FirstRand

# chairman's

*report*

for the year ended 30 June 2023

ROGER JARDINE *Chairman*

The financial year to 30 June 2023 has been characterised by a very challenging macroeconomic backdrop. An increasingly volatile and uncertain global operating environment has meant business leaders across the world have faced tough decisions to ensure the best outcomes for their shareholders, employees and the societies they serve. Similarly, global policy makers have tackled increasingly complex challenges and trade-offs.

The fraying of long-standing geopolitical relationships that have guided the flow of global trade and capital flows over the last few decades is having a significant impact on global macroeconomic outcomes. Examples of the growing complexities include the rise of trade and political blocks that rival institutions such as the Group of Seven (G7) countries, the International Monetary Fund and the World Bank. This includes the expansion of the BRICS block to embrace more countries of the "Global South". At the time of writing this report, the tragic events that continue to unfold in the Middle East have added further turmoil to the global geopolitical and macroeconomic landscape.

Along with a fracturing global environment, the fiscal picture also remains problematic across both developed and emerging markets. The highest global debt levels since World War II, combined with elevated interest rates, mean that most governments simply do not have the financial resources to ease the socio-economic challenges that their countries face. Increasing social unrest is an ever-looming threat as service delivery failures and the rising cost of debt push households into a survivalist mindset.

These global trends translated into a very difficult year for South African households as the cost of living soared and interest rates increased. Not only has the average South African household seen the price of its consumption basket lift by more than 7% this year, the price increases also prompted the South African Reserve Bank to lift the repo rate at the fastest pace in decades – from a low of 3.5% to above 8%.

These statistics, as bad as they look, hide the real pain felt by the most vulnerable households. In fact, the average consumer basket of lower income households increased nearly 10% over this period, compared to 6.4% experienced by higher-income households. The difference is explained by the fact that poorer households spend more than 50% of their income on food and transport – the two items that saw the most significant increases over the past year.

A multitude of factors contributed to the sharp rise in food price inflation, particularly the Russia/Ukraine war and subsequent sanctions and trade blockages imposed by the different actors in this geopolitical fallout. South African farmers' input costs soared as the dollar-based prices for oil, fertiliser, and chemicals sky-rocketed. In addition, with farmers across the globe suffering the same fate, the domestic prices for wheat, maize and sunflower oil lifted significantly as both export and import prices for these commodities rose. High levels of loadshedding added to cost-push pressures on food prices as producers were forced to increase spending on measures to ensure energy supply.

Against this challenging backdrop, it has been very encouraging to see how the South African private sector (businesses and households) has been investing in renewable energy solutions in response to the government's easing of regulations, which has added to South Africa's energy capacity.

The successes achieved with the private sector stepping into the energy supply chain begs the question of what could be achieved if it were able to step into other parts of the economy that are not functioning. It has been a consistent refrain in my chairman's reports that the private sector has both the financial resources and the skills to partner with the state to grow the economy, particularly given the parlous fiscal position of the country. Never has this been more urgent.

Unfortunately, it is highly unlikely that these challenges will reverse course anytime soon. However, addressing SA-specific vulnerabilities – such as fiscal fragility, low economic growth, low savings and investment rates, and weakening institutions – would significantly minimise the impact of the prevailing global macroeconomic volatility and uncertainty, particularly for households and small businesses with little financial wriggle room.

Despite this challenging macro backdrop, FirstRand delivered a strong performance for the financial year to 30 June 2023. The group's performance, in particular the composition and quality of its earnings and high return profile, continues to reflect the consistent and disciplined execution on strategies designed to maximise shareholder value, tightly managed through the group's financial resource management (FRM) process.

The strength of the customer-facing businesses in the portfolio has allowed the group to capitalise on profitable growth opportunities across all markets, sectors and segments, demonstrated in the 12% increase in the group's normalised earnings which was driven by good topline growth. This in turn was supported by continued momentum in new business origination in all of the large lending portfolios, ongoing growth from the deposit franchise and the resilience of the group's transactional franchise.

