FirstRand

MATERIAL RISK FACTOR DISCLOSURE **2020**

as required in terms of Paragraph 7.F.7 of the JSE Listings Requirements

Risk relating to FirstRand Limited (the issuer)

1. THE INVESTMENTS, BUSINESS, PROFITABILITY AND RESULTS OF OPERATIONS OF THE ISSUER MAY BE ADVERSELY AFFECTED AS A RESULT OF POLITICAL, SOCIAL AND ECONOMIC RISKS IN SOUTH AFRICA, THE UK, CERTAIN COUNTRIES IN SUB-SAHARAN AFRICA AND GENERAL GLOBAL ECONOMIC CONDITIONS

The issuer's operations are predominantly concentrated in South Africa, with the majority of its revenues derived from operations in South Africa. The issuer is, therefore, highly exposed to South African macroeconomic conditions and, as a result of their impact on the South African economy, global economic conditions. Any material deterioration in global or South African macroeconomic conditions could lead to a reduction in business activity, higher impairment charges, increased funding costs, reduced revenues and profitability.

Beyond the South African economy, the issuer also has operations in the United Kingdom (UK) and several other countries in sub-Saharan Africa. A material deterioration in UK economic conditions or that of the other African countries it operates in could also have a meaningful negative impact on the issuer's performance.

1.1 Global economic conditions

The South African economy is exposed to the global economy through the current and capital accounts of the balance of payments. South Africa's exports are impacted by economic activity of some of the world's largest economies including China, the United States (US), the UK and Europe. Commodity prices and the rand exchange rate also have a material impact on South African exports. The South African economy is also reliant on foreign capital inflows.

If global economic growth or global financial conditions deteriorate materially, it is likely to have a negative impact on macroeconomic conditions in South Africa.

While the global economy is recovering from COVID-19-related contraction, the longer-term consequences to the macroeconomy remains uncertain. In addition to concerns around permanent damage to production capacity, there are also concerns about the potential for a second wave of COVID-19 outbreaks and the negative consequences for global economic activity. A fall in global production capacity will have a negative impact on South African economic activity through lower exports and higher import prices. It could also have negative consequences for capital flows towards South Africa. A severe resurgence in COVID-19 will weigh on global risk appetite, capital flows to South Africa and will likely result in financial market pressure and rand weakness.

Looking beyond risks to the global recovery, permanent global trade impediments (including tariffs), social tensions, natural disasters and environmental damage represent risk factors that could permanently derail global demand for South African goods and global risk appetite towards South Africa.

In addition, a further fall in precious metal and/or base metal prices could also result in a deterioration in the value of the rand, higher interest rates and bond yields.

1.2 South African economic conditions

Even before the COVID-19 crisis, the South African macroeconomic environment was characterised by low private sector investment growth, weak employment growth, high levels of public sector debt and downward pressure on domestic demand. In addition, domestic consumer and business confidence was low. Despite a bounce back in activity from the depths of the COVID-related contraction, the issuer expects the longer-term trends to remain in place.

Structural changes, including financial and business reforms at state-owned enterprises, an improvement in the quality of education, much higher fixed capital investment and labour market reforms are now more critical to change the long-term trajectory of the country. The solvency and liquidity challenges at some state-owned enterprises remain a significant concern.

1.3 South African political conditions

The issuer currently anticipates there will be strong political debates around the need to implement measures to ensure fiscal sustainability. These will include debates around implementation of measures that will lift South Africa's potential growth rate. In addition, the issuer expects debates in respect of various sensitive issues such as land expropriation and the mandate of the South African Reserve Bank (SARB) which has become a hallmark of the South African political landscape. The impact of COVID-19 on employment and poverty will likely fuel further debate on transfers (either through taxes or intertemporally through borrowing) to the vulnerable in the South African society. Ongoing political developments may impact private sector investment, foreign investment and business confidence towards South Africa.

The high unemployment rate and unequal wealth and income distribution may fuel socio-economic pressure and encourage government to change its current macroeconomic policies.

1.4 South African conditions specific to the banking sector

The South African banking sector remains well capitalised, funded, regulated and managed. The South African financial sector is widely regarded as one of the country's key pillars of economic strength. The banking sector is, however, highly exposed to South African macroeconomic conditions including the sovereign and will be impacted by negative macroeconomic developments and a deterioration in the government's fiscal position.

Although household and corporate affordability conditions are currently benefiting from low inflation and low interest rates, weak economic growth and increased unemployment have pushed household and corporate income growth towards decade lows. A deterioration in the country's institutions, especially the independence of the SARB and policy conduct at National Treasury, can also have a negative impact on the banking sector.

The issuer's financial performance has been and is likely to remain linked to the performance of the South African and global economy.

1.5 United Kingdom economic conditions

Economic activity in the UK is also recovering from the COVID-19-related hit. That said, the issuer expects unemployment to increase soon as policy support starts to unwind. Higher unemployment and related risk to household disposable income could have negative consequences to the operating environment.

Other risks to the UK economy include:

- Significant uncertainty around the UK's future relationship with the European Union (BREXIT). Risks that the UK and the European Union could fail to reach an agreement on their future trade relationship has increased. Failure could result in a sharp slowdown in UK business and consumer confidence, the pound and overall economic activity.
- A reversal in the policy support that was put in place to cushion households and businesses in the face of the COVID-19 growth slowdown.

1.6 Economic conditions in the rest of Africa

Several other countries that the issuer operates in on the sub-Saharan Africa continent faces macroeconomic risks that could have a negative impact on the issuer's operating environment. These include (listed per country):

- Zambia: Significant risk to sovereign debt sustainability and associated macroeconomic pressure. Volatility in the copper prices, drought and uncertainty around the policy environment adds to the heightened risk associated with the Zambian macroeconomic outlook.
- Nigeria: Weak global growth and low oil prices pose downside risk to the outlook for the exchange rate and the fiscus. This, along with policy uncertainty, poses downside risks to the growth outlook.
- Ghana: The Ghanaian economy is exposed to fluctuations in oil, gold and cocoa prices. A fall in these commodities will have negative consequences to the operating environment. The Ghanaian economy is also exposed to fiscal risks.
- Namibia, Eswatini and Lesotho: These economies are particularly exposed to the South African economy and the rand. A severe fall in South African growth, trade and/or rand weakness will have adverse consequences for their outlooks. In addition, the Eswatini government faces fiscal challenges while fiscal risks in Namibia are also increasing.
- Botswana: A significant fall in diamond prices and/or activity in the South African economy will have adverse consequences for the Botswana operating environment.
- Mozambique: High levels of policy uncertainty, commodity prices and global economic activity poses risk to the Mozambican outlook. Insurgent activity in Northern Mozambique is another risk factor to the operating environment.

2. RISK MANAGEMENT

The issuer, in common with other issuers in South Africa and elsewhere, is exposed to commercial and market risks in its ordinary course of business, the most significant of which are credit risk, market risk in the trading book, operational risk, equity investment risk and insurance risk.

Credit risk is the risk of loss due to 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.

Counterparty credit risk is the risk of a counterparty to a contract, transaction or agreement defaulting prior to the final settlement of the transaction's cash flows. Counterparty credit risk measures a counterparty's ability to satisfy its obligations under a contract that has positive economic value to the group 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 issuer or the client.

