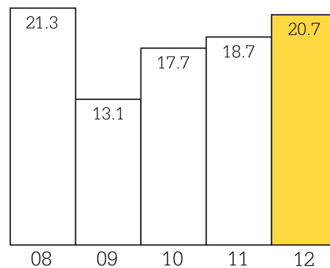
The Group believes that ROA is **the key metric** for assessing management's ability to provide **real returns** to shareholders.

JOHAN BURGER / COO & CFO

KEY PERFORMANCE INDICATORS

FirstRand uses the key financial performance indicators below to measure the Group's performance against its core purpose to create long-term franchise value.

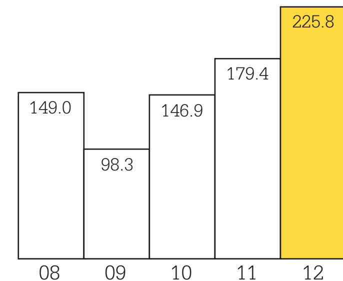
Normalised ROE (%)



Comparatives prior to 2011 are for banking activities pre-unbundling of Momentum.

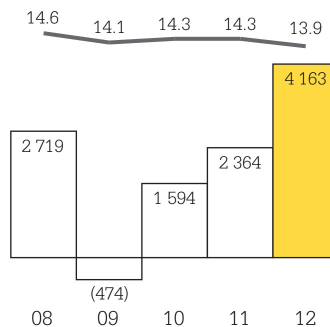
When the Group analyses ROE, it also takes into account the relationship between ROA and gearing levels. The Group's long-term ROE target range is 18% to 22%.

Normalised EPS (cents)



The Group targets earnings growth of 3% to 5% in excess of nominal GDP growth over the long-term, as this will vary from year-to-year dependent on economic cycles.

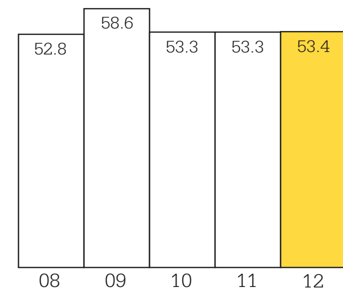
Net income after cost of capital (NIACC)



Comparatives prior to 2011 are for banking activities pre-unbundling of Momentum.

Growth in NIACC is the Group's internal benchmark for assessing performance.

Cost-to-income ratio (%)

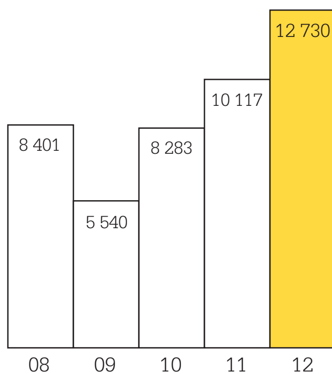


The Group monitors efficiency through the cost-to-income measure. Whilst the Group views the cost-to-income ratio as an outcome rather than a target, it recognises that balancing revenue growth and cost growth are key to value creation.

OVERVIEW OF RESULTS

The primary results and accompanying commentary are presented on a continuing normalised basis as the Group believes this most accurately reflects its economic performance. The continuing normalised operations specifically exclude the profit on unbundling of Momentum, the earnings contribution of Momentum, the profit on disposal of OUTsurance, as well as the earnings contribution of OUTsurance for the comparative periods.

Group continuing operations – normalised earnings (R million)



FOR THE 12 MONTHS TO JUNE 2012 FIRSTRAND ACHIEVED **26% GROWTH** IN **NORMALISED EARNINGS** TO **R12.7 BILLION** AND A NORMALISED **ROE OF 20.7%.**

OTHER KEY RATIOS ARE INDICATED IN THE TABLE BELOW.

Group key ratios

	Year ended 30 June	
	2012	2011
Normalised earnings (R million)	**12 730**	10 117
Normalised return on equity (%)	**20.7**	18.7
Diluted normalised earnings per share (cents)	**225.8**	179.4
Return on average assets (%)	**1.73**	1.49
Normalised credit loss ratio (%)	**1.08**	0.93
Normalised net asset value per share (cents)	**1 142.4**	1 044.0
Dividend per share (cents)	**102.0**	81.0
Cost-to-income ratio (%)	**53.4**	53.3
Tier 1 ratio (%)	**13.2**	15.0
Core Tier 1 ratio (%)	**12.3**	13.9
Net interest margin (%)	**4.92**	4.58
Normalised gross advances (R billion)	**536**	475

A breakdown of earnings from each operating franchise is shown below.

