cfo's report

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THERE WAS GOOD GROWTH IN ALL REVENUE DRIVERS AND THE GROUP'S VALUABLE LENDING AND TRANSACTIONAL FRANCHISES REMAIN SIGNIFICANT CONTRIBUTORS. THERE WAS ALSO PLEASING TRACTION FROM INSURANCE.

The group remains well capitalised with a CET1 ratio in excess of its stated targets.

INTRODUCTION

FirstRand delivered a solid financial performance for the year to June 2018, with growth in normalised earnings within the group's long-term target range and the ROE at 23.0% remaining above target despite difficult operating conditions.

FirstRand also increased net income after cost of capital (NIACC), the group's primary measure of shareholder value creation, 4% to R9 968 million.

Normalised earnings increased 8% to R26.4 billion, underpinned by quality topline growth.

Strong growth in NII was driven by lending and deposit activities. NIR benefited from higher fee and commission income, reflecting higher volumes across FNB's digital and electronic channels and increased customer numbers. Private equity realisations also supported group NIR, albeit at lower levels than the previous year, and the group's insurance activities also contributed to revenue growth.

Despite NPL increases, the group's credit loss ratio of 90 bps (84 bps including Aldermore) declined marginally and remains well below the group's through-the-cycle threshold, reflecting the positive impact of the group's origination strategies and provisioning policies over the past two financial years. Many of the group's lending books are trending in line or better than expectations. The group remains prudently provided with portfolio impairments as a percentage of the performing book still exceeding the annual credit charge at 94 bps (excluding Aldermore).

Investment continued in insurance and asset management activities, platforms to extract further efficiencies and the build-out of the group's footprint in the rest of Africa, however, the group's cost-to-income ratio only increased marginally from 51.0% to 51.2% due to the resilient topline growth.

Post the Aldermore acquisition, the group remains well capitalised with a CET1 ratio of 11.5%, still in excess of its stated targets. This, combined with the group's high return profile, allowed the board to maintain the dividend cover at 1.7x, which continues to track below its stated long-term cover range of 1.8x to 2.2x.

The group's performance includes a three-month profit contribution from Aldermore, which was acquired by FirstRand effective 1 April 2018. The contribution to group earnings was R276 million post the AT1 dividend payment.

Any reference to financial information "excluding Aldermore" represents the subtraction of the Aldermore-specific information (refer pages 206 to 209) from the group's normalised income statement and statement of financial position (refer pages 212 to 217).

	Group (excluding Aldermore)		
R million	**2018**	2017	% change
Earnings performance			
Normalised earnings	**26 135**	24 471	7
Balance sheet			
Advances (net of credit impairments)	**957 810**	893 106	7
Deposits	**1 094 270**	983 529	11
ROE (%)	**22.8**	23.4	
ROA (%)	**2.03**	2.07	
Credit loss ratio (%)	**0.90**	0.91	
Performing book coverage ratio (%)	**0.94**	0.95	
Cost-to-income ratio (%)	**51.1**	51.0	

CHALLENGING MACROECONOMIC BACKDROP

South Africa's macroeconomic operating environment for the year to June 2018 was characterised by two distinctly different six-month periods.

In the first half of the group's financial year, policy ambiguity and political uncertainty weighed on domestic risk appetite, economic activity, and investor and consumer sentiment. This was particularly acute following the medium-term budget policy statement in October 2017 and the resultant S&P downgrade of South Africa's local currency sovereign rating to below investment grade.

The second half of the group's financial year started more positively following the change in leadership of the ruling party, the appointment of President Ramaphosa as head of the government and a relatively investor-friendly cabinet reshuffle in February 2018. These changes allowed the country to avoid further downgrades and were followed by new board and management appointments at key state-owned enterprises (SOEs) and other government agencies. This resulted in improved foreign and domestic confidence.

It is clear, however, that progress on meaningful structural reform will be difficult and slow. GDP expanded only 1% over the first three quarters of the group's financial year, credit growth remained in the mid-single digits and the unemployment rate remained static.

Relatively muted inflation provided some support to households and this allowed the South African Reserve Bank (SARB) to cut interest rates 50 basis points over the course of the year.

In the rest of the sub-Saharan region, conditions remained mixed. Economic activity in Namibia and Botswana was subdued mainly because of South African macroeconomic weakness. The Nigerian economy continued to recover, and the macroeconomic outlook will improve on the strength of supportive oil prices.

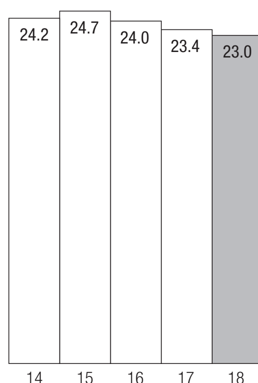
In the UK, macroeconomic uncertainty continued to be driven by Brexit, which will formally take effect at the end of March 2019. This has weighed somewhat on UK economic activity, although unemployment continued to drift lower and wages trended upwards, resulting in consumer demand and house prices holding up reasonably well.

KEY PERFORMANCE METRICS

The group continued its track record of growth in earnings and superior returns, as shown below.

ROE

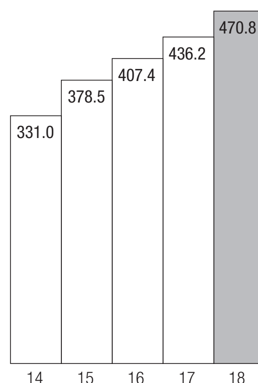
%



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% for normal economic cycles.

DILUTED NORMALISED EPS

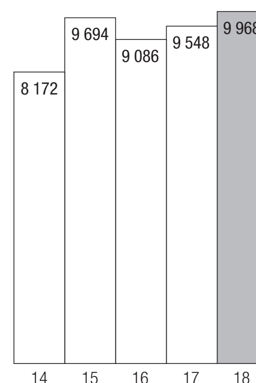
cents



The group targets earnings growth of nominal GDP growth plus >0% to 3%.