The issuer distinguishes between traded market risk and non-traded market risk. Traded market risk is the risk of adverse revaluation of any financial instrument as a consequence of changes in market prices or rates. For non-traded market risk, the issuer distinguishes between interest rate risk in the banking book (IRRBB) and structural foreign exchange risk. IRRBB relates to the sensitivity of a bank's financial position and earnings to unexpected, adverse movements in interest rates. Foreign exchange risk is the risk of an adverse impact on a bank's financial position or earnings or other key ratios as a result of movements in foreign exchange rates impacting balance sheet exposures.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

Equity investment risk is the risk of an adverse change in the fair value of an investment in a listed or unlisted company, fund or bespoke financial instrument.

Insurance risk arises from the inherent uncertainties of liabilities payable under an insurance contract. These uncertainties can result in the occurrence, amount, or timing of the liabilities differing from expectations. Insurance risk can arise throughout the product cycle and is related to product design, pricing, underwriting or claims management.

Any failure to control these risks adequately or unexpected developments in the future economic environment could have an adverse effect on the financial condition and reputation of the issuer.

2.1 Credit risk

Credit risk arises primarily from advances and certain debt investment securities. Other sources of credit risk include reinsurance assets, cash and cash equivalents, accounts receivable, off-balance sheet exposures and derivative balances.

The issuer's lending and trading businesses are subject to inherent risks relating to the credit quality of its counterparties and the recoverability of loans and advances due from these counterparties. Changes in the credit quality of the issuer's lending and trading counterparties or arising from systemic risk in the financial sector could reduce the value of the issuer's assets, resulting in increased credit impairments.

Many factors affect the ability of the issuer's clients to repay their loans, including adverse changes in consumer confidence levels due to local, national and global factors, levels of consumer spending, bankruptcy rates, and increased market volatility. These factors might be difficult to predict and are completely outside of the issuer's control. The issuer performs regular stress tests on its credit portfolios to identify the key factors impacting the credit risk profile, to anticipate possible future outcomes, and to implement necessary actions to constrain risk.

The issuer continues to apply origination strategies which are aligned to its broader financial resource management processes and macroeconomic outlook. Based on the issuer's credit risk appetite, as measured on ROE, NIACC and volatility-of-earnings basis, credit risk management principles include holding the appropriate level of capital 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 risk appetite, credit origination strategy, risk quantification and measurement, as well as collection and recovery of delinquent accounts. Credit risk is managed through the implementation of comprehensive policies, processes and controls to ensure a sound credit risk management environment with appropriate credit granting, administration, measurement, monitoring and reporting of credit risk exposure. Credit risk appetite measures are set in line with overall risk appetite. The aim is to deliver an earnings profile that will perform within acceptable levels of volatility determined by the issuer's overall risk appetite.

Within South Africa, persistent political and policy uncertainty, ongoing governance issues at state-owned enterprises and continued erosion of confidence in institutional strength and independence all continue to have a negative impact on confidence, which in turn constrains private sector investment, places pressure on employment and ultimately undermines gross domestic product (GDP) growth. Such a macroeconomic environment will be characterised by low domestic demand growth (consumption, investment and government spending), downward pressure on personal income and further rating downgrades. This could result in increased levels of impairment in the issuer's South African credit portfolio and have an adverse impact on the issuer's ability to grow its revenues as well as credit impairments and, therefore, on its financial condition.

The impact of COVID-19 on the economy and on companies and individuals is expected to increase the credit risk in advances and investment securities. The Prudential Authority (PA) issued *Directive 3 of 2020, Matters related to the treatment of restructured credit exposures due to the Coronavirus (COVID-19) pandemic,* where government and business have called upon the banking sector to continue to extend credit to sectors in need, particularly households and small businesses, and to provide relief measures to reduce the strain on these sectors in an effort to sustain the local economy and maintain financial stability. The PA is supportive of the COVID-19 relief initiatives, such as payment holidays being offered by banks in order to provide relief to certain borrowers in the retail sector in an effort to mitigate the impact of the pandemic. The PA is also cognisant of the possible effect of the pandemic on the corporate sector. The PA has, therefore, decided to amend the requirements specified in *Directive 7 of 2015* to provide temporary relief on the minimum capital requirements for banks, controlling companies and branches of foreign institutions relating to credit risk during this time.

2.2 Concentration risk

Credit concentration risk is the risk of loss 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.

The issuer's business is significantly focused on the South African market and, the issuer, therefore, faces a geographic concentration risk. Operations in South Africa are subject to various risks which include political, social and economic risks, such as general economic volatility, low growth, relatively high inflation, exchange rate risks, exchange controls, crime and diseases (including, for example, HIV/AIDS). The existence of such factors may have a negative impact on South African economic conditions generally, and more specifically on the business and results of the issuer in ways that cannot be predicted.

Any adverse changes affecting the South African economy are likely to have an adverse impact on the issuer's ability to grow revenues as well as credit impairments and, therefore, on its financial condition.

2.3 Liquidity risk

Structural characteristics impacting the funding profile of South African banks

South Africa is an emerging market with significant socio-economic challenges. These include high levels of poverty and social security needs. Addressing these challenges require a high level of funding which constrains domestic savings and results in low household savings rates.

In addition to a low domestic savings rate, South Africa's financial system is characterised by structural features which pose additional liquidity challenges for the domestic banking system. A key characteristic is the fact that the available savings in the economy are mostly contractual savings and funded pension liabilities. These savings are concentrated in institutions such as pension and provident funds as well as providers of asset management services. In addition, they tend to have a higher allocation to the equities market relative to fixed income assets (relative to developed market norms) and are invested at banks in the form of institutional funding, comprising wholesale funding from financial institutions across a range of deposits, loans and other financial instruments.

Furthermore, the operational liquidity management needs of institutions are largely met by their investments into the banking sector via the money market. These institutional deposits have a higher liquidity risk than retail deposits.

Given the relative reliance on institutional deposits, liquidity risk in the South African banking system is structurally higher than in most other markets.

However, this risk is to some extent mitigated by the following market dynamics:

- the "closed rand" system, whereby all rand transactions (whether physical or derivative) must be cleared and settled in South Africa through registered banks and clearing institutions domiciled in South Africa. FirstRand Bank Limited is one of the major clearing/settlement banks;
- the institutional funding base is stable as it is, in effect, recycled contractual retail savings;
- the country has a prudential exchange control framework in place; and
- relative to emerging market peers, South African banks have a low dependence on foreign currency funding (i.e. low foreign currency roll-over risk).

These factors contributed to South Africa's resilience during the 2007 – 2008 global financial crisis. While COVID-19 initially resulted in liquidity stress for financial market participants, as many funds shortened their duration to remain liquid and meet margin calls as well as client requirements, these effects, however, remained short lived. The SARB introduced various actions to support the markets through this stress. The aftereffects of the pandemic and SARB interventions included a reduction in bank funding spreads as the COVID-19 lockdown resulted in increased deposit levels because of precautionary savings and reduced spending. Risks remain that funding costs could increase as the country emerges from the crisis and growth begins to pick up.

Foreign currency funding risks

The low level of discretionary savings in South Africa, and its high investment and social welfare requirements increase the economy's reliance and vulnerability to foreign capital inflows, driven by the country's fiscal and current accounts.

The issuer seeks to mitigate its exposure to its foreign currency funding by operating a prudent foreign currency management framework and operating within limits on its foreign currency borrowing that are more conservative than the macro-prudential limits applied by the SARB. The issuer seeks to avoid exposing itself to undue liquidity risk and to maintain liquidity risk within the risk appetite approved by the board and risk committee.

The issuer believes that its level of access to domestic and international inter-bank and capital markets will allow the issuer to meet its short-term and long-term liquidity needs due to the strategy, flexibility and diversification of its liquidity risk management policy in both foreign and domestic currencies. However, any maturity mismatches may have a material adverse effect on its financial condition.