I would like to particularly reference the credit performance which was in line with expectations and a direct outcome of the group's origination strategy from mid-2020 to late 2021, as the country emerged from the Covid-19 pandemic. The decision to tilt origination to low- and medium-risk customers has resulted in a credit loss ratio below the group's through-the-cycle range, despite a higher interest rate and inflation cycle than initially anticipated.

FirstRand's normalised return on equity (ROE) of 21.2% (2022: 20.6%) remains at the top end of the target range of 18% to 22%, and the group produced R12.0 billion of economic profit (2022: R10.1 billion), or net income after cost of capital (NIACC), which is our key performance measure.

Given the high return profile, the group remained capital generative, with the Common Equity Tier 1 (CET1) ratio at 13.2% (2022: 13.9%). The final dividend of 384 cents per share represents an increase of 12% year-on-year.

FirstRand's dividend strategy is to provide its shareholders with an appropriate, sustainable payout over the long term. Given the high-return profile and ongoing capital generation, the board was comfortable to pay a dividend at 1.7 times cover representing a payout ratio of 58.8%.

The board is appreciative of the efforts of the group's management team. They are excellent stewards of capital, always carefully balancing growth and returns, whilst meeting the needs of customers.

Staying with the topic of capital allocation, as a systemic bank and allocator of financial resources to the economy and broader society, FirstRand acknowledges its responsibility to use these resources to provide solutions for climate resilience and a just transition. Economic sectors and customer segments within the group's portfolio are already and will further be impacted by climate change. Also, given that 90% of FirstRand's earnings emanate from the African continent, which is already economically and socially vulnerable, and expected to be severely impacted by climate change, we have focused on responding innovatively.

Within the broader context of climate change, as I mentioned earlier, South Africa also currently faces a severe energy deficit, requiring energy "addition" to support economic recovery. The improved economics and rapid deployment of "green energy" means that addition and transition can be tackled simultaneously through the funding of climate solutions for the country to ensure that the bulk of the electricity deficit is replaced with renewables. This continues to play out across the private sector and if we can keep up the momentum, I have no doubt we can further accelerate the country's journey to a lower-carbon economy.

FirstRand has a well-developed, dynamic climate programme that can be tracked through three years of TCFD reporting. We recognise that climate change presents both risks and opportunities for growth, so our businesses are particularly focused on scaling client solutions.

The board also recognises the need to hold business accountable to delivering on its stated climate-related commitments, so this year climate was elevated to the strategic section of senior leadership's remuneration score cards and accorded the same weighting as other material growth strategies FirstRand is pursuing. Lack of progress on the group's climate roadmap can result in a downward adjustment of the long-term incentive vesting outcome. A detailed unpack of these scorecards can be found in the group's remuneration report (at https://www.firstrand.co.za/investors/integrated-reporting-hub/governance/).

FirstRand board succession planning is a multi-year process. We have an underlying philosophy that management changes at a senior level are most optimal if they are internal, as handover is seamless and disruption kept to a minimum. If you can achieve this, then change is a healthy dynamic for the organisation. Our long-standing track record of executive succession has always succeeded in unlocking new energy and bringing fresh eyes to bear on strategy and execution. The ability to promote from within also ensures that the transition of responsibilities is collaborative, and that the individuals moving into these new roles have had the necessary experience, tenure and track records of delivery.

When the board asked Alan Pullinger to take on the role of FirstRand CEO in early 2018, he indicated that he would be available to the group for a further six years, which meant that succession planning for the role was anchored to his expected departure in 2024. That planning process resulted in a seamless "baton change" from Alan to Mary Vilakazi, who will take over as FirstRand CEO on 1 April 2024. Alan will remain with the group fulltime until the end of June 2024.

Mary joined FirstRand in 2018 and has worked closely with Alan and the senior executive team on strategy execution. She has successfully led several key growth and diversification strategies, such as broader Africa and insurance. Mary is close to the strategies and operations of the customer franchises and, as CEO of FCC, she has oversight of the key central functions of risk, compliance, treasury, and audit.

The board has full confidence in Mary. She is an exceptional leader who values the things that set FirstRand apart from its peers and underpin its success.