NIACC

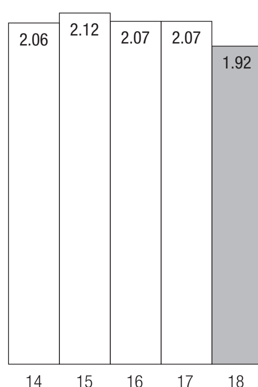
R million



Growth in NIACC is the group's internal benchmark for assessing performance. The group continues to achieve returns above its cost of equity, resulting in NIACC growth despite higher levels of capital.

ROA

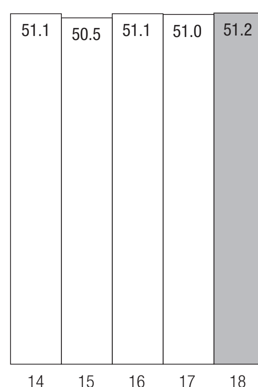
%



Maximising ROA is a key objective in creating shareholder returns. Although the group's ROA reduced with the acquisition of Aldermore, it remains structurally higher due to portfolio mix and strategic choices.

COST-TO-INCOME RATIO

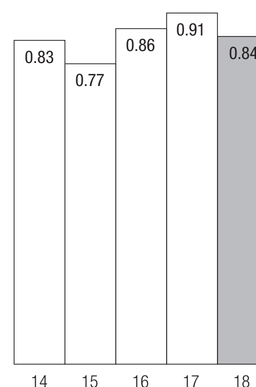
%



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.

CREDIT LOSS RATIO

%

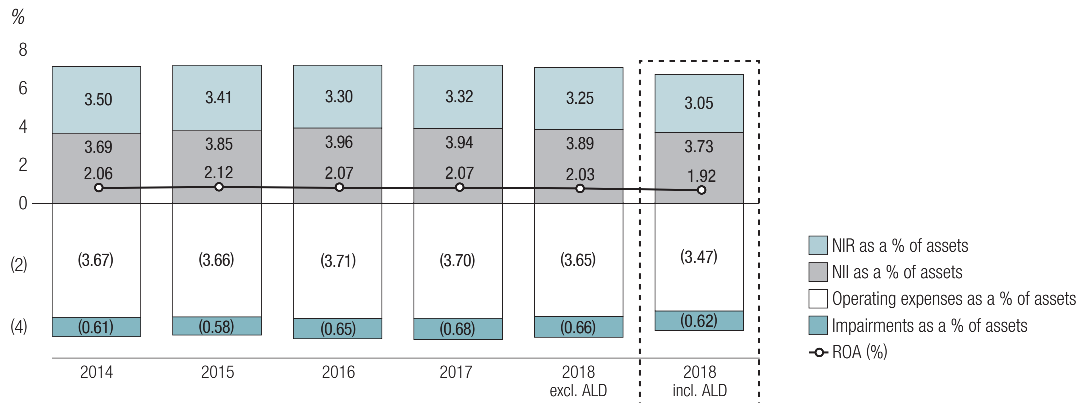


The group believes that pricing appropriately for credit risk is a key requirement for sustainable returns and targets a through-the-cycle charge range of 100 to 110 bps (excluding Aldermore).

STRATEGIC ACTIONS SUPPORT SUSTAINABILITY OF RETURNS

The group's ROE continues to be driven by its structurally higher ROA, the composition of which is depicted in the following graphic.

ROA ANALYSIS



The group continues to seek avenues to protect and grow returns, including expanding and enhancing its transactional banking business, which (excluding Aldermore) delivers roughly half of gross revenue.

FirstRand's relative advances mix compared to the sector also enhances ROA as the group has a lower proportion of low-yielding assets, with credit underwriting and pricing models anchored around preserving returns.

The group's disciplined allocation and pricing of financial resources (capital, funding and liquidity and risk capacity) has also provided an underpin to its superior ROA.

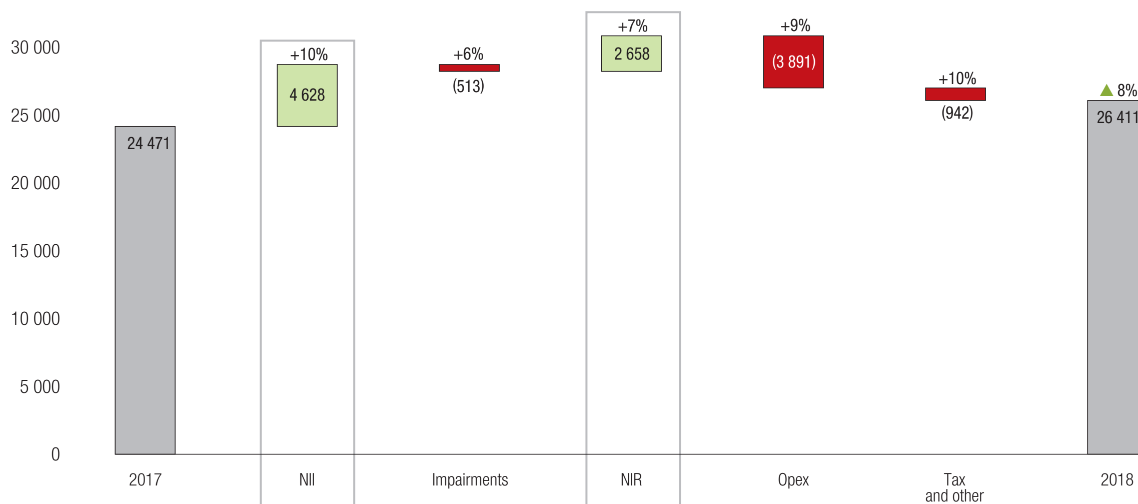
FirstRand's private equity franchise is also a key differentiator and has consistently delivered high returns, although the business is currently in an investment cycle.

Traditional banking revenues will, however, come under pressure in the fullness of time. This is primarily going to come from the competitive environment, with new entrants into the space. FirstRand is focused on its integrated financial services offering and diversifying into the adjacent activities around banking in order to preserve its return profile over the longer term.