Funding and other risks relating to securitisations

Securitisation is the process whereby loans and other receivables are packaged, underwritten and sold in the form of asset-backed securities to investors. The issuer makes use of securitisations to complement its overall funding strategy. This can, however, constitute a significant proportion of a particular asset class within the broader group balance sheet.

While an important component of its overall funding strategy, the issuer limits the use of securitisation to ensure appropriate strategy diversification and agility. Further, the issuer does not aim to execute securitisations specifically for credit or capital relief purposes, and typically retains subordinated notes within the wider FirstRand group structure. Consequently, the FirstRand group retains all risks and rewards associated with the underlying assets. In addition, the use of securitisation transactions as part of the issuer's funding strategy generates risks such as:

- funding and liquidity risk in respect of any potential repurchase of the transferred assets (for example, in circumstances where there is a breach of contractual representations and warranties relating to the underlying assets);
- operational risks related to the servicing of the transferred assets; and
- interest rate and other risks through derivatives transacted with the securitisation entities.

The issuer engages in securitisation transactions in order to mitigate and not add to the funding and liquidity risk profile.

2.4 Operational risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It includes, for example, fraud and criminal activity (internal and external), project risk, legal risk, business continuity, information and IT risk, process and human resources risk.

The principal operational risks currently facing the issuer are:

- **business continuity risk** due to the rapid spread of COVID-19;
- **cyber risk** (including information security), given the growing sophistication of cyber attacks both locally and globally, and the potential for cyber attacks brought about by the COVID-19 pandemic;
- **technology risk**, due to the pace of technology change and increasing digitisation;
- **vendor risk**, due to lack of direct control over external service providers and potential impact of COVID-19 on their ability to continue to deliver services;
- **people risk**, due to the impact of the COVID-19 pandemic on the physical and emotional wellbeing of employees over time, and potential employee non-adherence to health and safety protocols in the workplace; and
- **execution, delivery and process management risk** (risk of process weaknesses and control deficiencies) as the business adjusts to a new way of operating due to COVID-19, while still trying to grow and evolve under tough economic conditions.

The issuer may suffer a failure or interruption in or breach of its information technology systems

Information technology (IT) risk encompasses both IT risk and IT change risk. The issuer's IT risk refers to the risk associated with the use, ownership, operation, involvement, influence and adoption of IT. It consists of IT-related conditions that could potentially impact the business. IT change risk refers to the risk arising from changes, updates or alterations made to the IT infrastructure, systems or applications that could affect service reliability and availability.

The issuer's main IT risks include the failure or interruption of critical systems, cybercrime, unauthorised access to systems and the inability to serve its customers' needs in a timely manner.

The issuer has a high dependency on its IT systems and operations infrastructure to conduct its business. The issuer regards these systems as critical to improving productivity and maintaining the issuer's competitive edge. Any failure, interruption or breach in security of these systems could result in failures or interruptions in its risk management, general ledger, deposit servicing, loan servicing, debt recovery, payment custody and/or other important systems. If the issuer's information systems fail, even for a short period of time, it could be unable to serve some or all customers' needs on a timely basis which could result in a loss of business. In addition, a temporary shutdown of the issuer's information systems could result in costs that are required for information retrieval and verification. The occurrence of any failures or interruptions in the issuer's IT systems and operations infrastructure could have a materially adverse effect on the issuer's business, financial condition and/or results of operations.

Cybercrime could have a negative impact on the issuer's operations

The issuer's operations are dependent on its own IT systems and those of its third-party service providers. The issuer could be negatively impacted by cyber attacks on any of these. As the issuer moves banking to digital and mobile platforms, the risk of cybercrime increases, especially as infiltrating technology is becoming increasingly sophisticated, and there can be no assurance that the issuer will be able to prevent all threats.

Technology has been central to the way people, companies and governments have managed the COVID-19 pandemic and the contact-free economy may also create new employment opportunities in the post-pandemic world. However, a greater dependence on technology has increased cybersecurity risks and privacy concerns. New working patterns may increase cyber attacks and data fraud.

The issuer's business is subject to its ability to quickly adapt to disruptions while maintaining continuous business operations

The issuer has established a business resilience policy and standards to govern business continuity (including disaster recovery) and to improve the capability of the business to effectively respond to disruptive events from internal failures or external events. This is achieved through the business continuity strategies including regular review of business continuity plans (including disaster recovery) and testing. Any failure in the continuity of the issuer's operations and services could have a material adverse effect on its business, financial condition and/or results of operations.

The issuer may not be able to detect money laundering and other illegal or improper activities fully or on a timely basis, which could expose it to additional liability and have a material adverse effect on it

The issuer is required to comply with applicable anti-money laundering, anti-terrorism laws and other regulations in all of its operating jurisdictions insofar as reasonably practicable. These laws and regulations require the issuer, among other things, to adopt and enforce "customer due diligence" policies and procedures and to report suspicious and large transactions to the applicable regulatory authorities. While the issuer has adopted policies and procedures aimed at detecting and preventing the use of its banking platforms for money laundering and terrorist-related organisations and individuals generally, such policies and procedures may not completely eliminate instances in which the issuer may be used by other parties to engage in money laundering or other illegal or improper activities. To the extent the issuer may fail to fully comply with applicable laws and regulations, the relevant government agencies to which it reports have the power and authority to impose fines and other penalties on the issuer. In addition, the issuer's business and reputation could suffer if customers use it for money laundering or illegal or improper purposes.

The issuer may be unable to recruit, retain and motivate key personnel

An engaged workforce is critical to the successful delivery of the issuer's objectives. The issuer's performance is dependent on key personnel. The issuer's continued ability to compete effectively and further grow its businesses also depends on its ability to attract new staff. In relation to the development and training of new and existing employees, the issuer is reliant on the continued development of South Africa's educational sector, including access to facilities and educational programmes.

Terrorist acts, hostility arising from competing political groups, acts of war, and other types of event risk could have a negative impact on the business

Acts of terrorism, hostility from competing political parties, acts of war, government expropriation or confiscatory acts, currency inconvertibility, financial market closure, health pandemics and other types of event risk and responses to those acts and events, may have both direct and indirect negative impacts on the economic conditions of South Africa, the rest of Africa and internationally, and more specifically on the business and results of the issuer in ways that cannot be predicted.

2.5 Equity investment risk

Equity investment risk in the issuer arises primarily from equity exposures from private equity and investment banking activities, e.g. exposures to equity risk arising from principal investments or structured lending. Other sources of equity investment risk include certain strategic investments which are core to individual businesses' daily operations and are managed as such.

The issuer's asset management business also contributes to equity investment risk. This risk emanates from long-term and short-term fund seeding activities both locally and offshore. Short-term seeding typically ranges between one and three years. Long-term seeding is provided if there is alignment with the business strategy, the business case meets the group's internal return hurdle requirements, and the liquidity and structure of the funds imply that an exit will only be possible over a longer period. This maturity period typically ranges from five to eight years post investment in the fund.

Equity investment risk 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.

The impact of COVID-19 on the economy is expected to increase the equity investment risk in the portfolio.

2.6 Insurance risk

Insurance risk arises from the issuer's third-party insurance operations housed in FirstRand Insurance Holdings Limited. Long-term insurance operations are underwritten through its subsidiary FirstRand Life Assurance Limited, and short-term insurance operations are underwritten through its subsidiary FirstRand Short-term Insurance Limited.

Insurance risk manifests when the decrement rates (e.g. mortality rates, morbidity rates, etc.) and associated cash flows are different from those assumed when pricing or reserving. These risks can further be broken down into parameter risk, random fluctuations and trend risk. As a result of these insurance risk exposures, the issuer is exposed to catastrophe risk, stemming from the possibility of an extreme event such as COVID-19.