Sources of normalised earnings

for the year ended 30 June

R million	2012	% composition	2011	% composition	% change
Total FNB	**6 673**	**53**	5 327	53	25
– FNB South Africa	**6 157**	**49**	4 787	47	29
– FNB Africa	**516**	**4**	540	6	(4)
RMB and GTS	**3 646**	**29**	3 842	38	(5)
WesBank	**2 599**	**20**	1 862	18	40
Corporate Centre and consolidation adjustments	**(702)**	**(6)**	(711)	(7)	(1)
FirstRand Limited (company)*	**789**	**6**	98	1	>100
NCNR preference dividend	**(275)**	**(2)**	(301)	(3)	(9)
Normalised earnings from continuing normalised operations	**12 730**	**100**	10 117	100	26

* *Included in this amount is the consolidation adjustment of R818 million to bring the IFRS 2 costs from cash settled in the underlying subsidiaries to equity settled at the Group level resulting in zero impact on overall group results. The significant increase in this amount from previous years is due to the 33% increase in the FirstRand share price year-on-year.*

CONSISTENT STRATEGIES DRIVING FINANCIAL PERFORMANCE

The Group's strong financial performance was driven by its focus on specific strategies which are outlined in the table below. Further analysis on these strategies and their impact on financial performance follows.

		Strategies
Earnings resilience (income statement)		• improve diversification; • grow the client franchise businesses; • improve margins; • reduce the contribution from trading activities; and • cost containment.
Balance sheet strength	Assets	• improve the balance between corporate and retail lending activities; • shift the retail asset mix; and • improve asset quality.
Balance sheet strength	Liabilities and equity	• grow the deposit franchise; and • maintain ROEs and the Group's strong capital position post-Basel III.
Performance management		• maintain ROE within target range; and • consistently improve the premium above cost of equity (NIACC).

IMPROVE DIVERSIFICATION

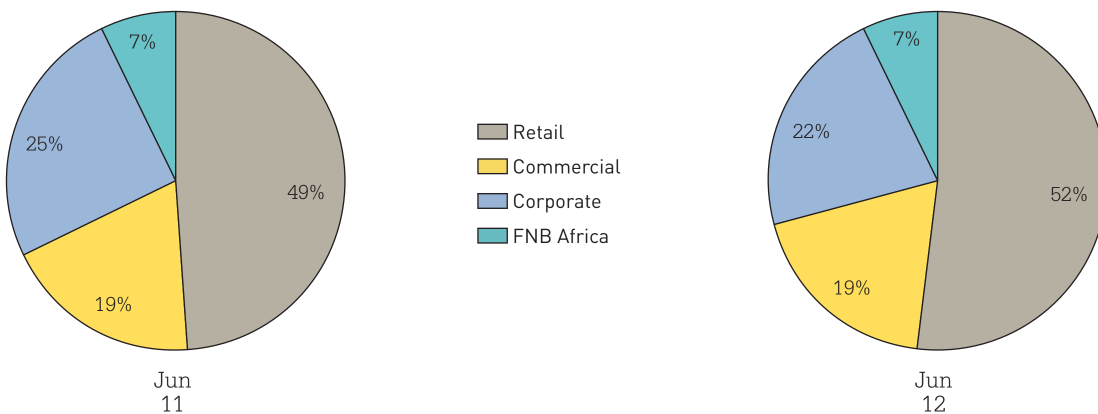
FirstRand's portfolio of franchises provides good diversification. Although FNB South Africa remains the largest contributor to earnings, the Group believes its portfolio represents the appropriate mix of business activities, at both a franchise and segment level.

Franchise diversification

Based on PBT, excluding Corporate Centre and consolidation adjustments.

The shift in segment diversification in the year under review is a reflection of the macro economic conditions which favoured the retail and consumer businesses of FNB and WesBank whilst conditions in corporate and investment banking remained subdued. This resulted in the overall contribution from retail increasing to 52% of gross revenue.

