GT Ferreira Chairman

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CHAIRMAN'S

STATEMENT

It is with more than a touch of sadness that I am writing my 10th and last Chairman's statement this year. However, since I had occasion to celebrate both my 60th birthday as well as my 10th anniversary as Chairman of the FirstRand Group during 2008, I believe it to be the opportune time to pass on the baton.

As a group we are incredibly fortunate to have a person of the calibre of Laurie Dippenaar to take the baton from me. Laurie was one of the founders of RCI/RMB and has been intimately involved in the creation and growth of the FirstRand Group. He was CEO for the period 1998 to 2005 and is, in the FirstRand board's opinion, the ideal person to run the next lap of the relay for us as Chairman of the Group.

There were times during this past year when I wished that I had already handed him the baton at the end of 2007, however, on reflection, I am actually glad that I am offering him the baton after, and not before, the most difficult year in our short history. In fact, I do not think I would be exaggerating if I had said "the most difficult year for the banking sector in living memory" especially since most people with any firsthand experience of 1929 today probably have very few memories left. While the year/s ahead will certainly not be easy, Laurie is inheriting a very stable and diversified financial services group, with excellent management, lots of experience and enormous potential.

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WHY DID THIS HAPPEN?

It appears as if two of the horsemen of the Apocalypse namely "Leverage" and "Greed" initially entered the race under the banner "this time it is different". They thus started running the race at breakneck speed, creating sophisticated collateralised debt obligations as if there was no tomorrow and pushed the US mortgage market (as well as other securities markets) to unprecedented heights. Just when it seemed as if this time these two horsemen and their horses would never tire, two new horsemen namely "Lack of Liquidity" and "Fear" entered the race and proved, once again, that cycles are never different. If you spend too much energy during the first part of the race you never have the stamina to finish well. When last seen "Lack of Liquidity" and "Fear" were leading by a mile and are likely stay ahead for the foreseeable future.

Since my statement in last year's annual report, a multitude of US and European banks have failed and Freddie Mac and Fanny Mae have been rescued by the US Government. Deleveraging on a massive scale has been the theme of the last 12 months and should probably be regarded as one of the key determinants of the depth and duration of the current cycle and going forward will have a significant impact on global growth.

Despite the deployment of hundreds of billions of dollars of liquidity into the global banking systems, financial markets remained extremely fractious and I believe we are likely to experience ongoing financial turbulence and economic strain for an extended period of time. In fact as I write this year's statement Bear Sterns is long gone, Merrill Lynch has been acquired by Bank of America and Lehman Brothers has filed for bankruptcy – great names of investment banking have become victims of a relentless meltdown of markets.

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WHAT HAVE WE LEARNT OVER THE LAST 12 MONTHS?

I am sure that by the time you read this document there would have been hundreds of articles about what went wrong and why it went wrong and I do not want to bore you with my lengthy version of the "truth". However, for what it is worth, the following are a few of my own observations of what happens to the value of assets in the financial markets when things go wrong and liquidity dries up:

- it is not the price of credit that matters but the availability of credit;
- it is not the quality of the asset that matters but the quality of the holder of the asset;
- it is not the realistic value (NAV) of the asset that matters but the market value of the asset;
- it is not the strongest holder of the asset that determines the market value but the weakest holder (fire sale); and
- it is not what you think the asset is worth (even if you are correct) but what someone else (the buyer) thinks the asset is worth.

So beware the third horseman, ie "lack of liquidity" – he is, in my opinion, probably the most dangerous of them all.

FINANCIAL PERFORMANCE

Someone somewhere once said that "success is never permanent and failure is rarely fatal". I believe it was said by a rueful coach in the context of his baseball team which had finally, after a long successful run, hit a bad patch.

I feel a bit like that coach. FirstRand records ten years of operations this year, and nine of those ten years can only be described as successful. The Group consistently delivered superior returns to its shareholders (NAV and ROE) and I believe fulfilled much of its potential. However, there is no doubt that the year under review did not match our previous performances with normalised earnings growth significantly below the Group's target. Returning briefly to our rueful coach it is important to acknowledge that although profoundly disappointing this under-performance is not, however, fatal. The franchise remains in good shape, testament to the strength of its diversified earnings base, which withstood some big hits in the offshore equity trading business. The Group still made R10.4 billion of profit and will return R4.6 billion in dividends to its shareholders.

If we analyse the reason for this year's "under-performance" part of it lies in the base effect of last year's 32% earnings increase, which was driven by a stellar performance from RMB, particularly the trading businesses. It is one of these businesses that in the year under review did a complete reverse and negatively impacted RMB and the Group's earnings, showing a massive R1.4 billion loss.

Looking at the overall financial performance of the Group; FirstRand's results reflect the resilience of its diversified portfolio of banking and insurance businesses. It allowed the Group to post earnings of R10.4 billion which on a normalised basis were 8% lower than the exceptional performance of the year to 30 June 2007.

Normalised net asset value increased 11% to R51.6 billion partly as a result of the R0.9 billion profit on VISA shares, but mainly due to the strong profitability of the Group. This also allowed us to maintain our 2007 dividend. The ROE of 22% was respectable given market conditions.

These results were achieved within an operating environment characterised by high inflation and high interest rates, which placed significant pressure on consumers and resulted in a dramatic increase in bad debts in the retail lending books of banks. The absolute level of our bad debts highlights the severity of the current cycle, but they are in line with expectations and are priced for.