The issuer manages its insurance risk to be within its stated risk appetite. This is translated to risk limits for various metrics that are monitored and managed. The assessment and management of risk focuses on rigorous and proactive processes to ensure sound product design and pricing, management of the in-force book, and reinsurance agreements to manage catastrophe risk.

2.7 The issuer's risk management policies and procedures may not have identified or anticipated all potential risk exposures

The issuer has devoted significant resources to developing its risk management policies and procedures, particularly in connection with credit, concentration and liquidity risks, and expects to continue to do so in the future. Nonetheless, its risk management techniques may not be fully effective in mitigating its risk exposure in all market environments or against all types of risk, including risks that are unidentified or unanticipated. Some of the issuer's methods of managing risk are based upon its use of observed historical market behaviour. As a result, these methods may not predict future risk exposures, which could be greater than historical measures indicate. Other risk management methods depend upon evaluation of information regarding the markets in which the issuer operates, its clients or other matters that are publicly available or otherwise accessible by the issuer. This information may not be accurate in all cases, complete, up-to-date or properly evaluated. Any failure arising out of the issuer's risk management techniques may have an adverse effect on the results of its operations and financial condition.

2.8 Competitive landscape

The issuer is subject to significant competition from other banks operating in all of its operating jurisdictions, including competitors that may have greater financial and other resources, particularly in the corporate and investment banking market. Many of these banks operating in the issuer's markets compete for substantially the same customers as the issuer. The issuer also faces competition from other non-bank entities that increasingly provide similar services to those offered by banks, e.g. asset managers, insurers, retailers, mobile phone operators, shadow banking players and fintech companies. Increased competition from non-bank entities in the money and capital markets could impact the issuer's ability to attract funding.

In particular, competition may increase in South Africa as a result of the approval of an amendment to the Banks Act on 7 March 2019, which will allow state-owned entities to establish a bank but only at national level.

Increasing competition could also require that the issuer increases its rates offered on deposits or lower the rates it charges on loans, which could also have a material adverse effect on the issuer, including its profitability. Although the issuer's financial resource management approach requires it to price appropriately for financial resources, should competitive forces prevent the issuer from pricing for these resources appropriately it may withdraw from offering certain products which may also negatively affect the issuer's business results and prospects, by, among other things, limiting its ability to generate revenue, increase its customer base and/or expand its operations.

If the issuer's customer service levels were perceived by the market to be materially below those of its competitor financial institutions, the issuer could lose existing and potential new business. If the issuer is not successful in retaining and strengthening customer relationships, the issuer may lose market share, incur losses on its activities, fail to attract new deposits or retain existing deposits which could have a material adverse effect on its operating results, financial condition and prospects.

2.9 Environmental, social and climate risk

Environmental risk is defined as the impact of the natural environment on business as well as the impact and dependencies of the business on the environment and natural capital. These impacts can manifest in legal or regulatory requirements, potential financial losses, operational costs, physical damage, credit risk, or reputational risk because of an issuer's failure to comply with responsible environmental practices, laws, regulations, rules, related self-regulatory organisational standards, and codes of conduct applicable to its activities. Environmental risks can be grouped into two areas of impact for the issuer, namely direct environmental risk (own operations and climate resilience), and indirect environmental and climate risk (lending, financing and investment).

Social risk references social impacts associated with activities conducted through a business relationship with customers, investee companies or stakeholders as a result of financial exposure, lending/financing, investment and equity interest that may lead to a risk of legal or regulatory sanctions, material financial loss or reputational damage. The issuer may suffer in any of these aspects because of its client or stakeholder organisation's failure to comply with all applicable laws, voluntary agreements, regulations and/or supervisory requirements. Social risks include product responsibility and inclusion issues, labour-related issues, occupational health and safety, community involvement, community security, human resettlement, indigenous people's rights and human rights. These risks could lead to criminal sanction, termination of operations, production losses and subsequently pose a financial, reputational or credit risk to the issuer.

Climate risk is defined as a risk resulting from climate change, causing an increase in physical risks (stemming from increased incidences of natural disasters), transition risks (resulting from changes in laws, regulations or customer preferences) and third-party liability risks (due to non-compliance with climate regulations). The impact of climate change is expected to prompt substantial structural adjustments to the global economy. Several sectors, such as fossil fuels, are expected to experience disruption from changes in investor or end-user preferences, or changes in regulations whilst others, such as renewable energy and other green energy sources, and carbon capture and adaptation technologies, are likely to benefit. Such fundamental changes will inevitably impact the balance sheets and operations of banks, leading to both risks and opportunities. Regulators are beginning to act, and investors, clients and civil society are looking for actions, mitigation, adaptation and transparency on the issue.

Environmental, social and climate risk is typically a cross-cutting risk issue and, therefore cannot be managed in only one risk management function:

- Reputational: Damage to reputation from association with environmental and social impacts.
- Market and liquidity: Higher levels of market volatility, shift in asset valuations, dislocations, shift in market appetite with regards to the type of assets funded.
- Credit: Adverse impact on customers' ability to pay, impaired collateral values mainly driven by an increase in physical risks (e.g. drought or property damage) or transition risks (lower demand of product).
- Legal action, regulatory sanction or reputational damage may occur as a result of the group's approach to environmental risk.
- Disruptions to the group's operations, infrastructure, workforce, processes and supply chain may result from acute environmental events.

Fiscal capacity has focused on the COVID-19 pandemic with a resultant shortfall of investment in climate adaptation and mitigation efforts. However, worldwide lockdowns resulted in reduced emissions due to decreased industrial activity, travelling and commuting. As economies reopen, global emissions will increase and there is emerging evidence that large-scale infectious disease outbreaks may become more frequent due to a warming climate and biodiversity loss. Many governments have announced green recovery packages that aim to address both economic recovery and climate change. The South African cabinet recently approved the National Climate Change Adaptation Strategy, which acknowledges that a climate resilient economy is vital for job protection and economic growth.

2.10 Downgrade of the issuer's credit ratings or credit rating of South Africa could have an adverse effect on the issuer's liquidity sources and funding costs

FirstRand Bank Limited (the bank) remains the rated entity within the group and from which debt is primarily issued, and its credit ratings affect the cost and other terms upon which the issuer can obtain funding. Rating agencies regularly evaluate the issuer and the ratings of its long-term debt are based on a number of factors, including capital adequacy levels, quality of earnings, business position, credit exposure, funding and liquidity risks, the risk management framework as well as the sovereign ratings and the macro risk profiles for its country of incorporation and that of its operating jurisdictions. These parameters and their possible impact on the issuer's credit ratings are closely monitored and incorporated into its liquidity risk management and contingency planning considerations. In particular, as rating agencies impose a cap on the issuer's rating at the level of the sovereign rating, a change to the sovereign rating will, therefore, impact the issuer's rating.

In addition, a downgrade or potential downgrade of the South African sovereign rating or a change in rating agency methodologies relating to systemic support provided by the South African sovereign could also negatively affect the perception by rating agencies and the ratings of the issuer and the bank. Any downgrade of the credit ratings of the issuer and/or the bank would likely increase its borrowing costs and could require the issuer or the bank to post additional collateral or take other actions under some of its derivatives contracts and could limit the issuer's access to capital markets.

There can also be no assurance that the rating agencies will maintain the current ratings of the bank or the issuer or the rating outlooks, or those of South Africa. Failure to maintain favourable ratings and outlooks could increase the issuer's cost of funding and adversely affect interest margins, which could have a material adverse effect on the issuer. Ratings are not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency. Each rating should be evaluated independently of any other rating.

