CHAPTER 3

TRENDS IN SOUTH AFRICAN BANKS

As in previous years, 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 2001 annual report

Aggregated information of individual banks is contained in the reports and graphs in sections 3.1 to 3.7 below. Certain comparative figures in respect of 2001 may differ from those contained in the 2001 annual report because of the subsequent submission of amended returns by banking institutions.

The reports and graphs that follow are largely affected by the position of the four biggest banks, which constituted 74,2 per cent of the banking sector in December 2002 (69,3 per cent in December 2001). The six biggest banks constituted 84,3 per cent of the banking sector as at the end of December 2002 (80,9 per cent in December 2001).

3.1 BALANCE-SHEET STRUCTURE

type and spread of a bank's business activities

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 2002, equalled R1 100,8 billion, as opposed to R1 050 billion as at 31 December 2001 and R819,2 billion as at 31 December 2000.

FIGURE 1: AGGREGATED BALANCE SHEET

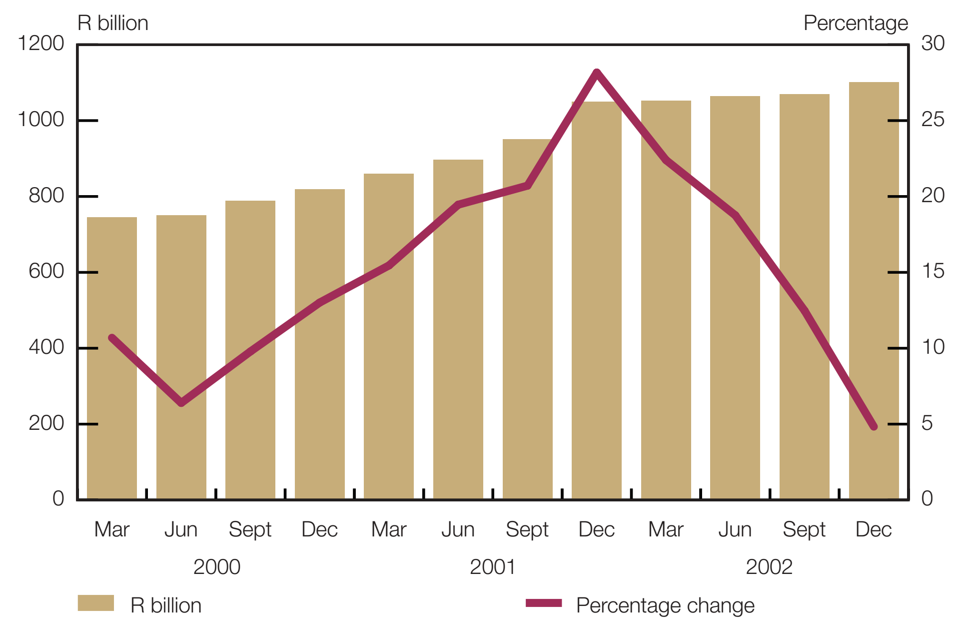
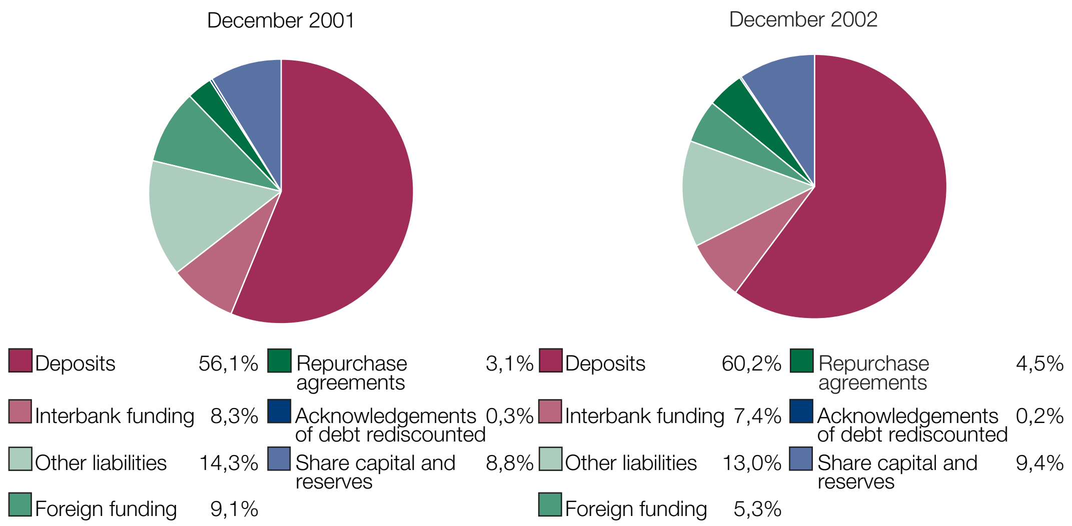


Figure 1 graphically depicts the quarter-end value of, and percentage growth (measured over 12 months) in, the aggregated balance sheet of the banking sector for the period from March 2000 to December 2002. Growth in the aggregated balance sheet increased markedly from June 2000 to December 2001, but had moderated to 4,8 per cent by the end of December 2002, mainly as a result of a moderation in the growth of total loans and advances.