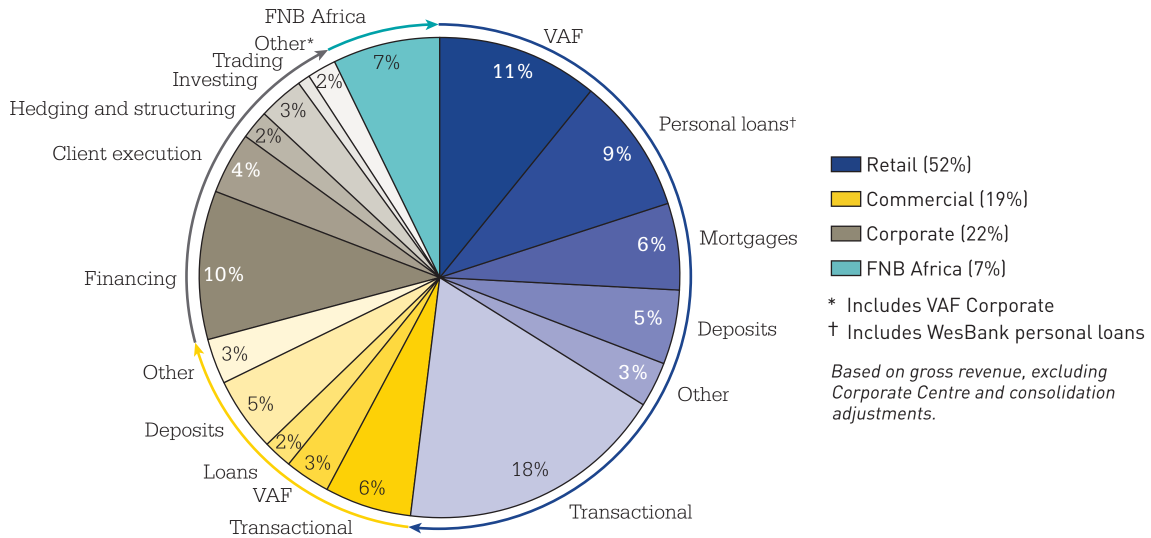
Segment diversification



Based on gross revenue, excluding FNB Other and support.

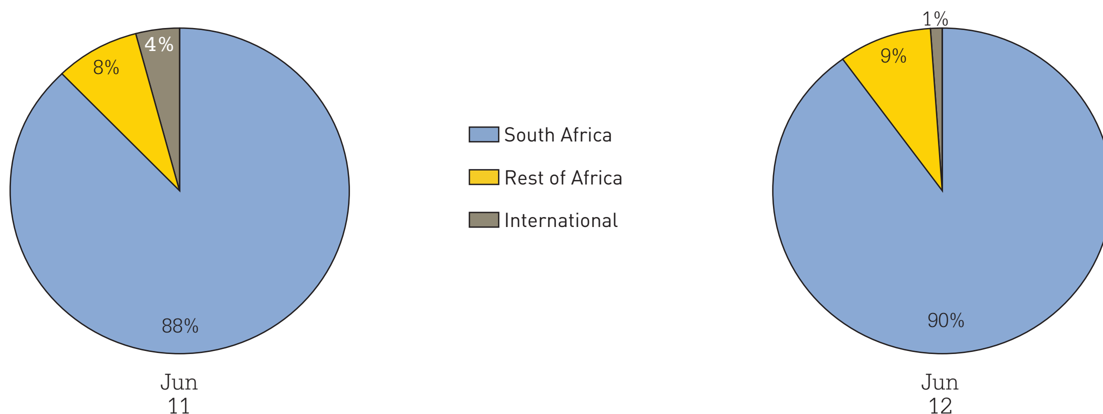
The Group's product diversification across the various segments provides further underpin to reduced earnings volatility and mitigates against reliance on specific revenue streams.

Product diversification



The Group remains concentrated in its domestic market and therefore believes it is important to seek geographic diversification albeit within a disciplined strategic framework. FirstRand's approach is to limit dilution of the return profile, therefore, a significant shift in geographic diversification will take time.

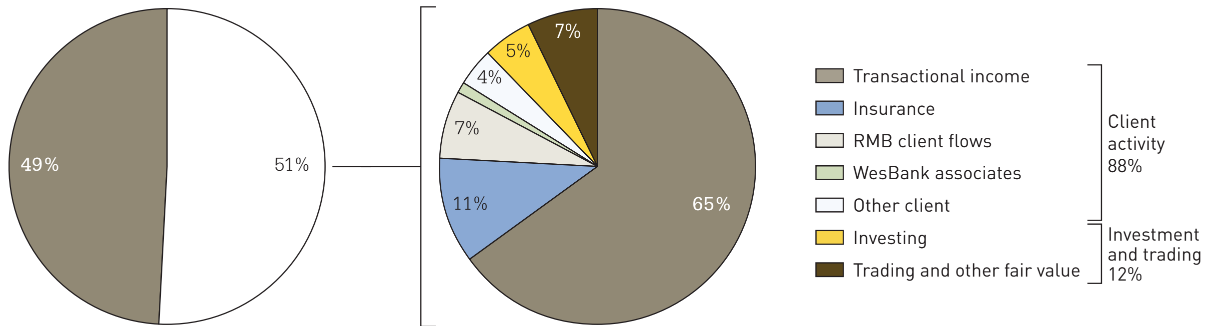
Geographical diversification



Based on gross revenue, excluding Corporate Centre and consolidation adjustments.

GROW CLIENT FRANCHISE BUSINESSES AND REDUCE CONTRIBUTION FROM TRADING ACTIVITIES

As can be seen from the chart below, interest income now represents 49% of gross revenue (2011: 43%), reflecting the Group's focus on higher margin business and appropriate pricing strategies. The Group's focus on growing its client businesses has resulted in 88% of NIR derived from client activities with only 6% from trading and investment, if NII is included 94% of gross revenue emanates from the client franchises.