2.11 The issuer is subject to capital requirements that could affect its operations

In South Africa, the issuer, and its regulated banking entities are subject to capital adequacy guidelines adopted by the PA, which provide for minimum capital requirements for Common Equity Tier 1 (CET1), Tier 1 and Total Capital. Any failure by the issuer to maintain its minimum capital in terms of Basel III and the PA Regulations relating to banks, for example the capital conservation and countercyclical buffer (CCyB), could result in restrictions being placed on distributions, including dividends and discretionary payments.

The Regulations relating to banks (as amended from time to time) are based on the Basel III framework and provide the minimum risk-based capital ratios. The minimum requirements for the issuer on a consolidated basis is CET1, Tier 1 and total capital of 7.75%, 9.63% and 12%, respectively. These minimum ratios exclude the confidential bank-specific individual capital requirements but includes the domestic systemically important bank (D-SIB) requirement for the issuer. In response to the COVID-19 pandemic, the PA implemented temporary measures to provide additional capacity to counter economic risks to the financial system and promote ongoing lending to the economy. The PA published *Directive 2 of 2020, Matters related to temporary capital relief to alleviate risks posed by the COVID-19 pandemic,* which temporarily reduced the Pillar 2A capital requirement from 1% to 0%, effective 6 April 2020, as well as allow banks to draw down against the capital conservation buffer as the PA considers this to be a period of financial stress. The minimum leverage ratio requirement has not been adjusted for any COVID-19 relief measures.

Directive 4 of 2020, Capital framework for South Africa based on the Basel III framework, was also published on 27 August 2020, and incorporated the reduction in the Pillar 2A capital requirement to 0%. *Directive 4 of 2020* requires banks to also disclose their D-SIB add-ons as part of its regulatory disclosures. The D-SIB requirement for both the group and bank is 1.5%.

In addition, the Prudential Regulation Authority reduced the UK CCyB requirement from 1% to 0% in March 2020. The reduction in the CCyB requirement impacts the issuer's UK operations, i.e. Aldermore and the bank's London branch.

The issuer's internal capital targets were not adjusted following the temporary COVID-19 capital relief measures, as the issuer aligns its capital targets to the minimum requirements incorporating a fully-phased in Pillar 2A capital requirement.

The PA's *Guidance Note 4 of 2020, Recommendations on the distribution of dividends on ordinary shares and payment of cash bonuses to executive officers and material risk takers, in light of the negative economic impact of the Coronavirus Disease (COVID-19) pandemic and the temporary regulatory capital relief provided by the Prudential Authority,* was also released as an additional temporarily capital relief measure. The PA expects that no distribution of dividends on ordinary shares and payment of cash bonuses to executive officers and material risk takers to take place in 2020.

In addition, the issuer's sub-Saharan African and UK operations are also subject to the relevant regulatory capital requirements in each jurisdiction. Entities are required to comply with both the PA and in-country regulations in the rest of Africa and UK. Failure to comply with the minimum requirements in each jurisdiction could result in loss of banking licenses and restrictions being placed on distributions, including dividends and discretionary payments.

2.12 The issuer is subject to liquidity requirements that could affect its operations

Basel III prescribes two minimum liquidity standards for funding and liquidity:

- Liquidity coverage ratio (LCR) which aims to ensure that banks maintain an adequate level of high-quality liquid assets (HQLA) to meet liquidity needs for a 30-calendar day period under a severe liquidity stress scenario.
- Net stable funding ratio (NSFR) which aims to promote medium and long-term funding of banks' assets and activities.

In order to allow markets to continue to operate smoothly and provide banks with temporary liquidity relief during the crisis, the PA issued *Directive 1 of 2020, Temporary measures to aid compliance with the liquidity coverage ratio during the Coronavirus (COVID-19) pandemic stress period,* which temporarily reduced the prudential LCR requirement from 100% to 80%, effective 1 April 2020.

The PA introduced the committed liquidity facility (CLF) to assist banks meet the LCR. *Guidance Note 8 of 2020, Continued provision of a committed liquidity facility by South African Reserve Bank to banks,* was released on 9 September 2020, and provides revised guidelines and conditions relating to the continued provision of the CLF, specifically covering the period from 1 December 2020 to 30 November 2021. The guidance note also reiterates the PA's intention to phase out the CLF by 1 December 2021. The PA will, in consultation with banks, investigate possible alternatives to the CLF, if necessary.

Guidance Note 8 also noted the introduction of a restricted-use committed liquidity facility (RCLF) to be made available to all banks by the PA annually from 1 December 2020 onwards. The provision and terms of the RCLF is legislated in the Regulations relating to banks. Similar to the CLF, the facility is made available contractually for a year covering the period 1 December 2020 to 30 November 2021. The collateral eligible for both facilities are the same, though unlike the CLF, the RCLF is included in level 2B HQLA and is subject to the overall limit of 15% of level 2B HQLA. Collateral for the RCLF attracts a 50% haircut irrespective of the quality of the underlying instruments.

The NSFR is a structural balance sheet ratio focusing on promoting a more resilient banking sector. The ratio calculates the amount of available stable funding relative to the amount of required stable funding. The issuer supports the amended framework issued by the PA in August 2016, whereby funding received from financial corporates, excluding banks, maturing within six months receives an available stable funding factor of 35%. The issuer also supports the clarity provided by the PA in relation to the CLF and NSFR, applying a 5% required stable funding factor to the assets (post haircut) eligible for CLF purposes. These changes have been anchored in the assessment of the true liquidity risk and assist the South African banking sector in meeting the NSFR requirements. With the discontinuation of the CLF the favourable NSFR treatment of CLF collateral noted above will fall away. Under the RCLF, the assets underpinning the facility will attract the standard required stable funding factors for level 2B assets.

2.13 Changing regulatory environment

The issuer is subject to the laws, regulations, administrative actions and policies of South Africa and each other jurisdiction in which it operates, and the issuer's activities may be constrained by such legal and regulatory requirements. Changes in regulation and supervision, particularly in South Africa, could materially affect the issuer's business, the products or services offered, the value of its assets and its financial condition. Although the issuer works closely with its regulators and continuously monitors the regulatory feedback and proposals, future changes in regulation, fiscal or other policies cannot be predicted and are beyond the control of the issuer.

Applicable laws and other requirements, as amended from time to time, include, among other:

- Banks Act, 1990 and related Regulations.
- Collective Investment Schemes Control Act (CISCA), 2002.
- Companies Act, 2008.
- Competition Act, 1998.
- Consumer Protection Act, 2008.
- Currency and Exchanges Act, 1993 and Exchange Control Regulations, 1961.
- Financial Advisory and Intermediary Services (FAIS) Act, 2002.
- Financial Intelligence Centre (FIC) Act, 2001.
- Financial Markets Act (FMA), 2012.
- Financial Sector Regulation Act, 2017.
- Foreign Account Tax Compliance Act, 2010.
- Insurance Act, 2017.
- King Code of Governance Principles for South Africa, 2016 (King IV).
- Long-term Insurance Act, 1998.
- National Credit Act (NCA), 2005.
- National Payment System Act, 1998.
- Prevention and Combating of Corrupt Activities Act (PRECCA), 2004.
- Protected Disclosures Act, 2000.
- Protection of Personal Information Act (PoPIA), 2013.
- Short-term Insurance Act, 1998.
- Legislation and rules related to listed instruments on various exchanges.
- Statutory codes of conduct, standards, joint standards and other subordinate legislation issued by, among others, the Financial Sector Conduct Authority (FSCA) and the PA.

