, spreads initially reduced to a low point in October 2013, after which they started to increase slowly through to December 2013. Between January and June 2014, spreads increased considerably, as illustrated in the graph below. This appears to be a result of banks competing for longer term funding, while savings flows are not increasing.

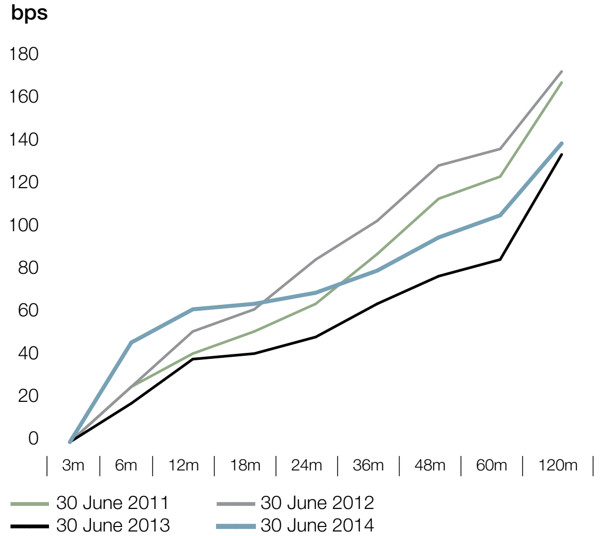
12-month liquidity spread



Source: Bloomberg (RMBP screen) and Reuters

The following graph shows that long-term funding spreads are elevated from a historical perspective. On the basis of the Group's improved risk profile, higher capital adequacy and greater predictability of earnings, the credit risk component of the funding spreads should be lower. Long-term funding spreads, therefore, still appear to be reflecting a high liquidity premium. The Group is consistently able to raise funds in the capital markets in line with its funding curve, which it views as an important test as the Group's asset origination is linked to its funding curve.

Long-term funding spreads

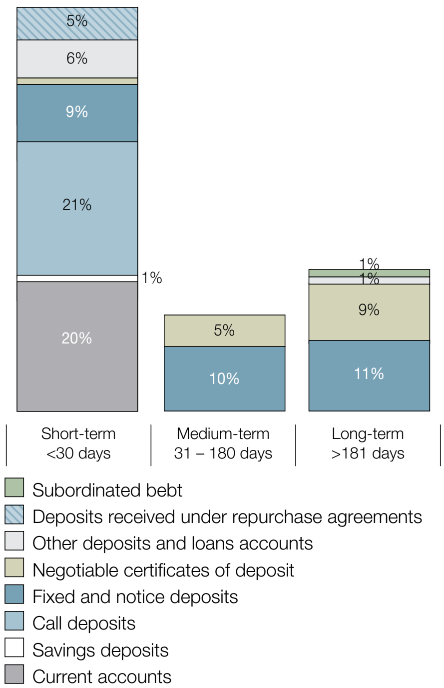


Source: Bloomberg (RMBP screen) and Reuters

As a result of the Group's focus on growing its deposit and transactional banking franchise, a significant proportion of funds are contractually short-dated. As these deposits are anchored to clients' service requirements and given the balance granularity created by individual clients' independent activity, the resultant liquidity risk profile is improved.

The following charts illustrates a breakdown of the Group's funding liabilities by instrument type and term.

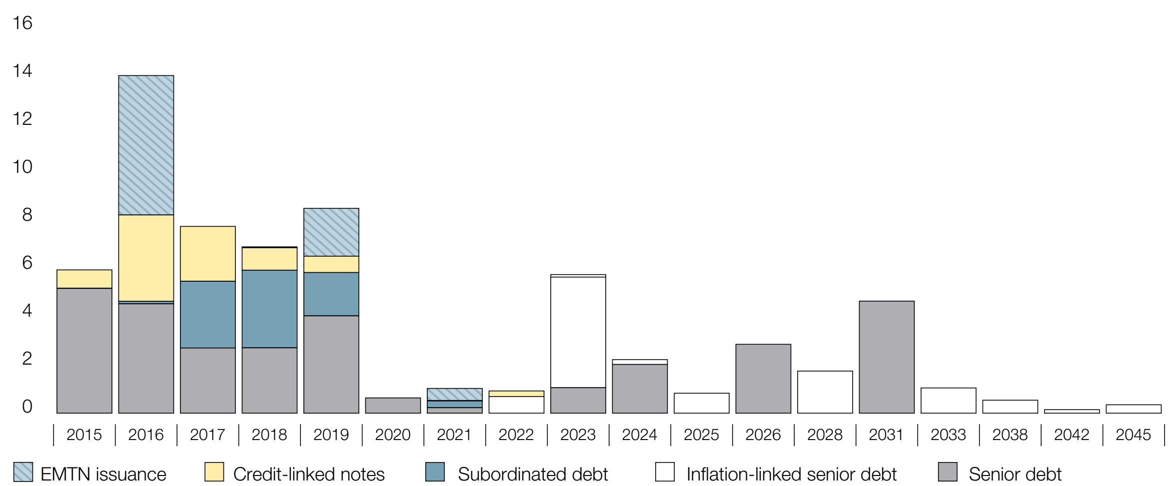
Group's funding liabilities by instrument type and term at 30 June 2014



The maturity profile of all issued capital markets instruments is shown below. The Group does not have concentration risk in any one year and seeks to efficiently issue across the curve with consideration of investor demand.

Maturity profile of Bank's capital market instruments

R billion



Funding structure of foreign operations

In line with the Group's focus on growing franchises, foreign operations are categorised in terms of their stage of development from greenfields to mature subsidiaries and are characterised from a funding perspective as follows:

- mature deposit franchises – all assets are largely funded in-country. The pricing of funding is determined via in-country funds transfer pricing, which is already in place;
- growing deposit franchises – assets are first funded in-country at attendant funds transfer pricing rates. Any excess over and above the in-country capacity would be funded by the Group's USD funding platforms. This is a temporary arrangement which allows these subsidiaries time to develop adequate in-country deposit bases; and
- no deposit franchises – all activities are funded by the Group's USD funding platforms.

Group support

Any funding provided by the Group is constrained by the appetite set independently by the credit risk management committee or the board. In arriving at limits, the credit risk management committee considers the operating jurisdiction and any sovereign risk limits that should apply, but is indifferent between liquidity and funding facilities. Group Treasury, therefore, has to ensure that any resources availed to foreign entities are appropriately priced.