MAINTAINING HIGH QUALITY TOPLINE GROWTH

The graph below unpacks the group's performance by income statement category and shows that the group's performance was underpinned by high quality revenue growth of just over 9% achieved in tough market conditions.

NORMALISED EARNINGS
R million

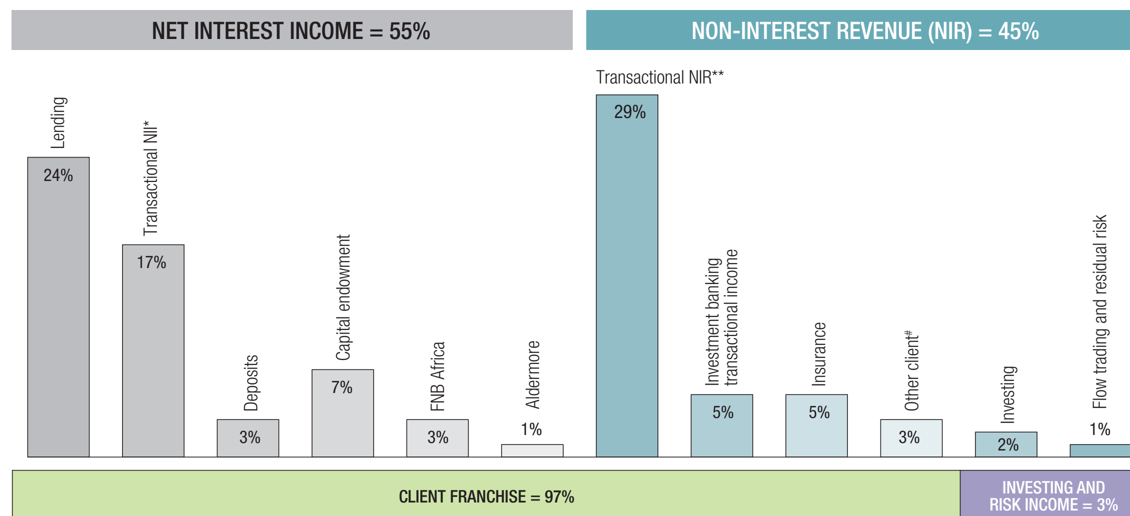


GENERATING QUALITY, SUSTAINABLE REVENUE

Client activities account for 97% of revenues, with the balance from investing and risk income.

The group has maintained a good balance between NIR and NII as can be seen from the chart below.

GROSS REVENUE ANALYSIS



* *Includes transactional accounts and related deposit endowment, overdrafts and credit card.*
** *From retail, commercial and corporate banking.*
\# *Includes WesBank associates.*

There was good growth in all revenue drivers and the group's valuable lending and transactional franchises remain significant contributors to overall revenue and growth. There is also pleasing traction in insurance, as discussed in the CEO report.

A further breakdown of NII is provided in the following table.

NET INTEREST INCOME*

R million	**2018**	2017[#]	% change
Lending	**22 023**	20 227	9
Transactional NII**	**15 600**	14 306	9
Deposits	**3 071**	2 957	4
Capital endowment	**6 097**	5 664	8
Group Treasury	**637**	584	9
FNB Africa	**3 027**	3 178	(5)
Other NII (negative endowment, e.g. fixed assets)	**(425)**	(290)	47
Total NII excluding Aldermore	**50 030**	46 626	7
Aldermore	**1 224**	–	n/a
Total NII including Aldermore	**51 254**	46 626	10

* *After taking funds transfer pricing into account.*

** *Includes NII relating to credit cards, overdrafts and transactional deposit products, and deposit endowment.*

[#] *2017 figures restated to reflect refined allocation methodology for lending. For transactional and deposit NII there has been a reallocation between segments to better reflect the nature of transactions.*

The following commentary excludes Aldermore.

Lending NII was supported by strong advances growth and a slight increase in margins.

Transactional NII, which relates to NII from overdrafts, credit card and transactional deposits, reflect the strength of FNB and RMB's transactional franchises, covered in more detail in the review of operations.

There was good growth in deposit NII despite competitive pricing pressures.

Capital endowment benefited from higher capital levels, despite two rate cuts of 25 basis points each during the year under review.

Group Treasury NII reflects the drag of higher high quality liquid assets (HQLA) holdings as well as the impact of foreign exchange management, offset by the positive benefit of interest rate management activities.

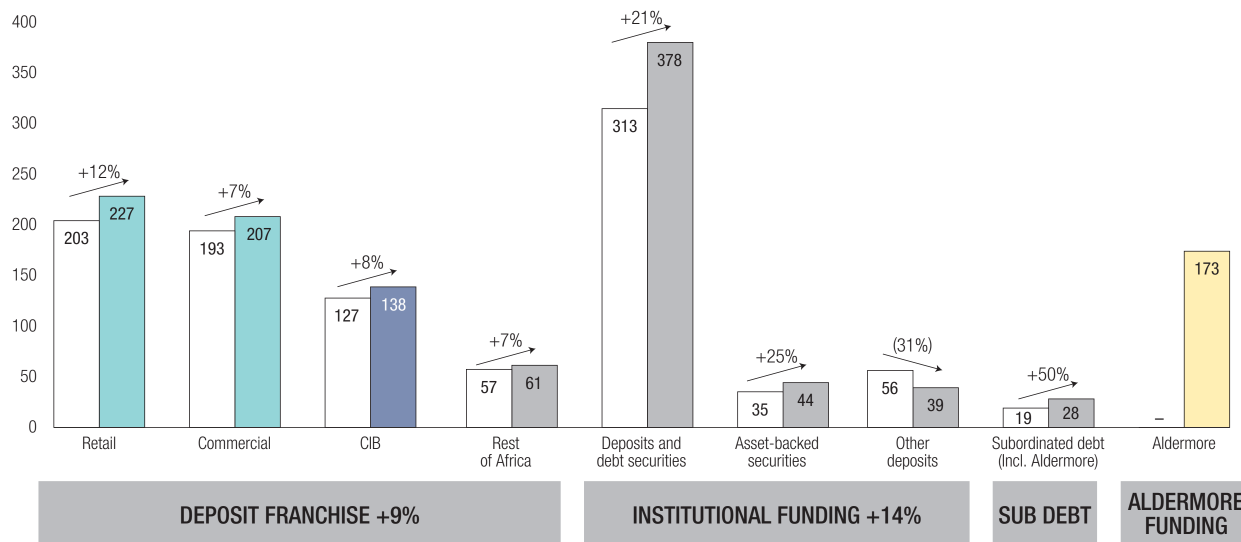
EXCLUDING ALDERMORE, MARGINS EXPANDED SLIGHTLY

Margin expansion was driven by asset pricing and a change in funding mix, due to the continued growth of the deposit franchise. This has come at a cost, as strong competition for deposits resulted in deposit pricing negatively impacting margins.