Liabilities

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

FIGURE 2: LIABILITIES – YEAR-ON-YEAR COMPARISON



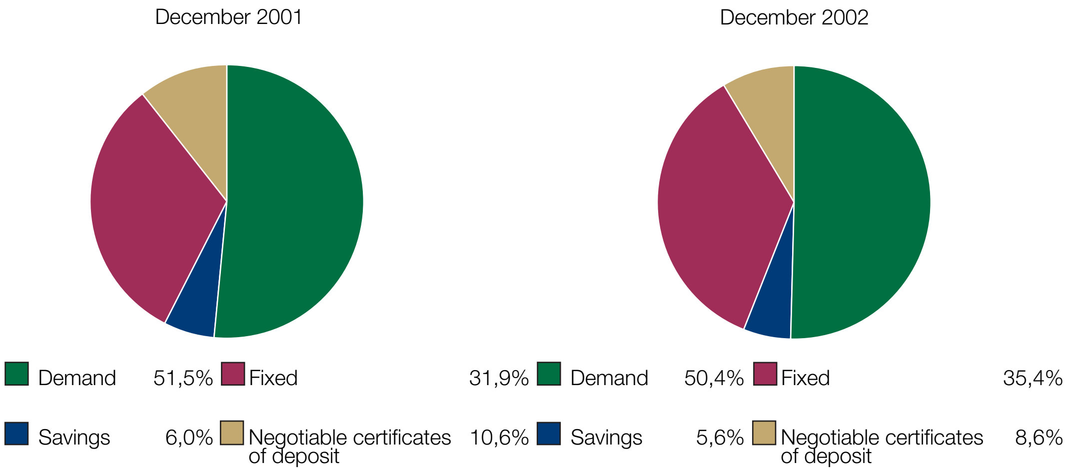
domestic deposits from the public remained the main source of funding

Domestic deposits from the public in the amount of R662,5 billion remained the main source of funding for the banking sector and constituted 60,2 per cent of total liabilities in December 2002, compared to 56,1 per cent in December 2001 and 65,5 per cent in December 2000. Foreign funding and interbank funding as a percentage of total liabilities, on the other hand, decreased from 9,1 per cent and 8,3 per cent, respectively, in December 2001 to 5,3 per cent and 7,4 per cent, respectively, in December 2002. Repurchase agreements, on the other hand, increased from 3,1 per cent in December 2001 to 4,5 per cent in December 2002.

Composition of non-bank deposits

Figure 3 reflects a year-on-year comparison of the composition of non-bank deposits. Compared to the previous year, fixed and notice deposits increased by 3,5 percentage points. Demand deposits as a percentage of total non-bank deposits decreased from 51,5 per cent to 50,4 per cent. The share of non-bank deposits represented by negotiable certificates of deposit decreased from 10,6 per cent at the end of December 2001 to 8,6 per cent a year later.

