LAUREE DIPPENAAR | Chief Executive Officer

CEO'S REPORT

There is no doubt that **innovation** is what makes this Group different, both in banking and insurance. This approach has its roots in our **entrepreneurial culture** and it has flourished because of our decentralised and empowering structure and culture. **We reward innovators** and in many areas of financial services we "have changed the rules of the game".

INTRODUCTION

In last year's report I spent some time talking about the four pillars of our growth strategy. Since then we have added capital management as a further pillar, particularly given the Group's very strong focus on active capital management to deliver superior shareholder returns (in fact I am not sure why it was left off the list in the first place, it is such an obvious one).

In this report I shall cover some of the major deliverables of our growth strategy which now, I can confirm, rests on five pillars, none of which are mutually exclusive:

- Organic growth – growing but staying efficient;
- Collaboration – leveraging off the building blocks in the different businesses;
- Acquisitions – adding "load for the truck" or more diversification to the income base;
- "Greenfields" – creating completely new businesses and new sources of growth; and
- Capital management – optimising capital.

In the past, when presenting the results to the investment community, I have said that although our strategy has remained very consistent over the past 20 years, it often doesn't appear that way as its five components do not all "kick in" every year. This year was interesting in that our performance benefited from all five pillars making a contribution. The benefits of our capital management strategy are dealt with in detail in Johan Burger's CFO Report.

Strong organic growth continued

Strong organic growth was experienced across all of our main businesses, which resulted in excellent top-line growth for the Group as a whole. Whilst there is no doubt that the favourable economic conditions we are currently experiencing in South Africa provided very good natural growth there was also good "man made" growth created by our continuous efforts to innovate and collaborate.

Quantifying organic growth	Market	FirstRand
WesBank new business	24%	32%
FNB HomeLoans new business	57%	91%
FNB Card advances	30%	32%
RMB Private Bank advances	20 – 25%	41%
Momentum recurring new business	4%	21%
Discovery Life new business	4%	18%
Consumer investment products	11%	76%

The table above, which is not an exhaustive list, provides a good barometer of how these efforts allowed the Group to perform ahead of the growth provided by the market, and in many areas grow our market share.

FNB HomeLoans is a typical example. The business experienced extremely strong growth in new business of 91%, significantly ahead of the market and particularly evident in the second half of the year. The main reason for this is that during the year we improved our turnaround processes in the unit and in a market where speed of response is critical, this made all the difference.

Innovation remains key to our success

Another "man made" effort that I believe made a significant contribution to the organic growth we delivered, was our relentless (almost obsessive) focus on innovation.

There is no doubt that innovation is what makes this Group different, both in banking and insurance. This approach has its roots in our entrepreneurial culture and it has flourished because of our decentralised and empowering structure and culture. We reward innovators and in many areas of financial services we "have changed the rules of the game".

An example of this at First National Bank (FNB) is the One Account, which is a single credit facility for the middle market. We launched this last year and already have a book of R1.3 billion and sales are accelerating on a month-by-month basis.

This year FNB was the first bank in South Africa to launch cellphone banking as an sms channel and in six months we have signed up 74 000 customers.

Rand Merchant Bank (RMB) has, over the past few years, built a leadership position in BEE transactions and this continued apace during the year. In March **RMB created, launched and listed** a new investment company, **Makalani Holdings Limited** (Makalani), which is designed to invest solely in large BEE transactions and other targeted investments such as infrastructure, low cost housing, SMME's and emerging agriculture.

The first company of its kind, Makalani will invest in a diversified portfolio of mezzanine-type instruments which will provide investors with commercially acceptable, risk adjusted returns. These investments will be compliant with the Financial Services Charter and as a result will enable investors to earn Charter scorecard points. This innovative vehicle opens up a new market in South Africa.

The insurance industry faces significant structural challenges, and a very significant one is the recent rulings by the Pension Fund Adjudicator on retirement annuities. I believe that Momentum is responding to the issue with a great deal of creative thinking and innovation. We see the problem as two dimensional – dealing with past legacies and providing future solutions. To deal with the former Momentum has put aside R100 million to assist customers swapping from so-called old legacy products to new age products such as Momentum's Investo range.

Collaboration is happening throughout

Collaboration a big driver of organic growth. We have always emphasised that collaboration at FirstRand has a much broader meaning than simply cross-selling. The integrated structure of the Group allows us to leverage off all the building blocks of the businesses, such as IT systems, client bases and skills etc.