The inclusion of Aldermore results in a structural shift in the group's net interest margin, given the large proportion of lower-margin secured advances on its balance sheet. Aldermore does not currently have a transactional business and therefore has no deposit endowment. Its deposit market is also more rate-sensitive. The net impact is a reduction in the group's net interest margin from 530 bps to 489 bps. This structural shift does, however, come at a better risk-adjusted return profile.

Bps	FirstRand excl. Aldermore	Aldermore
Advances margin	359	315
Deposit margin	236	128
Total margin	530	273
Overall weighting of average assets	84%	16%

DEPOSIT STRATEGY BEARING FRUIT – DEPOSITS UP 29% (11% EXCLUDING ALDERMORE)



Note: Percentage growth is based on actual rather than rounded numbers shown in the bar graphs.

As discussed in the CEO report, the group's South African deposits have exceeded growth in M3 money supply over a number of years. Retail and commercial deposit growth in the year under review was supported by continued product innovation, improved utilisation of channels, cross-sell to existing customers and financial resource management strategies. CIB deposits benefited from ongoing momentum in RMB's corporate and transactional business.

The strong growth in institutional funding reflects the issuance of debt securities given favourable market conditions, and the group's focus on maintaining a weighted average funding term in excess of 30 months. Growth in foreign currency funding also contributed to the growth in institutional funding and was affected by rand depreciation during the year. There were also some point-in-time cash deposits at year end.

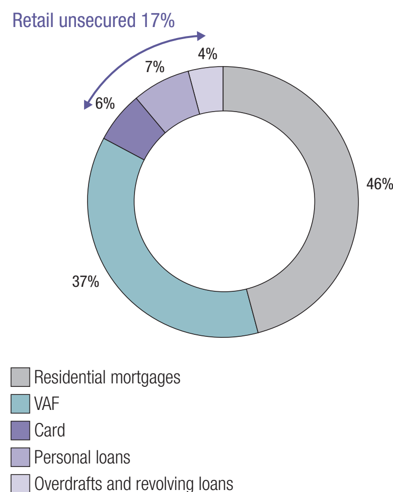
RETAIL ADVANCES UP 7% (EXCLUDING ALDERMORE)

The growth in retail advances reflects the continued targeted nature of the group's origination approach across products and client segments.

R million	2018	2017	% change
Residential mortgages	**204 969**	195 498	5
VAF*	**165 214**	155 084	7
– WesBank	**104 864**	102 322	2
– MotoNovo*, **	**60 350**	52 762	14
Card	**27 140**	23 800	14
Personal loans*	**33 181**	28 441	17
– FNB	**17 161**	14 372	19
– WesBank	**14 985**	13 574	10
– MotoNovo*	**1 035**	495	>100
Transactional account-linked overdrafts and revolving term loans#	**15 852**	14 863	7
Retail advances excluding Aldermore#	**446 356**	417 686	7
Aldermore – retail	**107 734**	–	n/a
Retail VAF securitisation notes	**23 674**	19 223	23
FNB and WesBank rest of Africa advances†	**53 094**	52 842	–

* *Restatement of MotoNovo personal loan book out of VAF.*
** *8% UK VAF advances growth in pound terms.*
# *Restatement of prior year advances in FNB from retail to commercial based on current client segmentation.*
† *Includes in-country advances of FNB and WesBank.*

RETAIL ADVANCES BREAKDOWN
%



Drivers of retail advances growth are discussed in more detail in the FNB and WesBank *review of operations*.

CORPORATE AND COMMERCIAL ADVANCES UP 6% (EXCLUDING ALDERMORE)

The composition of, and growth in the corporate and commercial advances portfolio is shown below.

R million	2018	2017	% change
CIB core advances – South Africa	**246 906**	235 596	5
– Investment banking*	**190 146**	185 222	3
– HQLA corporate advances	**18 629**	18 544	–
– Corporate banking	**38 131**	31 830	20
CIB core advances – rest of Africa**	**43 811**	36 862	19
CIB total core advances#	**290 717**	272 458	7
WesBank corporate	**32 150**	31 365	3
FNB commercial†	**93 987**	84 146	12
RMB repurchase agreements	**23 233**	29 047	(20)
Corporate and commercial advances	**440 087**	417 016	6
Aldermore corporate advances	**56 142**	–	n/a

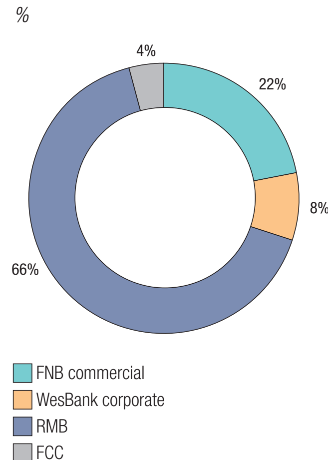
* *Prior year figure restated to exclude the portion relating to Ashburton Investments, now reported under FCC.*