The issuer is also subject to any applicable regulatory instruments issued pursuant to any of the abovementioned legislation.

In accordance with its Basel III and G20 commitments, the SARB is developing a resolution framework.

The Financial Sector Laws Amendment Bill (FSLAB) was recently tabled in Parliament. The bill is part of the Twin Peaks reforms of the South African financial sector regulatory system and will reinforce and strengthen financial stability in South Africa. It introduces critical elements relating to, among other, how to deal with failing banks and other systemically important financial institutions, the ultimate objective of which is to protect financial stability in South Africa. Aligned to the aforesaid, the bill proposes necessary amendments to various acts, including, among other, the Financial Sector Regulation Act, 2017, the Insolvency Act, the South African Reserve Bank Act, the Banks Act, the Competition Act, the Financial Markets Act and the Insurance Act. The bill also provides for the establishment of a framework for the resolution of designated institutions to ensure that the impact or potential impact of a failure of a designated institution on financial stability is managed appropriately, the designation of the SARB as the resolution authority and the establishment a deposit insurance scheme, including a Corporation for Deposit Insurance (CoDI) and a deposit insurance fund. The bill is also necessary to enable South Africa to meet certain post 2008 global financial crisis international standards, as endorsed by G-20 countries and outlined in the Financial Stability Board's document, *Key Attributes of Effective Resolution Regimes for Financial Institutions,* which sets out the international standard for resolution regimes to address the problem of banks which are considered "too big to fail". The underlying policy approach to resolution is contained in two policy papers, namely *Strengthening South Africa's Resolution Framework for Financial Institutions* and *Designing a Deposit Insurance Scheme for South Africa,* which were published by the National Treasury and the SARB during 2015 and 2017, respectively. As referred to above, one of the key amendments included in the bill is the establishment of the CoDI designed to protect depositors' funds and enhance financial stability.

The SARB released a discussion paper, *Ending too big to fail: South Africa's intended approach to bank resolution,* on 23 July 2019. The discussion paper outlines the objectives of the resolution framework, planning and conducting a resolution with an emphasis on open-bank resolution, especially in relation to systemically important financial institutions. The intended bank resolution provides more clarity on the SARB's approach to further enhance financial stability in South Africa.

The FSLAB introduced a new tranche of loss-absorbing instruments, i.e. flac instruments, which are subordinated to other unsecured creditors and intended for bail-in in resolution. Flac requirements will be applicable to banks with open bank resolution plans. The SARB acknowledges the international approaches towards calibration of total loss-absorbing capacity but has not detailed how the quantum of required flac will be calculated for relevant institutions, nor the deadline for compliance. PwC, appointed by the World Bank and SARB, conducted a survey to analyse various aspects relevant to flac instrument requirements. The survey was completed during the first quarter of 2020 and the results are currently subject to review by the SARB.

Risks relating to South Africa

1. RISKS RELATING TO EMERGING MARKETS

South Africa is an emerging market with significant socio-economic challenges. Investors in emerging markets such as South Africa should be aware that these markets carry risks which are different from those which apply to investment in more developed markets. These risks include economic and financial market volatility which may be exacerbated by global economic volatility, as well as, in some cases, significant legal and political risks.

Economic and financial market instability in South Africa has been caused by many different factors, including:

- high interest rates;
- high levels of inflation;
- exchange rate volatility;
- exchange controls;
- commodity price fluctuations;
- industrial action;
- the slowdown in the economic activity of its trading partners;
- wage and price controls;
- changes in economic and tax policies;
- the imposition of trade barriers;
- wide current account deficit;
- capital outflows;
- perceived or actual internal security issues; and
- general social, economic and business conditions.

Any of these factors, amongst others (such as the current COVID-19 crisis), as well as volatility in the markets for securities, may adversely affect the value or liquidity of the securities issued.

Accordingly, investors should exercise particular care in evaluating the risks involved and must decide for themselves whether, in light of those risks, their investment is appropriate. Generally, investment in emerging markets is only suitable for sophisticated investors who fully appreciate the significance of the risks involved, and prospective investors are urged to consult with their own legal and financial advisers before making an investment in the securities.

Investors should also note that developing markets, such as South Africa, are subject to rapid change and that the information set out in this document may become outdated relatively quickly.

2. REGULATORY ENVIRONMENT

The issuer is subject to formal regulation in South Africa. Regulatory agencies have broad jurisdiction over many aspects of the issuer’s business, including safety and soundness (prudential) requirements such as, capital adequacy and risk management requirements in its broadest sense.

Changes in government policy, legislation or regulatory interpretation applying to the financial services industry in the markets in which the issuer operates may adversely affect the issuer's product range, distribution channels, capital requirements, environmental and social obligations and, consequently, reported results and financing requirements. In this regard, any change in regulation to increase the requirements for capital adequacy or liquidity, or a change in accounting standards, could have a material adverse impact on the issuer's business, results, financial condition or prospects.

During 2011, the government issued a policy paper, *“A Safer Financial Sector to Serve South Africa Better”,* which articulated its strategic regulatory objectives. The document identified policy priorities to reform the financial sector, most notably: financial stability, consumer protection and market conduct, expanding access of financial services through inclusion, and combating financial crime. Achieving these objectives evidently necessitated a change in the South African regulatory landscape from both a structural and a policy perspective which necessitated the introduction of a “twin-peaks” approach to financial sector regulation. In terms of the twin peaks approach, equal focus is placed on prudential and market conduct regulation with separate but equally important focus on financial stability. A phased-in approach was followed for the implementation of the Twin Peaks system of financial regulation in South Africa.

The Twin Peaks system of financial regulation in South Africa was implemented on 1 April 2018. The SARB is responsible for financial stability whilst the PA and the FSCA took effect. It is important to note that a key objective of the Twin Peaks system of financial regulation in South Africa is to ensure that there is effective co-operation and collaboration among the SARB, the PA, the FSCA, the National Credit Regulator (NCR), the Financial Intelligence Centre and the Competition Commission, which may result in additional complexities for financial services and product providers in managing regulatory and conduct risks. The issuer will continue to work closely with its regulators on matters pertaining to the above.

Conduct Standard for Banks

The FSCA published *Conduct Standard for Banks on 3 July 2020 (Conduct Standard 3 of 2020).* This standard is being implemented in a staggered manner, with some of the provisions being effective immediately and other provisions being implemented within a period of eight and 12 months of publication. This standard entrenches the FSCA's oversight over products and services being offered by banks. The standard requires compliance with the treating customers fairly regime, including requirements relating to culture and governance (including reward and remuneration), product approval, disclosures, post-sale services (including complaints handling). To some extent, there is overlap with existing regulatory requirements (such as required by the Financial Advisory and Intermediary Services Act and the National Credit Act). In order to avoid excessive disruption to operations, it is necessary to ensure harmonisation of the requirements emanating from this standard, with existing regulatory and customer obligations, where possible. This exercise is currently being conducted internally. Similarly, the request for information from regulators may overlap or be duplicated and should ideally be managed through the memoranda of agreements between regulators. Non-compliance with the requirements imposed in terms of this standard may result in enforcement actions taken against the issuer.