Collaboration is now endemic within the Group and is delivering growth at all levels. In the Review of Operations there are a large number of examples of where businesses have collaborated to create growth, I would like to mention just one now – the Discovery Card – which really flew this year.

Last year we were projecting that in two years Discovery would issue 325 000 cards. Given that the card is both a credit card, with some excellent benefits with major retailers such as Woolworths, and a Discovery Medical Scheme membership card, we believed that a large number of these cards would be taken up and activated. In fact we finished the first year with over 200 000 card holders in total which also helped FNB Card significantly grow its market share.

Making acquisitions is a core competency

Turning now to another pillar, acquisitions, and all the action has been from Momentum.

The ability to do mergers and acquisitions is one of **Momentum's core competencies** and it applied those skills very effectively this year to do transactions with Sage, Advantage, Sovereign and African Life Health.

The detail of these transactions can be found in the Momentum section of the Review of Operations, however I would like to touch on them briefly. The four acquisitions can be split between "load" and strategic with Sage very much a load transaction. Momentum currently has a small presence in the market segment that is serviced by agents and Sage provides benefits of scale, increasing Momentum's policy book by 25%, without a commensurate increase in costs. The acquisition of Sage adds a total of 590 agents to Momentum's current agency force and is expected to boost Momentum's new recurring premium income by 15%.

The acquisition of Advantage provides critical mass in the multi-manager market which is required to compete more effectively for new mandates.

We continue to create new Greenfields

The fourth pillar is what we call "greenfields" or new age businesses. FirstRand is well recognised for its ability to start completely new businesses which often take on the established players in the market. OUTsurance and Discovery are classic examples of this and both these businesses, started from scratch in 1999 and 1992 respectively, provided good contributions to this year's growth.

In the creation of these businesses we always leverage off the existing infrastructure (or what we call building blocks) within the Group, Discovery for instance was created off the distribution backbone of Momentum. Since the year end we have repeated this exercise, this time using the existing infrastructures of OUTsurance and Momentum.

Momentum will launch a short-term insurance offering in January 2006. To be known as Momentum Short Term Insurance (Momentum STI), the new company's strategy is to provide personal-lines and commercial-lines insurance products to that segment of the market that prefers to deal through brokers. To achieve this, distribution will take place through Momentum Distribution Services, which is a network of broker consultants that call on thousands of brokers who sell both long-term and short-term products to their customers.

The creation of Momentum STI was made easier by the fact that Momentum, as part of the FirstRand Group, had access to the existing short-term insurance back-office infrastructure of OUTsurance.

To facilitate the initiative, FirstRand will create FirstRand Short Term Insurance Administrator which will be the entity providing the back office and administration platform to both Momentum STI and OUTsurance. This will ensure a very efficient operation and ensure no duplication of costs or resources.

We are very excited about the prospects of this initiative and the fact that we have been able to use the various building blocks of FirstRand to create another new company and another new source of revenue.

Our international end game

One of the perceived gaps in FirstRand's armoury is our somewhat cautious approach to African and international expansion.

It is fair to say that FirstRand has been **most successful** expanding across industry boundaries in South Africa, rather than geographical boundaries, however we do continue to make good progress in Africa and other markets.

There are a few key principles that underpin our international strategy and the first is that we cannot replicate FirstRand overseas and we will therefore only expand the activities of those businesses within the Group that are of an "Olympic standard". This has meant that international expansion has been driven at business unit level and in many cases it is working well. However, many of these units are running very hard to capitalise on the growth opportunities within South Africa, so in order to provide momentum and support to their initiatives we have created a resource at the centre – the Africa and Emerging Markets Division.

Another key principle is that we would seek to establish joint ventures with partners who can provide brand credibility and distribution in chosen markets. Following its experiences with Destiny in the United States, Discovery has entered the UK with the Prudential who has a formidable presence in its markets and provides substantial benefits in terms of brand credibility and distribution muscle.

Our expansion into Africa remains conventional where appropriate and unconventional wherever possible.

In the category of unconventional we have made two investments. A commitment of $30 million to African International Financial Holdings ("AIFH"), a $96 million private equity fund which is focused on building retail banking networks, primarily acquired through privatisations in Africa; and the acquisition of Celpay, an embryonic cellphone payments operator in Zambia and the Democratic Republic of Congo (DRC).

