material risk factor disclosure

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

FOR THE YEAR ENDED 30 JUNE 2022

Risks 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 United Kingdom (UK) and 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, and reduced revenues and profitability.

Beyond the South African economy, the issuer also has operations in the UK and several other countries in sub-Saharan Africa. A material deterioration in UK economic conditions or that of the other African countries in which it operates 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, the UK and Europe. Commodity prices and the rand exchange rate 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, this 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 for the macro economy remain uncertain. This uncertainty has also been exacerbated by an increase in global inflation and geopolitical tensions. 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 macroeconomic shock will weigh on global risk appetite and capital flows to South Africa, and will likely result in financial market pressure and rand weakness.

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 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 higher 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 bounceback in activity from the depths of the Covid-19-related contraction, the issuer expects the longer-term trends to remain in place.

Structural changes, including financial and business reforms at state-owned enterprises (SOEs), 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 SOEs remain a significant concern.

1.3 South African political conditions

The issuer currently anticipates that there will be strong political debates around the need to implement measures to balance fiscal sustainability with socio-economic pressures in the country. These will include debates around the 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). 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 South African society. Ongoing political developments may impact private sector investment, foreign investment and business confidence towards South Africa.

The country's high unemployment rate and unequal wealth and income distribution may fuel socio-economic pressure and encourage the 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.

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, could 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 UK economic conditions

Economic activity in the UK is being negatively affected by inflation pressures and its impact on the cost of living. The issuer expects unemployment to increase and higher unemployment and related risk to household disposable income could have negative consequences for the operating environment.

Other risks to the UK economy include:

- that the UK services sectors may be unable to comply with the terms of the Brexit agreement. Failure could result in a slowdown in UK business and consumer confidence, the pound and overall economic activity; and
- a reversal of the policy support that was put in place to cushion households and businesses in the face of the Covid-19 growth slowdown and subsequent inflation pressures.

1.6 Economic conditions in broader Africa

Several other countries in which the issuer operates on the sub-Saharan African continent face macroeconomic risks that could have a negative impact on the issuer's operating environment. These include:

- **Zambia:** Volatility in copper prices and production, drought, inflation, and slow progress on external commercial and official debt restructuring are risk factors that could slow down domestic reforms and the growth momentum domestically. Price pressures across the economy are a risk to consumption growth. There is significant risk to sovereign debt sustainability and associated macroeconomic pressure if reform momentum slows.
- **Nigeria:** A lack of diversification in export and fiscal revenues remains a weakness for the country's outlook. Elections in 2023, low oil production due to operational issues, volatile global oil prices and the high costs of the fuel subsidy pose downside risks to growth and government finances, alongside significant policy uncertainty on the exchange rate and foreign currency convertibility.
- **Ghana:** There are significant risks to sovereign debt sustainability from domestic and external factors. Broad-based inflation, tighter monetary policy and currency pressures pose a risk to growth, alongside austerity measures to stabilise government finances, either domestically driven or prescribed under an International Monetary Fund (IMF) programme from 2023 onwards. The Ghanaian economy is exposed to fluctuations in oil, gold and cacao prices and production volatility. A fall in the price of these commodities has negative consequences for the operating environment and outlook.
- **Namibia, Eswatini and Lesotho:** These economies are particularly exposed to the South African economy and the rand. A severe fall in South African growth and trade, and/or rand weakness will have adverse consequences for their outlooks. All three countries face higher inflation and have to follow the SARB in tightening policy rates, with risks to consumption growth. In addition, a dependency on Southern African Customs Union revenues increases the fiscal vulnerability of all three governments.
- **Botswana:** Persistently high inflation is posing a risk to growth. 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 inflation, policy uncertainty, commodity prices and global economic activity pose a risk to the Mozambican outlook. Insurgent activity in northern Mozambique is another risk factor in the operating environment, particularly in terms of delays to large liquefied natural gas projects coming online.

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 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, securitisation risk and climate risk (physical and transitional risks).

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 balance sheet and earnings to unexpected, adverse movements in interest rates. Foreign exchange risk is the risk of an adverse impact on the issuer'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 or systems, or from external events.

Equity investment risk is the risk of an adverse change in the fair value of an investment in a company, fund or listed, unlisted 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 and 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 those 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 beyond the issuer's control. The issuer performs regular stress tests on its credit portfolios to identify the key factors impacting the credit risk profile in order 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, measuring return on equity (ROE), net income after cost of capital (NIACC) and earnings volatility, 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. 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.

Global developments, manifesting in increased inflation and interest rate outlook, and local developments (e.g. electricity supply constraints) impacting the growth outlook negatively are being monitored closely, and could warrant additional risk responses.

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, 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 on 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, including high levels of poverty and social security needs. Addressing these challenges requires 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 to 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, life insurers and 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, money market securities and capital market instruments.

Furthermore, the operational liquidity management needs of institutions are largely met by their investments in 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, where rand transactions are cleared and settled through registered banks and clearing institutions domiciled in South Africa. FirstRand Bank Limited is one of the major clearing/settlement banks;
> concentration of customer current accounts with the large South African banks;
> the prudential exchange control framework; and
> South African banks' low dependence on foreign currency funding.

These factors contributed to South Africa's resilience during the 2007-2008 global financial crisis, and more recently the liquidity stress sustained during the initial stages of the Covid-19 pandemic. The prudential liquidity requirements instituted post the global financial crisis improved the bank's ability to better withstand the stress. The various liquidity enhancing actions introduced by the SARB also helped to support the markets through this stress.

While the immediate effects of the pandemic have now abated, the issuer continues to monitor and stress test its liquidity access and maintain adequate liquidity buffers. The pandemic has given way to renewed global and local macroeconomic risks as outlined above, which may lead to increased funding costs and/or changes in the composition of available funding pools. These may impact the cost and availability of funding.