Gross revenue breakdown

NIR breakdown

NII before impairments

Non-interest revenue (NIR)

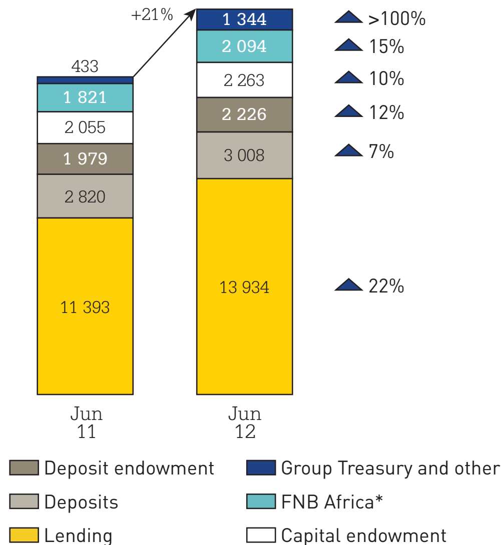
The higher level of revenues generated from client activities reflects the change in strategy in 2009/2010 in the investment bank. The chart below demonstrates the significant shift in RMB's earnings since 2008 as it focused on growing its client franchise.

Pre-2008

2012

IMPROVE MARGINS

Historically banks' ROE's were flattered by gearing levels rather than the generation of appropriate ROAs. The Group's margins are now benefiting from a deliberate strategy to reprice appropriately for risk and originate a larger proportion of higher margin new business, such as VAF and unsecured.



* *Reflects statutory view.*

	%
June 2011 normalised margin	4.58
Accounting mismatches	0.09
	4.67
Capital and deposit endowment	(0.06)
Advances	0.22
Changes in balance sheet mix	0.18
Asset pricing	0.04
Liabilities	0.10
Changes in balance sheet (deposits)	0.04
Changes in balance sheet (capital)	0.02
Term funding cost	0.07
Deposit pricing	(0.03)
Interest rate risk hedges	(0.01)
June 2012 normalised margin	**4.92**

Although advances still dominate net interest income (NII), the Group's deposit franchises are increasingly contributing to NII growth and the improvement in net interest margin (NIM).

THE GROUP'S MARGINS ARE NOW BENEFITING FROM A **DELIBERATE STRATEGY** TO REPRICE APPROPRIATELY FOR RISK AND ORIGINATE A **LARGER PROPORTION OF HIGHER MARGIN** NEW BUSINESS.

MANAGING IMPAIRMENTS WITHIN THE LONG-RUN AVERAGE

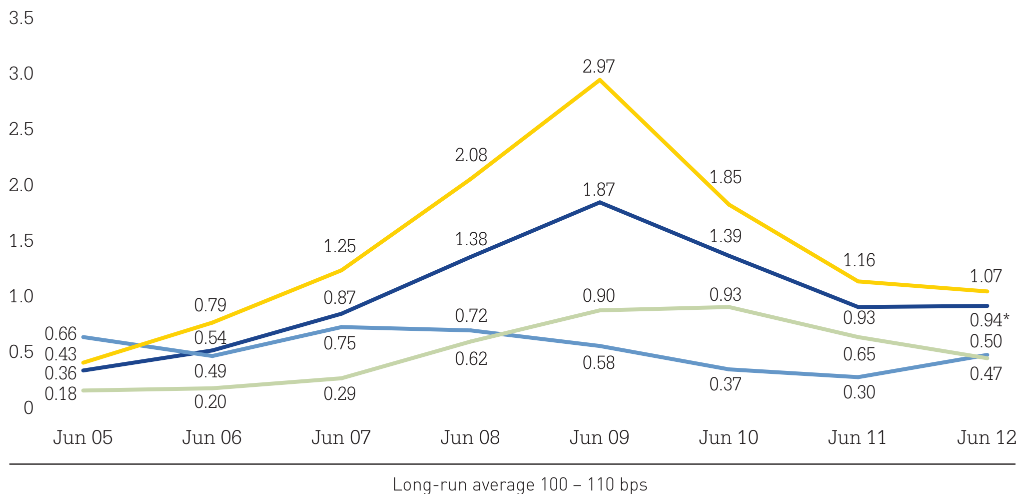
NPLs continued to trend downwards and the core impairment trend is in line with expectations, however, the overall increase in the impairment charge was driven by:

- the creation of certain portfolio provisions at the centre, reflecting the Group's view that the benign credit cycle has now bottomed; and
- a specific impairment for unrecovered amounts in FNB's merchant acquiring business.