FOREIGN CURRENCY BALANCE SHEET

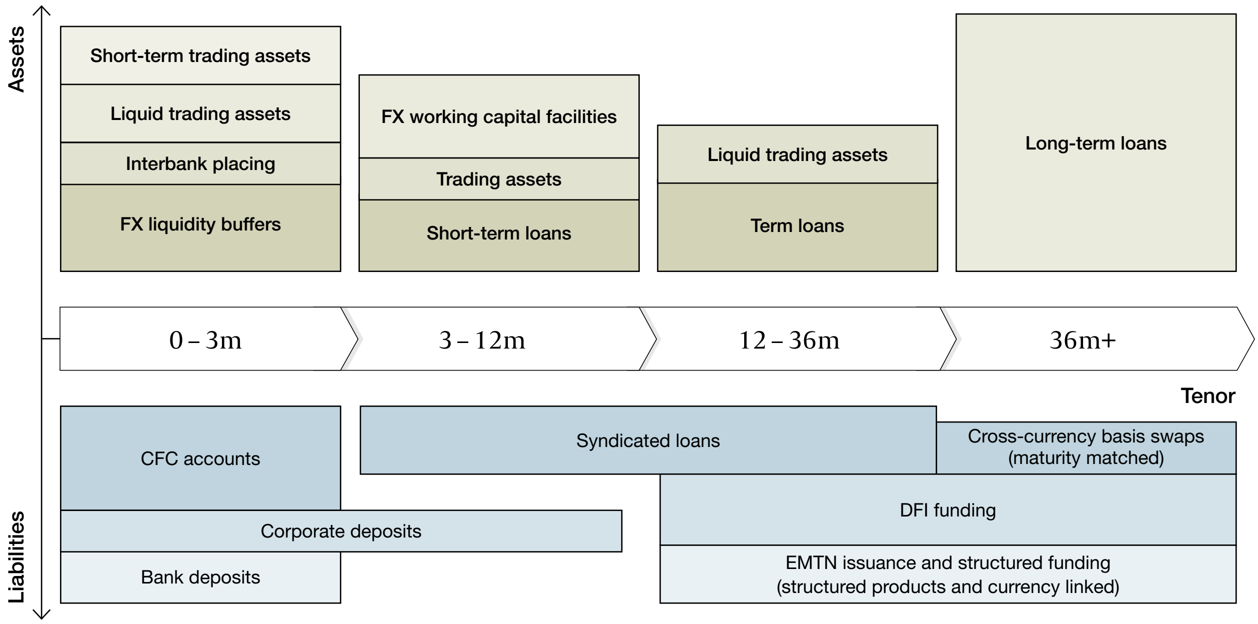
Given the Group's objective to grow its franchise in the rest of Africa, India and the corridors, and given the size of MotoNovo, the active management of foreign currency liquidity risk continues to be a strategic focus. The Group seeks to avoid exposing itself to undue liquidity risk within the risk appetite approved by the board and risk committee. The SARB via *Exchange Control Circular 9 of 2011* introduced macro-prudential limits applicable to authorised dealers. The Group utilises its own foreign currency measurement balance sheet measures based on economic risk and has set internal limits below those which are allowed by the macro-prudential limit framework.

FirstRand's expansion strategy means that its foreign currency activities, specifically lending and trade finance, have increased. It is, therefore, important to have a sound framework for the assessment and management of foreign currency external debt, given the inherent vulnerabilities and liquidity risks associated with cross-border financing. This limit includes the Bank's exposure to branches, foreign currency assets and guarantees.

Philosophy on foreign currency external debt

A key determinant in an institution's ability to fund and refinance in currencies other than its domestic currency is the sovereign risk and associated external financing requirement. The framework for the management of external debt takes into account sources of sovereign risk and foreign currency funding capacity. In order to achieve this, the Group considers risks arising from unsustainable debt path, liquidity, exchange rate and macroeconomic crises. To determine South Africa's foreign currency funding capacity, the Group considers the external debt of all South African entities (private and public sector, financial institutions) as these entities all utilise the South African system's capacity – confidence and export receipts.

Graphical representation of the foreign currency balance sheet



LIQUIDITY RISK MANAGEMENT

The Group acknowledges that liquidity risk is a consequential risk that may be caused by other risks. This was demonstrated by the reduction in liquidity in many international markets as a consequence of the recent credit crisis. The Group is, therefore, focused on continuously monitoring and analysing the potential impact of other risks and events on its funding and liquidity position and aims to ensure that business activities preserve and improve funding stability. This will enable the Group to operate through periods of stress when access to funding is constrained.

The Group recognises two types of liquidity risk:

- **funding liquidity risk** is the risk that a bank will not be able to effectively meet current and future cash flow and collateral requirements without negatively affecting its normal course of business, financial position or reputation; and
- **market liquidity risk** is the risk that market disruptions or lack of market liquidity will cause a bank to be unable (or able, but with difficulty) to trade in specific markets without affecting market prices significantly.

Mitigation of market and funding liquidity risks is achieved via contingent liquidity risk management. Buffer stocks of highly-liquid assets are held either to be sold into the market or to provide collateral for loans to cover any unforeseen cash shortfall that may arise.

The Group's approach to liquidity risk management distinguishes between structural, daily and contingency liquidity risk management across all currencies, and various approaches are employed in the assessment and management of these on a daily, weekly and monthly basis as illustrated in the following table.

Liquidity risk management approaches

Structural liquidity risk	Daily liquidity risk	Contingency liquidity risk
Managing the risk that structural, long-term on- and off-balance sheet exposures cannot be funded timeously or at reasonable cost.	Ensuring that intraday and day-to-day anticipated and unforeseen payment obligations can be met by maintaining a sustainable balance between liquidity inflows and outflows.	Maintaining a number of contingency funding sources to draw upon in times of economic stress.
liquidity risk tolerance; liquidity strategy; ensuring substantial diversification over different funding sources; assessing the impact of future funding and liquidity needs taking into account expected liquidity shortfalls or excesses; setting the approach to managing liquidity in different currencies and from one country to another; ensuring adequate liquidity ratios; ensuring an appropriate structural liquidity gap; and maintaining a funds transfer pricing methodology and process.	managing intraday liquidity positions; managing daily payment queue; monitoring net funding requirements; forecasting cash flows; performing short-term cash flow analysis for all currencies individually and in aggregate; management of intragroup liquidity; managing central bank clearing; managing net daily cash positions; managing and maintaining market access; and managing and maintaining collateral.	managing early warning and key risk indicators; performing stress testing including sensitivity analysis and scenario testing; maintaining product behaviour and optionality assumptions; ensuring that an adequate and diversified portfolio of liquid assets and buffers are in place; and maintaining the contingency funding plan.