** *Includes cross-border and in-country advances.*

\# *Excludes RMB repurchase agreements.*

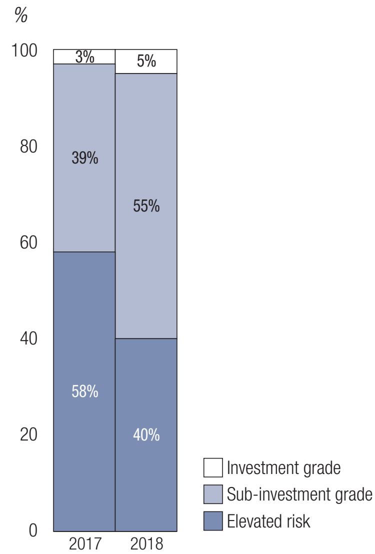
† *Restatement of prior year advances in FNB from retail to commercial based on current client and business segmentation.*

CORPORATE AND COMMERCIAL ADVANCES BREAKDOWN†
%



The table above shows strong growth of 12% in FNB commercial advances in a difficult environment, reflecting good customer acquisition, successful cross-sell strategies (especially in the small business segment) and good growth in the agric and property sectors. WesBank corporate continued to experience a tough reinvestment cycle. CIB advances growth was supported by the conclusion of a number of deals in the last quarter and growth in rest of Africa corporate advances (cross-border advances grew 13% in dollar terms).

The next chart shows the composition of RMB's advances book and the substantial change in the counterparty ratings to sub-investment grade following the local currency sovereign downgrade last year.



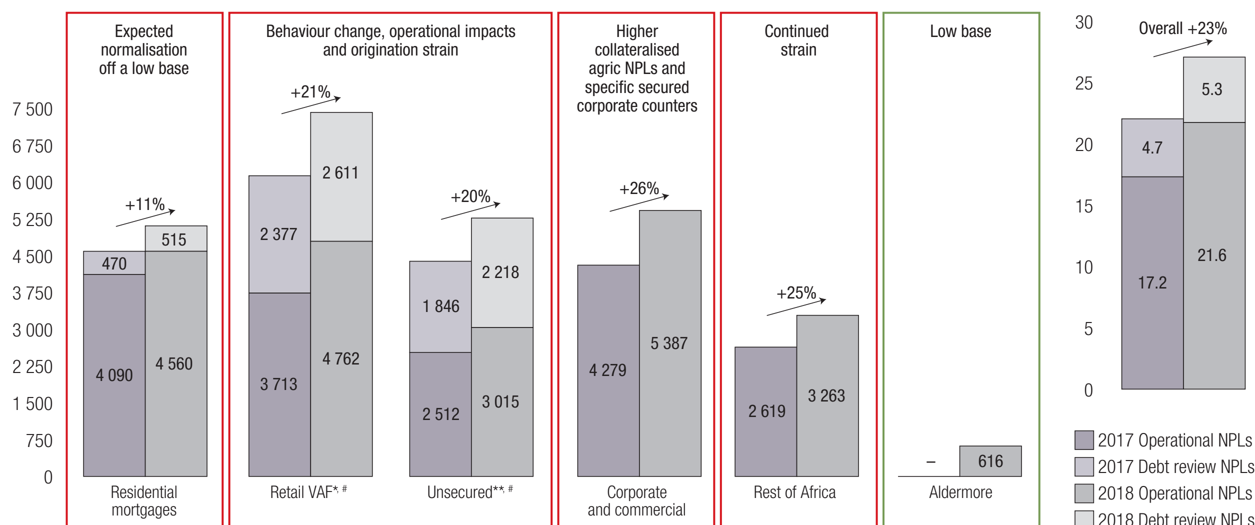
* *International scale based on exposure at default (EAD).*

The underlying quality of RMB's portfolio remains strong and largely unchanged, with only a marginal increase in the elevated risk category driven by some specific sectors and counterparties. This was offset by an improvement in the previously stressed oil and gas sector.

CREDIT PERFORMANCE BENEFITS FROM PRUDENT ORIGINATION STRATEGIES AND PROACTIVE PROVISIONING IN PRIOR YEARS

Excluding Aldermore, NPLs increased 20%, with more than 60% of the growth emanating from the secured books across segments.

The group continues to include paying debt review customers in NPLs. The following graph also shows that the impact of debt review is still more pronounced in the VAF and unsecured portfolios.



* *Retail VAF includes NPLs from MotoNovo, to which debt review is not applicable (SA only 2018: R6 818 million; 2017: R5 797 million).*

** *Unsecured includes NPLs relating to MotoNovo personal loans (amounts immaterial).*

\# *Operational NPLs include older debt-review accounts from WesBank that migrated into NPLs prior to May 2016, as well as other types of restructured exposures and special arrangements undertaken by the bank that are non-performing.*

There was cyclical normalisation in residential mortgage NPLs, which increased 11%. This was expected given historically low levels and new business strain in affordable housing.

Retail VAF NPLs reflect specific issues in the vehicle finance sector, such as increasing later -stage arrears and NPL levels. Overall NPLs continued to be impacted by lengthening recovery timelines and an increasing number of customers opting for court orders for repossessions.

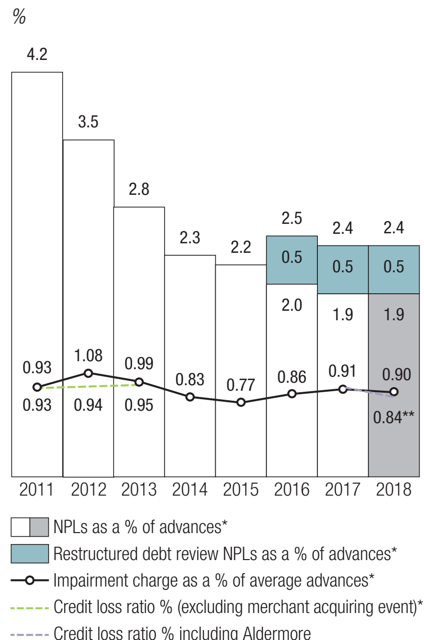
As explained at the half year, higher than expected NPLs in the self-employed and small business segments resulted from operational issues with some scorecards, including third-party data quality, and this issue continued to play out in the second half. MotoNovo NPLs also increased significantly off a low base as a result of strong book growth in prior years.