NPLs continued to decline (down 6%), and mortgages still dominate. It is also important to understand that the lifecycle of NPLs has changed given the severity of the last cycle and the introduction of the NCA (debt counselling processes). NPLs are therefore stickier and take longer to work out. The Group remains prudent in provisioning, and although the specific impairment charge remained similar to last year, the higher portfolio provisions have increased the total coverage ratio to 60.0% (2011: 50.4%).

The Group believes the higher portfolio provisions are appropriate given the current cycle, some signals from both the macro economic environment and portfolio trends. Bad debts are expected to start trending up to the long-run average of the portfolio of 100-110 bps.

Credit loss ratio (%)



* *Core impairment charge.*

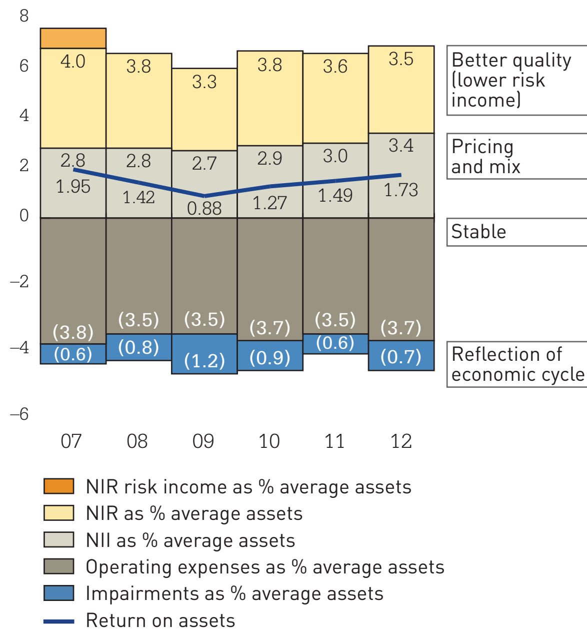
- Retail
- Total
- Africa
- Corporate

ROA – THE KEY METRIC

The Group believes that ROA is the key metric for assessing management's ability to provide real returns to shareholders.

When assessing the trend in and composition of ROA over five years, it is pleasing to note that the NIR component is of a much higher quality (with risk income a significantly lower proportion). The NII component reflects the success of the Group's repricing strategies and the recent shift in mix. The cost-to-asset ratio has remained stable and the volatility in the impairment component is as expected given the accounting treatment. The Group is pleased to have produced a high-quality ROA, but recognises that this is now at a cyclical high because bad debts are at the bottom of the long-run average.

ROA (%)



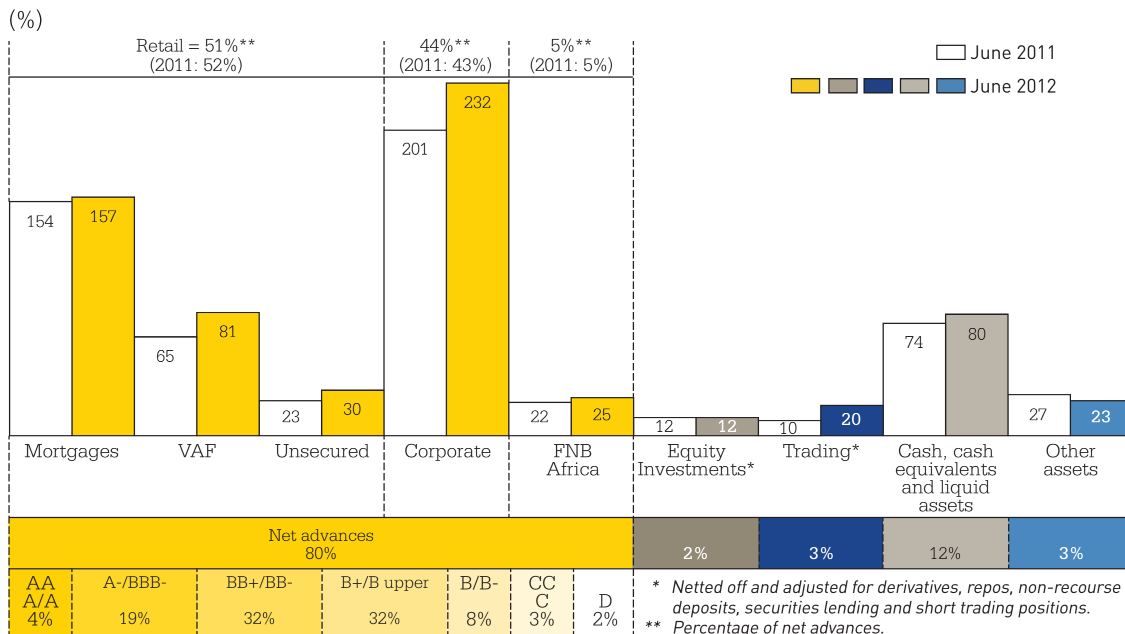
Pre-June 2011 figures are for FirstRand Banking Group and are not presented on a normalised basis.