AIFH is a private equity fund managed by WPA, Inc. and was formed in April 2003 to invest in the commercial banking sector in sub-Saharan Africa. This investment allows us to participate in the very attractive privatisation opportunities that arise in African countries that adopt strong economic reform programmes. FirstRand Bank's first right of refusal on the assets sold by the fund creates the opportunity to acquire, in time, direct control of good quality banking networks. In terms of our agreement we have a number of exit opportunities should AIFH be unable to find appropriate investments.

Celpay provides a mobile banking service between users, including the ability to make payments in real time via a cell phone, including airtime recharge. Celpay is functioning in two markets, Zambia and the DRC, and the service can be expanded in existing markets as well as new geographical markets in Africa and beyond.

In certain countries in Africa it is expected that technology will enable countries to leap-frog traditional payment methods. For example in the DRC there are approximately 20 000 active bank accounts but over two million cellphones. We made a small investment in Celpay, it is a start up operation and not yet profitable, however it is already doing in excess of 100 000 transactions a day.

Looking forward – structural or cyclical shift?

The question that everyone is asking in South Africa is whether the robust growth we are currently experiencing in our economy is cyclical or structural.

I believe that it is both, but overwhelmingly structural. Political and economic reform has delivered a continuation of the free market economy, increased competition across all sectors and fiscal discipline. Micro economic reform has increased social delivery and we have seen formal employment expanded.

There have been some cyclical windfalls. Firstly, we have experienced a commodity boom fuelled by demand from the hungry Asian tiger – China, and it could be said that this demand in itself has a strong structural component to it. The second cyclical factor is the strong capital inflows we experienced as an emerging market. Worldwide, emerging markets have become a more attractive asset class and once again there is a strong structural bias to what are essentially seen as cyclical capital inflows. The economic boom we are experiencing is, I think, based on very sound fundamentals.

We are in good shape – but some challenges ahead

The Group is definitely in good shape to face the future. We have a well-diversified earnings base that has been carefully assembled over a long period of time and this, combined with a benign operating environment, should allow us to continue to grow our top-line and increase market share.

We will continue to invest for the future across all our businesses in order to create new revenue sources and ensure the sustainability of our growth record. However we must also start to focus more rigorously on costs.

It is in the DNA of this Group to acknowledge and reward revenue growth and we recognise that we need to apply the same vigour and enthusiasm to cost management.

However we must be careful not to cut into "muscle" at a time when the Group, across the board, is experiencing unprecedented growth.

Many of the Group's companies have increased their costs this year, but in most cases they have experienced good operational leverage and therefore "positive jaws" – growth comes at a price!

Having said that, there is no doubt that a structurally lower inflation environment means that we have to take cost out of the system. Management consultants recently identified certain areas within FNB where cost savings could be realised, specifically in areas such as capacity management and processing in the branches, operational processes in HomeLoans and central procurement. FNB has now embarked on a three-year plan to extract these cost savings and we expect to limit cost growth at FNB to single digits by 2007.

The other big challenge facing many of our businesses is rising consumerism and the need to provide value for money, and earlier in my report I covered some of the responses Momentum is pursuing in its market. Bank charges have also been in the press a great deal this year and this is a specific challenge for FNB. We strongly believe that FNB is one of the lowest, if not the lowest, cost provider in all the segments it services and has structured its fees to encourage customers to use less costly services.

The final challenge I would like to cover briefly is the entry of Barclays into the South African market – their arrival will certainly "lift the bar". We are, I stress, not in any way complacent about this increased level of competition and we have already been very busy analysing where we might be vulnerable. However I am confident that the different divisions in the Group will rise to the challenge and probably emerge better businesses than they already are.

Thank you

In his Chairman's Statement GT Ferreira has covered the recent management changes at FirstRand. This is my last year as CEO of the Group and I am looking forward to my new non-executive role as I feel it will provide me with the "mental space" to spend more time on the big ticket issues coming down the road.

I have enjoyed my seven years at the helm of FirstRand, it really is a very unique organisation, full of fantastic people with great ideas and boundless energy. I would like to firstly thank our shareholders for their long-term support and secondly I would like to say thank you to every single member of staff for providing seven years of superior growth and value creation for shareholders. I have been very proud to present the results of your efforts.

LL Dippenaar

Laurie Dippenaar
Chief Executive Officer
FirstRand Limited

Sandton
19 September 2005

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