CHAPTER 3

TRENDS IN SOUTH AFRICAN BANKS

This chapter reflects the main trends and industry statistics that are apparent from the information received from registered banks.

comparative figures may differ from those in 2000 Annual Report

Aggregated information of individual banks is contained in the reports and graphs in sections 3.1 to 3.7 below. Certain of the comparative figures in respect of December 2000 may differ from those reported in the 2000 Annual Report because of, firstly, banking institutions subsequently submitting amended returns and, secondly, the implementation of the amended Regulations relating to Banks on 1 January 2001.

The reports and graphs that follow are largely affected by the position of the "big four" banks, which constituted 69,5 per cent of the banking sector in December 2001 (70,4 per cent in December 2000). The six largest banks constituted 81,2 per cent of the banking sector as at the end of December 2001 (83,2 per cent in December 2000).

3.1 BALANCE-SHEET STRUCTURE

type and spread of a bank's business

The balance-sheet structure is analysed to determine the type and spread of a bank's business activities, as well as to consider the impact of any changes thereto on the risk profile of the banking sector. The aggregated balance sheet of the banking sector in South Africa, as at 31 December 2001, equalled R1045,6 billion, as opposed to R819,2 billion as at 31 December 2000 and R724,9 billion as at 31 December 1999.

FIGURE 1: AGGREGATED BALANCE SHEET

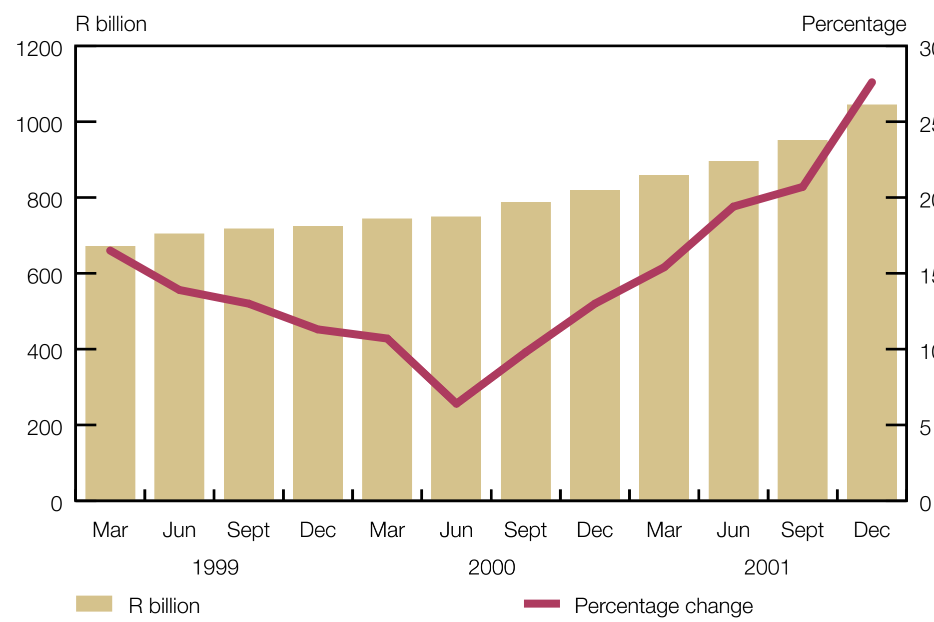
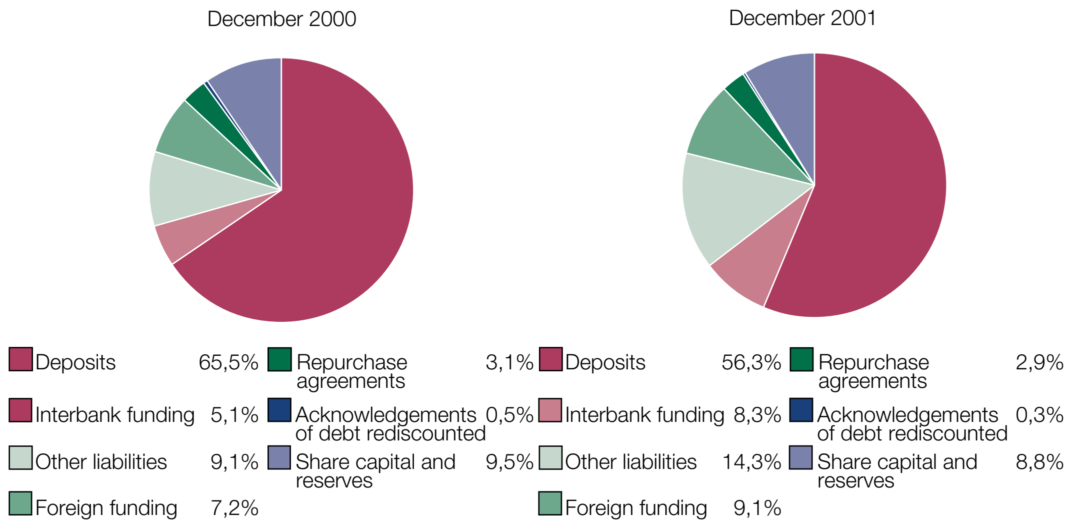


Figure 1 graphically depicts the quarter-end value of, and percentage growth (measured over 12 months) in, the aggregated balance sheet of the banking sector for the period from March 1999 to December 2001. Growth in the aggregated balance sheet picked up markedly from June 2000 and, by the end of December 2001, had increased by 27,6 per cent.

Liabilities

A year-on-year comparison of the composition of liabilities is reflected in Figure 2.

FIGURE 2: LIABILITIES – YEAR-ON-YEAR COMPARISON



domestic deposits from the public remained the main source of funding

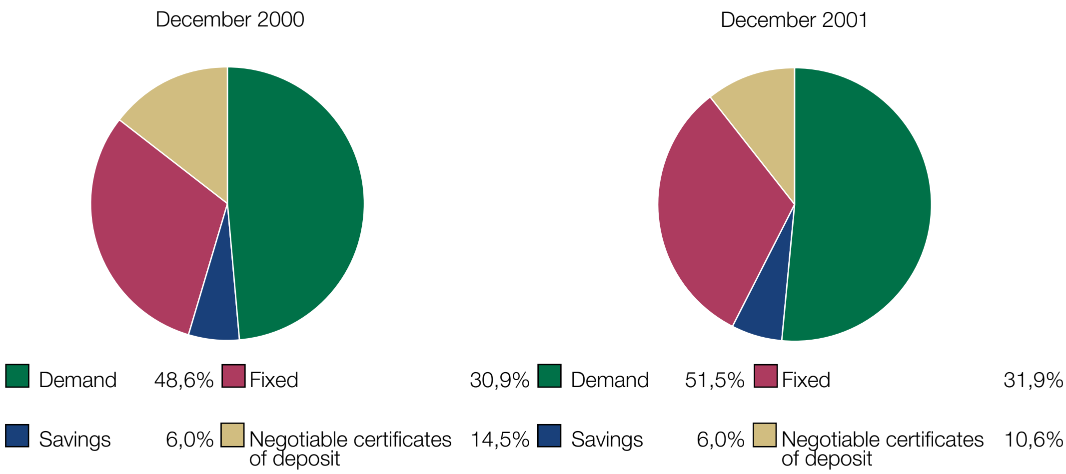
Domestic deposits from the public in the amount of R588,9 billion remained the main source of funding for the banking sector and constituted 56,3 per cent of total liabilities in December 2001, compared to 65,5 per cent in December 2000 and 68,8 per cent in December 1999. Foreign funding as a percentage of total liabilities, on the other hand, increased from 7,2 per cent in December 2000 to 9,1 per cent in December 2001, mainly because of the depreciation of the South African rand. Interbank funding increased from 5,1 per cent in December 2000 to 8,3 per cent in December 2001.

Composition of non-bank deposits

changed slightly in favour of demand deposits

Figure 3 reflects a year-on-year comparison of the composition of non-bank deposits. The composition of non-bank deposits changed slightly in favour of demand deposits. Compared to the previous year, demand deposits increased by 2,9 percentage points, whereas negotiable certificates of deposit decreased by 3,9 percentage points. Negotiable certificates of deposit as a percentage of total non-bank deposits decreased from 14,5 per cent to 10,6 per cent. This was due to an amendment to the Regulations relating to Banks, in terms of which the amount of negotiable certificates of deposit that banks issue to banks in the same group have to be included in intragroup bank funding.

FIGURE 3: COMPOSITION OF NON-BANK DEPOSITS

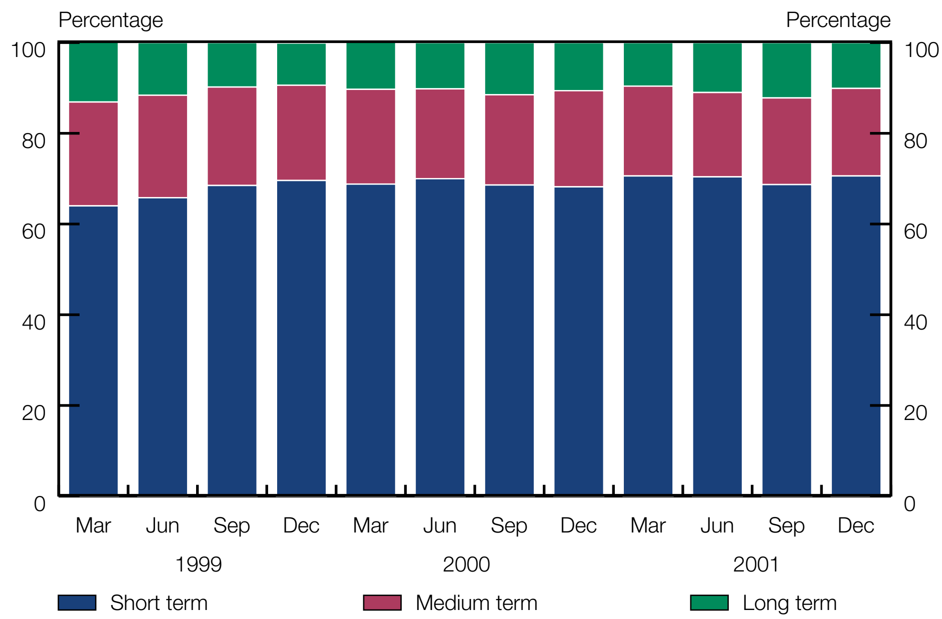


Maturity structure of non-bank deposits

short-term deposits remained the biggest component of total non-bank funding

Figure 4 reflects the composition of non-bank deposits (according to maturity) for the period from March 1999 to December 2001. As can clearly be seen from this figure, short-term deposits remained the biggest component of total non-bank funding and accounted for 70,6 per cent of total non-bank funding as at 31 December 2001, compared to 68,2 per cent at the end of December 2000 and 69,6 per cent at the end of December 1999. Long-term deposits, on the other hand, remained the smallest component of total non-bank funding and accounted for 10,1 per cent of total non-bank funding as at 31 December 2001, compared to 10,6 per cent and 9,3 per cent at the end of December 2000 and the end of December 1999, respectively. Medium-term deposits accounted for the remaining 19,3 per cent as at December 2001, compared to 21,2 per cent and 21 per cent at the end of December 2000 and the end of December 1999, respectively.

FIGURE 4: COMPOSITION OF NON-BANK FUNDING ACCORDING TO MATURITY

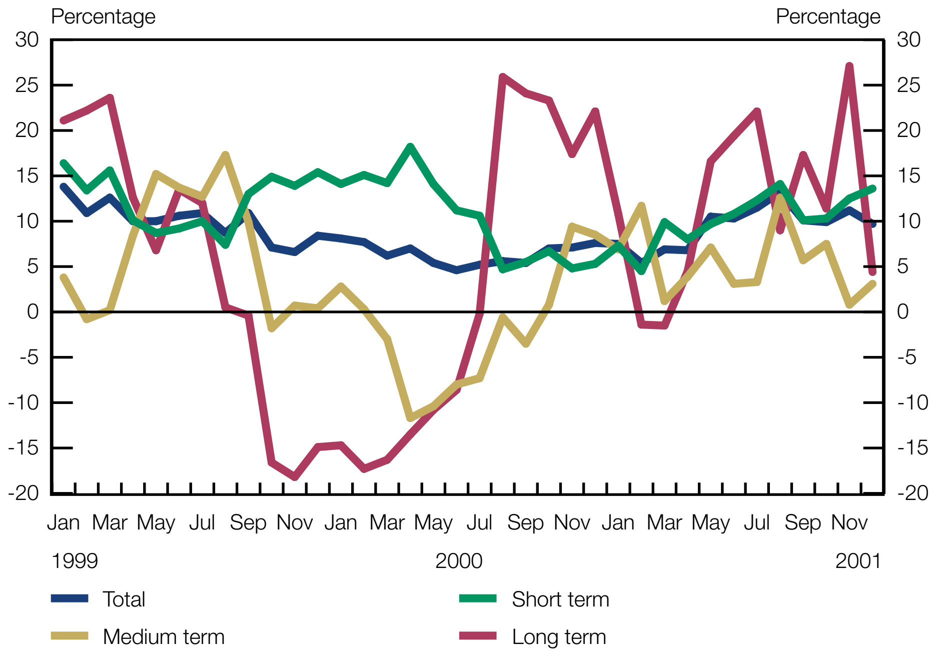


The slight increase in the proportion of total deposits represented by short-term deposits resulted in a slightly higher percentage of the banking sector's assets (consisting mainly of non-bank loans and advances) being financed by short-term funding. Thereby, the liquidity risk to which banks are exposed increased.

growth in long-term deposits was volatile

As indicated above, long-term deposits remained the smallest component of total non-bank funding, but growth in long-term deposits was volatile throughout 2001 (see Figure 5). Measured over a 12-month period, growth in long-term deposits declined by 1,5 per cent during February and March 2001, but had increased by about 22,1 per cent by the end of July 2001. By the end of December 2001, however, growth in long-term deposits had moderated to 4,4 per cent. The big six banks held more than 73,2 per cent of long-term deposits.