FIGURE 3: COMPOSITION OF NON-BANK DEPOSITS

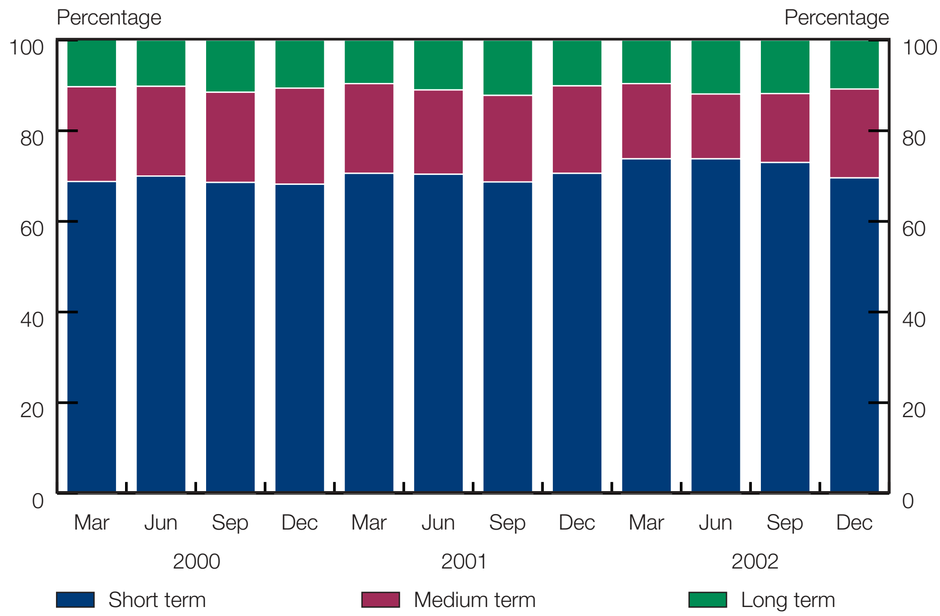


Maturity structure of non-bank deposits

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 2000 to December 2002. As can clearly be seen from figure 4, short-term deposits remained the biggest component of total non-bank funding and accounted for 69,6 per cent of total non-bank funding as at 31 December 2002, compared to 70,6 per cent at the end of December 2001 and 68,2 per cent at the end of December 2000. Long-term deposits, on the other hand, remained the smallest component of total non-bank funding and accounted for 10,8 per cent of total non-bank funding as at 31 December 2002, compared to 10,1 per cent and 10,6 per cent at the end of December 2001 and the end of December 2000, respectively. Medium-term deposits accounted for the remaining 19,6 per cent as at December 2002, compared to 19,3 per cent and 21,2 per cent at the end of December 2001 and the end of December 2000, respectively.

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

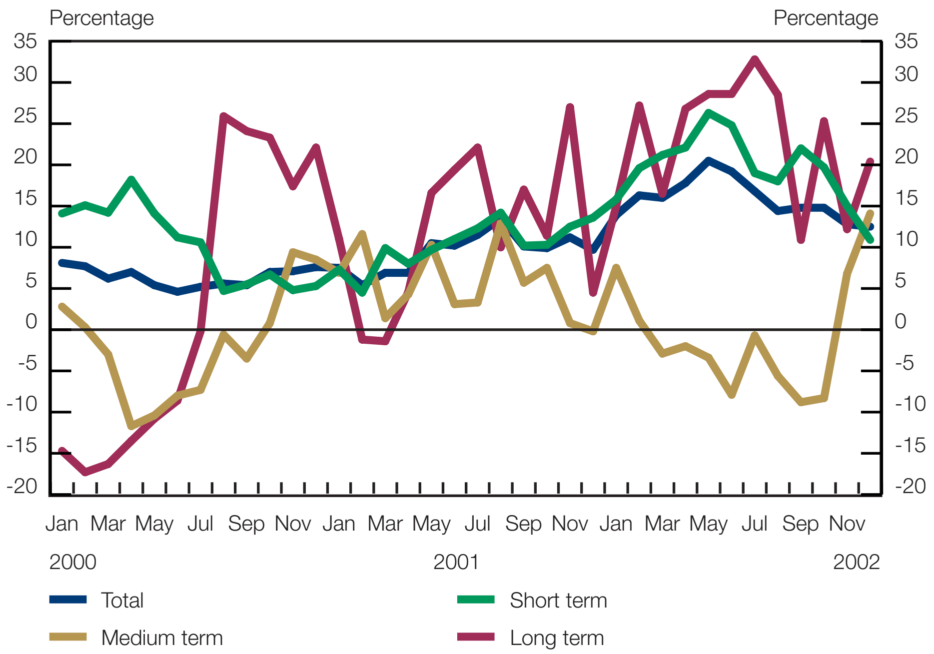


The slight decrease in the proportion of total deposits represented by short-term deposits resulted in a slightly lower percentage of the banking sector's assets (consisting mainly of non-bank loans and advances) being financed by short-term funding. As a result, the liquidity risk to which banks are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

growth in long-term deposits was volatile

As indicated above, long-term deposits remained the smallest component of total non-bank funding. Growth in long-term deposits was volatile throughout 2002 (see figure 5) and increased from 15 per cent in January 2002 to 32,8 per cent in July 2002 and then decreased to 10,9 per cent in September 2002, before ending the year at 20,4 per cent. By the end of December 2002, the six biggest banks held more than 92,1 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 2002, but had moderated somewhat by the end of the year. Growth in short-term deposits increased by 10,9 per cent in December 2002, compared to 13,6 per cent in December 2001. Growth in medium-term deposits, on the other hand, was negative for eight consecutive months until October 2002. From November 2002, however, growth in medium-term deposits became positive and, by the end of December 2002, had increased markedly to 14,1 per cent.