Stress testing and scenario analysis

Regular and rigorous stress tests are conducted on the funding profile and liquidity position as part of the overall stress-testing framework with a focus on:

- quantifying the potential exposure to future liquidity stresses;
- analysing the possible impact of economic and event risks on cash flows, liquidity, profitability and solvency position; and
- proactively evaluating the potential secondary and tertiary effects of other risks on the Group.

Liquidity contingency planning

Frequent volatility in funding markets and the fact that financial institutions can and have experienced liquidity problems even during benign economic conditions highlight the importance of quality liquidity risk and contingency management processes.

The Group's ability to meet all of its daily funding obligations and emergency liquidity needs is of paramount importance and, in order to ensure that this is always adequately managed, the Group maintains a liquidity contingency plan.

The objective of liquidity contingency planning is to achieve and maintain funding levels in a manner that allows the Group to emerge from a potential funding crisis with its reputation intact and to maintain its financial condition for continuing operations. The plan is expected to:

- support effective management of liquidity and funding risk under stressed conditions;
- establish clear roles and responsibilities in the event of a liquidity crisis; and
- establish clear invocation and escalation procedures.

The liquidity contingency plan provides a pre-planned response mechanism to facilitate swift and effective responses to contingency funding events. These events may be triggered by financial distress in the market (systemic) or a bank-specific events (idiosyncratic) which may result in the loss of funding sources.

It is reviewed annually and tested regularly via a Group-wide liquidity stress simulation exercise to ensure the document remains up to date, relevant and familiar to all key personnel within the Group that have a role to play should it ever experience an extreme liquidity stress event.

FirstRand's recovery plan

The Group has submitted its first recovery plan to the SARB, which will become an annual requirement. The Group recovery plan is an extension of the liquidity contingency plan inclusive of all other risk-contributing factors that influence capital adequacy, liquidity and operational processes. FirstRand is currently engaged with the industry and regulators on the recovery and resolution regime development for South Africa.

REGULATORY UPDATE

Basel III

Post the financial crisis, the BCBS instituted a framework for sound and prudent liquidity risk management. The liquidity reforms seek to address two aspects of liquidity risk:

- the LCR addresses short-term liquidity risk and cash management; and
- the Net Stable Funding Ratio (NSFR) addresses the structural liquidity risk of the balance sheet.

In January 2013, the BCBS released an amendment to the LCR and finalised minimum requirements and implementation dates.

The BCBS released an update on the NSFR in January 2014, proposing a better alignment between the LCR and NSFR. The Group believes that the calibration and alignment has improved the NSFR, however, some concerns remain with respect the treatment of secured funding transactions, such as repos and the application of the calibration to derivative transactions. The Group will continue to participate in the consultative process on the NSFR.

Liquidity coverage ratio

The LCR has been fully adopted by the SARB with the inclusion of a committed liquidity facility and will be phased in from 2015 to 2019. The minimum LCR requirement will be 60% at 1 January 2015, with 10% incremental step ups each year to 100% on 1 January 2019.

In addition to level 1 assets, eligible collateral will include levels 2A and 2B with qualifying criteria and ratings requirements referenced to national scale ratings for liquidity risk in that local currency.

Disclosure requirements

In March 2014 the BCBS published the *Liquidity coverage ratio disclosure standards* proposing consistent and transparent disclosure of banks' liquidity positions as measured by the Basel III regulations. The objective of the document is to reduce market uncertainty around these liquidity positions.

Disclosure is effective from the first reporting date after 1 January 2015 and will form part of the quarterly Pillar 3 disclosures. It is the Group's intention to comply with these requirements from 2015 onwards.

The LCR disclosure standards require banks to provide in a standardised template:

- available sources of liquidity by level of liquidity;
- cash outflows attributed by customer, category type and relationship; and
- cash inflows attributed by source.

Committed liquidity facility

On 2 August 2013, the SARB released *Guidance Note 6 of 2013* which outlines the provision of a committed liquidity facility to assist banks in meeting the LCR. The guidance note confirms that the maximum facility size would initially be set at 40% of high-quality liquid assets. Banks would, therefore, be required to meet the 60% requirement through adjustment to their balance sheets. It is envisaged that, as capital markets develop and the liquid asset shortage is addressed, the SARB will reduce the size of the committed liquidity facility.

The committed liquidity facility remains broadly as defined in *Guidance Note 5 of 2012* but with revisions to acceptable collateral. The SARB has, however, provided a detailed operational notice on the committed liquidity facility as an addendum to *Guidance Note 6 of 2013*.

Eligible collateral for the committed liquidity facility includes but is not limited to:

- listed debt securities (minimum A- national scale credit rating);
- listed equities on the main board of the JSE;
- notes of self-securitised eligible residential mortgages; and
- selection of on-balance sheet ring-fenced assets.

In order to include the committed liquidity facility in banks' available liquidity resources, a considerable amount of work is required to appropriately structure and prepare the bank's assets to access this facility. The collateral requirements include structuring features, eligibility criteria and haircuts designed to protect all counterparties. The committed liquidity facility has provided more clarity on the nature of liquidity transactions under stress and is a step towards reducing systemic risk in the banking sector. The Bank is in the process of applying to the SARB for a committed liquidity facility.

FirstRand is in the process of LCR implementation and expects to comply with the phase-in requirements.

Net Stable Funding Ratio

The latest consultative paper of the BCBS reflects the NSFR as a more structural balance sheet ratio and no longer a one-year stressed balance sheet ratio. The BCBS maintains the principle that a stable funding profile in relation to the composition of a bank's assets and off-balance sheet items promotes a more resilient banking sector. The ratio calculates the amount of available stable funding relative to the amount of required stable funding. The ratio has to at least equal 100%. It is anticipated that the ratio will become a requirement on 1 January 2018, once the calibration has been finalised.

Recovery and resolution regime

Financial Stability Board member countries are required to have recovery and resolution plans in place for all systemically significant financial institutions as per paper *Key Attributes of Effective Resolution Regimes*. The SARB has adopted this requirement and has, as part of the first phase, required the South African domestically significant banking institutions to develop their own recovery plans. Improving the stability of the banking system by strengthening banks' ability to manage themselves through a potentially severe stress situation is of national importance. Guidance issued by the Financial Stability Board and the SARB has been incorporated into the Group's comprehensive recovery plan.