FIGURE 5: GROWTH IN NON-BANK FUNDING ACCORDING TO MATURITY (percentage change over 12 months)



growth in short-term deposits remained strong

Growth in short-term deposits, on the other hand, remained strong throughout 2001 and, compared to December 2000, increased by 13,6 per cent in December 2001. Growth in medium-term deposits remained volatile and growth rates varied between 1,2 per cent in March 2001 and 12,6 per cent in August 2001. By the end of December 2001, however, medium-term deposits had declined by 0,1 per cent (measured over a 12-month period).

other major liabilities

Other major liabilities of the banking sector as at 31 December 2001 included foreign funding of R95,1 billion, which increased by 60,6 per cent when compared to December 2000. This increase in foreign funding was boosted by the depreciation of the rand. Capital and reserves increased by 19,1 per cent, to R92,4 billion from R77,5 billion in December 2000. Other liabilities increased to R149,2 billion (representing a growth rate of 100,1 per cent when compared to the December 2000 level of R74,6 billion), and interbank funding increased to R87,1 billion (representing a growth rate of 107,4 per cent when compared to the amount of R42 billion at the end of December 2000). Other liabilities included amounts owing to the South African Reserve Bank, trade creditors, deferred income, deferred tax balances, impairments and other funding liabilities.

Assets

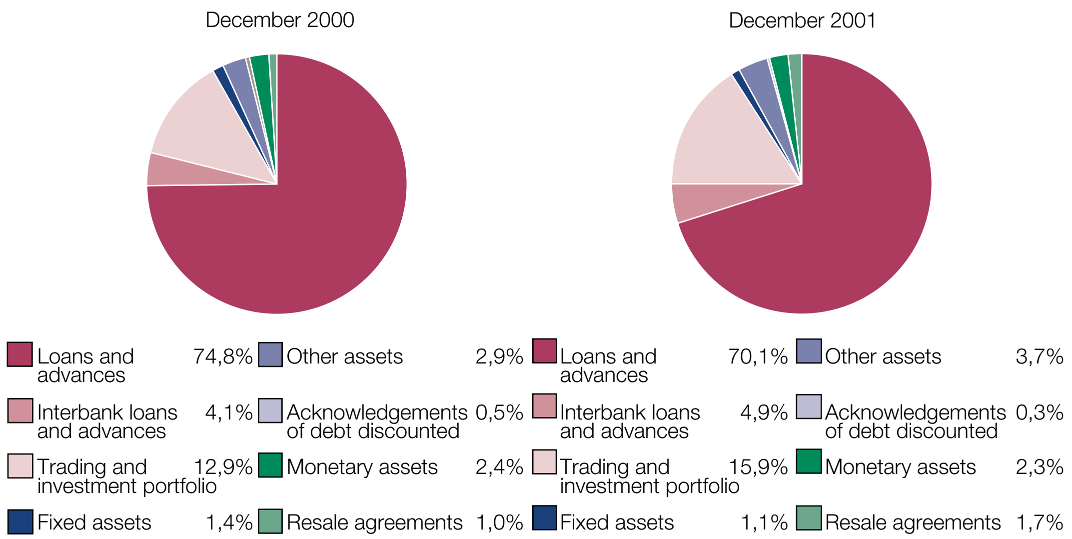
assets increased by R226,3 billion

Figure 6 graphically reflects a year-on-year comparison of the composition of assets as at 31 December 2001 and that as at 31 December 2000. The banking sector's assets increased by R226,3 billion (representing a growth rate of 27,6 per cent) during the year, to a total of R1 045,6 billion at the end of December 2001. Factors contributing to this growth were the following:

factors contributing to growth

- Monetary assets grew by 21,1 per cent, from R19,9 billion as at 31 December 2000 to R24 billion as at 31 December 2001.
- The trading and investment portfolio increased from R105,5 billion as at December 2000 to R166,8 billion as at December 2001, representing a growth rate of 58 per cent.
- Non-bank advances grew by R120,2 billion (representing a growth rate of 19,6 per cent), from R612,5 billion at the end of December 2000 to R732,7 billion a year later.
- Interbank advances increased by 54,7 per cent, from R33,3 billion at the end of December 2000 to R51,5 billion at the end of December 2001.
- Loans granted under resale agreements increased from R8,6 billion at the end of December 2000 to R17,9 billion at the end of December 2001.
- Non-financial assets increased by 6 per cent, from R11,2 billion at the end of December 2000 to R11,9 billion at the end of December 2001.
- Other assets increased by 58,2 per cent, from R24 billion at the end of December 2000 to R37,9 billion at the end of December 2001.

FIGURE 6: ASSETS – YEAR-ON-YEAR COMPARISON



It is apparent from Figure 7 that growth in total loans and advances was very volatile during 1999, but slowed down somewhat in the first half of 2000. From June 2000, however, growth in total loans and advances recovered and increased nearly uninterruptedly until the total loans and advances accounted for about 78 per cent of total assets

end of 2001. By the end of December 2001, loans and advances had increased by 22,3 per cent (measured over a period of 12 months). The increase in the growth of total assets can therefore be attributed to an increase in total loans and advances, which accounted for about 78 per cent of total assets by the end of December 2001 (see Figure 8).

FIGURE 7: TOTAL LOANS AND ADVANCES

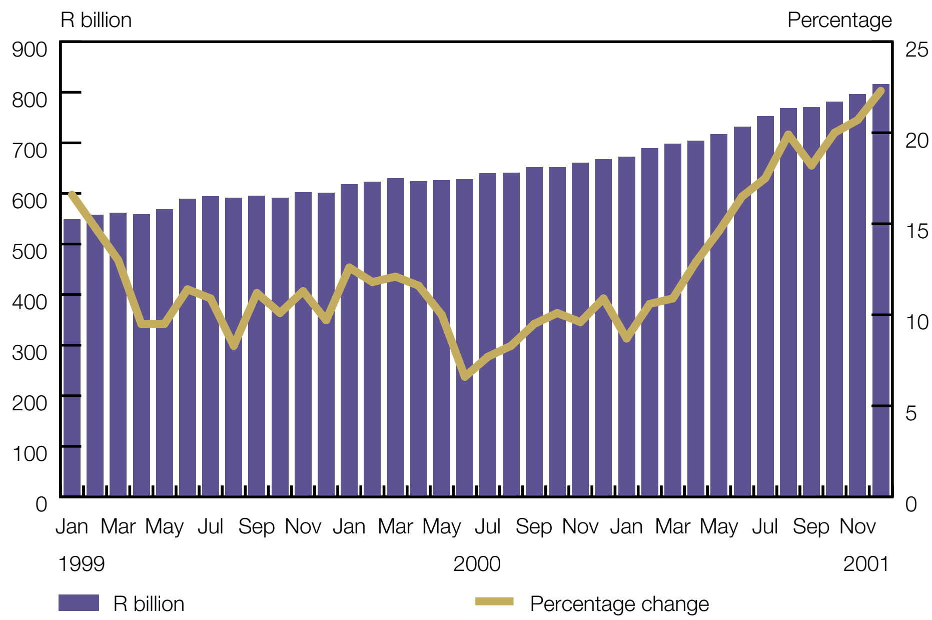
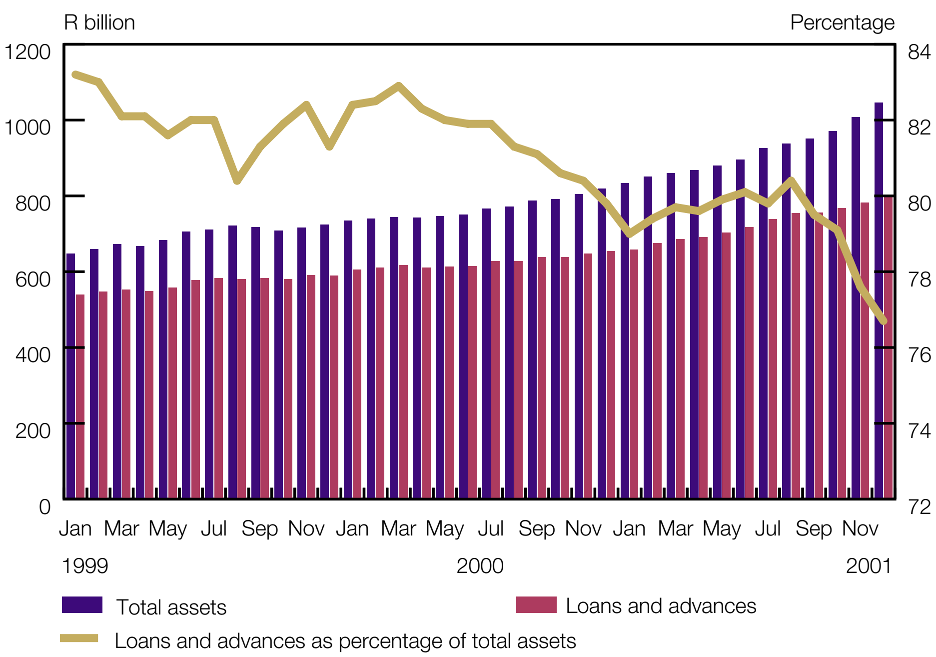


FIGURE 8: LOANS AND ADVANCES AS A PERCENTAGE OF TOTAL ASSETS



increase in the trading and investment portfolio

Loans and advances as a percentage of total assets have been decreasing since August 2001 (see Figure 8). The lower percentage of loans and advances to assets was due mainly to the above-mentioned increase in the trading and investment portfolio of banks as a percentage of total banking sector assets.

Composition of loans and advances

mortgage loans and overdrafts and loans decreased

The composition of loans and advances is shown graphically in Figure 9. A comparison of the composition of loans and advances in 2000 and 2001 clearly shows that instalment debtors remained fairly unchanged, whereas mortgage loans and overdrafts and loans decreased as a percentage of total loans and advances. Mortgage loans decreased from 32,7 per cent in December 2000 to 30,9 per cent in December 2001, and overdrafts and loans decreased from 32,7 per cent in December 2000 to 28,3 per cent in December 2001.

Foreign loans, on the other hand, increased from 8,4 per cent in December 2000 to 13,5 per cent in December 2001, and resale agreements increased from 1,3 per cent in December 2000 to 2,2 per cent in December 2001. Acknowledgements of debt discounted decreased from 2,1 per cent in 2000 to 1,9 per cent in 2001, whereas other loans and advances increased from 8,9 per cent in December 2000 to 9,9 per cent in December 2001.

non-bank loans and advances represented main area of focus for the management of on-balance-sheet credit risk

As at the end of December 2001, non-bank loans and advances constituted 70,1 per cent (December 2000: 74,8 per cent) of the banking sector's assets and, thus, represented the main area of focus for the management of on-balance-sheet credit risk. The increase of R120,2 billion (2000: R60,8 billion), representing a growth rate of 19,6 per cent (2000: 11 per cent), achieved in respect of non-bank advances during the year under review can be attributed to the following areas (Figure 10):

reasons for increase in non-bank advances

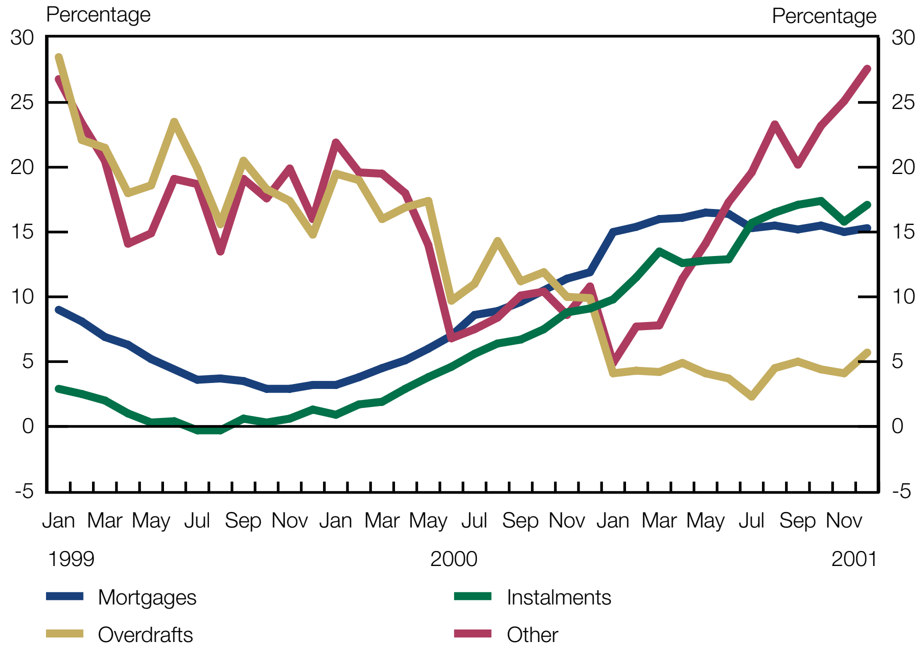
- ▲ Mortgage loans increased by R33,4 billion to a level of R251,9 billion, representing an increase of 15,3 per cent measured over a 12-month period.
- ▲ Overdrafts and loans increased by R12,4 billion to a level of R230,7 billion, representing a growth rate of 5,7 per cent.
- ▲ Instalment debtors increased by R13,8 billion to a level of R94,8 billion, representing an increase of 17,1 per cent.
- ▲ Foreign-currency loans and advances increased by R54 billion to a level of R109,9 billion, representing an increase of 96,6 per cent.
- ▲ Credit cards increased by R1,4 billion to a level of R13,5 billion, representing an increase of 11,2 per cent.

FIGURE 9: COMPOSITION OF LOANS AND ADVANCES

December 2000				December 2001			
Mortgage loans	32,7%	Foreign loans	8,4%	Mortgage loans	30,9%	Foreign loans	13,5%
Instalment debtors	12,1%	Overdrafts and loans	32,7%	Instalment debtors	11,6%	Overdrafts and loans	28,3%
Other*	8,9%	Acknowledgements of debt discounted	2,1%	Other*	9,9%	Acknowledgements of debt discounted	1,9%
Resale agreements	1,3%	Credit-card debtors	1,8%	Resale agreements	2,2%	Credit-card debtors	1,7%

* Negotiable certificates of deposit and redeemable preference shares

FIGURE 10: GROWTH IN SELECTED LOANS AND ADVANCES



3.2 CAPITAL ADEQUACY

Capital provides a safety net to depositors and other providers of loan finance against losses that a bank might incur. For this reason, it is very important that only banks that are adequately capitalised be authorised to accept deposits from the public. As experience has shown, however, the existence of adequate capital does not provide a guarantee against the failure of a bank that is badly managed.

capital-adequacy ratio was 11,4 per cent

For the year under review, the average capital and reserves held by the banking sector amounted to R92,4 billion (R76,3 billion in December 2000), R73,5 billion (2000: R66,9 billion) of which constituted qualifying capital and reserves for purposes of assessing capital adequacy. The capital-adequacy ratio for the year ended December 2001 was 11,4 per cent (2000: 12,5 per cent).

banks that did not meet the required minimum ratio had phase-in programmes

An analysis of the percentage distribution of banks in terms of capital adequacy at the end of December 2001 (see Figure 11) reveals that 11,5 per cent (2000: 20,4 per cent) of the total number of banking institutions did not meet the new minimum capital-adequacy ratio of 10 per cent, whereas 34,6 per cent of banking institutions (2000: 44,4 per cent) had capital-adequacy ratios that exceeded 20 per cent. Banks that did not meet the required minimum capital-adequacy ratio of 10 per cent had in place phase-in programmes, which had been approved by the Registrar.