COST CONTAINMENT

The Group's cost-to-income ratio remained flat at 53.4% despite continued investment in a number of growth initiatives. Core costs were well controlled increasing only 10% year-on-year.

BALANCE SHEET STRUCTURE – ASSETS

Asset profile (R billion)



When assessing the underlying risk in the balance sheet, the Group's asset profile is dominated by a balanced advances portfolio, which constitutes 80% of total assets. In terms of credit quality, 88% of advances are rated B+ or better. Cash and liquid assets represent 12% of total assets, with only a small portion related to the investment and trading businesses.

Market risk arising from trading activities has declined as a result of RMB's decision to exit outright proprietary trading businesses. The most significant impact was the reduction in the size of the Group's listed equities trading book. RMB continues to assume market risk in relation to its client activities (market making in local markets, hedging and client facilitation). Market risk exposures are strictly monitored and managed with risk appetite and limits set in relation to the size of the earnings and capital base. VaR limits are dealt with in more detail on page 189 of the *Risk and capital management report*.

Equity investment risk stems primarily from RMB's private equity activities. The Group's portfolio is diversified across different investment teams, industries and counters.

The private equity portfolio is equity accounted, and not marked-to-market. The significant unrealised value of approximately R1.6 billion (2011: R1.2 billion) mitigates earnings volatility.

IMPROVE THE BALANCE BETWEEN CORPORATE AND RETAIL LENDING ACTIVITIES AND SHIFT THE RETAIL ASSET MIX

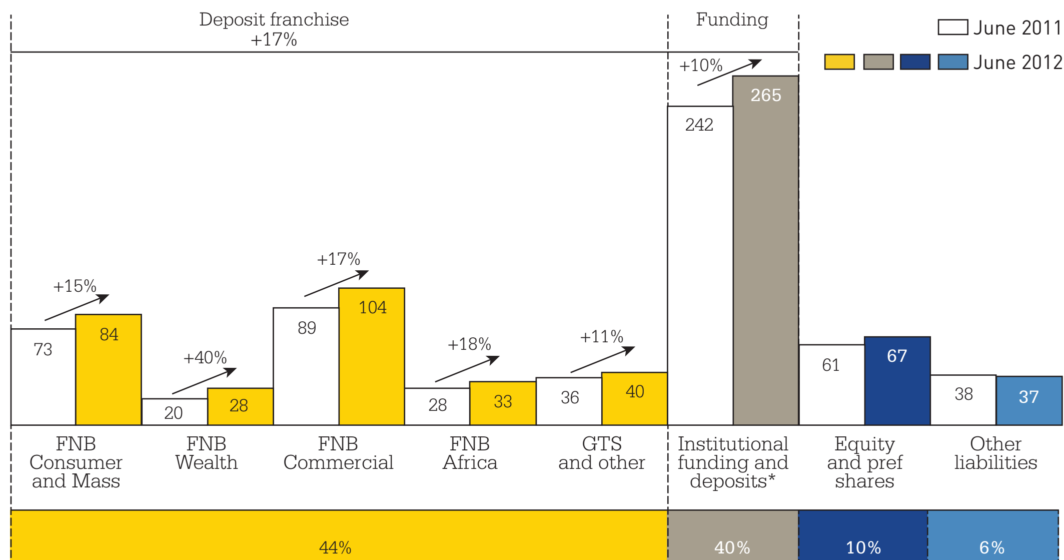
Although the Group made significant progress in growing its lending activities in the corporate market, retail remains a larger component given the strong consumer cycle. Corporate advances were driven by very good growth in investment banking advances, through a continued focus on defensive, investment-grade counterparties and an increase in prudential limits.

As can be seen from the chart opposite a shift has also taken place in the mix of retail advances, reflecting the good growth in VAF and unsecured lending. Mortgages have remained flat.

Retail advances mix

BALANCE SHEET STRUCTURE – LIABILITIES AND EQUITY

Liabilities and equity (R billion)

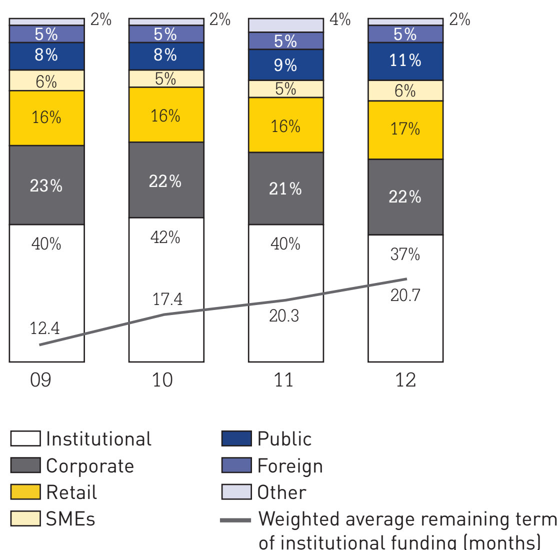


* *Excluding securities lending, derivatives, repos and short trading positions.*

The chart above shows that the Group's liability profile improved due to good growth in the retail and commercial deposit bases.