Recovery planning

The purpose of the recovery plan is to document how the board and management of FirstRand including its franchises and key subsidiary, FirstRand Bank, will recover from a severe stress event/scenario that threatened the Group's commercial viability. The recovery plan:

- analyses the potential for severe stress in the Group that causes material disruption to the South African financial system;
- identifies the type of stress event/s that would be necessary to trigger its activation;
- analyses how the Group might potentially be affected by the event/s;
- lists a menu of potential recovery actions available to the board and management to counteract the event/s; and
- assesses how the Group might recover from the event/s as a result of those actions.

The recovery plan forces the Group to perform an extensive self-assessment exercise to determine if there are any potential idiosyncratic vulnerabilities that it may be exposed to, and then to reconcile these exposures to its own risk appetite and strategy. Strategies to optimise the balance sheet structure and preserve the Group's critical functions to support the recovery from severe stress event with the least negative impact are being considered. This process enables banks to better understand what functions are critical for its customers and for the financial system as well as which assets are most marketable to facilitate recovery. Where inefficiencies are identified, these can be amended to make the Bank more streamlined, adaptable and resilient to stress.

Resolution plan

To date the SARB has focused on bedding down the recovery plans for the South African banks, but it is expected that the SARB is likely to issue guidance related to resolution planning for banks before the end of 2014. These resolution plans will allow the SARB to pre-plan for an event from which the Group is unable to recover. It is envisaged that based on global best practice, the resolution plan would be owned and managed by the SARB. This would, however, require individual banks to submit a significant amount of data to the SARB.

LIQUIDITY POSITION

The table below provides details on the sources of liquidity by Basel LCR definition and management assessment.

Bank's composition of liquid assets

	As at 30 June 2014			
		After Basel III haircut		
R billion	**High quality liquid assets**	**Level 1**	**Level 2**	**Management buffer after haircuts**
Cash and deposits with central banks	21	–	–	21
Government bonds and bills*	68	68	–	66
Corporate bonds	4	–	3	3
Other liquid assets	–	–	-	22
Total	**93**	**68**	**3**	**112**

* *SARB-specified haircuts for management buffers.*

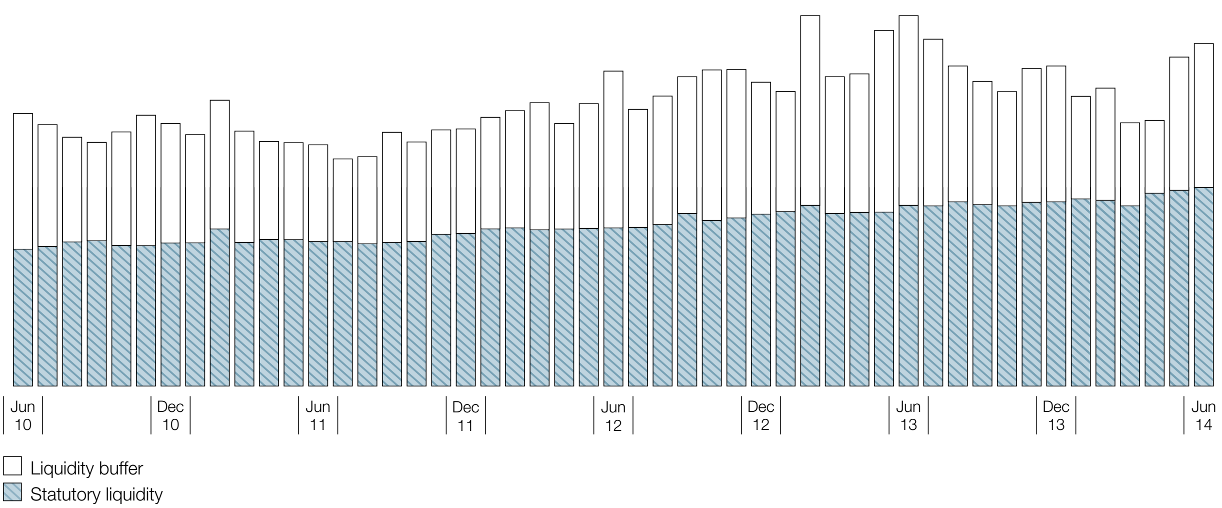
Liquidity buffers are actively managed via high quality, highly-liquid assets that are available as protection against unexpected events or market disruptions. The quantum and composition of the available sources of liquidity are defined by the behavioural funding liquidity at risk and the market liquidity depth of available liquidity resources. In addition, adaptive overlays to the liquidity requirements are derived from stress testing and scenario analysis of the cash inflows and outflows related to business franchise activity.

Funding from institutional clients is the largest contributor to the Group's net cash outflows as measured under the LCR at nearly 40%, and reflects the South African market structure. Other significant contributors to cash outflows are corporate funding and off-balance sheet facilities granted to clients, specifically those related to corporate clients. The Group has strategies in place to increase funding sourced through its deposit franchise and reducing reliance on institutional funding, as well as to offer utilised facilities more efficiently.

The graph below presents a historical view of statutory liquid assets. The Bank has sought to hold buffers in excess of regulatory minimums based on its own risk assessment and operational liquidity requirements, these are also reflected in the chart below.

Bank's liquidity buffer and statutory liquidity requirements*

R million

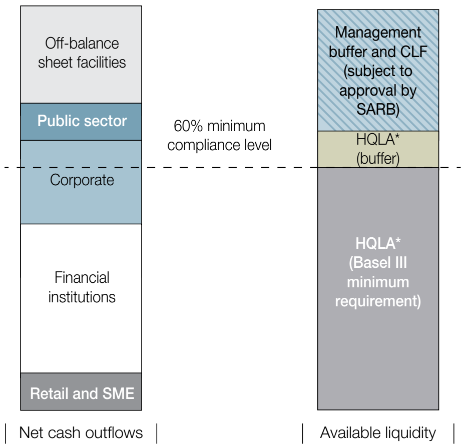


* *Reflects solo supervision, FRB excluding foreign branches.*

The graph below gives an indication of FRB's LCR position as at 30 June 2014 and demonstrates the Bank's compliance with the 60% minimum requirement.

Bank's LCR

%



* *High-quality liquid assets.*

LIQUIDITY RISK PROFILE

Undiscounted cash flow

The following tables present the undiscounted cash flows of liabilities and includes all cash outflows related to principal amounts as well as future payments. These balances will not reconcile to the balance sheet for the following reasons:

- balances are contractual, undiscounted amounts whereas the balance sheet is prepared using discounted amounts;
- the tables include contractual cash flows with respect to items not recognised on the balance sheet;
- all instruments held for trading purposes are included in the call to three-month bucket and not by contractual maturity as trading instruments are typically held for short periods of time; and
- cash flows relating to principal and associated future coupon payments have been included on an undiscounted basis.