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 on and vulnerability to foreign capital inflows, driven by the country's fiscal and current accounts.

The issuer seeks to mitigate exposure to 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 macroprudential 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 committees.

The issuer believes that its level of access to domestic and international interbank and capital markets will allow it 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 materially adverse effect on its financial condition.

Funding and other risks relating to securitisations

Securitisation is the process whereby assets (such as illiquid 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, however investor appetite and pricing will dictate the distribution of lower-rated subordinated tranches. These would typically be retained within the wider FirstRand group. 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 to manage and mitigate rather than 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 or systems, or from external events. It includes, for example, internal and external fraud risk, people risk, information technology risk, information risk, legal risk, business resilience risk, process risk, cyber risk and third-party risk.

The principal operational risks currently facing the issuer are:

> **business resilience risk** due to susceptibility to external factors, e.g. floods, civil unrest and power supply constraints as well as system downtime incidents;

> **cyber risk** (including information security), given the growing sophistication of cyberattacks both locally and globally;

> **technology risk** due to the pace of technology change and increasing digitisation;

> **payment risk** due to the manual nature of certain payment processes, as well as ongoing regulatory and industry payment-related initiatives;

> **vendor risk** due to lack of direct control over external service providers, the potential impact of external events on the group's supply chain and reliance on critical service providers who may pose as single points of failure;

> **people risk** due to changes associated with blended working, social and economic pressures on employees, and the shortage of skilled staff, particularly in the IT environment; and

> **execution, delivery and process management risk** (risk of process weaknesses and control deficiencies) as the business continues to employ a risk-adjusted approach through the blended working model while still trying to grow and evolve the business under tough economic conditions.

Business resilience risk: The issuer's business is subject to its ability to quickly adapt to disruptions while maintaining critical business services.

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 its business continuity strategies including regular review of business continuity plans (including disaster recovery), scenario planning, testing and due diligence on key outsourced vendors. 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.

Cyber risk: 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 cyberattacks 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. Whilst there are ongoing enhancements to information and cyber-security controls, cyber risk remains a key risk focus area for the FirstRand group due to the ever-changing external threat landscape and the growing complexity of the attacks. Risk-based rollout of group cyber capabilities has prioritised the securing of key environments across the cyber-security program focus areas. A defence-in-depth response to the priority threats is applied. This includes various operational practices and continuous monitoring activities across the following key focus themes: data protection, reliable access, attack surface reduction, and secure perimeter and network.

Technology risk: The issuer may suffer a failure of, interruption in or breach of its information technology systems.

The issuer's IT risk refers to the risk associated with the use of, ownership of, operation of, involvement in, influence over and adoption of IT. It consists of IT-related conditions that could potentially impact the business. The issuer's main IT risks include cyber-security, the failure or interruption of critical systems and third-party risk.

The issuer has a high dependency on its IT systems and operations infrastructure in order to conduct its business. The issuer regards these systems as critical to improving productivity and maintaining its competitiveness. 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, 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 prolonged 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.

Payment risk: Amendments introduced via the regulatory environment will fundamentally change how the industry operates.

International and local industry reforms expose the payment system and all participants to increased risk. Consequences of these changes will result in the removal of the current payments system management body and its replacement by a new payments industry body which

may carry a different mandate and function. This will eventually translate to operational changes to systems and processes for the issuer. The issuer's ability to maintain system stability and straight-through processing is vital as the issuer is a systemically important participant in the national payment system. Initiatives are under way to ensure this ability. In-flight initiatives are top priority and delivery targets are closely monitored to ensure minimal negative impact on customers.

Vendor risk: The issuer is exposed to delivery risk from key vendors due of lack of direct oversight over these unrelated parties.

The issuer's business operations are dependent on the products and services provided by key vendors. Accordingly, failure or interruption in the provision of such products and services may adversely affect the issuer's reputation as well as its ability to meet customer requirements and regulatory obligations.

The nature of the services provided by certain vendors requires the issuer to share personal information of its customers, which leads to a security risk where data is shared. Uncertainty over the cyber-security posture of the group's key vendors therefore remains an area of concern, however the use of cyber-security ratings from an external cyber-security rating agency should provide some comfort in this regard going forward.

The sensitivity of key vendors to global supply chain challenges, as well as the issuer's susceptibility to incidents impacting national infrastructure, expose it to additional second order risks.

Given the large number of key vendors that form a critical part of service delivery of the group to customers, the monitoring of service level agreements remains a priority.

People risk: 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.

Execution, delivery and process management risk: The issuer remains susceptible to process and control breakdowns.

In conducting its business the issuer makes use of complex processes and IT systems that support these processes. Due to this complexity, as well as the manual nature of some of the processes, control activities and ongoing redesign to automate, there is an increased risk of failure in delivering of services. Failure could result in financial loss, detriment to clients/third parties, litigation, reputational harm and regulatory risk.

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 operational 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 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 group's equity investment risk portfolio has not been materially impacted by Russia's invasion of Ukraine, since it has no direct exposure to these countries.

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 a rigorous and proactive process to ensure sound product design and pricing, management of the in-force book, and reinsurance agreements to manage catastrophe risk.

2.7 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, material financial losses, operational costs, physical damage, credit risk or loss of reputation that a financial institution may suffer 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. They can be the result of financial exposure, lending/financing, investment or equity interest that may lead to the risk of legal or regulatory sanctions, material financial loss, or reputational damage. The issuer may suffer in any of these areas because of failure by a client or stakeholder organisation 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 or production losses, and subsequently pose a financial, reputational and credit risk to the group.