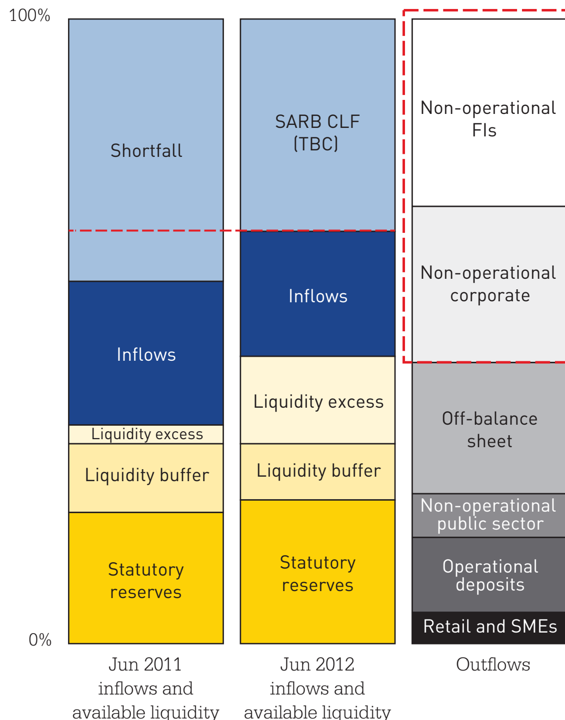
FirstRand's funding profile continues to reflect the structural funding issues associated with the South African banking sector, however, the Group has continued to reduce its reliance on institutional funding and has further improved the term profile of institutional funding from a weighted average remaining term of 12.4 months in 2009 to 20.7 months in 2012.

Funding profile



The growth in deposits across the portfolio reduced the need to grow in the institutional funding market with 70% of advances growth funded by the deposit franchise. This resulted in improved margins and a better liquidity position.

The Group's funding strategy is influenced by its preparations for the implementation of the Basel III Liquidity Coverage Ratio (LCR), in particular as it seeks to restore the correct risk-adjusted pricing of deposits. The chart opposite shows that the Group continues to improve its liquidity position and is well prepared for the implementation of the LCR.



INTEREST RATE RISK IN THE BALANCE SHEET

The Group does not take interest rate views in the banking book. All interest rate positions are consolidated in Group Treasury and hedged out in the market. The Group has to assume an interest rate profile in its endowment portfolio (capital and lazy deposits). Endowment accounts for the majority of interest rate risk in the banking book and the Group is exposed to cuts in interest rates. The Group evaluates hedging options on an ongoing basis. A 100 bps cut in interest rates would reduce margins between 15 and 20 bps before any hedging activities.

MAINTAIN ROEs AND THE GROUP'S STRONG CAPITAL POSITION POST-BASEL III

The Group's capital ratios remained strong – the year-on-year reduction can be ascribed to the special dividend payment in the year to June 2012 and the introduction of Basel 2.5.

FirstRand's capital management strategy is aligned to the Group's overall objective to deliver sustainable returns to shareholders within appropriate levels of volatility. The Group's current philosophy, given the uncertain macro economic and regulatory environment, is to operate at the higher end of its targeted capital levels to ensure balance sheet resilience. Current targeted levels and ratios are summarised in the table following.

%	FirstRand		Regulatory minimum
	Actual	Target	
Capital adequacy ratio	**14.7**	12.0 – 13.5	9.5*
Tier 1 ratio	**13.2**	11.0	7.0
Core Tier 1 ratio	**12.3**	9.5 – 11.0	5.25

* *The regulatory minimum excludes the bank-specific (Pillar 2b) add-on and capital floor.*

%	FirstRand Bank (FRB)*		Regulatory minimum
	Actual	Target	
Capital adequacy ratio	14.6	11.5 – 13.0	9.5**
Tier 1 ratio	12.6	10.5	7.0
Core Tier 1 ratio	11.8	9.0 – 10.5	5.25

* *Reflects solo supervision, i.e. FirstRand Bank excluding foreign branches.*

** *The regulatory minimum excludes the bank-specific (Pillar 2b) add-on and capital floor.*

The Group does not seek to hold excess capital for large acquisitions, however, as previously indicated to shareholders, it is holding a buffer for investments in selected growth opportunities in certain African jurisdictions. Given the current economic conditions in South Africa and the subdued credit appetite amongst consumers and corporates, the Group's operating franchises continue to generate good returns at a time when there is limited opportunity to grow risk weighted assets (RWA). The Group, therefore, continues to review the appropriate level of payout to shareholders on a sustainable basis.

