Our operating franchises **FNB, RMB and WesBank** all **outperformed** both the macro economic conditions and the market.

SIZWE NXASANA / CEO

ceo's report

A STRONG PERFORMANCE

FirstRand's diversified financial services portfolio produced **another strong performance** for the year to June 2012, once again demonstrating the quality and resilience of our operating franchises, **FNB, RMB and WesBank,** all of which **outperformed** both the macro economic environment and the market.

DRIVEN BY A CONSISTENT STRATEGY

The Group's ultimate objective is to create long-term franchise value and deliver superior and sustainable returns to our shareholders. It pursues this objective through a consistent strategy to;

- become a leading player in all of the financial services profit pools in South Africa, growing in existing markets and those where we are under-represented;
- grow our franchise in the broader African continent, targeting those countries expected to show above average domestic growth and which are well positioned to benefit from the trade and investment flows between Africa, China and India.

Focusing for a moment on growth in our existing markets, in South Africa FNB has successfully grown core transactional accounts. It has achieved this through offering customers a compelling value proposition, supported by exciting rewards programmes and platform innovations such as the Banking App, cellphone banking and e-Wallet. A positive outcome from this strategy has been the strong increase in transactional volumes, which, along with robust advances growth, contributed significantly to FNB's overall growth.

RMB's decision to focus more on client-driven activities has resulted in structurally lower ROEs, however these levels are much more sustainable and earnings are of a much higher quality with less volatility.

WesBank's domestic point of sale dominance means that it has been able to capitalise on the strong domestic replacement cycle that has played out over the past two years.

Now turning to those markets or profit pools where we remain under-represented, there are some specific initiatives already underway to grow our share in these markets. As I mentioned in my report last year, at RMB we have created a CIB business to more effectively service the large corporate market. This strategy has continued to gain traction as we have grown out the coverage team, particularly into those segments and economic sectors where we have been historically under-represented. In addition we have attracted key talent to supplement our growing African footprint which better positions us to take advantage of clients who trade across the corridors which link Africa to both Asia and Europe. The year also saw continued investment into the technology platform which is key to providing a holistic transactional capability for clients. In WesBank, the focus on growing the corporate and Full Maintenance Rental business remains a strategic priority.

Another gap in our portfolio, particularly since we unbundled Momentum, is asset management. When we looked at the opportunities to enter this market again we took the decision to position the strategy as an alternative investment management offering, as this plays to the strengths and track records of our existing investment, origination and structuring businesses. We will continue to offer traditional products, particularly to our wealth clients.

To facilitate this strategy we have created an asset management pillar alongside the Bank. In line with our multi-branding strategy we have branded the new asset management franchise, Ashburton Investments, and through this franchise we will market traditional and alternative products. Traditional products will in the main be originated by the original Ashburton business, which has a 30-year track record as an active investment manager. The alternative products will initially be provided by RMB.

GROWING IN NEW MARKETS TAKES PATIENCE AND DISCIPLINE

In the franchise operating reviews on pages 30 to 39 there is further detail on these growth initiatives, I would now like to focus on the progress we are making in our non-domestic growth strategies, in the rest of Africa and India.

As Laurie Dippenaar points out in his chairman's statement (page 6) our approach in new markets will not move the earnings needle in the short-term. However given our relative size in the South African market, and the subdued domestic macro growth we predict over the next few years, pursuing profitable growth in the rest of Africa remains an imperative for us. We therefore seek to generate incremental growth, executing on the ground through our operating franchises. We fundamentally believe that this is an appropriate and sustainable strategy; however it is very long-term in nature. I often comment that it will be the next generation of leadership at FirstRand that witnesses the non-domestic earnings needle really move. As we pursue this strategy, there are a few golden rules we apply:

1. Build scale but not a high cost base; in particular leverage existing platforms wherever possible.
2. Establish comprehensive universal banking operations by deploying RMB on-the-ground presence in FNB subsidiaries.
3. Don't grow at the expense of the domestic market where the current strategy has allowed us to significantly outperform GDP.
4. Only deploy up to 10 per cent of Group capital in new countries (unless something truly compelling emerges and then we would ask shareholders).
5. Always send the A Team to new countries.
6. Lead with innovation as far as possible, don't apply/rely on legacy thinking.
7. Don't plant a flag in every African country; focus only on our priority territories for the next three to five years (these being Mozambique, Zambia, Tanzania, Ghana, Nigeria and Kenya).

Ultimately the Group seeks to protect its ROE, it prefers greenfields operations or small-to-medium size rather than significant acquisitions. Whilst this can mean expansion takes longer, potential dilution of returns can be contained. Bolt-on acquisitions to existing greenfields operations are also preferable, as these can bring additional scale more rapidly.

AFRICA IS PRESENTING GOOD OPPORTUNITIES IN SELECT MARKETS

If we look at these objectives and where we have made steady progress, FNB is continuing to organically build full service banking in Zambia, Mozambique and Tanzania, and the larger more established franchises such as Namibia and Botswana produce very healthy returns. In both the established and new territories FNB has introduced a number of its innovative SA products and delivery channels. It is successfully growing customers and transaction volumes.

The benefits of RMB's ongoing investment in the FNB African subsidiaries has proved successful, with the deployment of specific Fixed Income, Currency and Commodities (FICC) and investment banking skills. Earnings grew strongly in the current year driven by Botswana, Namibia, Zambia and Mozambique. RMB also has a very active representative office in Nigeria and recently received agreement in principle to its application for an investment banking licence.