Climate risk, a subset of environmental risk, is defined as the 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 a single risk function. The issuer's environmental, social and climate risk management framework consists of an outline of programmes and initiatives which are designed to manage and mitigate the following areas and types of environment-related risk.

- **Reputational:** Damage to reputation from association with environmental and social impacts.
- **Market and liquidity:** Higher levels of market volatility, shift in asset valuations, dislocations and shifts in market appetite with regards to 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 for product).
- Legal action, regulatory sanction or reputational damage may occur as a result of the issuer's approach to environmental risk.
- Policy risk due to the impact of new requirements, such as the impact of carbon taxes, prudential requirements and emissions reporting.
- Substitution of a client's existing products and services with lower-emission options, or the unsuccessful investment in new technologies.
- Disruptions to the group's operations, infrastructure, workforce, processes and supply chain may result from acute environmental events.

The issuer has established a climate change policy to guide the businesses' approach to climate change risk, including short-, medium- and long-term commitments to support clients' and society's climate resilience and a just transition to a low-carbon world. This policy is supported by sector-specific policies and limits that address industries that are more sensitive to transition risk, such as thermal coal. The issuer is focusing on adapting strategies across its operating jurisdictions to respond to emerging climate risks and opportunities.

2.8 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, or complete, or 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.

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

The issuer and its regulated banking entities are subject to capital adequacy guidelines adopted by the Prudential Authority (PA). The issuer's subsidiaries in the UK and broader Africa 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 their respective jurisdictions. Failure to comply with the minimum requirements in each jurisdiction could result in loss of banking licences and restrictions being placed on distributions, including dividends and other discretionary payments.

The PA's Regulations relating to Banks (the Regulations), (as amended from time to time) are based on the Basel III framework and specify the minimum risk-based capital ratios. The minimum requirements for the issuer on a consolidated basis are Common Equity Tier 1 (CET1), Tier 1 and total capital of 8.50%, 10.75% and 13.0%, respectively. These minimum ratios exclude the confidential bank-specific individual capital requirements. The issuer aligns its capital targets to the end-state minimum requirements and also considers various other stakeholder requirements.

The Prudential Regulation Authority reduced the UK countercyclical buffer (CCyB) requirement in March 2020 given the Covid-19 pandemic, and this impacted the CCyB requirement for the issuer's UK operations, i.e. Aldermore and FirstRand Bank Limited's (the bank's) London branch. It is expected that the UK CCyB requirement of 1% will be reinstated in December 2022.

2.10 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.

During the Covid-19 pandemic stress period, the PA provided banks with temporary liquidity relief by reducing the minimum LCR requirement during the crisis. Following the recovery in market conditions and funding and liquidity availability, the PA issued *Directive 8 of 2021, Withdrawal of the temporary relief measure related to the liquidity coverage ratio*, to withdraw the temporary relief measures and phase in the LCR requirement as follows:

> 1 January 2022: minimum LCR of 90%; and

> 1 April 2022: minimum LCR of 100%.

The PA introduced the committed liquidity facility (CLF) to assist banks in meeting 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 continues to remain in force. The CLF introduced to assist banks in meeting the LCR has been withdrawn. The PA continues to make the replacement restricted use committed liquidity facility available to all banks, as legislated in the Regulations. The facility is made available contractually for a year, covering the period 1 December to 30 November. The eligible collateral for the facility remains the same and 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%. 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.

2.11 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

The bank remains the rated entity within the group 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 and the risk management framework, as well as the sovereign ratings and the macroeconomic risk profiles for its country of incorporation and those 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/bank's rating at the level of the sovereign rating, a change to the sovereign rating will, therefore, impact the issuer/bank'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 of the ratings of the issuer and/or 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/bank to post additional collateral or take other actions under some of its derivatives contracts and could limit the issuer/bank's access to capital markets.

There can also be no assurance that the rating agencies will maintain the current ratings of the bank/issuer or the ratings 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 materially 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.

2.12 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. 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.

To the extent that SOEs will be licensed as banks in future, competition in the South African banking landscape will increase further. 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 materially adverse effect on the issuer, including on its profitability. Although the issuer's financial resource management approach requires it to price appropriately for financial resources, should competitive forces prevent it from pricing for these resources appropriately it may withdraw from offering certain products, which may also negatively affect its 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 or fail to attract new deposits or retain existing deposits, which could have a materially adverse effect on its operating results, available financial resources, and financial condition and prospects.

2.13 Changing regulatory environment

The issuer is subject to applicable laws, regulations and related frameworks, including the possibility of administrative actions in South Africa and in each of the other jurisdictions in which it operates.

Changes in legal and regulatory requirements in South Africa and the various jurisdictions in which the issuer operates may materially affect the issuer's business, products and services being offered, the value of its assets and its financial condition. Although the issuer works closely with its regulators and continually monitors regulatory feedback and proposals, changes in applicable legal and regulatory requirements and related frameworks or other policies cannot be predicted and are beyond the control of the issuer.

The issuer has devoted significant resources to developing its compliance risk management governance arrangements, which include, among others, policies and procedures particularly in connection with the laws listed below, and subordinated regulatory instruments issued in terms thereof. Nonetheless, its compliance risk management governance arrangements may not be fully effective in mitigating all compliance-related risk exposures, including compliance risks that are unidentified or unanticipated. It follows that any failure arising out of the issuer's compliance risk management governance arrangements may have an adverse effect on its operations and financial condition.