Banking institutions that reported capital-adequacy ratios of above 20 per cent (that is, 34,6 per cent of institutions) represented only 2,6 per cent of total banking-sector assets (see Figure 12). Banking institutions with a capital-adequacy ratio of between 10 per cent and 12 per cent (30,8 per cent of banking institutions) represented the biggest portion of total banking-sector assets, namely, 48,9 per cent. The banking institutions that did not meet the minimum capital-adequacy requirement of 10 per cent represented 39,1 per cent of total banking-sector assets.

FIGURE 11: DISTRIBUTION OF BANKS IN TERMS OF CAPITAL ADEQUACY

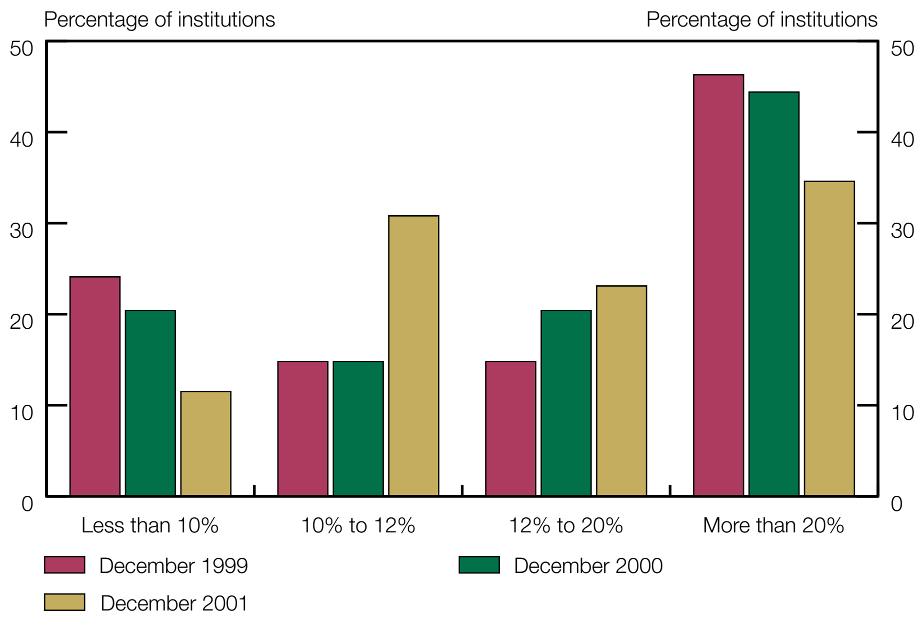
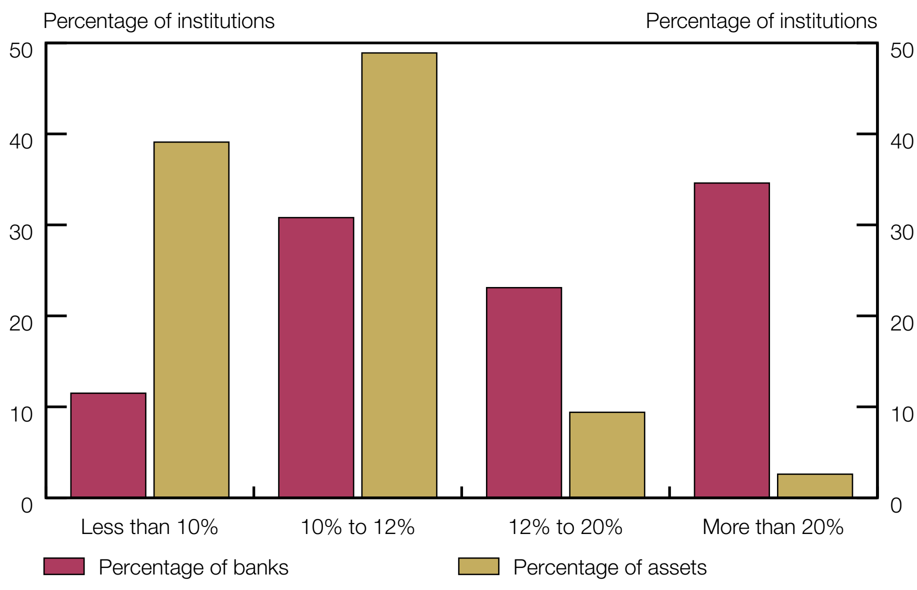


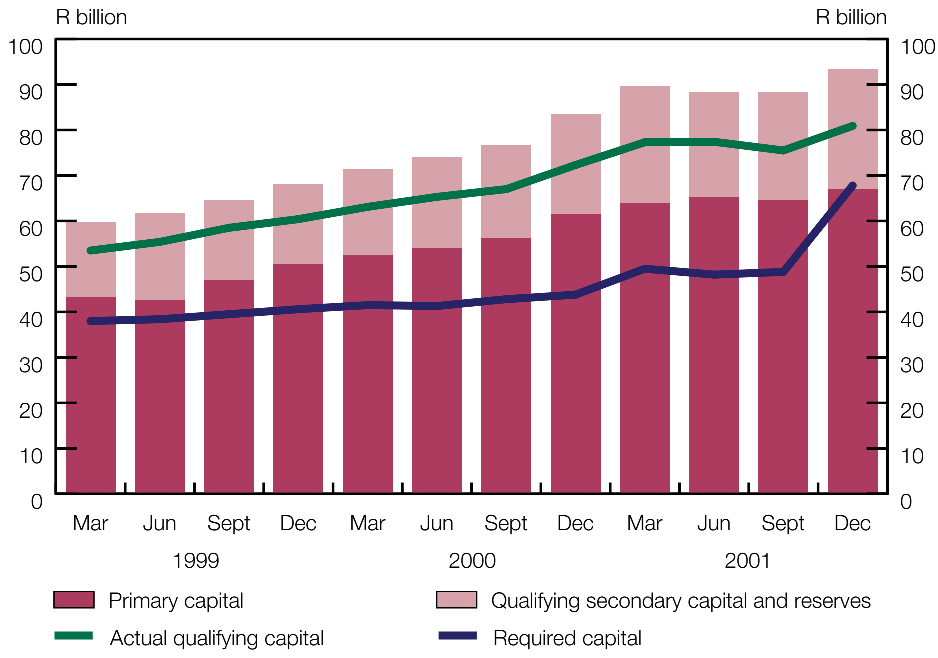
FIGURE 12: BANKS' CAPITAL ADEQUACY IN TERMS OF TOTAL ASSET VALUE



net qualifying caital and reserves growth was lower than the growth in the total balance sheet

Figure 13 reflects the split, over time, between primary and secondary capital, as well as the rand values of required capital and actual qualifying capital. At the end of December 2001, primary capital and reserves constituted 71,8 per cent (2000: 73,7 per cent) of qualifying capital and reserves before deduction of impairments amounting to R12,4 billion (2000: R11,2 billion). Primary capital and reserves grew by 16,3 per cent (2000: 22,2 per cent) during the year, to R67 billion at the end of December 2001. Qualifying secondary capital and reserves, on the other hand, grew by 21,6 per cent during the year (2000: 19,8 per cent), to R26,4 billion at the end of December 2001. The net qualifying capital and reserves growth of 16,3 per cent was lower than the growth in the total balance sheet of 27,6 per cent.

FIGURE 13: QUALIFYING CAPITAL AND RESERVES



Risk profile of on- and-off-balance-sheet items

marked increase in off-balance sheet items was due mainly to amendments to the Regulations

For the year ended 31 December 2001, total assets and off-balance-sheet items (Figure 14) grew by 76,4 per cent (2000: 14,3 per cent), whereas total risk-weighted assets and off-balance-sheet items decreased by 2,8 per cent (2000: 15,9 per cent). The marked increase in off-balance sheet items in 2001 compared to 2000 was due mainly to amendments to the Regulations relating to Banks. In terms thereof, banks were required to report on central securities-depository participation, which, however, did not affect the average risk weighting of assets.

average combined risk weighting of 56,7 per cent

The composition of off-balance-sheet-items had the effect of increasing the average risk weighting of total assets, which amounted to 65,8 per cent for December 2001 (2000: 73,7 per cent), to an average combined risk weighting of 56,7 per cent (2000: 71 per cent) for assets and off-balance-sheet items. The latter accounted for approximately 42,9 per cent (December 2000: 11 per cent) of the combined total of assets and off-balance-sheet items at the end of December 2001. The risk-weighted percentages of assets and off-balance-sheet items and of the combined total of assets and off-balance-sheet items are graphically illustrated in Figure 14.

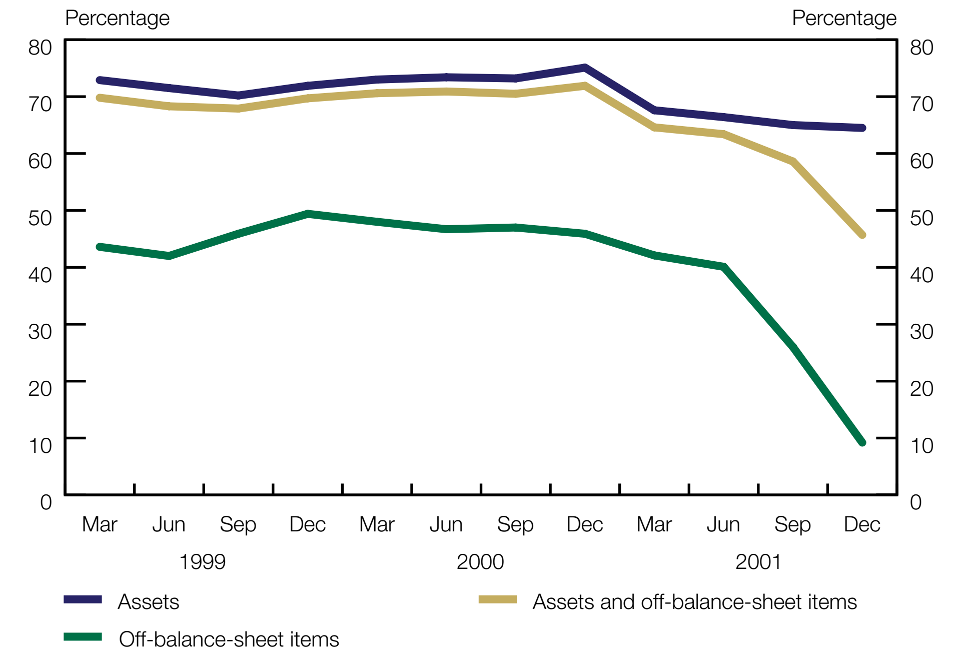
3.3 PROFITABILITY

An evaluation of the profitability of banks involves an assessment of the quality of income and the long-term sustainability of the activities that generate the income. For this reason, the analyses focus on the following aspects:

analysis focus on the following aspects

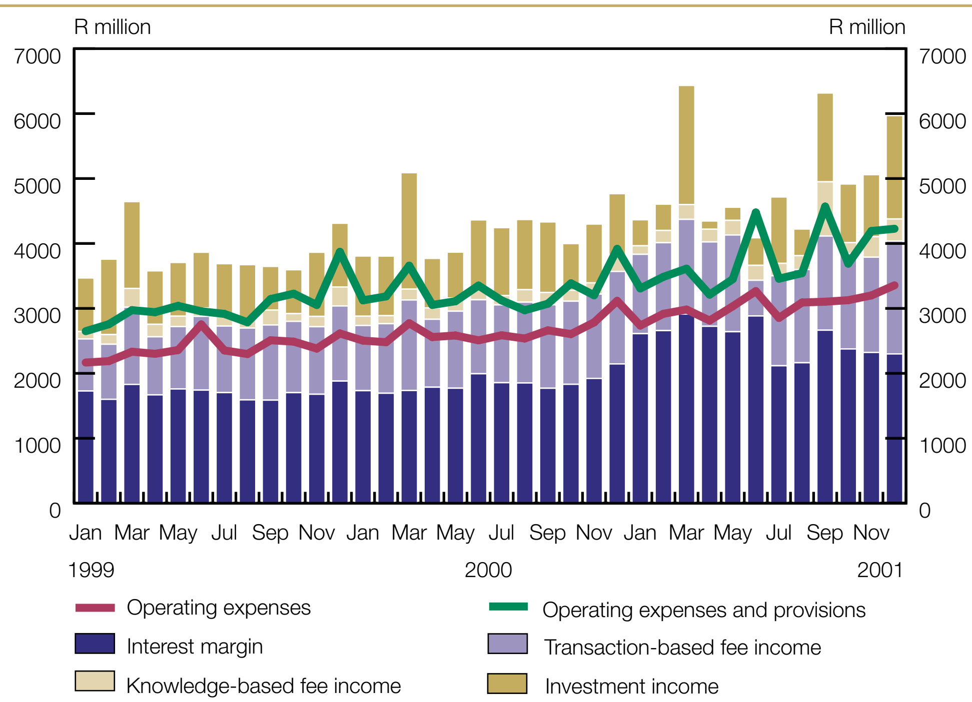
- Quality of earnings (riskiness of earnings).
- Balance in the various sources of income (such as, a good spread of income sources).
- Nature of income (such as, the intermediation function, advisory services or trading activities).
- Integrity of the information (whether the income statement is consistent with the balance sheet).

FIGURE 14: RISK PROFILE OF ON- AND OFF-BALANCE-SHEET ITEMS



- Profitability of assets and effectiveness of activities versus cost control and cost optimisation.
- Balance between the effort expended on activities and the income generated therefrom.
- Structural changes in profitability during the year.