Looking at the performances of the individual franchises; RMB's earnings were significantly impacted by the losses in its Equities Trading division, showing a 20% year on year decline. However, RMB's diversified portfolio mitigated to some extent the under-performance of this division, with the Investment Banking, Private Equity and FICC divisions showing excellent growth of 64%, 76% and 37% respectively.

WesBank showed a decrease of 38% in normalised earnings as a result of higher bad debts and the write off of certain operating assets in its Australian business which is in the process of being sold. WesBank has navigated several bad debt cycles in the past and has demonstrated that it is a profitable business through the cycle.

FNB posted solid growth in earnings and despite a slowdown in the top line continued to extract efficiencies, taking a further 2.9 percentage points off its cost to income ratio.

Momentum Group posted growth in normalised earnings of 20%, an excellent performance given the tough conditions facing the insurance industry. It reflects the incredible resilience of its business model and the benefits of its conservative capital management strategy.

Before I analyse the specific situation of our Equities Trading division, I would again like to briefly refer you back to my thoughts on the current scenario in global financial markets, as this does provide some real context to our experience.

How does this relate to our own international equities trading book? Well the losses occurred at a time of extreme dislocation and disruption in global equity markets and were compounded by the "arbitrage portfolio" being long of small and mid sized international equities while short of major indices. The hedge with the indices proved ineffective as investors moved from illiquid stocks to the highly liquid indices with the result that money was lost on both sides of the portfolio.

During the first half of 2008 it was decided to aggressively de-risk the exposure to this portfolio as the markets kept worsening and whilst there has been significant economic cost to this process, especially as a result of a lack of liquidity, hindsight shows it was exactly the right decision in these uncertain times.

We have consistently said that we are satisfied our risk processes were robust and capital allocation to these activities was within normal thresholds. These losses occurred as a result of feeding incorrect assumptions into the risk models and poor market judgement by management. It can be argued that "Lack of Liquidity" (the third horseman) in the markets magnified these losses, but we also have to recognise that the appetite for risk was just too big in this portfolio.

Obviously there is also the issue of "accountability" with regards to these mistakes. Our philosophy on this issue is that we take a view on our intellectual capital across entire careers; people are not punished on a single mistake as this kills innovation, which has been a cornerstone of RMB and FirstRand's success. Just because there have been no en masse firings does not mean that internally we did not embark on some heavy introspection. On behalf of the management and board I would like to apologise to all our shareholders for this hiccup and assure them that the lessons learnt will not easily be forgotten. We collectively have to take responsibility for what happened.

Whilst assessing the Banking Group's performance there is another issue I would like to address. That is the issue of bad debts.

The retail lending operations of the Banking Group were severely impacted by the dramatic increase in bad debts. This was as a direct result of the severity of the current credit cycle and is not a reflection of the structural asset quality issues we are seeing in other parts of the world such as the sub-prime markets in the USA.

What we have seen in this recent reporting period is that FirstRand's bad debts are in line with its peers. At the time of our interim results the Group was somewhat punished by the market for seemingly having worse bad debts than the rest of the domestic banks. In hindsight it is clear that it was purely a timing issue, both in terms of our reporting cycle and the dominance of the asset book of WesBank. Vehicle finance is one of the first lending books to be negatively impacted in a downward credit cycle. If we do a proper comparison now, we can see that on a product comparative basis, the Group is in line with its peers, if not better positioned in certain product categories.

PROSPECTS

In terms of our growth prospects, we still believe that despite the fact that the Group has high market shares in sections of the South African market, there are still opportunities to grow organically, particularly in the corporate and investment banking segments.

Whilst we believe that the interest rate cycle has peaked, it is difficult to predict, or time, the end of the current credit cycle. In the coming year we will continue to experience high bad debts, particularly in homeloans, and the required de-leveraging by the South African consumer will constrain overall growth. In addition, there is heightened risk of corporate defaults particularly in those sectors exposed to the consumer.

Against this background FirstRand's key focus therefore remains on maintaining a robust balance sheet and protecting the operating franchises to weather the current cycle, thus ensuring the Group is positively positioned for the future upturn.

We continue to pursue our strategy of seeking growth in markets outside South Africa and we are actively looking at exciting opportunities in Africa, Brazil and India.

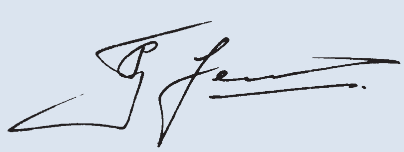
Given the current uncertain environment, particularly in global markets, we do not believe it is appropriate to provide short term earnings growth targets until stability returns. However, we remain committed to delivering superior real returns to shareholders in the medium to long term.

PERSONAL THANKS

I would like to thank my board of directors, our shareholders, our clients and, last but not least, our management and staff for the incredible support you have given me and the FirstRand Group over the last ten years. I trust that you shall continue to support the new Chairman and the Group in a similar fashion over the next decade.

I regard myself as having been incredibly privileged and I am also very, very proud and honoured to have been Chairman of an organisation with such a remarkable spirit and "can do" attitude. As a shareholder, I shall follow your progress with great interest. Good luck and goodbye.

In conclusion, I would like to leave all of you with some advice from Donald Keough, a former president of the Coca-Cola Company. In his book "The Ten Commandments for Business Failure" he explains that the first (and most important) of these commandments for business failure is when a company "quits takings risks". So, while it is natural (and correct) for a company to be more careful in turbulent times, especially when they have recently suffered heavy losses, one should always remember that a company is destined to mediocrity unless it is prepared to accept the risk that comes from trying to outperform the competition. Remember "Fear of failure guards the portals of possibility" (anon).



GT Ferreira
Chairman