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

- Banks Act, 1990 (Banks Act) and the regulations to that Act – Regulations relating to Banks
- Collective Investment Schemes Control Act, 2002
- Companies Act, 2008
- Competition Act, 1998
- Consumer Protection Act, 2008
- Currency and Exchanges Act, 1933 and Exchange Control Regulations, 1961
- Financial Advisory and Intermediary Services Act, 2002
- Financial Intelligence Centre Act, 2001 (FIC Act)
- Financial Markets Act, 2012
- Financial Sector Laws Amendment Act, 2021
- Financial Sector Regulation Act, 2017
- Foreign Account Tax Compliance Act, 2010
- Insurance Act, 2017
- Long-term Insurance Act, 1998
- National Credit Act, 2005 (as amended) (NCA)
- National Payment System Act, 1998 (NPS Act)
- Prevention and Combating of Corrupt Activities Act, 2004
- Protected Disclosures Act, 2000
- Protection of Constitutional Democracy Against Terrorism and Related Activities Act, 2004
- Protection of Personal Information Act), 2013 (PoPIA)
- Short-term Insurance Act, 1998
- King Code on Governance Principles for South Africa, 2016 (King IV)

- Legislation, listing requirements and rules related to listed instruments on various exchanges
- Protection of Constitutional Democracy Against Terrorism and Related Activities Act, 2004
- Statutory codes of conduct, standards, joint standards and other subordinate legislation issued by, among others, the Financial Sector Conduct Authority (FSCA) and the PA
- Applicable regulations and other regulatory instruments
- Applicable laws in the countries in which the issuer has operations

The issuer is subject to applicable regulatory instruments issued in terms of or related to, among others, any of the above-mentioned laws. The above-mentioned list of applicable laws is not exhaustive but merely indicates that the operations of the issuer are highly regulated.

2.14 Reference rate reform and transition

The London Interbank Offered Rate (LIBOR) is the reference interest rate that underpins trillions of dollars of loan and derivative contracts worldwide. A process is under way to replace these reference rates with alternative risk-free rates. The publication of dollar LIBOR (one-week and two-month tenors); and pound, euro, Swiss franc, and yen LIBOR for all tenors ceased at the end of December 2021. The publication of dollar LIBOR for the remaining tenors will cease after 30 June 2023. Due to the difference in the manner in which the LIBOR rate and alternative risk-free rates are determined, adjustments were applied to LIBOR referencing contracts to ensure economic equivalence on transition to the new alternative risk-free rates.

The following alternative risk-free rates replaced the following LIBORs which the group has exposure to. These alternative risk-free rates differ by region, currency, tenor and basis.

- $ – Secured Overnight Financing Rate (overseen by the Federal Reserve Bank of New York – secured rate)
- £ – Sterling Overnight Index Average (Bank of England – unsecured rate)
- € – Euro short-term rate (European Central Bank – unsecured rate)
- ¥ – Tokyo Overnight Average Rate (Bank of Japan – unsecured rate)
- CHF – Swiss Average Rate Overnight (Zurich-based SIX Exchange – secured rate)

The alternative risk-free rates are structured differently from LIBOR rates and impact the calculations of interest and other payments for transactions and products as follows:

- LIBOR is a forward-looking term rate, which means that the LIBOR rate for an interest period or calculation period is set at the start of that period and payment is due at the end. This provides certainty of funding costs to assist cash flow management. LIBOR also embeds a credit premium (it implies bank credit risk) and a liquidity premium (it includes a premium for longer-dated funds).
- The nominated alternative risk-free rates are mostly backward-looking overnight rates, and designed to be near risk-free, with no premium for term.

The transition of existing LIBOR-based contracts to contracts referencing alternative risk-free rates involve the payment of a spread adjustment and may impact the operation of certain financial covenants. There may also be cash flow and hedge accounting impacts if a mismatch arises on the transition between a loan and a related derivative.

The issuer established a steering committee consisting of key finance, risk, IT, treasury, legal and compliance personnel, and external advisors to oversee its interbank offered rate reform transition plan. The steering committee has put in place a transition project for affected contracts with the aim of minimising the potential disruption to business and mitigating operational and conduct risks and possible financial losses.

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 that apply to investing 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, 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. 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. Exchange controls

Non-residents may freely invest in South Africa, provided that suitable documentary evidence is viewed, and the transaction adheres to certain accepted market principles such as settlement at fair and market-related prices. Similarly, the local sale or redemption proceeds of non-resident-owned assets in South Africa may be regarded as freely transferable abroad provided the prescribed market-related principles alluded to above are adhered to. In certain circumstances where matters may not meet prescribed requirements but there is merit in the transaction, relief may be sought from the SARB with assistance provided by authorised dealers.

The South African Minister of Finance is supportive of exchange controls in South Africa being gradually relaxed. The extent to which the South African government (the government) may further relax such exchange controls cannot be predicted with absolute certainty. However, recent relaxations in respect of capital restrictions on emigrants and the abolishment of previously prohibited structures known as "loop structures" are positive signs of ongoing intended relaxations.

A new draft capital flow management framework is under development by the SARB in conjunction with the South African Minister of Finance and National Treasury. Authorised dealers and other interested parties have been granted the opportunity to provide comments in support of its development. This framework is intended to replace the existing currency and exchanges manual and it is anticipated to be implemented in the near term.

3. Regulatory environment

The issuer is subject to formal regulation, directly and/or indirectly, as the case may be, in both South Africa and in the foreign jurisdictions in which it operates. 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, regulatory requirements and interpretations applying to the sectors, markets and jurisdictions 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 materially adverse impact on the issuer's business, results, financial condition or prospects. Other changes arising from legislation which may require changes to key procedures and the customer value chain may impact the organisation.