other major liabilities

Other major liabilities of the banking sector as at 31 December 2002 included foreign funding of R58,4 billion, which decreased by 38,6 per cent during the year under review. This decrease in foreign funding was due mainly to the appreciation in the value of the rand during 2002. Capital and reserves increased by 12,1 per cent, from R92,2 billion in December 2001 to R103,4 billion a year later. Other liabilities, on the other hand, decreased to R143,1 billion (a decrease of 5,2 per cent compared to the December 2001 level of R151 billion), and interbank funding decreased to R81,6 billion (a decrease of 6,5 per cent compared to the amount of R87,3 billion at the end of December 2001). Other liabilities included amounts owing to the South African Reserve Bank, trade creditors, deferred income, deferred tax balances, impairments and other funding liabilities.

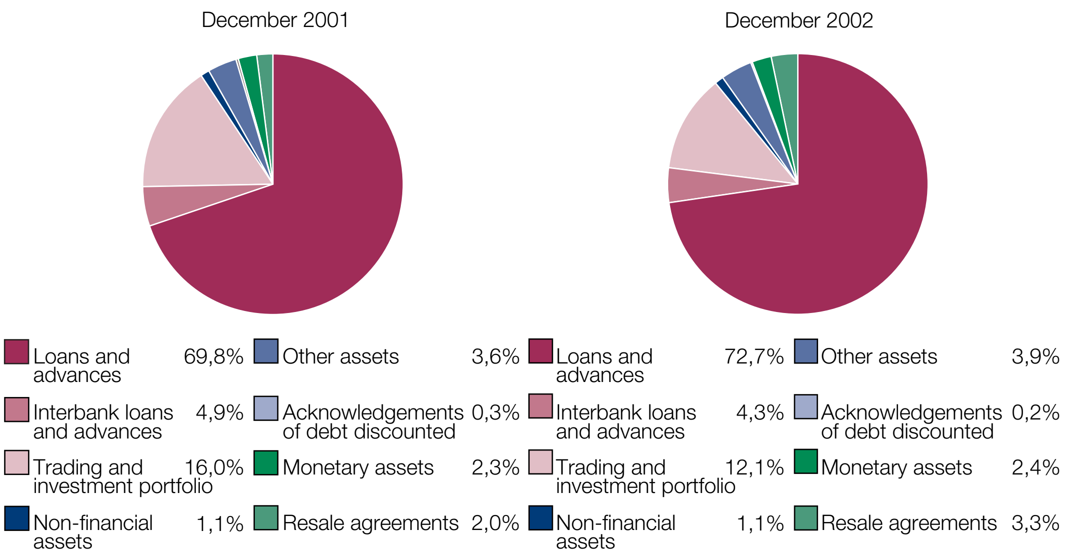
Assets

factors contributing to growth in assets

Figure 6 graphically reflects a year-on-year comparison of the composition of assets as at 31 December 2002 and 31 December 2001. The banking sector's assets increased by R50,8 billion (representing a growth rate of 4,8 per cent) during the year, to a total of R1 100,8 billion at the end of December 2002. Factors contributing to this growth were the following:

- Monetary assets grew by 10,4 per cent, from R24 billion as at 31 December 2001 to R26,5 billion as at 31 December 2002.
- Non-bank advances grew by R67 billion (representing a growth rate of 9,1 per cent), from R732,8 billion at the end of December 2001 to R799,8 billion a year later.
- Loans granted under resale agreements increased from R20,7 billion at the end of December 2001 to R36,8 billion at the end of December 2002, representing a growth rate of 78,3 per cent.
- Non-financial assets increased by 5,7 per cent, from R11,9 billion at the end of December 2001 to R12,5 billion at the end of December 2002.
- Other assets increased by 11,9 per cent, from R38,2 billion at the end of December 2001 to R42,7 billion at the end of December 2002.

FIGURE 6: ASSETS – YEAR-ON-YEAR COMPARISON



growth in total loans and advances slowed down significantly

It is apparent from figure 7 that growth in total loans and advances slowed down significantly during 2002. By the end of December 2002, loans and advances had increased by 10 per cent, compared to an increase of 22,8 per cent during 2001. The moderation in the growth of total loans and advances was the main contributor to the moderation in the growth of total assets. By the end of December 2002, loans and advances accounted for about 81,9 per cent of total assets (see figure 8).