With regard to the impact of Basel 2.5 and Basel III, the Group's level of Core Tier 1 capital is sufficient as it held buffers in anticipation of these changes. These buffers have now been allocated to the operating franchises as part of the capital allocation and performance management processes.

Each franchise has been through a process of assessing if any action is required to optimise returns given these new allocations. The most significant impact, particularly associated with Basel 2.5, is at RMB, which has already made the necessary adjustments to its business model as outlined in its operating review on page 34 of this report.

Following Basel III, including business model adjustments, the Group believes it can maintain ROEs between 18% and 22% through the cycle.

Basel III seeks to enhance the quality of loss absorbing capital. To this end, emphasis is placed on Common Equity Tier 1 as the predominant form of capital, whilst Additional Tier 1 and Tier 2 will receive more limited recognition.

Types of capital and proposed Basel III requirements

Common Equity Tier 1*	7.0%	Minimum; can be higher
Additional Tier 1	1.5%	Limit; higher level not recognised for total capital requirements
Tier 2	2.0%	Limit; higher level not recognised for total capital requirements

* *Does not include additional buffers required (e.g. countercyclical, D-SIB or bank-specific add-ons).*

It is the Group's intention to make use of these regulatory limits to optimise its capital structure. Future capital issuance will be balanced against the utilisation of these regulatory limits and the expected rundown profile of the existing capital instruments. Banks will need to consider how to optimise this mix against the backdrop of more costly instruments and uncertain investor appetite given potential regulatory intervention at different trigger levels and capital market conditions. Should banks be unable to issue these capital instruments they may have to rely on more expensive Core Tier 1, which would negatively impact ROEs.

STRATEGIC FOCUS MOVES TO INTEGRATED FINANCIAL RESOURCE MANAGEMENT

The COO and CFO is the custodian of the total balance sheet, ROE profile, earnings composition and mitigation of volatility. In line with this mandate, the Group has historically implemented an integrated/holistic balance sheet management approach. This requires a detailed understanding of the economic cycle and the interplay between the risks created by the cycle and the levers within the business that can be used to mitigate those risks. Ultimately, the aim is to optimise the natural position of the balance sheet, identify and implement appropriate macro hedges in the current structure and only make the balance sheet available to the origination businesses if the required risk-reward return can be met.

FirstRand's integrated balance sheet management approach seeks to deliver a sustainable return profile (i.e. ROE between 18% and 22%). It also assists the Group in managing its counterparty status by maintaining a balance sheet/risk profile which meets its targeted credit rating.

This approach has always worked on the basis that equity capital is an expensive and scarce resource, which was reflected in performance measures such as ROE and NIACC. These metrics were monitored closely and capital was allocated to maximise ROE and NIACC. Given the financial crisis and the revised strategy to deliver higher quality of earnings, the Group now believes that funding and risk capacity and utilisation should receive the same level of focus from an allocation and measurement perspective.

The Group is thus adopting an integrated financial resource management approach in which the price and availability of all financial resources will be inputs in the strategy setting and planning process (on a forward-looking basis). Targeted returns should be considered in the context of potential volatility and the portfolio of risks the Group is exposed to.

The objective is to optimise the portfolio such that the Group will deliver sustainable returns within an acceptable level of risk to produce long-term shareholder value. The focus is on:

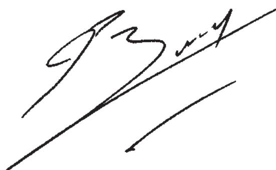
- balance sheet strength;
- earnings resilience (growth within an acceptable level of volatility); and
- performance management
  - ROE
  - ROA
  - NIACC

The chart below illustrates the Group's approach to integrated financial resource management.

Financial resources		
Capital • Levels • Mix • Efficient	**Funding** • Diversified • Flexible • Sustainable • Efficient	**Risk capacity utilisation** • Available capacity • Volatility • Sustainable ROE
Balance sheet strength		**Sustainable earnings**
Measurement and allocation (performance management)		
NIAAC Cost of equity Leverage	Targeted rating Cost of funds Liquidity profile (market and funding) Deposit franchise	ROE within 18 – 22% 1-year earnings reduction limit • normal cycle • turbulent cycle • stress cycle

CONCLUSION

When assessing the results for the year to June 2012 it is pleasing to note that FirstRand continues to deliver on its strategic objectives. Going forward the Group will measure, monitor and refine these objectives. FirstRand believes that the increase in focus on integrated financial resource management will allow it to fully optimise the financial, strategic and operational levers required to maximise returns to shareholders.



Johan Burger
Chief operating officer and chief financial officer