The board is deeply grateful to Alan for his exceptional stewardship of the group. Highly respected by his peers and competitors, his career at FirstRand has spanned 26 years, including the role of RMB CEO, until his promotion to FirstRand deputy CEO in early 2015. Alan's tenure as group CEO included navigating the Covid-19 pandemic, and his strong leadership through that unprecedented crisis meant that the group emerged in resilient shape, achieving pre-pandemic normalised earnings levels a year before initially anticipated. This is a remarkable achievement and testament to the intellectual and technical excellence Alan brought to the role.

After ten years as CEO of FNB, Jacques Celliers will take on an exciting new role with executive responsibility for the group's fintech strategy to grow revenue streams from activities outside of traditional financial services. Many of these activities have already been built within FNB including, amongst others, the mobile virtual network operator (FNB Connect) and the nav» lifestyle offerings – both of which are gaining good traction with customers. The group believes dedicated leadership is now required to scale and grow these offerings, both within our own customer base and eventually in the open market. Jacques's track record means he is uniquely placed to execute on our fintech strategy.

Harry Kellan takes over from Jacques as CEO of FNB after ten years as CFO of FirstRand, and having previously spent seven years as CFO at FNB. The board believes this combination of franchise and group experience positions him well to lead the largest customer franchise in the portfolio. He has, in partnership with the leadership teams at FNB and WesBank, been involved in shaping many of the current retail and commercial growth strategies.

Harry will be succeeded as group CFO by Markos Davias, the current CFO of FNB. Markos has now held the CFO positions at both RMB and FNB, the two largest franchises in the group, and this makes him the ideal candidate for the group CFO role. Markos has worked closely with Harry for over a decade, and this will ensure a smooth and efficient handover.

Gideon Joubert will replace Markos as the CFO of FNB. Gideon has been with the group for 12 years. He was the CFO of the investment banking division of RMB from 2014 to 2017, where he worked closely with Markos. In his subsequent role as CFO of the broader Africa portfolio, Gideon had oversight of the group's strategic finance function across the broader Africa portfolio including its eight African banking subsidiaries. Taufeeqa Waja, currently the head of finance for broader Africa, will take over from Gideon as CFO of the portfolio.

The fact that we could manage this level of change with such high-calibre internal candidates is testament to our succession planning, and it has been a privilege for me to oversee this process as chairman of the board. As I step down at this year's annual general meeting, I am confident that I leave behind executive stability and role longevity. I am also delighted that Johan Burger will be succeeding me as chairman. Johan is highly regarded in the industry for his knowledge of banking and broader financial services and the board is comfortable that he meets the requirements of independence following five years as a non-executive director.

In terms of board changes, I would like to welcome Tamara Isaacs, who was appointed to the board as an independent non-executive director in June 2023. Tamara was previously a partner at PwC and KPMG, and brings strong technical and financial skills to the role, combined with a track record in social upliftment given her long-standing role as a trustee on a number of foundations.

Mr Russell Loubser will be retiring effective 1 December 2023, after serving as a non-executive director for nine years. Russell has played a very active role on the board and in various committees – his insights and strategic guidance will be missed. On behalf of the board, I would like to thank him for his valuable contribution to the board over his tenure.

The board has undergone a reconstitution process in recent years. Once the reconstitution was completed and all vacancies were filled, the board elected Dr Sibusiso Sibisi to fulfil the role of lead independent director in September 2022. Dr Sibisi was first appointed to the board in April 2021.

FirstRand is an exceptional institution and it has been an honour to serve as a non-executive director for almost twenty years, of which the last six years have been as chairman. It has been a great privilege to be part of the team building on the legacy of the FirstRand founders, and to work with the board and an outstanding team of professionals across the group. I want to thank Alan Pullinger for his strong leadership of the group during my tenure, and I wish him well as he prepares to step down in April next year. I also want to wish Mary Vilakazi and her team all the best for the future and a successful tenure as they take FirstRand to even greater heights. I know that they will leave FirstRand in an even stronger position than where it is today.

Finally, thank you to each and every employee for their commitment and hard work, our customers for continuing to trust us with their financial services needs, and our shareholders for engaging with us in a rigorous and honest manner.

**ROGER JARDINE**
Chairman

FirstRand

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