FIGURE 15: COMPOSITION OF THE INCOME STATEMENT



intermediation function again constituted the main source of income

As can be seen in Figure 15, the intermediation function again constituted the main source of income for banks. The intermediation function consists of interest margin (an average of 3,3 per cent of total assets for the year, as opposed to 2,9 per cent in 2000) and transaction-based fee income (an average 1,8 per cent of total assets for the year, as opposed to 1,9 per cent in 2000). As can be observed from Figure 15, the income derived from the intermediation function (R46,7 billion) was generally just sufficient to cover the sum of operating expenses and provisions (R45,2 billion). It is thus clear that the generation of additional income (that is, from investments in Government stock and Treasury bonds, as well as knowledge-based fee income derived from trading activities, and agency type and advisory activities) remains critical to ensure the continued profitability of banks. Fee income and investment and trading income earned during the year were on average equivalent to 2,1 per cent and 1,0 per cent, respectively, of total assets (as opposed to 2,2 per cent and 1,6 per cent, respectively, during 2000).

Interest income increased by about 12,4 per cent for the year, which was 9,2 percentage points higher than the increase of 3,2 per cent in interest expense. The net result thereof was that the interest margin grew by 37,4 per cent (2000: 7,8 per cent). Interest derived from mortgage bonds and overdrafts and loans constituted 33,2 per cent and 30,1 per cent, respectively, of total interest income (as opposed to 35 per cent and 32,5 per cent, respectively, during 2000).

The main component of interest expense was interest on demand deposits and fixed and notice deposits. Interest paid in respect of demand deposits constituted 33,9 per cent (2000: 36,1 per cent) of the total interest expense, whereas interest paid on fixed and notice deposits constituted 28,9 per cent (2000: 25,7 per cent) of the total interest expense for the year.

FIGURE 16: INTEREST MARGIN

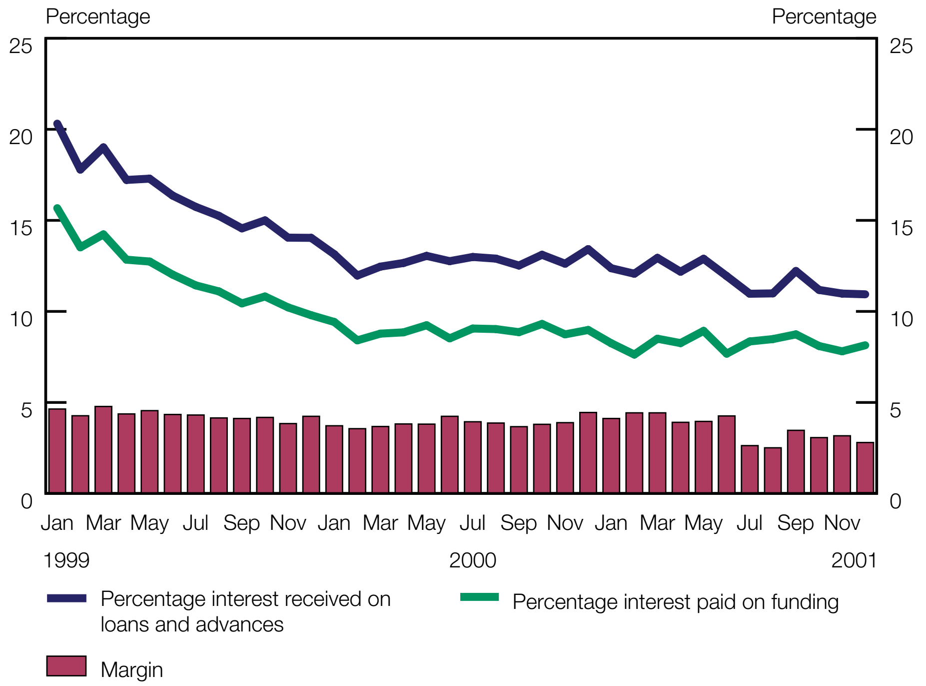
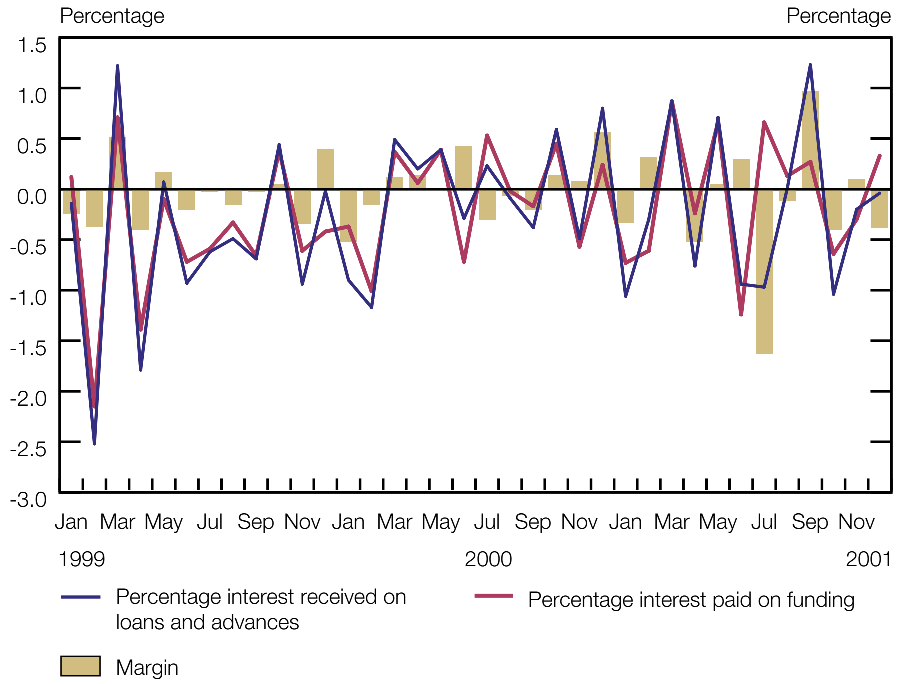


Figure 16 graphically displays the interest margin of the banking sector for the period from January 1999 to December 2001, whereas Figure 17 represents the percentage-point change in the components of the interest margin for the aforementioned period. As can clearly be seen from Figure 16, the interest margin for the year was on average higher

(4,2 per cent) than in 2000 (3,9 per cent). For the 12 months ended December 2001, the average interest margin was 3,5 per cent, compared to 4,3 per cent in 2000 and 4,2 per cent in 1999. An analysis of the relative monthly percentage-point change in the underlying components, as well as in the interest margin (Figure 17), displayed clear seasonal tendencies.

FIGURE 17: PERCENTAGE-POINT CHANGE IN INTEREST MARGIN



operating expenses increased by 15,1 per cent

The operating expenses of the total banking sector increased by 15,1 per cent (2000: 10,2 per cent) in 2001, mainly as a result of an increase of 13,8 per cent in total staff expenses, which accounted for about 55,0 per cent of total operating expenses. The increase in total staff expenses, however, was not due to an increase in the number of people employed. This is confirmed by Figure 18, which graphically displays the percentage change (meas-ured over a 12-month period) in total staff expenses, the number of people employed and the number of branches for the past three years. For the year 2001, employment in the banking sector decreased by 0,2 per cent, whereas the number of branches increased by 14,1 per cent compared to the year before.

Growth in operating expenses was also boosted by an increase in administrative expenses. Compared to the previous year, administrative expenses increased by 18,4 per cent and accounted for 47,6 per cent of total operating expenses.

lower efficiency in the banking sector

Growth in total income of 11,3 per cent could not offset the increase in operating expenses (15,1 per cent), resulting in lower efficiency in the banking sector (see Figure 19) during the year under review.

FIGURE 18: GROWTH IN STAFF EXPENSES, NUMBER OF PEOPLE EMPLOYED AND NUMBER OF BRANCHES AND AGENCIES

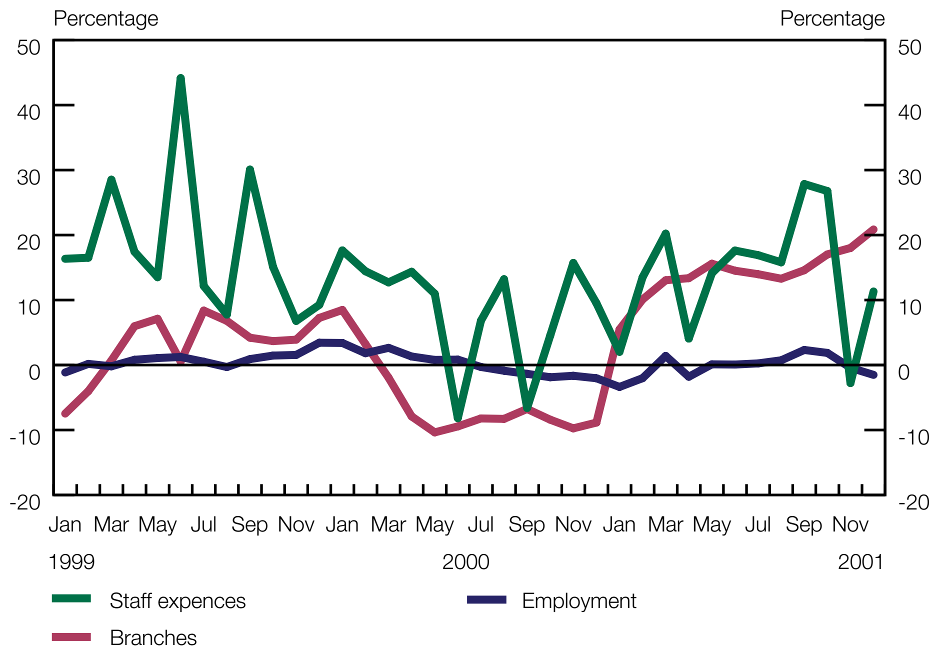
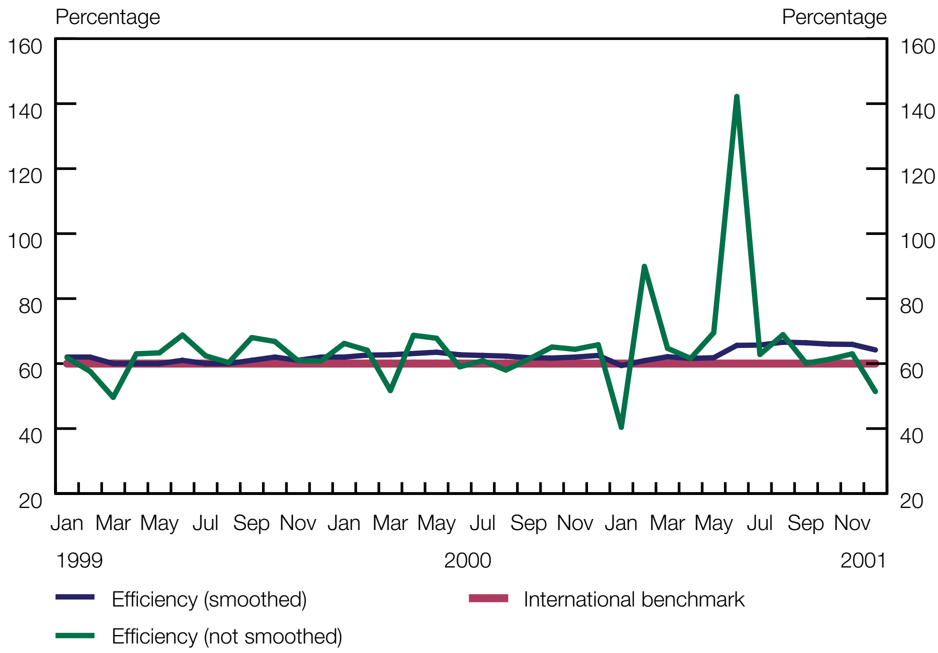


FIGURE 19: EFFICIENCY OF SOUTH AFRICAN BANKING SECTOR



The efficiency of the banking sector can be determined by expressing operating expenses as a percentage of total income. Currently, the international benchmark for efficiency is 60 per cent. In other words, banks that have an efficiency ratio of above 60 per cent are regarded as less efficient.

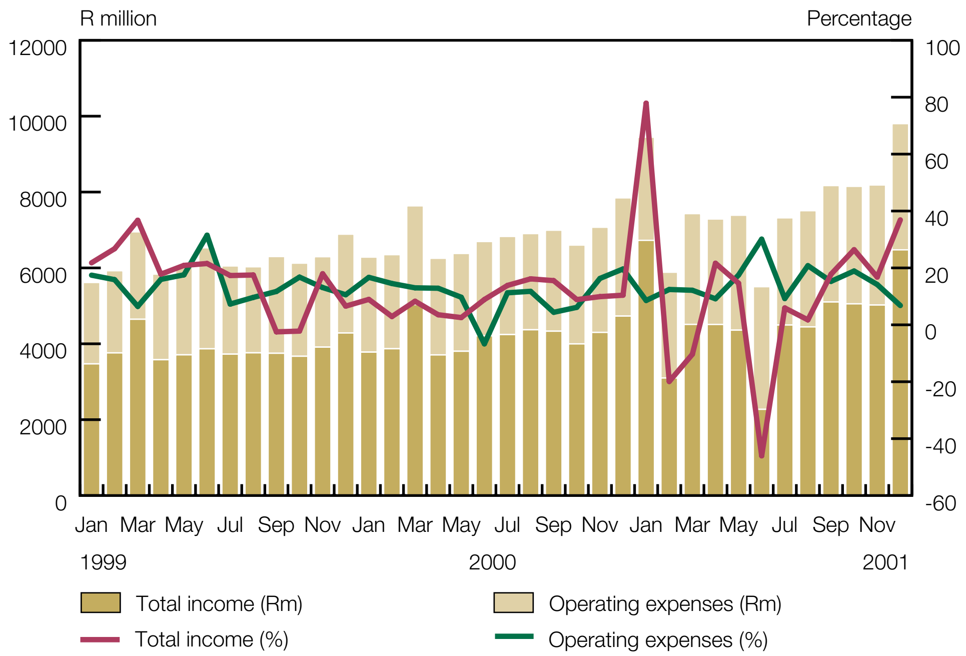
high volatility in efficiency was due mainly to the implementation of AC 133 by some banks

Figure 19 reflects the efficiency of the South African banking sector for the past three years. The high volatility in efficiency for the year 2001 was due mainly to the implementation of Accounting Standard AC 133 by some banks in January 2001. In terms of the disclosure requirements of AC 133, banks are required, in respect of financial-year periods commencing on or after 1 January 2001, to reflect the net mark-to-market adjustments of investments (fair-value accounting) in their financial statements, as opposed to the equity accounting (book value or purchase price) done previously.