National Credit Act

The National Credit Act, 2005 (NCA) which came into effect on 1 June 2007, has made significant changes to the interest, costs and fees which retail banks and other credit providers may charge consumers in South Africa. The maximum prescribed interest rates which may be levied on credit agreements are set out in the regulations to the NCA. The NCA further stipulates a closed list of costs and fees which may be recovered under a credit agreement in addition to the capital amount and interest. These relate to an initiation fee, a monthly service fee, default administration costs and collection costs. The initiation fee for arranging the credit agreement may not exceed the maximum prescribed amount, monthly service fees for the banks administration of the agreement are capped, default administration charges must be levied in accordance with the Magistrates Court Act, 1944 and collection costs are also limited. Other charges which may be applicable are strictly regulated and may only be levied if specifically listed in the NCA and to the extent permitted in the NCA. The NCA also requires certain qualifying credit providers to register with the NCR, and credit agreements entered into by entities which are not registered credit providers, as is required in terms of the NCA, will be *void ab initio.* In addition, certain credit agreements which contain unlawful provisions in terms of the NCA could potentially be rendered *void ab initio.*

The NCA has strict provisions which prohibit the selling or collection of outstanding debts which have prescribed. This means that credit providers can no longer collect on loans where no legal action has been taken and no payments have been received for three years. This will impact the ability of banks to collect existing non-performing and written-off loans which have prescribed and applies to all loans in existence at 13 March 2015 and new loans granted thereafter. In addition, affordability assessment regulations, which came into effect on 13 March 2015, and credit providers' commitments to combatting over-indebtedness, are important considerations for the NCR in consideration of the registration of credit providers, in terms of the NCA. During August 2019, the National Credit Amendment Act, Act 7 of 2019 was promulgated. The effective date has yet to be proclaimed by the Minister of Trade and Industry through publication in the Government Gazette. The proposed amendments include, among other, a debt intervention measure to assist consumers to whom insolvency measures are not accessible in practice. The process involves the extinguishment of debt, where applicable. The NCR will implement the debt intervention process and refer matters to the National Consumer Tribunal to adjudicate on debt intervention applications. Debt counsellors are required to investigate reckless credit agreements and report such to the NCR in respect of consumers who apply for debt review. The possibility of extinguishment of debt, though limited to certain income thresholds and unsecured debt, may result in negative consumer payment behaviour which can result in the credit industry adjusting credit risk appetites.

Protection of Personal Information Act 4 of 2013 (POPIA)

One of the key purposes of POPIA is to give effect to the section 14 constitutional right to privacy and ensuring harmony with international standards on data privacy. POPIA was enacted in 2013 and came into effect on 1 July 2020, save for certain provisions, but there is a one-year grace period within which to comply with POPIA. POPIA specifically regulates the processing of personal information, which is broadly defined as information relating to an identifiable, living, natural person, and where applicable, an identifiable, existing, juristic person. The term applied to these natural and juristic persons is "data subject".

In terms of section 3(1) of POPIA, its provisions apply to the processing of personal information entered in a record by or for a responsible party, using automated or non-automated means, where the responsible party is either domiciled in South Africa or makes use of automated or non-automated means to process personal information within South Africa. Each of the entities in the FirstRand group can be considered as a responsible party (also acting in conjunction with other entities) when determining the purpose of and means for processing personal information of its customers, employees and suppliers.

POPIA establishes eight minimum conditions for the lawful processing of personal information. These conditions can be summarised as follows:

(a) Accountability: The responsible party must comply with all the conditions for lawful processing.

(b) Processing limitation: Personal information must only be collected for a specific, explicitly defined lawful purpose related to a function or activity of the responsible party.

(c) Purpose specification: Processing must be justified on grounds recognised under POPIA (e.g. consent/legitimate interests of the data subject, responsible party or the third party to whom the information is supplied).

(d) Further processing limitation: Processing must be in accordance with or compatible with the purpose for which it was initially collected subject to limited exceptions.

(e) Information quality: Steps must be taken to ensure that the personal information is complete, accurate, not misleading and updated where necessary.

(f) Openness: Notification or disclosure requirements must be complied with when collecting personal information.

(g) Security safeguards: Appropriate, reasonable technical and organisational measures must be implemented and maintained to prevent loss of, damage to or unauthorised destruction of or unlawful access to personal information.

(h) Data subject participation: Data subjects have the right to request details of the personal information that a responsible party holds about them and, in certain circumstances, request access to such information.

Further conditions are specified for the processing of information relating to children, special personal information, direct marketing, transborder information flows, automated processing of information, and other specified matters and privacy rights afforded to data subjects.

It is within each of these conditions where material risks can emerge, if the responsible party does not adhere to the corresponding requirements and provisions. Such risks could attract sanctions for the responsible party, which includes a fine or imprisonment (or both) for a period of no longer than ten years, or alternatively, may lead to an administrative fine. Currently, the maximum fine that can be issued is R10 million.

Companies Act

The Companies Act 71 of 2008 as amended (the Act) by the Companies Amendment Act 33 of 2011 was effective from 1 May 2011. The Companies Act provides incorporation, registration and management of companies, capitalisation of profit companies, shareholder provisions, accountability and transparency, corporate finance, director's duties and board governance, mechanisms for efficient business rescue of financially distressed companies, fundamental transactions, takeovers and share purchases that could potentially have an impact on the rights and duties of the issuer and noteholders.

Consumer Protection Act

The Consumer Protection Act, 2009 (CPA) came into effect on 1 April 2011. The CPA will give consumers the right to demand quality service and to full disclosure of the price of goods and services, and protection against false, misleading or deceptive representations.

The CPA will fundamentally change the way business is done in South Africa. It requires businesses to transform the way in which they interact with consumers and to ensure that all dealings with consumers are fair, reasonable and honest. Credit agreements governed by the NCA do not fall within the ambit of the CPA, however, the goods or services that are the subject of the credit agreement are not excluded from the ambit of the CPA. The CPA provides that certain industries may be exempted from particular provisions of the CPA where there are existing consumer protection regimes in place in respect of those industries. Banks are exempted from section 14 of the CPA which deals with fixed-term contracts as there is concern in the banking industry that the said provision will adversely impact fixed term deposits and bank customer's ability to withdraw such deposit early.

Investors will have to familiarise themselves with the risks associated with this legislation as it remains untested in a court of law to date.

3. EXCHANGE CONTROL

Foreign-derived loan capital or equity capital may be introduced into South Africa through a formal system of exchange control. However, the proceeds from the sale of assets in South Africa owned by a non-resident are not remittable to the non-resident unless prior approval is received from an authorised dealer in foreign exchange or, if such authorised dealer in foreign exchange is unable to approve the request as per the requirements laid down in the Currency and Exchanges Manual, then prior approval is required from the SARB.

Since 1995, certain exchange controls in South Africa have been relaxed. The extent to which the South African government (the government) may further relax such exchange controls cannot be predicted with certainty, although the government has committed itself to a gradual approach of relaxation. Further relaxation, or abolition of exchange controls may precipitate a change in the capital flows to and from South Africa. If the net result of this were to cause large capital outflows, this could adversely affect the issuer's business and it could have an adverse effect on the financial condition of the issuer as a whole. In the event of the immediate abolition of exchange control there may be a sudden withdrawal of rand from the South African market by investors. Because South Africa has a fully-floating exchange rate and a flexible interest rate policy, this would result in a rapid depreciation of the rand exchange rate which would serve to stem the flight and would also result in an increase in interest rates due to the depreciation of the rand. The SARB may sell reserves to protect the value of the rand. Such reserve activity by the SARB is likely to be sterilised and as such should not have a significant impact on inflation.