Liquidity cash flows (undiscounted cash flows) – maturity analysis of liabilities based on the undiscounted amount of the contractual payment (audited)

	2014			
		Term to maturity		
R million	**Carrying amount**	**Call – 3 months**	**4 – 12 months**	**>12 months**
Liabilities				
Deposits and current accounts	**828 299**	**544 419**	**119 722**	**164 158**
Short trading positions	**5 442**	**5 442**	**–**	**–**
Derivative financial instruments	**41 844**	**39 066**	**796**	**1 982**
Creditors and accruals	**13 553**	**11 390**	**868**	**1 295**
Tier 2 liabilities	**16 969**	**1 829**	**21**	**15 119**
Other liabilities	**7 190**	**733**	**729**	**5 728**
Policyholder liabilities under insurance contracts	**540**	**22**	**21**	**497**
Financial and other guarantees	**40 702**	**37 443**	**1 483**	**1 776**
Operating lease commitments	**2 581**	**240**	**676**	**1 665**
Facilities not drawn	**78 785**	**78 254**	**508**	**23**

Liquidity cash flows (undiscounted cash flows) – maturity analysis of liabilities based on the undiscounted amount of the contractual payment (audited) continued

	2013			
		Term to maturity		
R million	Carrying amount	Call – 3 months	4 – 12 months	>12 months
Liabilities				
Deposits and current accounts	738 915	503 888	100 472	134 555
Short trading positions	2 991	2 991	-	-
Derivative financial instruments	53 166	51 280	508	1 378
Creditors and accruals	11 264	9 943	767	554
Tier 2 liabilities	11 494	151	556	10 787
Other liabilities	6 524	2 655	957	2 912
Policyholder liabilities under insurance contracts	646	19	19	608
Financial and other guarantees	39 332	35 003	2 295	2 034
Operating lease commitments	2 514	226	580	1 708
Facilities not drawn	78 783	59 165	4 348	15 270

Contractual discounted cash flow analysis

The following tables represent the contractual discounted cash flows of assets, liabilities and equity for the Group. Relying solely on the contractual liquidity mismatch when assessing a bank's maturity analysis would overstate risk, since this represents an absolute worst case assessment of cash flows at maturity.

Due to South Africa's structural liquidity position, banks tend to have a particularly pronounced negative (contractual) gap in the shorter term due to short-term institutional funds representing a significant proportion of banks' liabilities. These are used to fund long-term assets, e.g. mortgages.

Therefore, in addition to the analysis in the previous tables, the Group carries out an adjusted liquidity mismatch analysis, which estimates the size of the asset and liability mismatch under normal business conditions. This analysis is also used to manage this mismatch on an ongoing basis.

Contractual discounted cash flow analysis – maturity analysis of assets and liabilities based on the present value of the expected payment (audited)

	2014			
		Term to maturity		
R million	**Carrying amount**	**Call – 3 months**	**4 – 12 months**	**>12 months**
Total assets	**945 535**	**326 101**	**84 541**	**534 893**
Total equity and liabilities	**945 535**	**605 756**	**118 734**	**221 045**
Net liquidity gap	**–**	**(279 655)**	**(34 193)**	**313 848**
Cumulative liquidity gap	**–**	**(279 655)**	**(313 848)**	**–**

	2013			
		Term to maturity		
R million	**Carrying amount**	**Call – 3 months**	**4 – 12 months**	**>12 months**
Total assets	865 732	309 188	99 185	457 359
Total equity and liabilities	865 732	571 796	98 272	195 664
Net liquidity gap	–	(262 608)	913	261 695
Cumulative liquidity gap	–	(262 608)	(261 695)	–

As illustrated in the table above, the negative contractual liquidity short-term gap increased slightly in the short end on a cumulative basis. This is aligned to the funding strategy to grow the deposit franchise via transactional deposit accounts. Management continues to align stress funding buffers both locally and offshore, taking into account prevailing economic and market conditions.

OPERATIONAL RISK

INTRODUCTION AND OBJECTIVES

The Group believes that effective management of operational risk is key to the achievement of its business strategy. Accordingly, there is ongoing evaluation and enhancement of existing frameworks, policies, methodologies, processes, standards, systems and infrastructure to ensure that the operational risk management practices are practical and in line with regulatory developments and emerging best practices.

The focus for the year ahead remains on building an effective and forward-looking operational risk management programme, encompassing, amongst other things, the management and oversight of IT, infrastructure and information risks, internal and external fraud, litigation, business disruption and process risk. The key operational risk strategic objectives are:

- embedding the use of automated risk tool outputs for an integrated view of the operational risk profile;
- embedding and refining operational risk appetite limits at various levels in the Group;
- ongoing enhancement of the maturity of the AMA components and methodologies;
- facilitating greater use of risk information and analysis outcomes in risk management and strategic decision making;
- continuing improvements to the control environment;
- assessing operational risk-related regulatory developments and putting in place necessary actions for compliance;
- maintaining the AMA status; and
- implementing a new AMA capital modelling software and updating the AMA capital modelling methodology.

Year under review

The year under review was characterised by a number of initiatives aimed at addressing key operational risk themes identified as part of the risk identification and assessment process and improving operational risk maturity. The progress on these initiatives is tracked and reported at Group level through the risk governance process.

The principal operational risks currently facing the Group are:

- commercial and violent crime (including internal fraud) as economic growth slows;
- information security risk (risk of loss or theft of information), given the growing sophistication of cyberattacks globally; and
- execution, delivery and process management risk (the risk of process weaknesses and control deficiencies) as the business continues to grow and evolve.

Process automation projects have been initiated to reduce manual processes and thereby mitigate associated risks and improve efficiencies.

The Group's operational risk management and measurement tools have been successfully automated onto a single platform (risk management system) facilitating easy access to risk information and an integrated view of the business's operational risk profile based on the risk tool outputs. An exercise to improve the quality of risk tool data was undertaken prior to migration of all the risk tools onto the single risk management system. Enhancements were implemented on the risk management system to manage risk data quality on an ongoing basis and to improve efficiency in the internal validation of the risk tools.

The process-based risk and control self-assessment (PRCIA) methodology that aims to assess risk and controls on an end-to-end process basis has been implemented for all high-risk areas across the Group. Rollout of PRCIA is underway for offshore operations and new and medium/low risk areas. Further work is ongoing to refine PRCIA implementation coverage. A review of key risk indicators (KRIs) was conducted across the Group to improve the quality and value of KRIs tracked.