Unsecured NPLs increased in line with expectations, given the strong growth of the book in the prior year.

FNB commercial NPL increases reflect new business strain, which was expected given the continued growth in new customers, cross-sell and up-sell strategies, and the impact of the ongoing drought in certain areas of South Africa. Growth in RMB NPLs was linked to specific secured counterparties.

The rest of Africa picture remains volatile but was expected given the economic pressures and macros in the regions, especially in the subscale businesses.

NPL AND IMPAIRMENT HISTORY
%



* *Excluding Aldermore.*
** *Credit loss ratio including Aldermore.*

Credit loss ratio %	**2018**	2017
Retail – secured	**0.81**	0.74
Residential mortgages	**0.07**	0.15
VAF	**1.73**	1.48
– SA	**1.88**	1.54
– MotoNovo	**1.46**	1.36
Retail – unsecured	**5.38**	5.94
Credit card	**2.63**	3.05
Personal loans	**6.53**	7.63
– FNB	**5.03**	7.43
– WesBank	**8.20**	7.91
– MotoNovo	**6.41**	4.85
Retail – other	**7.62**	7.27
Total retail	**1.57**	1.56
Corporate and commercial	**0.23**	0.27
Rest of Africa	**1.71**	1.60
FCC (incl. Group Treasury)	**(0.02)**	(0.04)
Total excluding Aldermore	**0.90**	0.91
Aldermore	**0.12**	–
Total including Aldermore	**0.84**	0.91

The overall credit loss ratio of 90 bps (excluding Aldermore) is still below expectations. With the inclusion of Aldermore, the charge reduces to 84 bps.

The lower residential mortgage credit loss ratio of 7 bps benefited from loss given default credit model recalibrations, despite higher NPL formation, which reduced the level of coverage. Excluding this once off benefit, the charge would be similar to prior years.

Domestic VAF is the only portfolio where credit losses are above expectations, which can be attributed to the specific and sector-related issues covered above.

There was a continued normalisation of the MotoNovo impairment charge, reflecting new business strain given strong book growth over multiple periods, the impact of business written prior to the risk cuts in the previous year and continued conservatism in portfolio impairments.

The credit loss ratio in card, which is below 3%, continued to benefit from active collection strategies and post write-off recoveries.

FNB loans' credit charge declined given the significant origination cutbacks in 2017.

FNB commercial's charge increased to 75 bps reflecting book growth and the expected increase in NPLs, buffered to some extent by prior overlays.

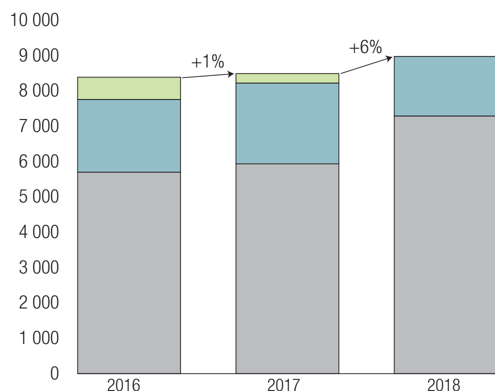
Proactive provisioning in prior year benefited the corporate impairment charge.

Further increases in FNB's and WesBank's rest of Africa charge reflected the ongoing tough macros in various of the jurisdictions the group operates in and increased conservatism in provisions.

The following chart shows that portfolio provisions increased in line with book growth and that overall coverage (excluding Aldermore) was maintained at 94 bps, which is still above the annual charge and remains conservative.

The graph also shows that model impairments have increased as some of the business overlays have been embedded in model developments.

PORTFOLIO IMPAIRMENTS*
R million



Central overlay
Franchise overlay
Franchise portfolio impairments

* *Excludes Aldermore.*

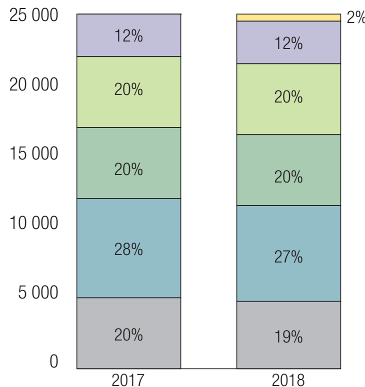
	2018 Including Aldermore	2018 Excluding Aldermore	2017	2016
Portfolio impairments as % of performing book	**0.83**	**0.94**	0.95	0.99
Credit loss ratio (%)	**0.84**	**0.90**	0.91	0.86
Portfolio impairments (R million)	**9 263**	**8 945**	8 471	8 359

As mentioned previously, the group does not reschedule paying debt-review customers out of NPLs. These accounts stay in NPLs until fully rehabilitated. They do, however, require lower coverage as most continue to pay. The following table shows coverage ratios across the different portfolios and demonstrates that as the debt-review proportion of the book increases, coverage reduces. Coverage is, therefore, appropriate given the higher payment profile of debt-review NPLs.

	COVERAGE						
	Operational NPLs		Restructured debt-review NPLs*		Total		
Coverage ratios %	**2018**	2017	**2018**	2017	**2018**	2017	Change y/y
FNB credit card	**73.3**	74.2	**50.5**	45.1	**66.9**	67.0	
FNB retail other	**82.5**	75.5	**35.2**	37.9	**72.4**	67.0	
FNB loans	**68.8**	69.2	**48.7**	48.2	**59.8**	61.9	
WesBank loans**	**71.8**	71.9	**14.4**	26.3	**36.9**	38.1	
SA retail VAF**	**41.9**	43.1	**9.5**	9.4	**29.5**	29.3	

* *Non-performing loans under debt review.*

** *Operational NPLs include older debt-review accounts that migrated into NPLs prior to May 2016, as well as other types of restructured exposures and special arrangements undertaken by the bank that are non-performing.*



* *Includes FNB and WesBank loans, and MotoNovo personal loans.*
** *Includes portfolio overlays.*