Having regard for the large volume and complexities of the legal and regulatory requirements which apply to the issuer's business operations, the issuer, despite having robust systems and processes in place to detect failures, may not be able to detect, in a timely manner, all instances of non-compliance and/or related matters which require improvement. This can also expose the issuer and its operations to regulatory sanctions and additional liability which may have a materially adverse effect on its business, financial condition and/or the results of operations.

From a South African perspective, the implementation of the Twin Peaks system of financial sector regulation in South Africa has resulted in numerous new and/or amended regulatory objectives and legal, regulatory and supervisory requirements. In addition, ongoing amendments to regulatory and supervisory requirements are also informed by the need to align to international best practice requirements. These are informed by, among others, jurisdictional member requirements of international

standard-setting bodies such as the Bank of International Settlements (BIS), including the Basel Committee on Banking Supervision (BCBS), the International Organisation of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors (IAIS). Banks and banking groups in South Africa are governed by a comprehensive legislative framework, most significantly the Financial Sector Regulation Act, read with the Banks Act, which is comparable to similar legislation in BCBS member jurisdictions such as the UK, Australia and Canada.

3.1 Financial stability

The overarching objective of the implementation of Twin Peaks was to make the South African financial sector safer and to ensure that the South African financial system remained effective, insofar as it would serve the interests of all South Africans. In broad terms, important objectives in relation to Twin Peaks are financial stability, the safety and soundness of financial institutions, the fair treatment and protection of financial customers, responsible lending and the combating of money laundering and terrorist financing.

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 cooperation and collaboration among the SARB, the PA, the FSCA, the National Credit Regulator (NCR), the FIC, the Competition Commission, the Financial Sector Transformation Council, the Information Regulator and other authorities, local and abroad, as the case may be, which may result in additional complexities in relation to the issuer's ability to effectively manage its legal and regulatory obligations and related risks. The issuer will continue to work closely with its regulators, both locally and abroad, on matters pertaining to the above.

On 28 January 2022 the President assented the Financial Sector Laws Amendment Bill and it is now an Act, i.e. the Financial Sector Laws Amendment Act 23 of 2021 (FSLAA). One of the key provisions of the FSLAA is that the SARB will become the designated resolution authority with the necessary powers to operationalise an effective resolution regime. The provisions of the FSLAA (including the granting of powers to the SARB to issue resolution standards) will, however, only become operational as outlined in a commencement schedule. This is due to be gazetted by the Minister of Finance in the near future.

The FSLAA introduces critical elements relating to, among others, how to deal with failing banks and other systemically important financial institutions, the ultimate objective of which is to ensure financial stability in South Africa. Aligned to the aforesaid, the creation of the new resolution regime in South Africa requires several amendments to various other acts, including the Financial Sector Regulation Act, the Insolvency Act, the South African Reserve Bank Act, the Banks Act, the Mutual Banks Act, the Competition Act, the Financial Markets Act and the Insurance Act.

FSLAA provides for the establishment of a framework for the resolution of designated institutions (including banks and their holding companies) to ensure that the impact or potential impact of a failure of a designated institution on financial stability is managed appropriately. In addition, FSLAA also provides for the designation of the SARB as the resolution authority and for the establishment of a deposit insurance scheme, including a corporation for deposit insurance and a deposit insurance fund. The FSLAA enables South Africa to meet certain post-2008 global financial crisis international standards, as endorsed by the G20 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 challenges in relation to banks which are considered "too big to fail". The relevant regulatory authorities are continually engaging with industry on matters relating to the intended resolution framework.

The SARB continues to publish discussion papers focusing on the key aspects that will affect and facilitate the implementation of the resolution framework in South Africa, as well as form the basis of secondary legislation and standards.

3.2 Prudential regulation

After the 2007-2008 global financial crisis, various international standard-setting bodies agreed to comprehensive measures and reforms to promote financial stability, and the safety and soundness of financial institutions. The BCBS also issued various new frameworks, standards and requirements for implementation by member jurisdictions. In addition, amendments to existing frameworks, standards and requirements were also proposed. In this regard, the outbreak of the Covid-19 pandemic necessitated revised proposed implementation dates for specified regulatory reforms in South Africa. These reforms include changes to the South African prudential frameworks and/or prescribed requirements in relation to large exposures (LEX) and total loss-absorbing capacity (TLAC) holdings. Proposed Basel III reforms include interest rate risk in the banking book (including disclosure requirements), revisions to the securitisation framework, a revised standardised approach for the credit risk framework, a revised internal ratings-based approach framework and a revised operational risk framework.

The LEX and TLAC holdings frameworks were implemented on 1 April 2022. Proposed implementation dates for the remaining Basel III reforms have been published by the PA in May 2022, with proposed implementation ranging from January 2023 to January 2028.

The Financial Sector Regulation Act introduced the prudential oversight of financial conglomerates[1] in South Africa. The financial conglomerate supervision framework introduces a Tier 3 supervisory approach aimed at financial institutions designated as financial conglomerates and is focused on the contagion risks that manifest in financial institutions involved in banking, insurance, market infrastructure and securities activities.

Prudential standards for financial conglomerates came into effect on 1 January 2022, covering intragroup transaction and exposures, auditor requirements for holding companies, governance and risk management and risk concentration requirements. The draft capital standard is currently subject to field testing by designated financial conglomerates and any financial institution on a voluntarily basis. FirstRand Limited has not been designated as a financial conglomerate but voluntarily participates in the field testing of the draft capital standard and the reporting on the final standards noted above.