The Group continues to look for opportunities to acquire a platform for retail and commercial activities in Nigeria as longer term we need access to local deposits to fund an in-country strategy. We also need a branch network, even if it is initially only a regional presence, so we can service customers in what remains very much a cash-based economy. Although financial deepening continues to take place in the retail sector, we see early opportunities in Nigeria to lie in the commercial and corporate sectors.

Ghana also offers scope for growth and since the year end we have made an offer for Merchant Bank Ghana (MBG) whereby FirstRand will invest (R746.2 million (GHs176.4 million)) in exchange for a 75% shareholding in the bank. MBG is a medium-sized retail and commercial bank with 22 branches and a well established client base and deposit franchise. It is ranked amongst the top ten banks in Ghana and we believe it will provide an excellent platform for FNB and RMB to roll out products and services in Ghana.

A Kenyan presence is important for building an east African corporate and investment banking hub, particularly given the strong trade flows with India. During the year FirstRand officially opened a representative office in Kenya from where RMB will market corporate and investment banking services. As the only African bank with a licence to operate in India, we are ideally placed to act as a conduit for transactions between the east African region and India. RMB is already a significant participant in the east African region and has a strong pipeline of potential transactions in infrastructure and project finance, resource finance, debt financing, structured trade and commodity finance, and fixed income, currency and commodity activities.

WHY WE LIKE INDIA

Whilst on the topic of India, our original strategy, which commenced in 2009, was to mine the trade and investment flows between India and the African continent. So why India at all?

Like South Africa (and indeed much of the rest of Africa), India displays sound economic fundamentals, bolstered by a solid and well regulated banking system and robust capital markets. Both countries enjoy vibrant and steadily growing corporate sectors and a strong entrepreneurial spirit that is, in many ways, driving continued economic growth and is recognised as a key requirement for future economic and social sustainability.

It's not surprising, then, that India and Africa have developed such a strong economic relationship over the past few decades. Since 1990, bilateral trade between India and Africa has flourished – as evidenced by the growth in trade value from US$1 billion two decades ago to its peak of around $42 billion in 2008. While trade values have declined slightly since then as a result of the global economic crisis, trade relationships between India and Africa are as strong as ever. This is particularly true of the sub-Saharan African region, where countries like Nigeria, Angola, DRC, Tanzania, Mauritius and Kenya continue to enjoy very strong export and import trade volumes with India.

In addition to this well-established economic cooperation, India and South Africa enjoy many other similarities. The governments of both countries are committed to driving economic and social development via infrastructure- and agriculture-led growth. Both also have very strong technology, manufacturing and resources sectors and the banking systems of both countries have been relatively unscathed by the global economic crisis thanks to robust policies and systems.

Of course, both countries also face many challenges. And even here, there are similarities. Like South Africa, India is faced with high levels of inflation and unemployment and poverty alleviation is an ongoing focus.

FirstRand's early presence in India was established by RMB, utilising both South African and local skills, and since commencing operations the investment banking business has demonstrated two consecutive years of profitability. More importantly, it is achieving its objective to be the African banker of choice in the Indian market and is actively involved in various advisory, structuring and financing transactions. RMB divisions, Global Markets and Global Transactional Services (GTS), have also been growing currency, commodities and trade activities in a measured manner. We are now selectively looking at in-country investment banking opportunities that align with the Group's risk appetite framework and product strengths. We believe this will ensure a balanced and sustainable earnings base for the business in the long-term.

During the year, FNB entered the Indian market through the opening of its first branch in Mumbai. The operations are branded FRB and will focus on introducing and carefully growing the innovative products and channels that have underpinned FNB's domestic customer franchise over the past few years.

This is also a greenfields or startup strategy, with the objective to eventually establish full retail and commercial banking capabilities in India. This will allow for incremental investment with reliance to be placed on established, home-grown systems and processes which we believe is an appropriate approach given the country's specific regulatory constraints and the strength of the Indian banking sector. Near term focus will be placed on growing the distribution footprint in selected Indian markets. To expedite this we are looking at forming partnerships with suitable Indian corporates which will allow us to bring our innovative products, complement their activities and leverage their distribution platforms. Ultimately we see our strategy in India to be long-term, reflecting a highly measured and incremental approach particularly in the retail and commercial activities.

ULTIMATELY THE GROUP SEEKS TO PROTECT ITS ROE, IT **PREFERS GREENFIELDS OPERATIONS** OR **SMALL-TO-MEDIUM SIZE** RATHER THAN SIGNIFICANT ACQUISITIONS.

LOOKING FORWARD, IT GETS A BIT TOUGHER TO GROW

The global economic situation will continue to place pressure on our earnings and growth potential in the 2012 financial year. Macro economic conditions are a large driver of earnings growth and are becoming tougher. The South African GDP growth is currently expected to be 2.5% for the 2012/2013 financial year, and, although interest rates are expected to remain flat for the rest of the year, there is downside risk if economic growth slows further. Consumer spending could reduce and growth in retail advances is likely to remain subdued, with mortgage lending expected to continue to lag nominal GDP growth. Business confidence has not fully recovered although, should some of the proposed government and public sector infrastructure spending start, this could provide some underpin to growth.

Despite these increased domestic headwinds FirstRand expects to continue to produce good organic growth. Increasing revenues remains a challenge, but our franchises have compelling strategies to grow their respective toplines.

In sub-Saharan Africa growth is expected to further strengthen and we will continue to build on our progress in our priority countries.

We are managing the business and have adjusted strategies appropriately;

- innovation becomes even more important;
- driving cost efficiency whilst investing for growth;
- origination strategies adjusted; and
- pricing for risk critical.

We continue to strive to become the African financial services company of choice.

Sizwe Nxasana
Chief executive officer