Coverage ratios %	2018	2017
Retail – secured	**26.0**	26.9
Residential mortgages	**17.8**	21.8
VAF	**31.6**	30.7
– SA	**29.5**	29.3
– MotoNovo	**57.5**	58.4
Retail – unsecured	**55.9**	56.6
Credit card	**66.9**	67.0
Personal loans*	**47.0**	49.4
Retail – other	**72.4**	67.0
Corporate and commercial	**40.4**	48.0
Rest of Africa	**46.3**	42.2
Specific impairments excl. ALD	**37.4**	38.8
Portfolio impairments excl. ALD**	**34.0**	38.7
Total excl. Aldermore	**71.4**	77.4
Aldermore	**22.9**	–
Specific impairments incl. ALD	**37.1**	38.8
Portfolio impairments incl. ALD**	**34.4**	38.7
Total incl. Aldermore	**71.5**	77.4

The above table shows a marginal decline in specific coverage which was driven by the mix change to more secured NPLs and the ongoing build-up of debt-review customers, both of which require lower coverage. Specific impairments increased 16% in absolute terms to R9.9 billion, excluding Aldermore.

In conclusion, the group believes that the various components of its credit provision metrics remain appropriate and in line with the group's risk appetite and origination strategies.

FirstRand adopted IFRS 9 from 1 July 2018, making this the last year in which credit is reported on the incurred basis.

SOLID GROWTH IN NON-INTEREST REVENUE

NIR increased 7%, reflecting strong fee and commission income growth of 10%, supported by higher volumes across FNB's digital and electronic channels and increased customer numbers.

Private equity realisations also supported group NIR, albeit at lower levels than the previous year.

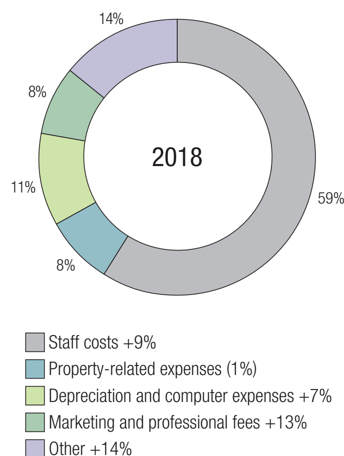
Insurance revenue increased 6%, benefiting from strong volume growth of 20% and 8%, respectively, in funeral and credit life policies, resulting in annual premium income increasing 35% year-on-year.

Fee, commission and insurance income represents 79% of group operational NIR. Refer to the *review of operations* for further information on drivers of NIR in the various businesses.

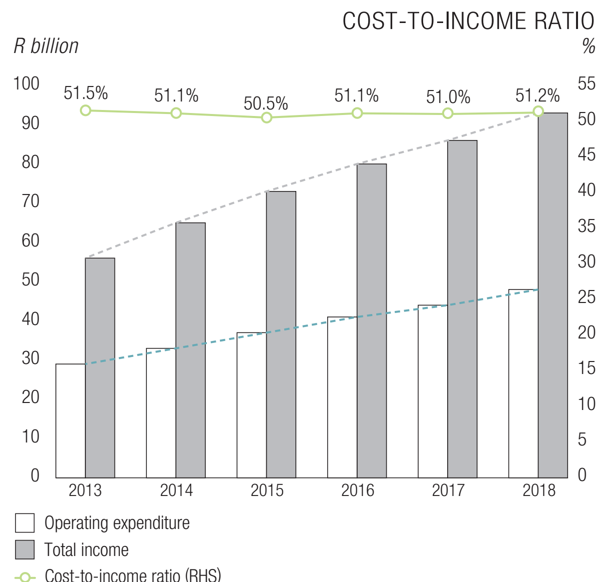
OPERATING EXPENSES RISING ON INVESTMENTS FOR GROWTH

Excluding Aldermore, operating cost growth of 7% was slightly lower than the first half of the year, but continues to trend above inflation due to ongoing investment in insurance and asset management activities, platforms to extract further efficiencies, and the build-out of the group's footprint in the rest of Africa. Despite these cost pressures, the group's cost-to-income ratio only increased marginally from 51.0% to 51.2% due to resilient topline growth.

BREAKDOWN OF OPERATING EXPENSES



COST-TO-INCOME RATIO



BALANCE SHEET STRENGTH AND QUALITY REFLECT CONSISTENT DISCIPLINED FINANCIAL RESOURCE MANAGEMENT AND ORIGINATION STRATEGIES

The structure of the balance sheet reflects the group's long-term strategy to increase balance sheet resilience, diversify credit exposures across sectors and segments, increase market liquidity, and reduce reliance on institutional funding.

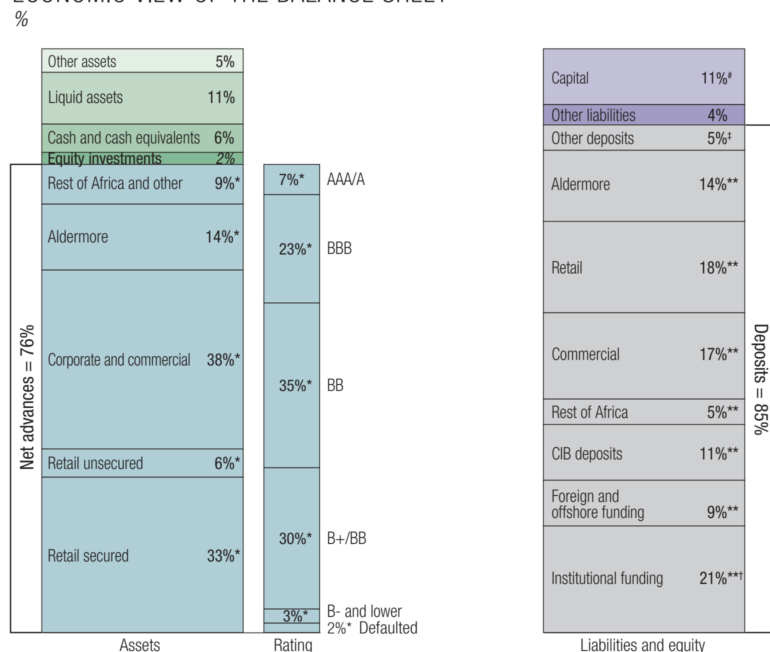
When assessing the underlying risk in the balance sheet, the group's asset profile is dominated by a balanced advances portfolio, which constitutes 76% of total assets. The composition of the net advances portfolio consists of retail secured (33%), retail unsecured (6%), corporate and commercial (38%), Aldermore (14%) and rest of Africa and other (9%). At 30 June 2018, total NPLs amounted to R26 947 million (2.36% as a percentage of advances) with a credit loss ratio of 0.84%.