1 *A financial conglomerate is a group of companies that operate both in the banking or investment sector and in the insurance sector. It was deemed necessary to supervise these financial groups at the conglomerate level in addition to solo and group supervision.*

3.3 Market conduct regulations

The Conduct of Financial Institutions Bill (COFI) was introduced as another overarching piece of intended legislation to amend and/or repeal certain existing financial sector laws. The COFI Bill is expected to be introduced to Parliament in the latter part of 2022. Once enacted and effective, COFI will, to a large extent, substantially reduce current fragmentation in the South African market conduct regulatory framework, including the introduction of a new licensing regime. COFI provides for the establishment of a consolidated, comprehensive and consistent regulatory framework for the conduct of financial institutions and thereby, among others, aims at streamlining the legal landscape for conduct regulation in the financial services sector; protecting and promoting the fair treatment of financial customers (including through the Treating Customers Fairly principles); promoting innovation and the development of and investment in innovative technologies, processes and practices, as well as trust and confidence in the financial sector; and assisting the SARB in maintaining financial stability. It is envisaged that COFI will consolidate the market conduct regulation of financial institutions and will regulate conduct in respect of credit and payment services. Further developments in relation to COFI are expected towards the latter part of 2022.

Market conduct regulators and/or central banks, as the case may be, in South Africa and in the jurisdictions in which the issuer operates, require the issuer to provide assurance that the fair treatment of customers is embedded within the culture of the group and that due procedures and controls exist to provide demonstrable evidence that the group is treating its financial customers fairly, throughout the product life cycle, from product design to after-sales service.

There are various regulatory developments with themes similar to those covered by the FSCA in some of the jurisdictions in which the issuer operates. In the UK, the Financial Conduct Authority has finalised consultation on a new consumer duty, which will directly impact the issuer's Aldermore business. This will require a higher level of consumer protection and standard of care for retail financial markets, to enable customers to make informed decisions. The principle will also apply to firms that manufacture products for or supply them to retail financial markets, even if there is no direct relationship with end customers.

On 3 July 2020, the FSCA introduced the Conduct Standard for Banks. This regulatory framework enables the FSCA to critically and urgently supervise the market conduct of the banking sector in South Africa, in accordance with its mandate, as outlined in the Financial Sector Regulation Act. The standard became fully effective on 3 July 2021. Non-compliance with requirements imposed in terms of the conduct standards may result in enforcement actions being taken against the issuer, which may include, among others, fines and penalties.

3.4 Anti-money laundering regulations

The South African government identified the combating of financial crime as a policy priority. South Africa has a well-established anti-money laundering (AML) and counter terrorist financing (CTF) legislative framework (which includes but is not limited to the FIC Act). The last mutual evaluation report (MER) issued in relation to South Africa by the Financial Action Task Force (FATF) confirmed that South Africa has a stable political system and has demonstrated commitment to implementing AML/CTF systems, which has involved close cooperation and coordination among a variety of government departments and agencies. This framework has been strengthened by the creation of the Inter-Departmental Committee to coordinate on AML/CTF matters at the national level.

Although South Africa has a solid legal framework, significant shortcomings remain. In particular, South Africa needs to pursue money laundering and terrorist financing in line with its risk profile. This would include proactively seeking international cooperation, detecting and seizing illicit cash flows, and improving the availability of beneficial ownership information. Authorities need to make better use of financial intelligence products. The country should also improve the application of the risk-based approach by obligated entities and supervisors. South Africa has been exposed to a prolonged period of corruption which generated large amounts of proceeds related to corruption and resulted in undermining the integrity and capacity of some key AML/CTF agencies. South Africa is at an elevated risk of being exploited for money laundering as a result of deficiencies identified in its system. Therefore, South Africa is in the FATF enhanced follow-up process for a year following publication of the MER in October 2021. If South Africa does not demonstrate progress at the end of the observation period it may be listed in the FATF's grey list, with negative impact across both the public and private sectors. The decision will be made in February 2023 based on progress demonstrated up until October 2022. However, it has been noted that anti-corruption efforts remain extremely high on government's agenda.

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 of assessing whether appropriate measures and controls are in place to ensure compliance with the provisions of the FIC Act and related regulations and regulatory requirements. The PA, as a financial sector regulator, is by law required to cooperate and collaborate with the FIC when performing its functions in terms of the FIC Act.

The issuer has implemented a financial crime framework which includes AML and CTF policies in its risk management and compliance programme and takes measures to effect continual improvement in its processes to address its money laundering and terrorist financing risks.

3.5 National Credit Act (as amended)

The NCA came into effect on 1 June 2007. In terms thereof, interest rates, costs and fees which retail banks and other credit providers may charge are regulated. By way of example, maximum prescribed interest rates which may be levied in terms of 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 credit agreements, in addition to the capital amounts and interest charges. These relate to initiation fees, monthly service fees, default administration costs and collection costs. Initiation fees for arranging credit agreements may not exceed the maximum prescribed amount, whilst monthly service fees in relation to the administration of credit agreements are capped. Administration charges must be levied in accordance with the Magistrates' Courts Act, 1944, and collection costs are also limited. The NCA also prescribes matters in relation to the registration of specified credit providers, which has the effect that credit agreements entered into by credit providers who are in non-compliance with registration requirements will be *void ab initio*. In addition, credit agreements which contain unlawful provisions in contravention of the NCA could potentially be rendered *void ab initio*.

The NCA has strict provisions in relation to the prohibition of selling and collecting outstanding debts which have prescribed. This means that credit providers can no longer collect on loans where no legal actions were taken and no payments were received for a period of more than three years. This applies to all loans which were in existence as of 13 March 2015 as well as to new loans granted thereafter. The said provisions may therefore impact on the ability of banks to collect existing non-performing and written-off loans which have prescribed. In addition, affordability assessment regulations, which came into effect on 13 March 2015, and credit providers' commitments to combating over-indebtedness, are important considerations for the NCR. These matters form part of considerations in relation to the registration of credit providers, in terms of the NCA. The National Credit Amendment Act, 2019 was promulgated during August 2019. The effective date has not yet been proclaimed by the Minister of Trade and Industry. The amendment in the Act includes, among others, a debt intervention measure to assist consumers to whom insolvency measures are not accessible in practice. This process will involve the extinguishment of debt, where applicable. The NCR will implement a debt intervention process and refer matters to the National Consumer Tribunal to adjudicate on debt intervention applications. Debt counsellors will be 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 adjustment of credit risk appetites by the credit industry.