Operational risk appetite setting enables the Group and its franchises to measure and monitor operational risk profiles against approved operational risk appetite levels, and to set the boundaries for operational risk within which business decisions can be made. Operational risk appetite at Group and franchise level was reviewed during the year. Further enhancements to operational risk appetite are ongoing.

Cybercrime was an area of focus during the year, as this is perceived to be the dominant future threat in the financial services sector globally. Risk mitigation strategies to combat cybercrime are being reviewed to ensure that controls implemented are adequate and effective.

The Group upgraded power supply, management equipment and infrastructure for key facilities. A third redundant data centre is being implemented to improve the Group's business resilience capability. The Group's IT risk and governance functions have been integrated within ERM, with relevant governance forums in place to ensure continued monitoring and mitigation of IT risk across the Group. The Group's IT and related frameworks are being reviewed to ensure alignment with changing business models and the technology landscape.

Information, whether the Group's or that entrusted to it by customers, staff or business partners, is a valuable asset and the management of information remains integral to the way the Group operates. To this end, an information governance framework was developed to ensure that information is managed in accordance with its value, sensitivity and the risks to which it is exposed.

The refinement of information governance structures, processes and the improvement of data quality and records management practices was undertaken during the year. Information governance committees have been established in all franchises and information governance now forms an integral part of the overall risk management framework of the Group.

Looking ahead, the Group will continue to focus on improving its information management capabilities by embedding governance structures, continuous improvement of the information control environment and rolling out awareness programmes on relevant topics including records management, data quality and data privacy management.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

The board has delegated its approval and review authority for operational risk to the operational risk committee. The operational risk committee is responsible for monitoring implementation of the operational risk management framework and oversight over the management of operational risk across the Group.

The operational risk management framework prescribes the authorities, governance and monitoring structures, duties and responsibilities, processes, methodologies and standards which have to be implemented and adhered to when managing operational risk.

Within operational risk, a number of key risks exist for which specialised teams, frameworks, policies, standards and processes have been established. Fraud and physical security, business resilience, legal, information governance and information technology have dedicated specialist teams who provide oversight that is integrated into the broader operational risk management and governance processes. The central operational risk management team in ERM is responsible for embedding the operational risk governance structure across the Group.

MEASUREMENT OF OPERATIONAL RISK

Basel – advanced measurement approach (AMA)

FirstRand applies AMA for the Group's domestic operations. Under AMA, FirstRand uses a sophisticated statistical model for the calculation of capital requirements, which enables more accurate risk-based measures of capital for all business units. Operational risk scenarios (covering key risks that, although low in probability, may result in severe losses) and internal loss data are inputs into this model.

Scenarios are derived through an extensive analysis of the Group's operational risks in consultation with business and risk experts from the respective business areas. Scenarios are cross referenced to external loss data, internal losses, key risk indicators, risk and control self-assessments and other pertinent information about relevant risk exposures. To ensure ongoing accuracy of risk and capital assessments, all scenarios are reviewed, supplemented or updated semi-annually, as appropriate.

The loss data used for risk measurement, management and capital calculation is collected for all seven Basel event types across various internal business lines. Data collection is the responsibility of the respective business units and is overseen by the operational risk management team in ERM.

The modelled operational risk scenarios are combined with modelled loss data in a simulation model to derive the annual, aggregate distribution of operational risk losses. Basel Pillar 1 minimum capital requirements are then calculated (for the Group and each franchise) as the operational VaR at the 99.9th percentile of the aggregate loss distribution, excluding the effects of insurance, expected losses and correlation/diversification.

Capital requirements are calculated for each franchise using the AMA capital model and then allocated to the legal entities within the Group based on gross income contribution ratios. This split of capital between legal entities is required for internal capital allocation, regulatory reporting and performance measurement purposes.

TSA and BIA capital calculations are based on a multiplication factor applied to gross income, as specified by Basel and SARB regulations. No risk-based information is used in these capital calculations or allocation. Business practices continuously evolve and the operational risk control environment is, therefore, constantly changing. The assessment of the operational risk profile and exposures and associated capital requirements take the following into account:

- changes in the operational risk profile, as measured by the various operational risk tools;
- material effects of expansion into new markets, new or substantially changed products or activities as well as the closure of existing operations;
- changes in the control environment – a continuous improvement in the control environment is targeted, but deterioration in effectiveness is also possible due to, for example, unforeseen increases in transaction volumes; and
- changes in the external environment, which drives certain types of operational risk.

ASSESSMENT AND MANAGEMENT

Operational risk assessment and management tools

The Group obtains assurance that the principles and standards in the operational risk management framework are being adhered to by the three lines of control model integrated in operational risk management. In this model, business units own the operational risk profile as the first line of control. In the second line of control, ERM is responsible for consolidated operational risk reporting, policy ownership and facilitation and coordination of operational risk management and governance processes. GIA, as the third line of control, provides independent assurance of the adequacy and effectiveness of operational risk management processes and practices.

In line with international best practice, a variety of tools are employed and embedded in the assessment and management of operational risk. The most relevant of these are outlined in the following chart.

Operational risk assessment and management tools

Risk control self assessments and process-based risk and control identification and assessments	**Key risk indicators**
• integrated in the day-to-day business and risk management processes; • used by business and risk managers to identify and monitor key risk areas and assess the effectiveness of existing controls; and • process-based risk and control identification and assessment (currently being rolled out) is the risk and control assessment per product/service based on key business processes.	• used across the Group in all businesses as early warning measures; • highlight areas of changing trends in exposures to specific key operational risks; and • inform operational risk profiles which are periodically reported to the appropriate management and risk committees and are monitored on a continuous basis.
Internal/external loss data	**Risk scenarios**
• the capturing of internal loss data is well entrenched within the Group; • internal loss data reporting and analyses occur at all levels with specific focus on the root cause and process analysis and corrective action; and • external loss databases are used to learn from the loss experience of other organisations and as an input to the risk scenario process.	• widely used to identify and quantify low frequency extreme loss events; • senior executives of the business actively participate in the biannual reviews; and • results are tabled at the appropriate risk committees and are used as input to the capital modelling process.

As process-based risk and control identification and assessments are rolled out across the Group, these will replace risk control self-assessments to ensure a comprehensive assessment of risks and controls across end-to-end business processes.

FirstRand uses an integrated and reputable operational risk system which provides a solid platform for automation of all operational risk tools. The automation and integration of all the operational risk tools on the operational risk system is near completion.