Cash and cash equivalents, and liquid assets represent 6% and 11%, respectively, of total assets. Only a small portion of assets relate to the investment and markets businesses. Market risk arising from trading activities has remained low and the group's equity investments relate primarily to RMB's private equity activities. The unrealised value in RMB's private equity portfolio has been maintained at R3.7 billion.

FirstRand's funding profile continues to reflect the structural funding constraints associated with the South African financial sector, however, the group has continued to enhance its risk-adjusted funding profile whilst targeting a lower proportion of institutional funding relative to peers. The weighted average remaining term of the group's institutional funding was 34 months at 30 June 2018 (2017: 33 months).

The group's capital ratios exceed its stated targets with a Common Equity Tier 1 (CET1) ratio of 11.5%, Tier 1 ratio of 12.1% and total capital adequacy ratio of 14.7%. Gearing increased slightly to 12.0 times (2017: 11.3 times).

ECONOMIC VIEW OF THE BALANCE SHEET
%



* *As a proportion of loans and advances.*

** *As a proportion of deposit franchise.*

Ordinary equity and non-controlling interests (10%) and NCNR preference shares and Tier 2 liabilities (2%).

† *Includes CIB institutional funding and foreign branch platform.*

‡ *Consists of liabilities relating to conduits and securitisation.*

Note: Non-recourse assets have been netted-off against deposits.

Derivative-, securities lending- and short trading position assets and liabilities have been netted off.

STRONG LIQUIDITY POSITION MAINTAINED

Given the liquidity risk introduced by its business activities across various currencies and geographies, the group's objective is to optimise its funding profile within structural and regulatory constraints to enable its businesses to operate in an efficient and sustainable manner.

Liquidity buffers are actively managed via the group's pool of HQLA that are available as protection against unexpected stress events or market disruptions as well as to facilitate the variable liquidity needs of the operating businesses. The composition and quantum of available sources of liquidity are defined by the behavioural funding liquidity at risk and the market liquidity depth of these resources. In addition, adaptive overlays to liquidity requirements are derived from stress testing and scenario analysis of the cash inflows and outflows related to business activities.

The group exceeds the 90% (2017: 80%) minimum liquidity coverage ratio (LCR) requirement set out by the SARB with the group's average LCR at 115% (2017: 97%). FirstRand Bank's average LCR was 118% (2017: 105%). At 30 June 2018, the group's average available HQLA sources of liquidity per the LCR amounted to R203 billion, up from R165 billion in the prior year.

The net stable funding ratio (NSFR) came into effect on 1 January 2018 with a regulatory requirement of 100%. At 30 June 2018, the group's NSFR was 112%, whilst FirstRand Bank's NSFR was 111%.

FIRSTRAND REMAINS WELL CAPITALISED

Current capital and leverage targeted ranges and actual ratios are summarised below.

	Capital			Leverage
%	CET1	Tier 1	Total	Total
Regulatory minimum*	7.5	9.0	11.2	4.0
Targets	10.0 – 11.0	>12.0	>14.0	>5.0
Actual**	11.5	12.1	14.7	7.1

* *Excluding the bank-specific capital requirements, but including the countercyclical buffer requirement.*

** *Includes unappropriated profits.*

The 280 bps year-on-year reduction in the group's CET1 ratio resulted from:

- The acquisition of Aldermore, which was funded from the group's existing cash resources, and reduced the group's CET1 ratio by 240 bps:
  - impairment of goodwill and intangibles (R8.3 billion); and
  - consolidation of Aldermore's RWA without a commensurate increase in the capital base, as Aldermore's purchased equity is eliminated at a group level.
- The local currency sovereign downgrade, contributing 3% to RWA growth or a 20 bps reduction in the CET1 ratio.
- Higher than expected RWA growth of 10% which resulted in a net consumption of capital. This RWA growth tracked the increase in total assets and was driven by the following:
  - significant advances growth late in the financial year on the back of certain RMB transactions;
  - increased high quality liquid assets (HQLA) in Group Treasury and certain securitisation structures; and
  - strong growth in unsecured lending in FNB's premium segment.

Following the Aldermore acquisition, the group has continued to operate well above its stated capital targets. Post-acquisition earnings from Aldermore added 20 bps to the group's ROE.

LOOKING AHEAD

In the medium to longer term, given the market-leading positions of its businesses in South Africa and the growth strategies it is pursuing, FirstRand considers itself strategically well-positioned to benefit from renewed system growth. FNB's momentum is expected to continue as it grows customers and volumes, and cross-sell and up-sell strategies will deliver higher insurance revenues and good deposit and advances growth.

RMB's private equity realisations are expected to be lower in the current year compared to previous financial years.

Regarding the rest of Africa, there are signs that economic activity in most of the other sub-Saharan African countries in which FirstRand operates are picking up. The Nigerian economy is experiencing an oil price-induced lift, and growth rates in Namibia and Botswana are also expected to improve. The group expects its portfolio to continue to show an improved performance.

In the UK, uncertainty over the outcome of Brexit continues to dominate the macroeconomic outlook and will continue to weigh on business and consumer confidence, which in turn will suppress investment spending to a certain degree. These ongoing headwinds were all anticipated when FirstRand acquired Aldermore and, as indicated previously, the group expects the growth trajectory to slow relative to the previous year, owing to competitive margin pressure and normalisation of credit costs.

The group expects to continue to deliver real earnings growth (defined as real GDP plus CPI) and superior returns to shareholders.

HARRY KELLAN
CFO