FIGURE 7: TOTAL LOANS AND ADVANCES

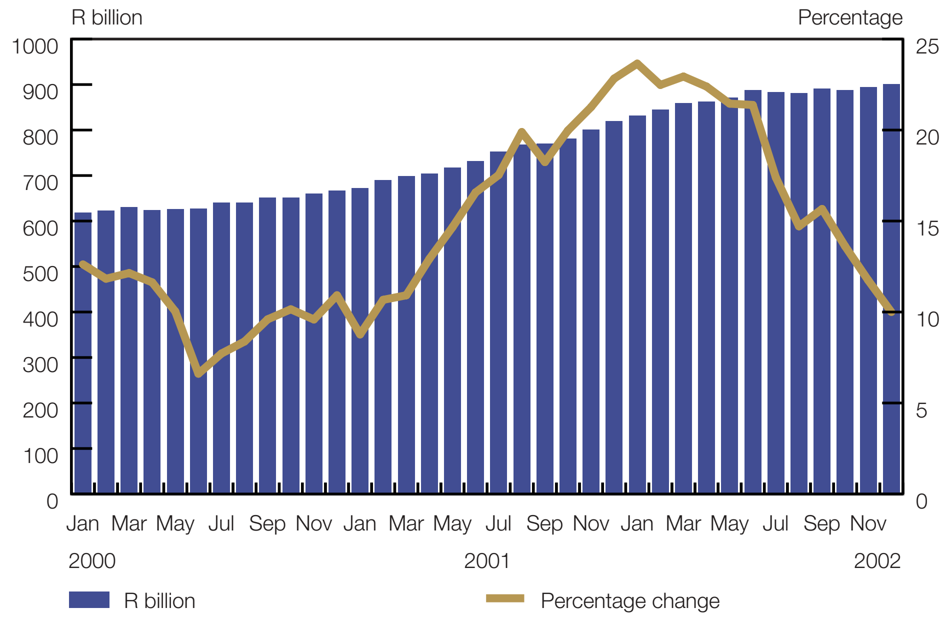
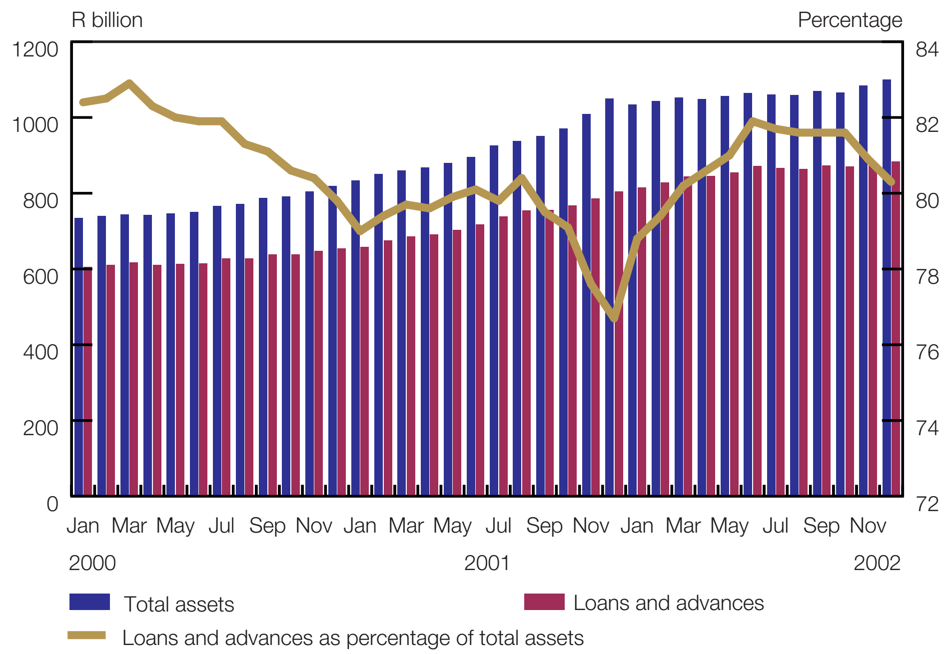


FIGURE 8: LOANS AND ADVANCES AS A PERCENTAGE OF TOTAL ASSETS



lower percentage of loans and advances to assets

During the second half of 2001, loans and advances as a percentage of total assets decreased significantly, from 80,4 per cent in August 2001 to 76,7 per cent in December 2001, but increased again throughout the first six months of 2002, to 81,9 per cent in June 2002. Loans and advances as a percentage of total assets, however, decreased somewhat during the second half of 2002 and ended the year at 80,3 per cent (see figure 8). The lower percentage of loans and advances to assets was due mainly to a moderation in the growth of loans and advances and an acceleration in the growth of the trading and investment portfolio of banks during that period.