Banking sector in South Africa

The South African banking system is well-developed and effectively regulated, comprising several large, financially strong banking groups and a number of smaller banks, mutual banks and co-operative banks. Many foreign banks and investment institutions have also established operations in South Africa. The government generally endorses the IMF and World Bank standards. South African banks are regulated by the PA, which is a juristic person operating within the administration of the SARB. As a member of the Basel Committee on Banking Supervision (BCBS), the SARB is committed to ensuring that the South African regulatory and legislative framework relating to the regulation and supervision of banks and banking groups remains compliant with international standards and best practice. Changes in international standards and requirements normally result in amendments to the South African prudential standards which usually result in amendments to, among other, the Regulations relating to banks. For example, the Basel III phase-in arrangements largely resulted in prudential regulatory changes, and new and/or amended requirements and standards. In line with the above, various other documents, frameworks and requirements that impact materially on the regulation and supervision of banks and banking groups in South Africa, are issued by the international standard-setting bodies on an ongoing basis, which will, going forward, continue to result in revised and additional and/or new regulatory requirements. The PA, which represents South Africa on the BCBS, actively participates in international regulatory and supervisory standard-setting forums at which it is represented and provides input into the continued refinement of the regulatory and related supervisory frameworks.

The National Payment System Act, 1998 (as amended) was introduced to bring the South African financial settlement system in line with international practice and systematic risk management procedures. In this regard, the national payment system (NPS) is regarded as one of the pillars of financial stability of the South African economic system. The SARB, through its national payment system department (NPSD), is the primary regulator and overseer of the NPS, also insofar as it relates to the safety and soundness of the NPS. This includes implementation of risk-reduction measures in the payment system to reduce systemic risk. The Payment Association of South Africa (PASA) was established during 1996 by the South African banking industry in conjunction with the SARB and is, as a recognised payment system management body, under the supervision of the NPSD. PASA's main objective is to regulate, manage and organise the participation of its members in the NPS and facilitated, among other, the introduction of payment clearing house agreements and introduced agreements pertaining to settlement, clearing and netting agreements, rules to create certainty and reduce systemic and other risks in inter-bank settlement. These developments brought South Africa in line with international inter-bank settlement practices. Electronic banking facilities are extensive, with a nationwide network of automatic teller machines, internet and mobile phone banking being available. Since payments systems and related international standards and best practice requirements pertaining thereto are evolving, various initiatives and developments are currently being undertaken by the SARB and its NPSD pertaining to, among other, the re-alignment of mandates, strategies and reforms of the regulatory model for the South African national payment system.

REGULATION

Financial sector regulatory legislation in South Africa is increasing following the implementation of the Twin Peaks system of financial sector regulation in South Africa and, as indicated above, alignment to new and additional international best practice requirements through the accords of, among others, international bodies such as the Bank of International Settlements (BIS), the International Organisation of Securities Commissions and the International Association of Insurance Supervisors. Banks in South Africa are governed by a comprehensive legislative framework, most significantly the Financial Sector Regulation Act 2017, read with the Banks Act (Act no. 94 of 1990 – the Banks Act), which is comparable to similar legislation in the UK, Australia and Canada.

As a bank, the issuer is subject to formal regulation in South Africa. Regulatory agencies have broad jurisdiction over many aspects of the issuer's business, which include capital adequacy, premium rates, marketing and selling practices, advertising, licensing, policy forms, terms of business and permitted investments. Changes in government policy, legislation or regulatory interpretation applying to the financial services industry in the markets in which the issuer operates may adversely affect the issuer's product range, distribution channels, capital requirements, environmental and social obligations and, consequently, reported results and financing requirements. In particular, any change in regulation to increase the requirements for capital adequacy or liquidity, or a change in accounting standards, could have a material adverse impact on the issuer's business, results, financial condition or prospects.

ANTI-MONEY LAUNDERING REGULATIONS

The government has identified the combating of financial crime as policy priority. South Africa has a well-established anti-money laundering (AML) and counter terror financing (CTF) legislative framework (which includes but is not limited to the FIC Act, 2001, as amended). The last mutual evaluation report issued in relation to South Africa by the Financial Action Task Force, the purpose of which is the development and promotion of national and international AML and CTF policies, confirmed that South Africa has demonstrated a strong commitment to implementing AML/CTF systems facilitated by close cooperation and coordination among a variety of government departments and agencies. The authorities sought to construct a system which uses, as its reference, the relevant United Nations Conventions and the international standards as set out by the Financial Action Task Force. In this regard, to the extent that the FATF had *inter alia* made recommendations on improvements to the legislative environment, these were affected by the authorities. The FATF is presently concluding on a mutual evaluation which commenced during the second half of 2019. In terms of the FIC Act, the SARB, through the PA, is mandated to supervise and enforce banks' compliance with the FIC Act. In line with this mandate, the PA will continue to conduct inspections on banks with the aim to assess whether appropriate measures and controls are in place to ensure compliance with the provisions of the FIC Act, related regulations and regulatory requirements. The PA, as a financial sector regulator, is by law required to co-operate and collaborate with the FIC when performing its functions in terms of the FIC Act. The issuer has implemented an AML framework which includes CTF policies and takes measures to effect continuous improvement in its processes to address its AML and CTF risks.

SOUTH AFRICAN RESERVE BANK

The SARB is, as South Africa's central bank and macro-prudential regulator, responsible for, among other things, contributing towards the achievement and maintenance of a stable financial system, protecting and enhancing financial stability, and restoring and maintaining financial stability in terms of systemic events. The SARB holds various international memberships including the G-20, the IMF, the BIS and the Committee of Central Bank Governors in the Southern African Development Community. The SARB serves on various BIS committees including the Basel Committee and the Committee on Payments and Settlement Systems.

PRUDENTIAL AUTHORITY

The SARB has, prior to the implementation of the new regulatory framework, performed its function as banking regulator through its bank supervision department, which issued banking licences to institutions and supervised their activities under the applicable legislation. The PA, which is a juristic person operating within the administration of the SARB, took effect on 1 April 2018. The PA is responsible for, among other, prudential regulation and supervision of banks, banking groups and financial conglomerates in South Africa, with the purpose of promoting and enhancing the safety and soundness of financial institutions and assist in maintaining financial stability. The PA has extensive regulatory and supervisory powers which, among other, oblige banks to furnish certain prescribed returns to the PA in order to enable the PA to monitor compliance with the various prudential and other regulatory requirements imposed on banks in terms of the Banks Act, 1990, the Regulations relating to banks, and other applicable regulatory instruments. The chief executive officer of the PA is a deputy governor of the SARB and a member of the SARB's Financial Stability Oversight Committee.

THE FINANCIAL SECTOR CONDUCT AUTHORITY

As a bank, the issuer's market conduct is regulated by the FSCA, which also took effect on 1 April 2018. The FSCA supervises, among other, how financial institutions conduct their business and treat customers. It is also responsible for the efficiency and integrity of financial markets. The FSCA is, similar to the PA, the other pillar of the new financial sector regulatory architecture.

GENERAL

The issuer's relationships with its regulatory authorities are largely managed by a dedicated regulatory and conduct risk management function and the FirstRand group's Public Policy and Regulatory Affairs Office. The issuer views its relationship with its regulators as being of the utmost importance. The issuer is a member of the Banking Association of South Africa, which is effectively the mandated representative of the banking sector in South Africa, as it facilitates the enablement of a conducive banking environment through robust engagement with government and relevant stakeholders. The issuer is supportive of the twin peaks regulatory objectives and endorses, as an active participant in the new regulatory landscape, improvements in risk management, governance and market conduct practices. The same approach is also applied in respect of the issuer's cooperation with other regulatory authorities and much effort and resources are dedicated in a cost-efficient manner in order to reap maximum benefits emanating from the implementation of best practice and the resultant enablement of its global business activities.

7 October 2020

FirstRand

www.firstrand.co.za