Operational risk events

As operational risk cannot be avoided or mitigated entirely, frequent events resulting in small losses are expected as part of business operations (for example, external fraud) and are appropriately budgeted for. Business areas minimise these losses through continuously monitoring and improving relevant business and control practices and processes. Operational risk events resulting in substantial losses occur much less frequently and the Group strives to minimise these and contain frequency and severity within risk appetite levels.

Operational risk management processes

A number of key risks exist for which specialised teams, frameworks, policies and processes have been established and integrated into the broader operational risk management and governance processes as described below for major operational risks.

Business resilience management

Business resilience management focuses on ensuring that the Group's operations are resilient to the risk of severe disruptions caused by internal failures or external events. The business resilience steering committee, a subcommittee of the operational risk committee, has oversight of business resilience management.

Business resilience practices are documented in the Group's business resilience policy and supporting standards, which are approved at the operational risk committee. The policy, a subframework of the operational risk management framework, requires the development and maintenance of business continuity strategies and plans. It also requires regular business continuity assessments and testing to be carried out in all business units and for the results to be reported to the business resilience steering committee.

The Group carries out regular reviews of business resilience management practices and any disruptions or incidents are assessed and regularly reported to the relevant risk committees.

Legal risk

The legal risk management framework, a subframework of the operational risk management framework, addresses areas such as the creation and ongoing management of contractual relationships, management of disputes (which do or might lead to litigation), protection and enforcement of property rights (including intellectual property) and failure to account for the impact of the law or changes in the law brought about by legislation or decisions by the courts. Whilst compliance with legislation is a major element of legal risk, RRM manages this aspect. Added to these substantive and direct risks is the management of risk around the procurement of external legal resources.

A legal risk management programme is in place to ensure that comprehensive, sound operational risk governance practices and solutions are adopted in respect of legal risk management, which represents best practice and aligns to the Group's overall risk management programme. Key legal processes and control measures were implemented to support business in assessing and addressing legal risks. The legal risk committee, a subcommittee of the operational risk committee, has oversight of legal risk management.

IT risks and information governance

Information risk is concerned with the quality and protection of information and information systems against unauthorised access, destruction, modification, use and disclosure. The goal of these functions is to ensure confidentiality, availability and integrity of all information and systems that maintain, process and disseminate this information. To this end, a distinction is made between:

- IT risk management and governance (protection of systems); and
- information governance (accountability for and quality of information).

The Group's IT risk management framework, information governance framework, acceptable use of information resources policy, information security policy and other supporting policies provide the basis for the management of IT risk, information security and data quality within the Group.

The IT risk management framework defines the objectives of IT risk management and processes that are to be embedded, managed and monitored across the Group for effective management of IT risk.

The information governance framework stipulates key requirements with respect to the management of information across the Group to ensure that FirstRand data, information and records are maintained at a level of integrity and quality sufficient to ensure regulatory compliance and effective operation of business.

Fraud and security risks

Fraud risk is defined as the risk of loss resulting from unlawfully making, with intent to defraud, misrepresentation which causes actual prejudice or which is potentially prejudicial to another. Fraud incorporates both internal (staff) criminal activities as well as those that emanate from an external source.

Fraud risk is governed by the fraud risk management framework, which is a subframework of the operational risk management framework. The Group utilises a deployed fraud risk management model that requires businesses to institute processes and controls specific and appropriate to operations within the constraints of a consistent governance framework. This is overseen by the fraud risk management function reporting to the FNB CRO with a Group mandate.

The Group is committed to creating an environment that safeguards customers, staff and assets against fraud or security risks by continually investing in people, systems and processes for both preventative and detective measures.

External fraud losses related to commercial and violent crime maintained similar or decreasing trends as improvement in controls were introduced. These include deployment of chip cards, improvement in user authentication processes and enhancements to detection capabilities at a transaction level. Employee (internal) fraud threats remain a primary concern given the risk of collusion with syndicates, and employee knowledge of controls. Additional tools and resources will continue to be invested against the growing threat of cybercrime. There is an increased focus on operational processes for fraud to align views on potential money laundering threats with anti-money laundering regulations.

Risk insurance

The Group has a structured insurance risk financing programme in place, which has been developed over many years, to protect the Group against unexpected material losses arising from non-trading risks. The insurance risk programme is continuously refined through ongoing assessment of changing risk profiles, organisational strategy and growth, and monitoring of international insurance markets. The levels and extent of insurance cover is reviewed and benchmarked annually.

The Group's insurance-buying philosophy is to self-insure as much as is economically viable and to only protect itself against catastrophic risks through the use of third-party insurance providers. Accordingly, the majority of cover is placed with the Group's wholly-owned first-party dedicated insurance company, FirstRand Insurance Services Company Limited (FRISCOL). All cover on the main programme is placed with reinsurers that have a minimum credit rating of A-. The insurance programme includes, *inter alia*, cover for operational risk exposures such as professional indemnity, directors' and officers' liability, crime bond, public and general liability, etc. The Group, however, does not consider insurance as a mitigant in the calculation of capital for operational risk purposes.

REGULATORY RISK

INTRODUCTION AND OBJECTIVES

The Group's RRM function plays an integral part in managing risks inherent in banking. The Group fosters a compliance culture in its operations that contributes to the overall objective of prudent regulatory compliance and risk management, by observing both the spirit and the letter of the law in its business activities. The compliance culture also embraces broader standards of integrity and ethical conduct which concern all employees.

The objective of the RRM function is to ensure that business practices, policies, frameworks and approaches across the organisation are consistent with applicable laws and that regulatory risks are identified and managed proactively throughout the Group. This culminates in the maintenance of an effective and efficient regulatory risk management framework with sufficient operational capacity to promote and oversee compliance with legislative and best practice requirements. In order to achieve the Group's regulatory risk management objectives, staff members are trained and made aware of compliance requirements in order to ensure a high level of understanding and awareness of the applicable regulatory framework.

Non-compliance may potentially have serious consequences, which could lead to both civil and criminal liability, including penalties, claims for loss and damages or restrictions imposed by regulatory authorities. It is, therefore, important that the Group ensures compliance with laws and regulations applicable to its operations. These include, among others, the provisions of the Banks Act, 1990, the Regulations relating to Banks, the Financial Intelligence Centre Act, 2001, the Financial Advisory and Intermediary Services Act, 2002 and the Consumer Protection Act, 2008. All compliance issues identified in this context should be effectively and expeditiously resolved by senior management with the assistance of RRM. This requires close cooperation with and interaction between RRM, other Group functions and various regulatory authorities.