Composition of loans and advances

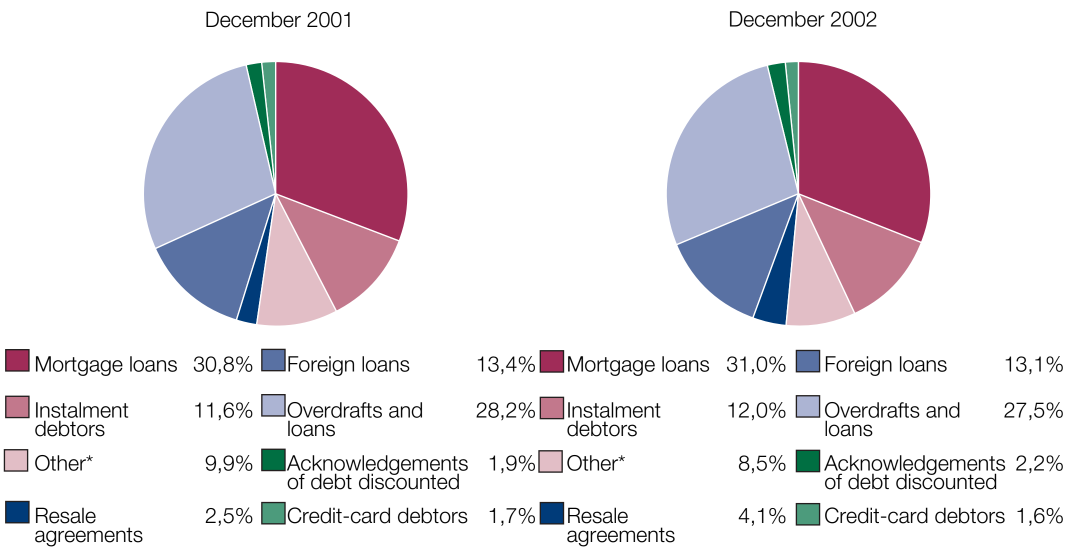
The composition of loans and advances is shown graphically in figure 9. A comparison of the composition of loans and advances in 2001 and 2002 clearly shows that the composition remained almost unchanged.

As at the end of December 2002, non-bank loans and advances constituted 72,7 per cent (December 2001: 69,8 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 R67 billion (2001: R120,3 billion) achieved in respect of non-bank advances during the year under review and representing a growth rate of 9,1 per cent (2001: 19,6 per cent) can be attributed to the following areas (figure 10):

reasons for increase in non-bank advances

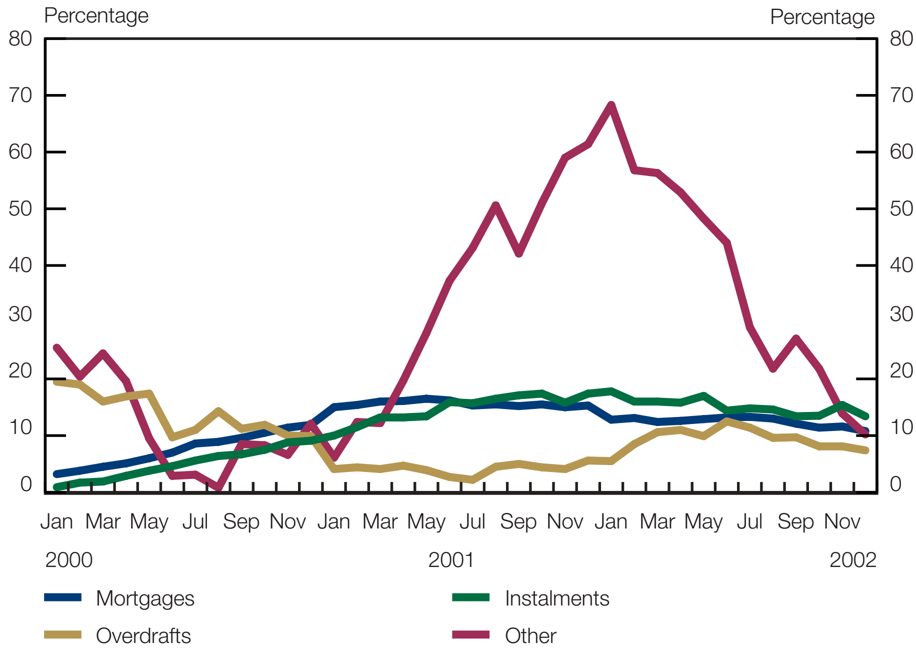
- Mortgage loans increased by R27,3 billion to a level of R279,3 billion, representing an increase of 10,8 per cent measured over a 12-month period.
- Overdrafts and loans increased by R17,1 billion to a level of R247,7 billion, representing a growth rate of 7,4 per cent.
- Instalment debtors increased by R12,8 billion to a level of R107,9 billion, representing an increase of 13,4 per cent.
- Foreign-currency loans and advances increased by R7,8 billion to a level of R117,7 billion, representing an increase of 7,1 per cent.
- Credit cards increased by R1,1 billion to a level of R14,6 billion, representing an increase of 8,3 per cent.
- Acknowledgements of debt discounted increased by R4,2billion to a level of R19,4 billion, representing an increase of 27,9 per cent.
- Redeemable preference shares increased by R2,7 billion to a level of R16,9 billion, representing an increase of 19,3 per cent.