The Accounting Practice Board, however, had reconsidered the implementation date of AC 133 and announced that AC 133 would become effective for financial years commencing on or after 1 July 2002. The objective of the delayed implementation was to enable companies to improve their business practices and systems and to complete the necessary training. Some banks, however, had already implemented AC 133 and reported data in accordance with the requirements of AC 133 for 2001. For the year as a whole, efficiency, at 64,2 per cent, was lower on average (smoothed over a 12-month period) than in the previous year (2000: 62,5 per cent).

The actual values of, and the percentage growth in, the determinants of efficiency are graphically displayed in Figure 20.

FIGURE 20: DETERMINANTS OF EFFICIENCY



banks with assets above R5 billion, but below R10 billion were the most efficient in December 2001

Figure 21 graphically displays the efficiency of the various categories (according to asset size) of banking institution for the year ended December 2001. The figure clearly shows that banks with assets above R5 billion, but below R10 billion, in value were the most efficient in December 2001, with an efficiency ratio of 45,1 per cent, followed by banks with assets above R100 billion, with an efficiency ratio of 46,4 per cent. The least efficient were banks with asset values above R50 billion, but below R100 billion, and banks with asset values below R1 billion. It should be borne in mind that these figures are compiled for one month at a time. Because operating expenses and total-income components can fluctuate drastically from one month to another, the average efficiency ratios of different banks would fluctuate accordingly.

average efficiency ratios fluctuate from one month to another

FIGURE 21: EFFIENCY OF BANKING INSTITUTIONS ACCORDING TO ASSET SIZE – DECEMBER 2001

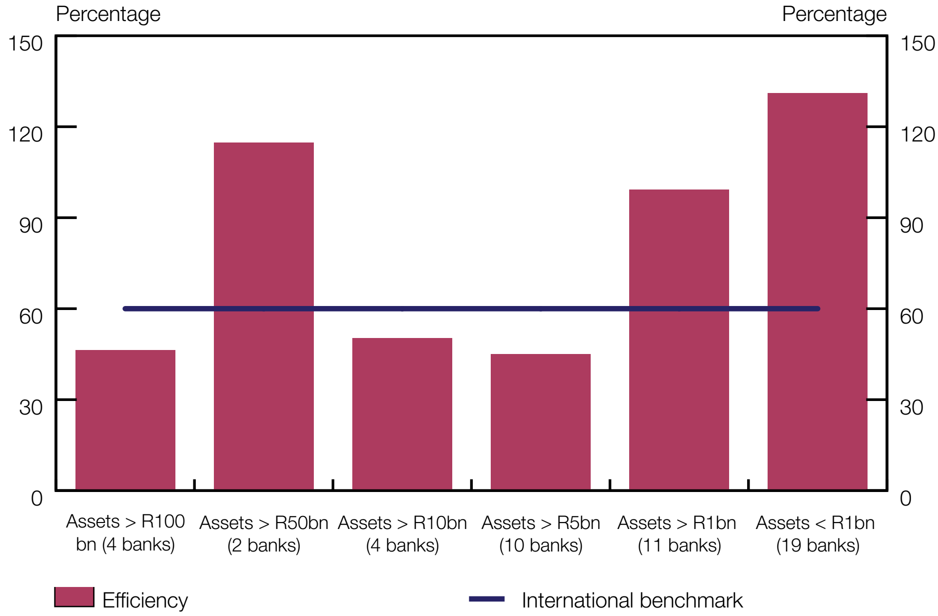
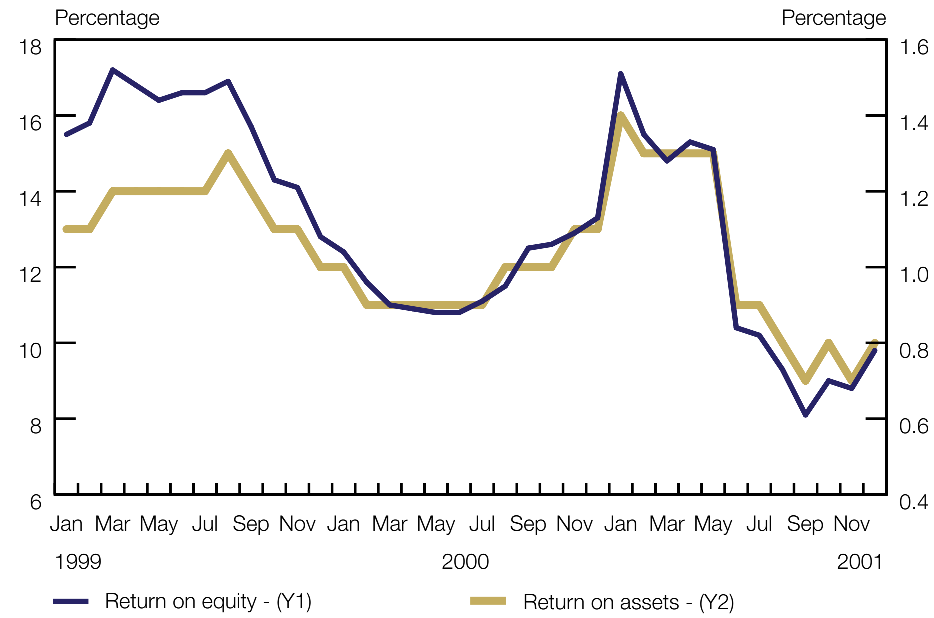


FIGURE 22: PROFITABILITY (12-month smoothed average)



The banking sector achieved a before-tax return equivalent to approximately 1,0 per cent of total assets (2000: 1,5 per cent). An after-tax return equivalent to approximately 0,7 per cent of total assets (2000: 1,1 per cent) was reported for 2001, whereas an after-tax return equivalent to approximately 9,2 per cent was reported on net qualifying capital and reserves (2000: 12,0 per cent).

marked deterioration in both ROA and ROE was due mainly to losses in the investment portfolio in terms of AC 133

The trends (calculated on the basis of a 12-month moving average) in return on equity (ROE) and return on assets (ROA) for the past three years are graphically displayed in Figure 22. After a marked deterioration in both the ROA and the ROE during the period from September 1999 until June 2000, both the ROA and the ROE improved noticeably until January 2001. This improvement was due mainly to a higher net income after tax resulting from slower growth in operating expenses. From January 2001, however, a marked deterioration in both ROA and ROE, however, can clearly be detected from Figure 22. This deterioration was due mainly to losses in the investment portfolio reported by some banks in terms of AC 133.

FIGURE 23: PRODUCTIVITY

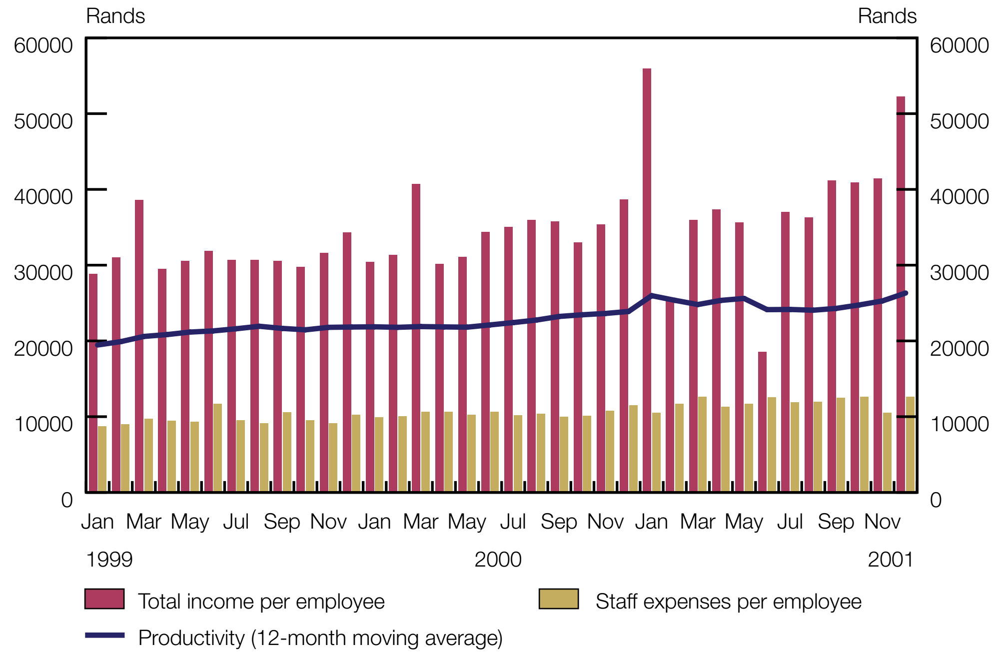


Figure 23 graphically displays the productivity of the banking sector for the past three years, measured by comparing the expenditure on employees with the amount of income generated. During the year under review, the total income generated per employee was on average equivalent to R38 200, as opposed to R34 300 in 2000. Staff expenses per employee, on the other hand, were on average R11 900 in 2001, as opposed to R10 400 during 2000. Also reflected in Figure 23 is the average (smoothed over 12 months) net income generated per employee. The net income generated per employee increased from R23 900 to R26 300, indicating that the productivity of employees in the banking sector improved during the year under review.

productivity of employees improved

3.4 LIQUIDITY RISK

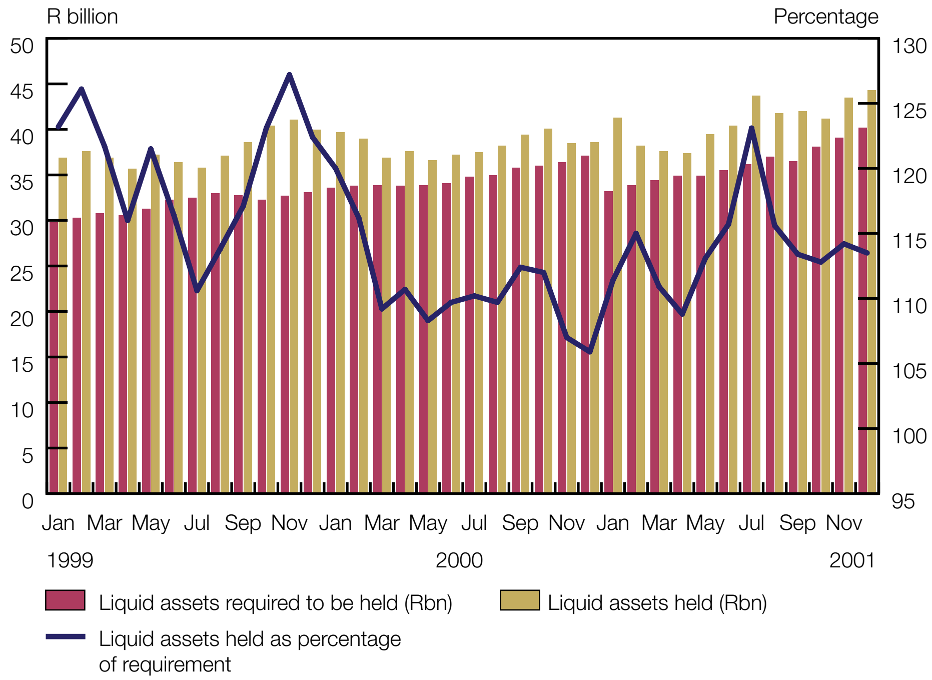
An evaluation of liquidity-risk management involves an assessment of the level of compliance with the statutory liquid-asset requirements, an analysis of the short-term liquidity mismatch in terms of its size (in relation to total funding) and its trend, an assessment of the sources of liquid funds available for funding such mismatches and a consideration of the volatility of funding sources available. Mismatches may develop in various future time bands, because management has taken a specific view of future interest-rate movements. Therefore, the relationship between interest-rate risk management and liquidity-risk management also has to be borne in mind.

Statutory liquidity

average daily amount of liquid assets held exceeded statutory requirement

The liquid-asset requirement is calculated on total liabilities less capital and reserves (referred to as adjusted liabilities). Figure 24 shows that the average daily amount of liquid assets held by banks exceeded the statutory liquid-asset requirement throughout the year under review.

FIGURE 24: STATUTORY LIQUID ASSETS – ACTUAL VERSUS REQUIRED



Approximately 66,1 per cent (2000: 48,9 per cent) of the average daily amount of liquid assets held during December 2001 consisted of securities issued by virtue of section 66 of the Public Finance Management Act, 1999, whereas 24,7 per cent (2000: 43,3 per cent) consisted of Treasury bills of the Republic of South Africa and 2,4 per cent (2001: 5,1 per cent) consisted of short-term bills issued by the Land Bank. Cash-management schemes managed on behalf of banks' clients increased by about 20,5 per cent (2000: 0,8 per cent). Set-off had increased by 9,7 per cent (measured over 12 months) as at the end of December 2001, and represented approximately 9,9 per cent (2000: 9,8 per cent) of adjusted liabilities. This means that the adjusted liabilities, which are used for purposes of computing the liquid-asset and reserve-balance requirements, were reduced by 13,4 per cent (2000: 12,9 per cent), or R124,7 billion (2000: R110 billion), because of use of cash-management schemes by banks' clients and the setting off of some asset balances against liabilities.

adjusted liabilities were reduced by 13,4 per cent

Volatility of funding

As at 31 December 2001, total wholesale deposits constituted 84,4 per cent (2000: 77,9 per cent) of total wholesale and retail deposits. As can be seen in Figure 25, wholesale deposits shorter than three months represented 47,9 per cent of total funding for December 2001. The sharp decline in wholesale deposits shorter than three months in January 2001 compared to December 2000 (from R364,2 billion in December 2000 to comparisons over time should be made with caution

R281,6 billion in January 2001) can mainly be explained by some banks having been unable to report in terms of the amended Regulations relating to Banks. Because of an amendment to the definition of wholesale deposits, however, comparisons over time should be made with caution.

The aggregate amount of the 10 largest depositors of individual banks averaged R112,8 billion (2000: R99,5 billion) during the year under review. Expressed as a percentage of the aggregate amount of total funding-related liabilities to the public, large depositors averaged 15,1 per cent (2000: 15 per cent) at the end of December 2001 (see Figure 25).