The year under review

Banking legislation

Subsequent to the implementation of the Basel III *Regulations relating to Banks,* which became effective on 1 January 2013, the Banks Act, 1990 was also amended through the Banks Amendment Act, 2013, which came into effect on 10 December 2013. The said amendments serve to amend, among others, banking legislation in line with BCBS requirements. Ongoing amendments to the Regulations are expected to ensure that the South African regulatory framework for banks remains aligned to internationally-agreed regulatory and supervisory standards.

Twin peaks

The most notable development and focus area of current regulatory reforms is the anticipated implementation of a twin peaks model of financial regulation in South Africa. In terms of the broad policy objectives, it is expected that these reforms will be implemented in two phases, along with the development of legislation necessary to enable the relevant regulators to deliver on their revised mandates. The Group will continue to foster close interaction and cooperation with regulators and other stakeholders in this regard.

The Group's ethics framework

The Group's ethics office is part of RRM and is responsible for an ethics framework. Several culture- and people-risk assessments were conducted, some of which resulted in strategic and operational changes in certain areas and the proactive identification and management of several risk types. The focus on promotion of responsible business conduct was maintained and included training on whistle-blowing, conflict of interest avoidance, anti-bribery and corruption. Another focus area is the promotion of responsible market conduct and ensuring that the Group remains compliant with market conduct regulations and related industry best practice. These developments specifically pertain to treating customers fairly in the context of the proposed twin peaks model of financial regulation in South Africa. Further enhancements to the Group's responsible competitive practice programme are expected to mitigate related risks.

Anti-money laundering and combating terrorist financing (AML/CFT) measures

Banking groups in South Africa have to ensure compliance with national and international regulations and counter-measures to combat money laundering and terrorist financing as prescribed and/or recommended by the Financial Intelligence Centre Act (FICA), 2001, the Financial Action Task Force (FATF) and the BCBS. The BCBS guidelines issued in January 2014 describe how banks should manage AML/CFT risks within overall risk management programmes. The BCBS supports the adoption and implementation of the FATF standards and the Group's objective remains to ensure compliance with these requirements. In terms of a recent consultation paper issued by the Financial Intelligence Centre, FICA will, going forward, be amended in order to align more closely with revised FATF recommendations such as that applicable to the risk-based approach.

Protection of Personal Information Act, 2013 (PoPI)

PoPI was signed into law in December 2013, with the effective date of compliance to be proclaimed. PoPI is applicable to all personal information held by the Group in respect of employees, customers and suppliers. The Group continues to devote substantial attention and resources to aspects such as security safeguards, processing and purpose specification of personal information, quality of personal information held, customer notification and consent, third party processors of personal information and complaints handling, in line with PoPI requirements.

Carbon disclosure project (CDP)

FirstRand participates in the annual carbon disclosure project (CDP) where the top 100 listed companies are invited to disclose their performance and leadership initiatives in carbon management. In 2013, in the South African JSE top 100 sample, FirstRand was one of the top eight companies in the South African Performance Leadership Index, continuing a trend of leadership that it has established in the last few years.

The Group is committed to the measurement and management of FirstRand's ecological footprint. This proactive approach will position the Group to meet expected carbon reporting requirements which will come into effect in 2016. The Group's commitment to good corporate citizenship and environmental sustainability aligns with the overall climate change policy and strategy of South Africa.

ORGANISATIONAL STRUCTURE AND GOVERNANCE

Responsibility for compliance with all relevant laws, related internal policies, regulations and supervisory requirements are delegated by the board to senior management and RRM. In order to assist board members in making informed judgements on whether the Group is managing its regulatory and compliance risks effectively, the head of RRM has overall responsibility for coordinating the management of the Group's regulatory risk. This includes monitoring, assessing and reporting on the level of compliance to senior management and the board. RRM complies with the prescribed requirements in terms of regulation 49 of the Regulations and its mandate is formalised in the Group's compliance risk management framework.

Governance oversight of the RRM function is conducted by a number of committees such as the RRM, RCC and audit committees, all of which receive regular detailed reports from RRM on the level of compliance and instances of material non-compliance. In addition to the centralised RRM function, each operating franchise has a dedicated compliance officer responsible for implementing and monitoring compliance policies and procedures related to the relevant franchise.

FirstRand has a formal social and ethics committee, which exercises oversight over the governance and functioning of the Group-wide ethics programme. The FirstRand Group code of ethics is the cornerstone of FirstRand's ethics management framework. RRM retains an independent reporting line to the Group CEO as well as to the board through its designated committees.

ASSESSMENT AND MANAGEMENT

RRM's board mandate is to ensure full compliance with statutes and regulations. To achieve this, RRM has implemented appropriate structures, policies, processes and procedures to identify regulatory and supervisory risks. RRM monitors the management of these risks and reports on the level of compliance risk management to both the board and the Registrar of Banks. These include:

- risk identification through documenting which laws, regulations and supervisory requirements are applicable to FirstRand;
- risk measurement through the development of risk management plans;
- risk monitoring and review of remedial actions;
- risk reporting; and
- providing advice on compliance-related matters.

Although independent of other risk management and governance functions, the RRM function works closely with GIA, ERM, external audit, internal and external legal advisors, and the company secretary's office to ensure effective functioning of compliance processes.

Public policy and regulatory affairs office

The Group's Public Policy and Regulatory Affairs Office provides the Group with a central point of engagement, representation and coordination in respect of relevant regulatory and public policy-related matters at strategic level. This function is differentiated from the existing and continuing engagement with regulators at an operational level, i.e. regulatory reporting, compliance and audit, with its main objective to ensure that Group executives and franchises are aware of key developments relating to public policy, legislation and regulation, which are considered pertinent to the Group's business activities and to support executives in developing the Group's position on issues pertaining to government policy, proposed and existing legislation and regulation.

This office reports directly to the Group CEO and indirectly, through designated subcommittees, to the board and maintains close working relationships with RRM, ERM and the business units where technical expertise reside.

REMUNERATION AND COMPENSATION

FirstRand's compensation policies and practices observe international best practice and comply with the requirements of the Banks Act, 1990 (Act No. 94 of 1990) and FSB Principles for Sound Compensation Practices. In accordance with the requirements of regulation 43 of the revised Regulations, full disclosure of the Group's compensation policies, practices and performance are included in the remuneration committee report in its annual integrated report, which is published on FirstRand's website, www.firstrand.co.za.