FIGURE 9: COMPOSITION OF LOANS AND ADVANCES



* Negotiable certificates of deposit and redeemable preference shares

FIGURE 10: GROWTH IN SELECTED LOANS AND ADVANCES

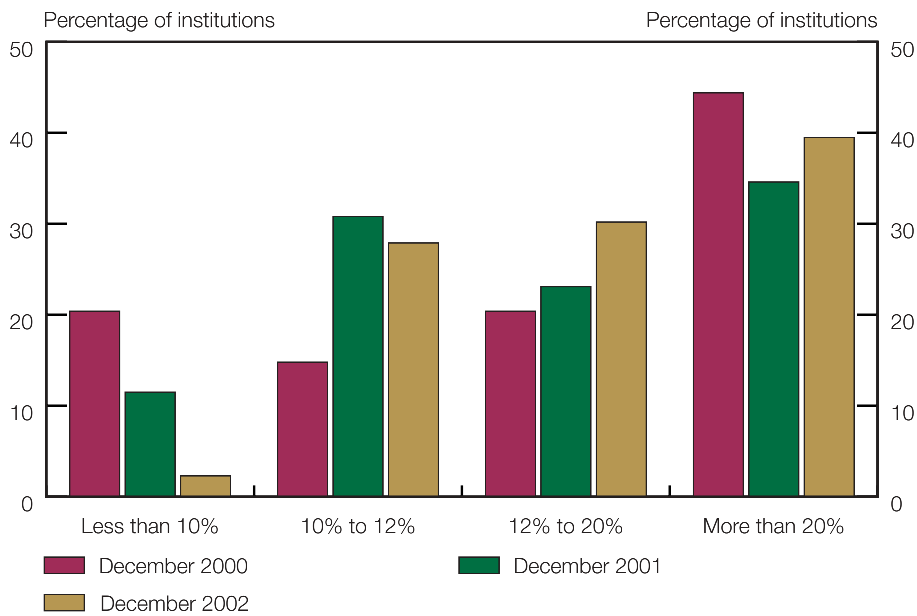


3.2 CAPITAL ADEQUACY

adequate capital does not provide a guarantee against failure

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, or, as indicated in chapter 1 of this annual report, a bank that is affected by contagion.

FIGURE 11: DISTRIBUTION OF BANKS IN TERMS OF CAPITAL ADEQUACY



capital-adequacy ratio was 12,6 per cent

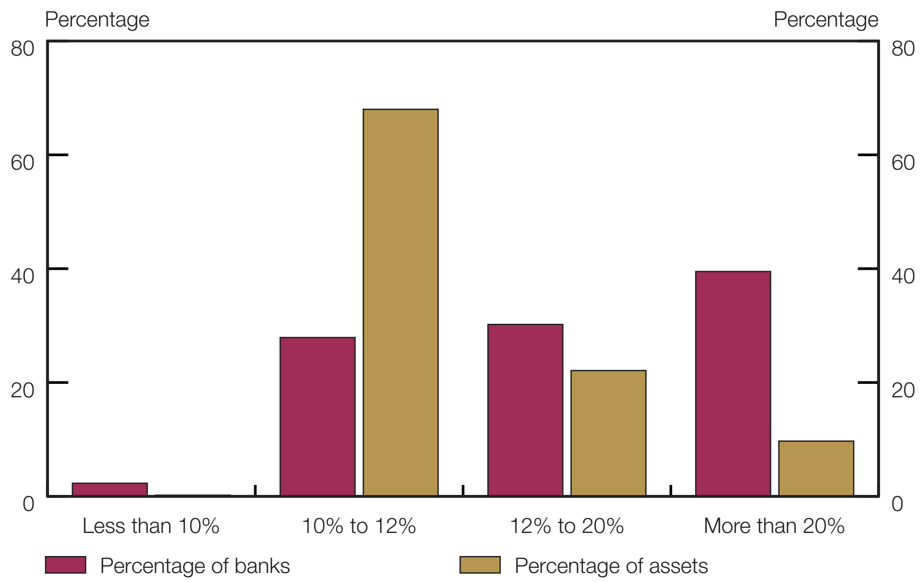
For the year under review, the average capital and reserves held by the banking sector amounted to R97,8 billion (R89,7 billion in December 2001), R84,4 billion (2001: R77,6 billion) of which constituted qualifying capital and reserves for purposes of assessing capital adequacy. The capital-adequacy ratio for the year ended December 2002 was 12,6 per cent (2001: 11,4 per cent).