FIGURE 25: WHOLESALE DEPOSITS SHORTHER THAN THREE MONTHS AND LARGE DEPOSITORS

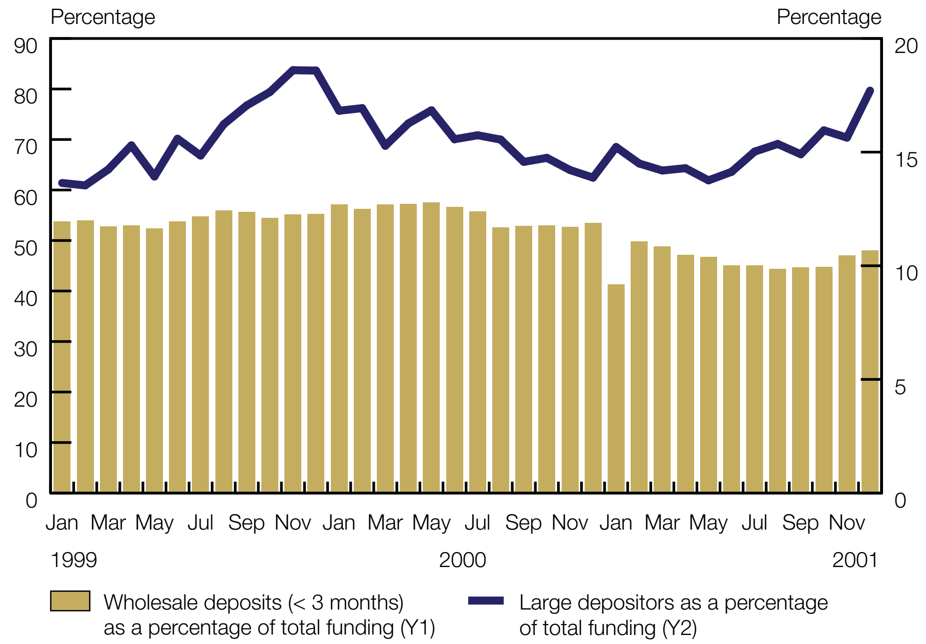
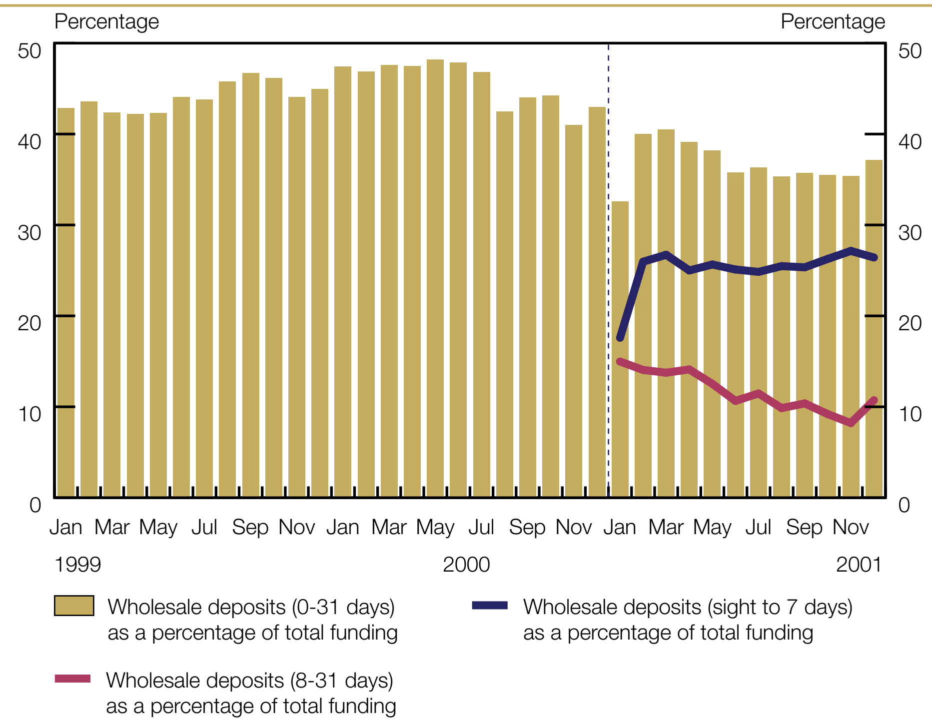


FIGURE 26: SHORT-TERM WHOLESALE DEPOSITS



Short-term wholesale deposits (0-31 days) represented 37,2 per cent of total funding in December 2001, as opposed to 43,0 per cent for December 2000 (Figure 26). As already mentioned, the sharp decline in short-term wholesale deposits from December 2000 to January 2001 can mainly be attributed to some banks not being able to report some information in terms of the amended Regulations relating to Banks. Wholesale deposits shorter than seven days and wholesale deposits between eight and 31 days are shown only from January 2001 onwards, owing to the requirements of the amended Regulations relating to Banks. As at the end of December 2001, wholesale deposits shorter than seven days and wholesale deposits between eight and 31 days represented 26,4 per cent and 10,7 per cent, respectively, of total funding.

FIGURE 27: COMPOSITION OF WHOLESALE DEPOSITS ACCORDING TO MATURITY

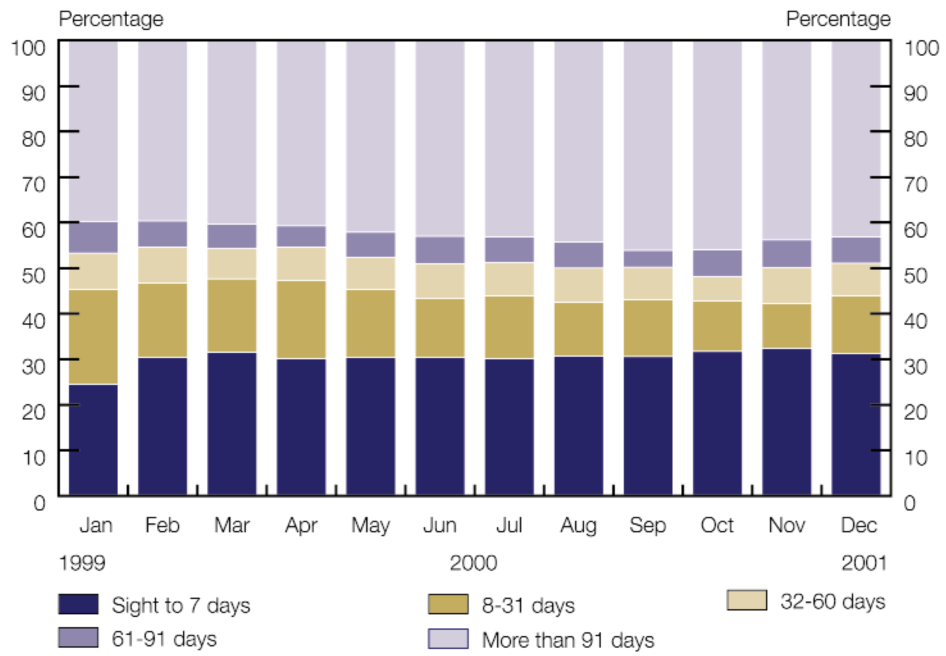


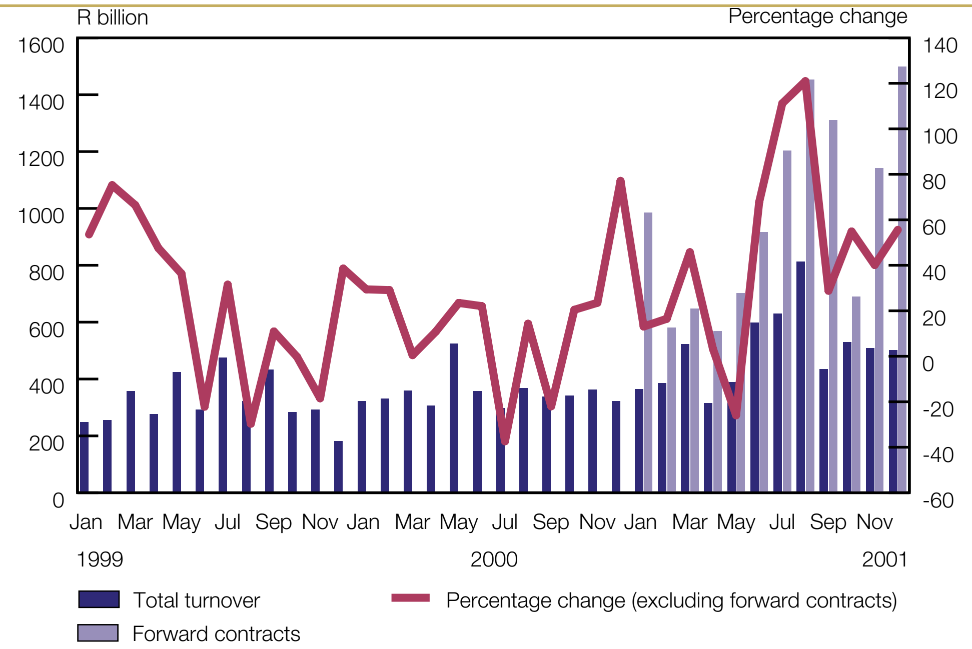
Figure 27 displays the composition (measured over a period of 12 months) of wholesale deposits according to maturity for the year under review. Wholesale deposits with a maturity shorter than seven days and wholesale deposits with a maturity greater than 91 days constituted the biggest portion of wholesale deposits in December 2001, namely, 30 per cent and 43 per cent, respectively. Wholesale deposits with a maturity of 32 to 60 days constituted only a small portion of total wholesale deposits, namely, 7 per cent, followed by deposits with a maturity of eight to 31 days (14 per cent of total wholesale deposits).

3.5 MARKET RISK

banks also required to report on forward contracts

Turnover in derivatives again fluctuated widely during the year, from approximately R364,5 billion in January 2001, to R814 billion in August 2001 and to R502,3 billion in December 2001 (see Figure 28). In terms of the amended Regulations relating to Banks, banks were also required to report on forward contracts. By the end of December 2001, forward contracts amounted to R1 500 billion.

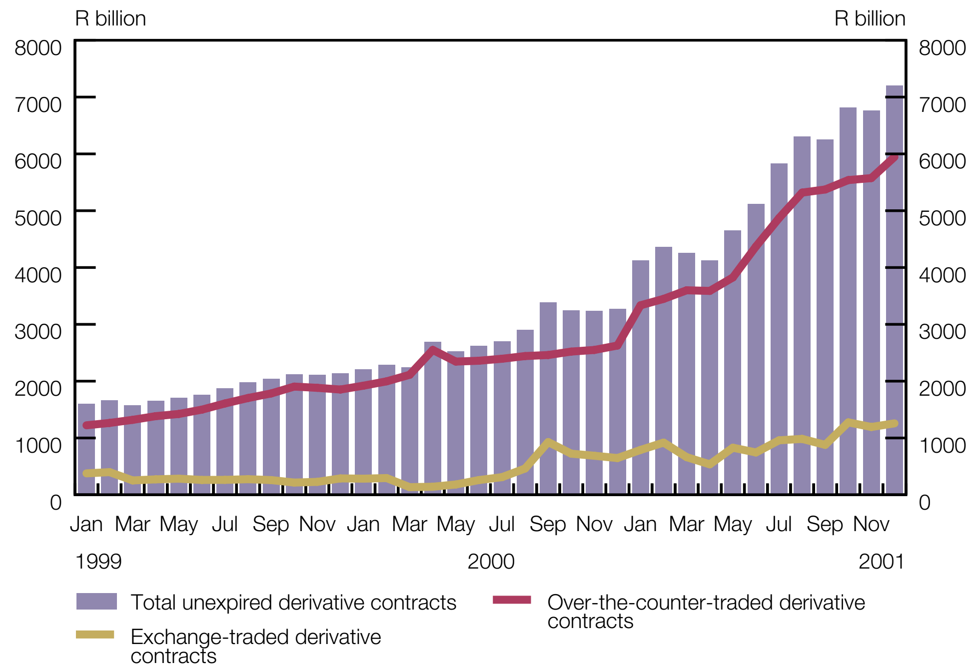
FIGURE 28: TURNOVER IN DERIVATIVE CONTRACTS



total unexpired derivative conracts increased by 120,1 per cent

Figure 29 reflects the value of and growth (measured over a period of 12 months) in total unexpired derivative contracts. Unexpired exchange-traded derivative contracts amounted to R1 257,3 billion in December 2001 (December 2000: R645,6 billion), or 120,2 per cent of the banking sector's total assets (December 2000: 78,8 per cent). Compared to the year before, total unexpired derivative contracts increased by 120,1 per cent. Average monthly balances, computed on a quarterly basis, were reported as R790,4 billion, R703,4 billion, R940,5 billion and R1 242 billion for the quarters ended March 2001, June 2001, September 2001 and December 2001, respectively. As at 31 December 2001, the total value of unexpired derivative contracts was R7 203,3 billion (December 2000: R3 273,5 billion), representing 689 per cent of total assets (December 2000: 399,6 per cent of total assets). As at 31 December 2001, over-the-counter traded derivatives accounted for 82,5 per cent (2000: 80,2 per cent) of all unexpired derivative contracts.

FIGURE 29: TOTAL UNEXPIRED DERIVATIVE CONTRACTS



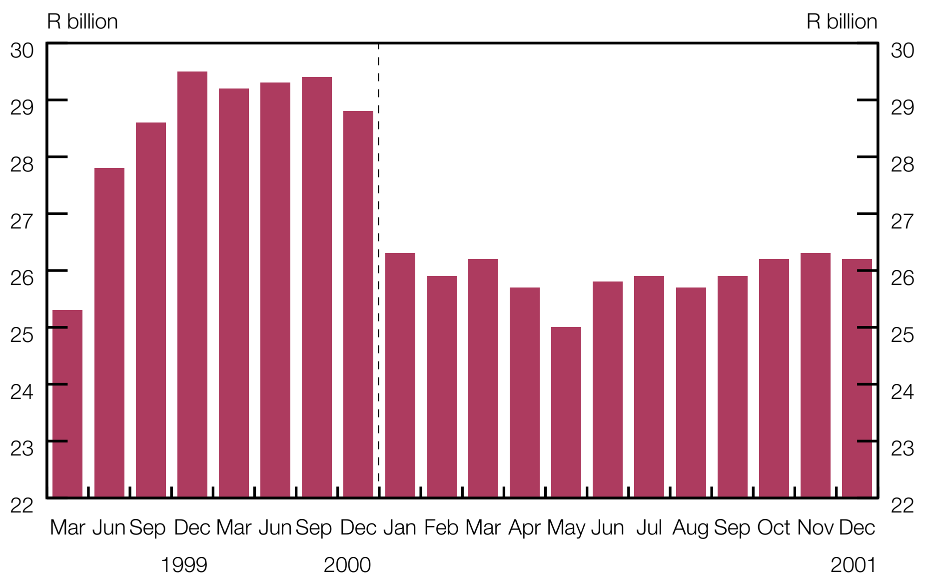
3.6 CREDIT RISK

Analysis of overdue amounts

Figure 30 graphically displays the level of total overdues for the banking sector for the period from March 1999 to December 2000 (in terms of the old Regulations relating to Banks) and from January to December 2001 (in terms of the amended Regulations relating to Banks). Owing to amendments to the definition and classification of overdue accounts in the amended Regulations relating to Banks, the gross overdues of the total banking sector decreased by R2,5 billion to a level of R26,3 billion in January 2001 (December 2000: R28,8 billion). Also, in terms of the old Regulations relating to Banks, banks had to submit credit-risk data on a quarterly basis, but on a monthly basis in terms of the amended Regulations.

banks submit credit-risk data on a monthly basis

FIGURE 30: TOTAL BANKING-SECTOR OVERDUES



In terms of the amended Regulations relating to Banks, which became effective on 1 January 2001, banks also had to classify all loans and advances according to the quality of the assets. Only those loans classified as “doubtful” and “loss” were regarded as “overdue” for purposes of this Annual Report. The impact of the amendment to the definition of overdues can also be seen clearly in Figure 30. A dotted line separates the overdues in terms of the old Regulations from the overdues in terms of the amended Regulations. Because of the amended definition of overdues, comparisons over time should be made with caution.