3.6 Companies Act

The Companies Act 71 of 2008, as amended (the Companies Act), provides for, among others, the incorporation, registration and management of companies, capitalisation of profit companies, shareholder provisions, accountability and transparency, corporate finance, directors' 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.

A new draft of an amendment bill to the Companies Act (the Companies Amendment Bill) was published for public comment on 1 October 2021. According to the explanatory memorandum published together with the bill, the three broad categories of policy objectives sought to be addressed by the proposed amendments to the Companies Act are (i) ease of doing business, (ii) achievement of equity as between directors and senior management on the one hand and shareholders and workers on the other and (iii) efforts to counter money laundering and terrorism. The changes in the bill include, among others, provision for (i) the preparation, presentation and voting on companies' remuneration policies and directors' remuneration implementation reports, (ii) the concept of a "true owner" (in essence the natural person who is the ultimate and true owner and last person in the chain of holders of a specific security in a company, who can direct the registered holder or for whose benefit the securities exist) and the filing of a copy of the company's securities register and register of disclosure of beneficial owner with the Companies and Intellectual Property Commission and (iii) the presentation and approval of the social and ethics committee report at a shareholders' meeting.

The period for public comment closed on 31 October 2021. A revised draft of the bill is awaited.

3.7 Consumer Protection Act

The Consumer Protection Act, 2009 (CPA) came into effect on 1 April 2011. The CPA gives consumers the right to demand quality service and requires full disclosure of the price of goods and services. The CPA also protects consumers against false, misleading and deceptive representations. The CPA fundamentally changed the way in which business is conducted in South Africa. It requires businesses to transform the way in which they interact with consumers and also demands that consumers are treated in a fair, reasonable and honest manner. Although credit agreements which are governed by the NCA do not fall within the ambit of the CPA, goods or services which were provided in terms of credit agreements are not excluded from the ambit of the CPA. The CPA allows certain industries to be exempt from specific provisions of the CPA where there are existing consumer protection regimes in place in respect of those industries. By way of example, banks are exempted from section 14 of the CPA, which deals with fixed-term contracts. In this regard, concerns were previously expressed by the banking sector that the said provision would adversely impact fixed-term deposits and thus bank customers' abilities to withdraw such deposits early. Amendments to the CPA are required to adequately and appropriately provide for matters relating to the manner in which business is conducted in a digital environment.

3.8 Protection of Personal Information Act

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 during 2013 and all private and public

bodies were required to ensure compliance with the provisions of PoPIA by 1 July 2021. 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". PoPIA also provides for the establishment of an Information Regulator.

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 subsidiaries of the issuer can be considered 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: 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).

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

(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 and reasonable technical and organisational measures must be implemented and maintained to prevent loss of, or damage to, 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. Data subjects can also request the correction or deletion of personal information which is inaccurate, irrelevant, excessive, out of date, incomplete, misleading or obtained unlawfully.

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 that material risks can emerge if the responsible party does not adhere to the corresponding requirements and provisions. Such risks can attract sanctions for the responsible party, which includes a fine, imprisonment, or both a fine and imprisonment, for a period of no longer than ten years, or alternatively may lead to an administrative fine. Security compromises can also result in irreparable reputational damage. Currently the maximum fine that can be issued is R10 million.

3.9 National Payment System Act

The draft amendments to the NPS Act have been included under the COFI Bill as consequential amendments to address certain urgent matters. The remaining NPS Act amendments will be effected through the Financial Services Laws General Amendment Bill (Omnibus Bill) at a later date. The drafting process, led by National Treasury, is ongoing, and the bill is yet to be published for public comments before tabling in Parliament. The draft bill is discussed in a policy paper titled *Review of the National Payment System Act 78 of 1998*, published by National Treasury and the SARB for public comment during late 2018. Amendments to the NPS Act are expected to determine how the payments industry will be regulated, particularly to give effect to Twin Peaks and to include non-bank participants in licensing, supervision and regulation. As such, payment services will fall within scope of the FSCA and will be included in the COFI Bill. It is also expected that the SARB's National Payment System (NPS) department will continue to work closely with the FIC on relevant requirements emanating from recommendations issued by the FATF in respect of FATF Recommendation 16. Non-adherence or non-compliance with payments-related requirements by the issuer can be expected to result in administrative and enforcement actions taken against the issuer.

In addition to proposed amendments to the NPS Act, it is expected that further changes will impact the South African payments landscape and how it operates. The role and operating model of the Payments Association of South Africa (PASA), the body recognised by the SARB as a payment system management body, is currently being reviewed. The review is expected to result in elements of current payment clearing house rules being incorporated in regulations and/or operating standards. PASA has been tasked by the SARB to develop, together with the broad payments industry stakeholders, a proposed design for a future payments industry body, with the aim of being more inclusive of the non-bank payments community. The Banking Association South Africa (BASA) embarked on a programme to define and outline a payments modernisation journey for South Africa and the role of banks in that journey.

Banking sector in South Africa

Similar to other jurisdictions, prior written approval from the PA, on application, is required for both local entities and banking institutions from other countries to conduct the business of a bank in South Africa. In this regard, and according to the latest available information, which is subject to change, the South African banking sector comprises, among others, locally controlled banks, foreign controlled banks, branches of foreign banks and foreign bank representatives. Other deposit-taking institutions include mutual banks and co-operative banks.