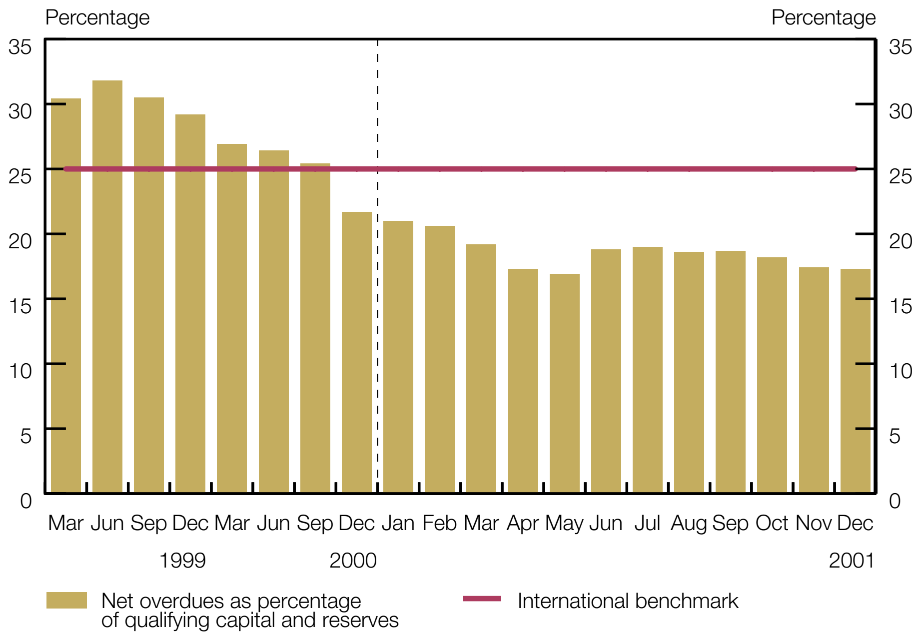
comparisons over time should be made with caution

During the year under review, gross overdues fluctuated between R25 billion and R26,3 billion. The net decrease in gross overdues of the total banking sector since January 2001 amounted to R192,4 million.

The ratio of net overdues (that is, gross overdues less specific provisions) to net qualifying capital and reserves is used internationally to benchmark the extent of amounts overdue in a banking sector. Figure 31 displays this ratio for the past three years. Net overdues as a percentage of net qualifying capital and reserves amounted to 21 per cent in January 2001 (December 2000: 21,7 per cent). By the end of December 2001, this ratio had improved to 17,3 per cent, which was well within the international benchmark of 25 per cent.

ratio of net overdues to net qualifying capital and reserves improved to 17,3 per cent

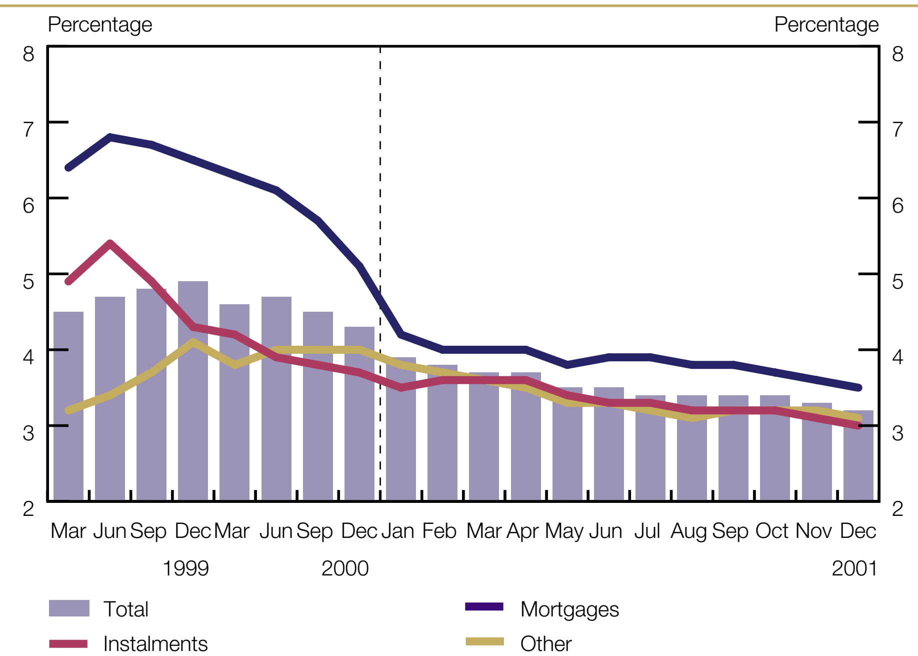
FIGURE 31: NET OVERDUES AS A PERCENTAGE OF NET QUALIFYING CAPITAL AND RESERVES



gross amount overdue amounted to 3,2 per cent

Expressed as a percentage of total loans and advances (see Figure 32), gross amounts overdue decreased from 4,3 per cent in December 2000 to 3,9 per cent in January 2001, mainly because of the implementation of the amended definition of overdues in January 2001. By the end of December 2001, the gross amount overdue (as a percentage of total loans and advances) amounted to 3,2 per cent. From January 2001 to December 2001, mortgage loans overdue (as a percentage of total mortgage loans and advances) decreased from 4,2 per cent to 3,5 per cent, instalment sales overdue (as a percentage of total instalment sales) decreased from 3,5 per cent to 3 per cent, and other loans and advances overdue (as a percentage of total other loans and advances) decreased from 3,8 per cent to 3,1 per cent.

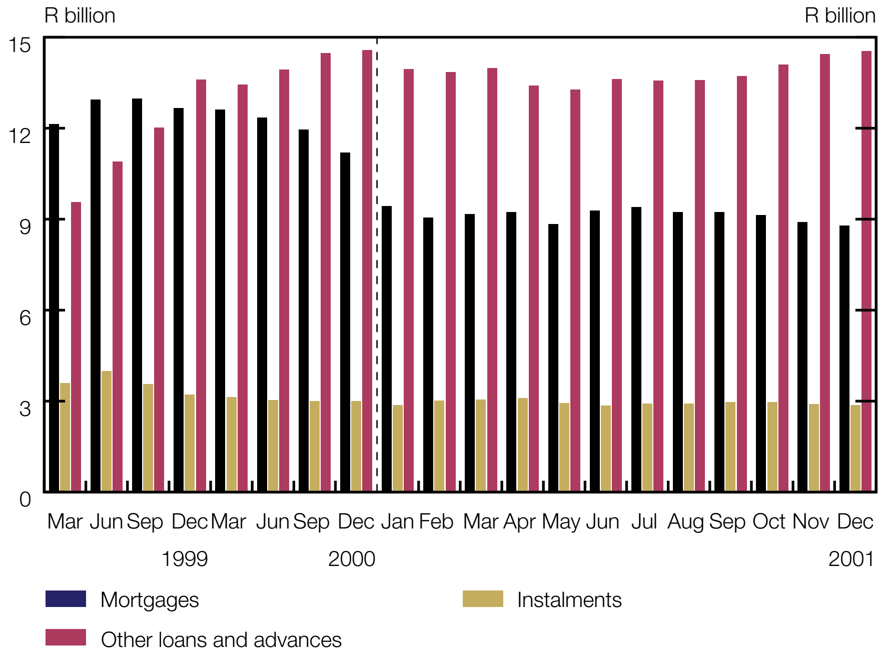
FIGURE 32: COMPOSITION OF OVERDUES (AS A PERCENTAGE OF LOANS AND ADVANCES)



overdues in respect of other loans and advances exceeded mortgage accounts overdue

Figure 33 graphically displays an analysis of overdue accounts for the period from March 1999 to December 2001. The gross amount overdue in respect of other loans and advances increased from R14 billion in January 2001 to R14,5 billion in December 2001. Overdues in respect of other loans and advances still constituted the biggest portion of amounts overdue and, by the end of December 2001, exceeded mortgage accounts overdue by R5,8 billion. Mortgage accounts overdue decreased from R11,2 billion in December 2000 to R9,4 billion in January 2001. From January 2001 to December 2001, the mortgage accounts overdue decreased to R8,8 billion, whereas instalment accounts overdue fluctuated between R2,9 billion and R3,1 billion.

FIGURE 33: ANALYSIS OF OVERDUE ACCOUNTS



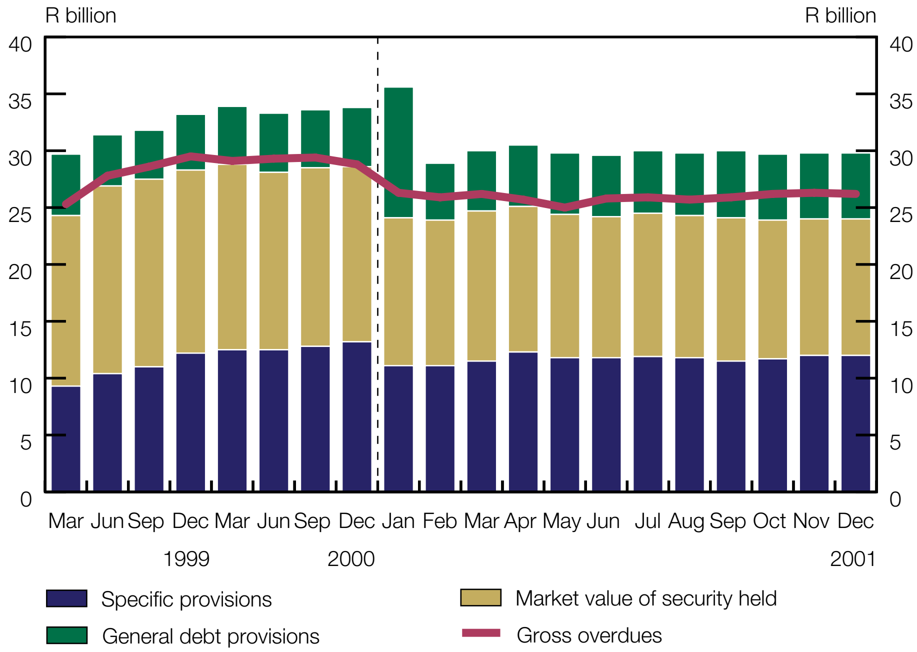
Provisioning policy for bad and doubtful loans and advances

The implementation of the amended Regulations relating to Banks made it possible to determine the exact amount of specific provisions made and the value of the security held against loans classified as non-performing. The Bank Supervision Department, therefore, decided to take into account only the specific provisions and security relating to loans classified as "doubtful" and "loss" when determining the adequacy of banks' provisioning.

provisioning by banks remained adequate

According to Figure 34, provisioning by banks remained adequate throughout the year under review. By the end of December 2001, specific provisions covered about 46 per cent (the same percentage as in December 2000) of all overdues. In January 2001, general provisioning increased noticeably, to a level of R11,5 billion (December 2000: R5,2 billion), that is, about 44 per cent of overdues. At the end of December 2001, about 22 per cent of overdues were covered by security.

FIGURE 34: ADEQUACY OF PROVISIONS



specific provisions by loan type

Specific provisions made at the end of December 2001, by loan type and expressed as a percentage of overdue amounts, were as follows:

- Mortgages - 27,4 per cent (21,9 per cent on 31 December 2000).
- Instalment sales - 54,1 per cent (49,4 per cent on 31 December 2000).
- Other loans and advances - 56,0 per cent (63,9 per cent on 31 December 2000).

conservative stance of South African banks

Figure 35 graphically displays the relationship of specific provisions to total gross overdues for the past three years. On average, about 45,1 per cent of overdues were covered by specific provisioning during 2001 (2000: 43,7 per cent). Internationally, it is generally accepted that specific provisioning should cover at least 40 per cent of non-performing loans, which indicates the slightly more conservative stance of South African banks in this regard.

Large exposures

As from January 2001, the amended Regulations relating to Banks require large exposures granted not to exceed 800 per cent of capital and reserves, in line with the guidelines of the European Economic Community. In terms of these guidelines, those large exposures granted that exceed 15 per cent of capital and reserves should not exceed, in total, 800 per cent of capital and reserves, and no single exposure should exceed 25 per cent of an institution's capital base. It should be borne in mind, however, that this refers only to large exposures to private-sector non-bank borrowers and that the total of the large exposures analysed in this Annual Report includes, amongst others, exposures to Government and interbank settlements.

The position of large exposures granted and utilised during the period from March 1999 to December 2001 is illustrated graphically in Figure 36. A dotted line separates the large exposures in terms of the old Regulations from those in terms of the amended Regulations, which require banks to report only the maximum amount (instead of the month-end balance) of the large exposures granted.

FIGURE 35: SPECIFIC PROVISIONS AS PERCENTAGE OF TOTAL OVERDUES

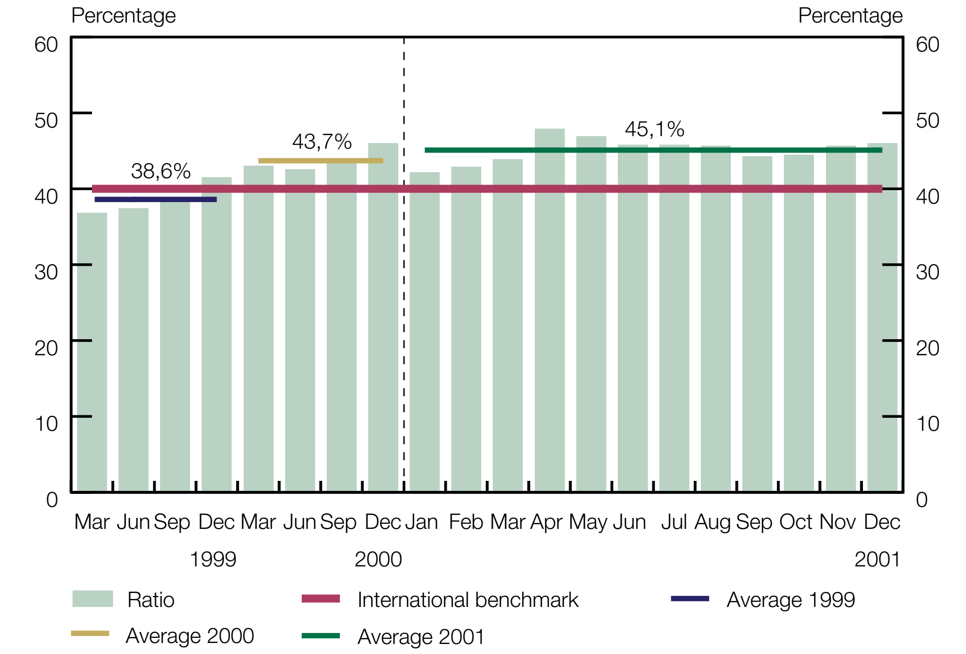
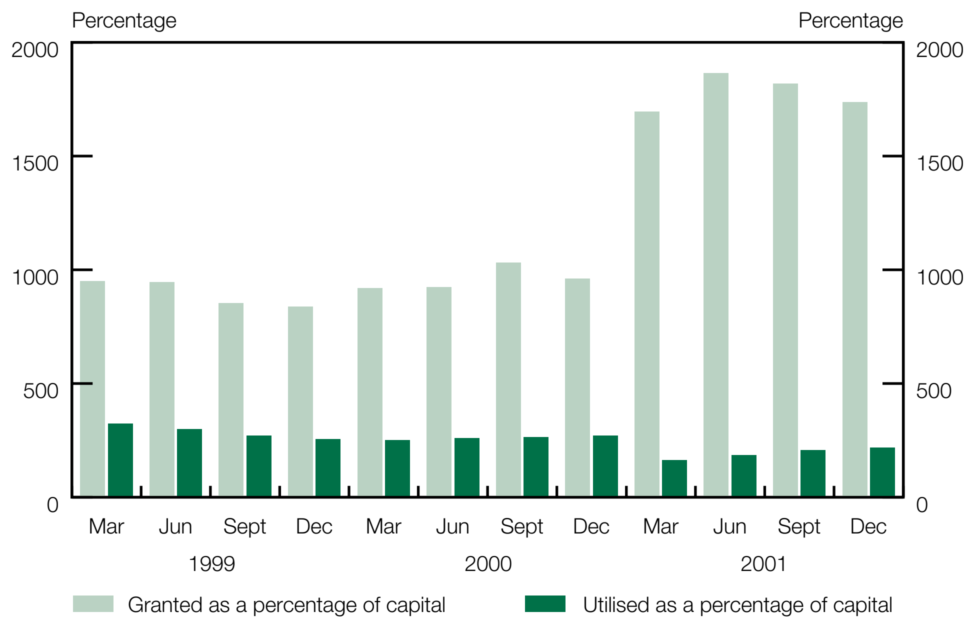


FIGURE 36: LARGE EXPOSURES GRANTED AND UTILISED AS A PERCENTAGE OF CAPITAL



overdues in respect of large exposure decreased

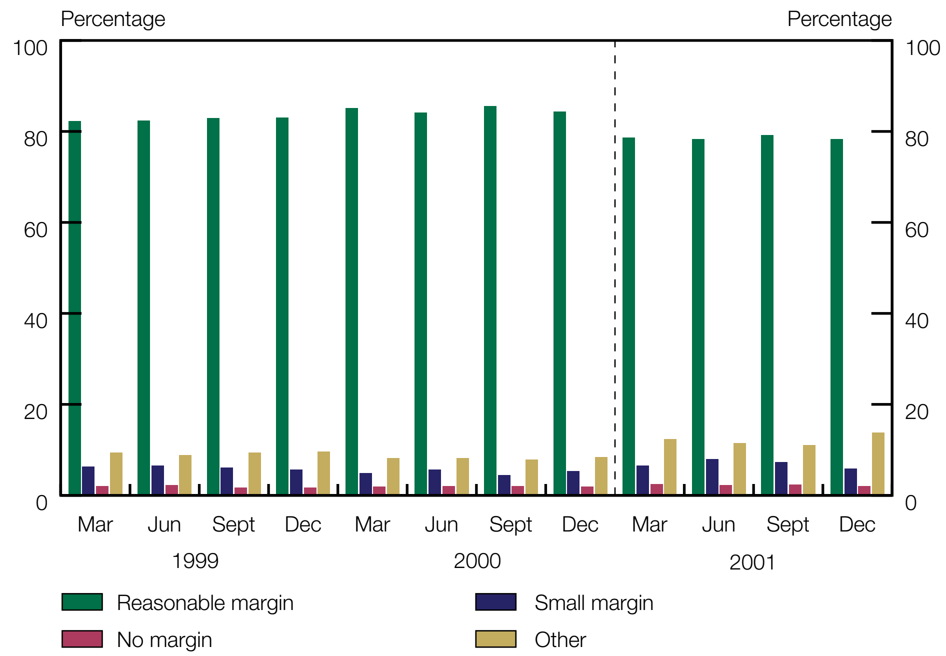
Large exposures granted increased by R664,4 million to a level of R1,4 billion in January 2001 (representing 1 874,8 per cent of net qualifying capital and reserves), compared to R690 million (representing 962,8 per cent of net qualifying capital and reserves) in December 2000. Overdues in respect of large exposures decreased from R437,7 million in December 2000 to R381,2 million in January 2001. By the end of December 2001, overdues in respect of large exposures had further decreased to a level of R216,7 million, and specific provisions covered about 75,9 per cent of overdues. The remainder of the overdues was covered by the value of the security held by banks.

Quality of assets

78,3 per cent earned a reasonable margin

About 78,3 per cent of the banking sector's assets (December 2000: 84,4 per cent) earned a reasonable margin, 5,9 per cent (December 2000: 5,3 per cent) earned a small margin, and the remaining 15,8 per cent (December 2000: 10,3 per cent), including infrastructure, earned no margin (see Figure 37).

FIGURE 37: ASSET PERFORMANCE

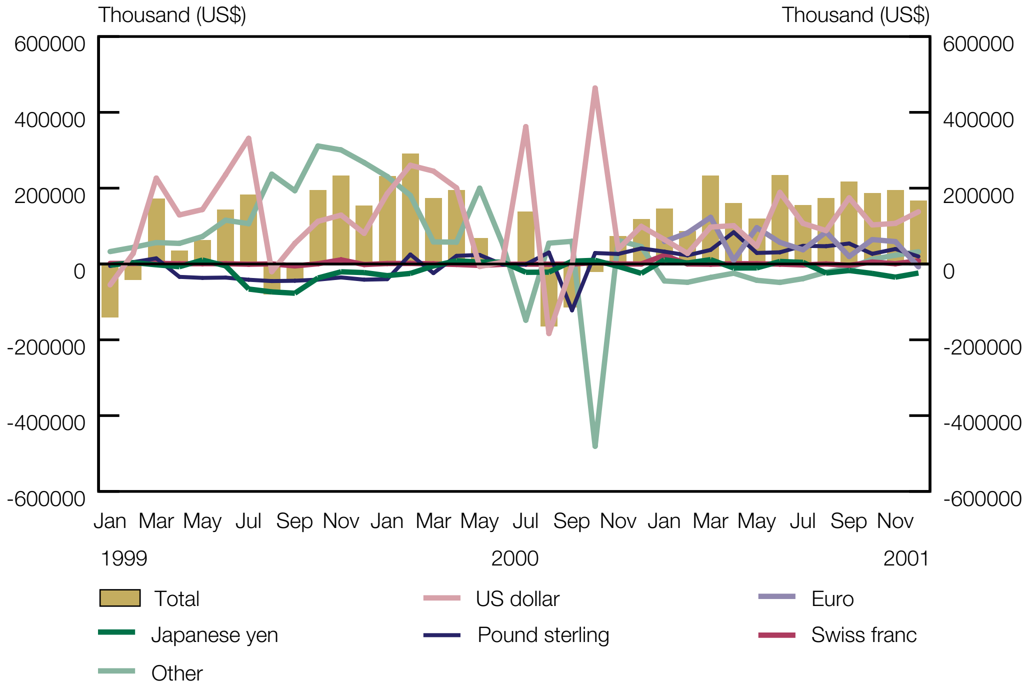


3.7 CURRENCY RISK

position remained within limit

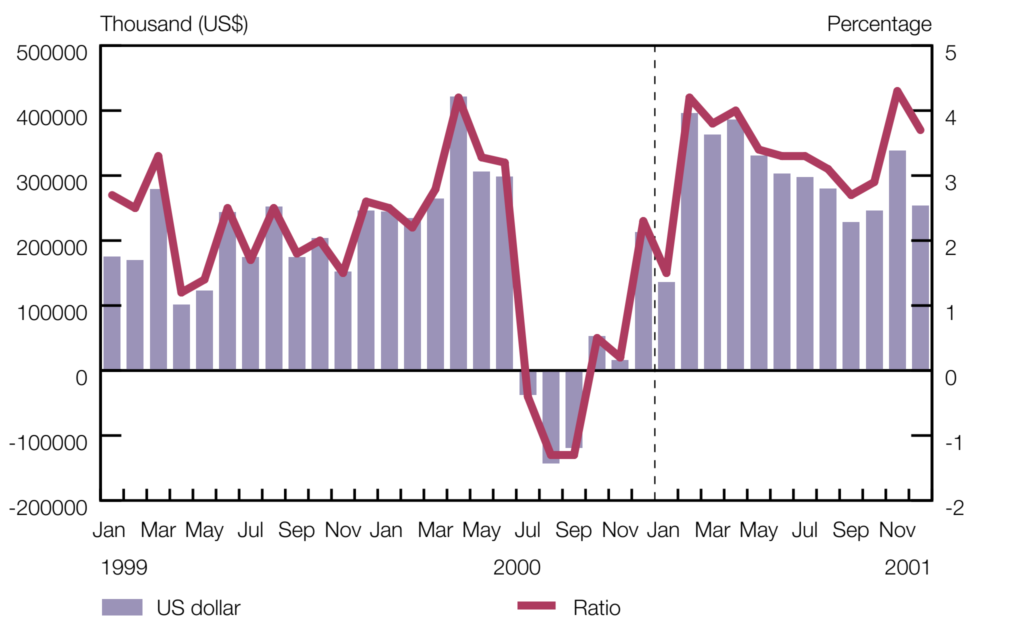
For the period under review, the aggregated net open foreign-currency position after hedging remained within the limit of 10 per cent of net qualifying capital and reserves. The aggregated net effective open foreign-currency position of individual banks, expressed as a percentage of net qualifying capital and reserves, amounted to 0,2 per cent in January 2001 and, by the end of December 2001, had remained unchanged at 0,2 per cent. The aggregated net effective open foreign-currency position of the total banking sector is displayed in Figure 38.

FIGURE 38: AGGREGATED EFFECTIVE NET OPEN FOREIGN-CURRENCY POSITION (all currencies converted to US dollars)



From December 2000 to January 2001, the maximum net open position in foreign currency after hedging decreased from 2,3 per cent to 1,5 per cent and remained safely within the limit of 10 per cent of net qualifying capital and reserves for the period under review. By the end of December 2001, the maximum net open position in foreign currency after hedging had increased to 3,7 per cent (see Figure 39).

FIGURE 39: MAXIMUM EFFECTIVE NET OPEN FOREIGN-CURRENCY POSITION AS A PERCENTAGE OF NET QUALIFYING CAPITAL AND RESERVES (compliance with 10 per cent limit)



The position in foreign-currency instruments and the liquidity-maturity structure of US dollar positions are shown in Figures 40 and 41, respectively.

FIGURE 40: POSITION IN FOREIGN-CURRENCY INSTRUMENTS

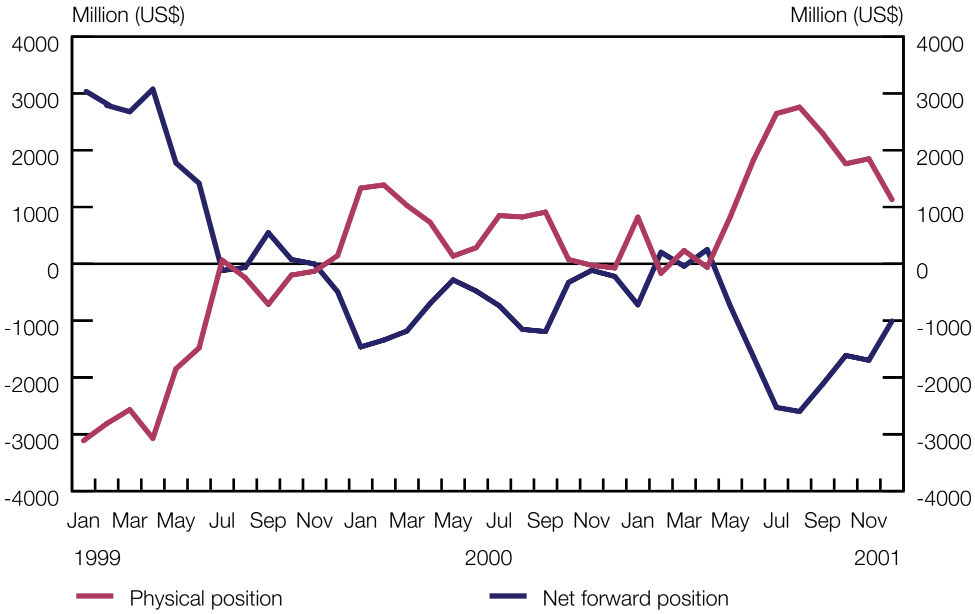


FIGURE 41: LIQUIDITY-MATURITY STRUCTURE (US dollars)