The South African banking system is well developed and effectively regulated. According to information published by the PA in its 2021/22 annual report, South Africa's banking sector is still dominated by the five largest banks which collectively held approximately 89.8% of the total banking sector assets at 31 March 2022. Local branches of international banks accounted for approximately 6.0% of the banking sector assets and other banks for approximately 4.2%. Although the South African banking sector remains well capitalised, funded, regulated and managed, it is highly exposed to South African macroeconomic conditions and it will be impacted by negative macroeconomic developments.

South African Reserve Bank

The SARB is, as South Africa's central bank and macroprudential regulator, responsible for, among others, contributing towards the achievement and maintenance of a stable financial system, protecting and enhancing financial stability, and restoring and maintaining financial stability in relation to systemic events. The SARB has a long and proud history of serving, chairing and actively contributing to the work of international and regional bodies, organisations and standard-setting bodies. In this regard, the SARB is represented on prominent regional and international forums such as the G20, the IMF, the World Bank, the Financial Stability Board (FSB), the BIS, the BCBS, the IAIS, the Committee on Payments and Market Infrastructures, the IOSCO, the FATF, the International Association of Deposit Insurers, the Committee of Central Bank Governors, the Southern African Development Community, the Association of African Central Banks, the Common Monetary Area and Brazil, Russia, India, China and South Africa (BRICS).

Prudential Authority

The South African PA, which is a juristic person operating within the administration of the SARB, commenced its mandate on 1 April 2018. The SARB had, prior to the implementation of South Africa's Twin Peaks regulatory framework on 1 April 2018, performed its function as banking regulator through its bank supervision department. The PA is responsible for, among others, the licensing of banks and the prudential regulation and supervision of banks, banking groups (consolidated supervision), licensed insurers and financial conglomerates in South Africa. The PA is responsible for the prudential regulation and supervision of the issuer in accordance with applicable financial sector laws, on a solo and consolidated basis. The PA's duties and responsibilities include the promotion and enhancement of the safety and soundness of financial institutions in support of the SARB's mandate of achieving and maintaining financial stability.

The PA has extensive regulatory and supervisory powers which, among others, oblige banks to furnish certain prescribed financial and risk returns to it, to enable it to monitor compliance with the various prudential and other regulatory requirements imposed on banks in terms of the Banks Act, 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 PA is also a member of the Sustainable Insurance Forum, the BCBS, the FSB and the Network for Greening the Financial System.

The PA has memoranda of understanding with other regulators in South Africa, such as the FSCA, the NCR, the FIC and the SARB. It is also responsible for the supervision of compliance by specific institutions, with AML/CFT legal and regulatory requirements. The global AML/CFT standard-setting body, the FATF, of which South Africa is a member, assessed South Africa during 2019. The final report in relation to this assessment was published during October 2021.

In addition to the above, the BCBS monitors the timely adoption of standards by its members and assesses its member jurisdictions' consistency with the Basel framework through the committee's regulatory consistency assessment programme (RCAP). The objective of the RCAP is not to assess individual banks, but rather to assess the consistency of domestic regulations with Basel standards and prescribed phase-in periods. South Africa was also subjected to an RCAP assessment, which commenced during the latter part of 2014. The RCAP for South Africa focused on both risk-based capital and Basel III standards on liquidity. The outcome of South Africa's assessment was published on 15 June 2015 and the local implementation of the Basel III framework (including Basel 2 and 2.5) was found to be compliant with the Basel standards. Information is available on the PA's website, setting out the revised proposed implementation dates for the Basel III post-crisis reforms.

National payment system department

The SARB's NPS department has responsibility for the national payment system, which it operates, regulates, supervises and oversees. It is also responsible for related policymaking. Since the NPS department regulates, among others, payment and settlement systems, the issuer's conduct in relation to payments and related services is also regulated, directly and indirectly, by the NPS department.

Financial Sector Conduct Authority

The FSCA is, similar to the PA, the other pillar of South Africa's Twin Peaks financial sector regulatory architecture (the first being the PA). The FSCA is the South African market conduct regulator of financial institutions which are licensed in terms of South African financial sector laws. These include, among others, banks, insurers, financial service providers, managers of collective investment schemes and market infrastructures. The FSCA's mandate includes enhancing and supporting the efficiency and integrity of financial markets, assisting in maintaining financial stability, protecting financial customers by promoting their fair treatment by financial institutions, and promoting and providing financial education to financial customers to ensure that these customers are adequately informed, and that the financial system is more efficient. The FSCA expects all licensed financial institutions to act with integrity and to treat their customers fairly. Furthermore, the FSCA expects financial institutions to have a culture that is

conducive to consumer protection and market integrity, supported by a conduct risk framework. On 3 July 2020, the FSCA introduced the Conduct Standard for Banks. This regulatory framework enables the FSCA to critically and urgently supervise the market conduct of the banking sector in South Africa, in accordance with its mandate, as outlined in the Financial Sector Regulation Act. The standard became fully effective on 3 July 2021.

Various aspects of the issuer's market conduct are regulated by the FSCA and it works closely with, among others, the PA and the NCR on various matters.

General

The issuer's relationships with its regulatory authorities are largely managed by a dedicated group compliance risk management function and FirstRand's Public Policy and Regulatory Affairs Office. The issuer views its relationships with its regulators as being of the utmost importance. The issuer is a member of BASA, 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 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. Much effort and numerous resources are dedicated in a cost-efficient manner in order to reap maximum benefits from the implementation of best practice and the resultant enablement of its global business activities.

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