only one bank was unable to meet the required ratio

An analysis of the percentage distribution of banks in terms of capital adequacy at the end of December 2002 (see figure 11) reveals that only 2,3 per cent (2001: 11,5 per cent) of the total number of banking institutions - in fact, one bank - did not meet the minimum capital-adequacy ratio of 10 per cent, whereas 39,5 per cent of banking institutions (2001: 34,6 per cent) had capital-adequacy ratios that exceeded 20 per cent. The only bank that was unable to meet the required ratio of 10 per cent was taken over by a bigger bank and is being deregistered.

The 39,5 per cent of banking institutions that reported capital-adequacy ratios of above 20 per cent represented only 9,7 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 (27,9 per cent of banking institutions) represented the biggest portion of total banking-sector assets, namely, 68 per cent. The bank that did not meet the minimum capital-adequacy requirement of 10 per cent represented only 0,2 per cent (as opposed to 39,1 per cent in 2001) of total banking-sector assets.

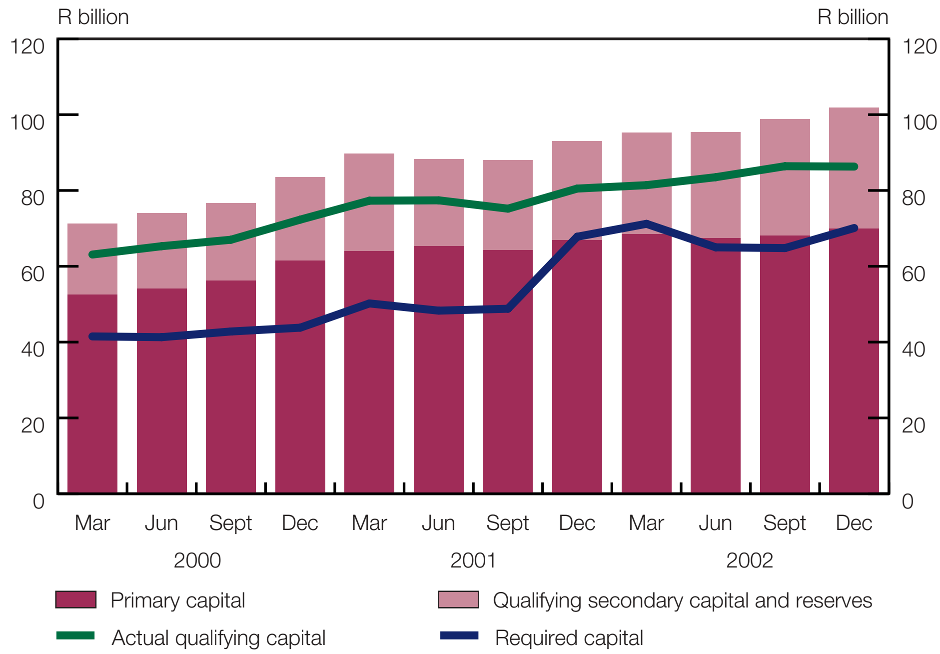
FIGURE 12: BANKS' CAPITAL ADEQUACY IN TERMS OF TOTAL ASSET VALUE



net growth in qualifying capital and reserves was higher than growth in 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 2002, primary capital and reserves constituted 68,8 per cent (2001: 86,6 per cent) of qualifying capital and reserves before deduction of impairments amounting to R15,5 billion (2001: R12,5 billion). Primary capital and reserves grew by 4,6 per cent (2001: 8,8 per cent) during the year under review, to R70 billion at the end of December 2002. Qualifying secondary capital and reserves, on the other hand, grew by 21,9 per cent during the year (2001: 18,7 per cent), to R31,8 billion at the end of December 2002. The net growth in qualifying capital and reserves of 7,2 per cent was higher than the growth in the total balance sheet of 4,8 per cent.

FIGURE 13: QUALIFYING CAPITAL AND RESERVES

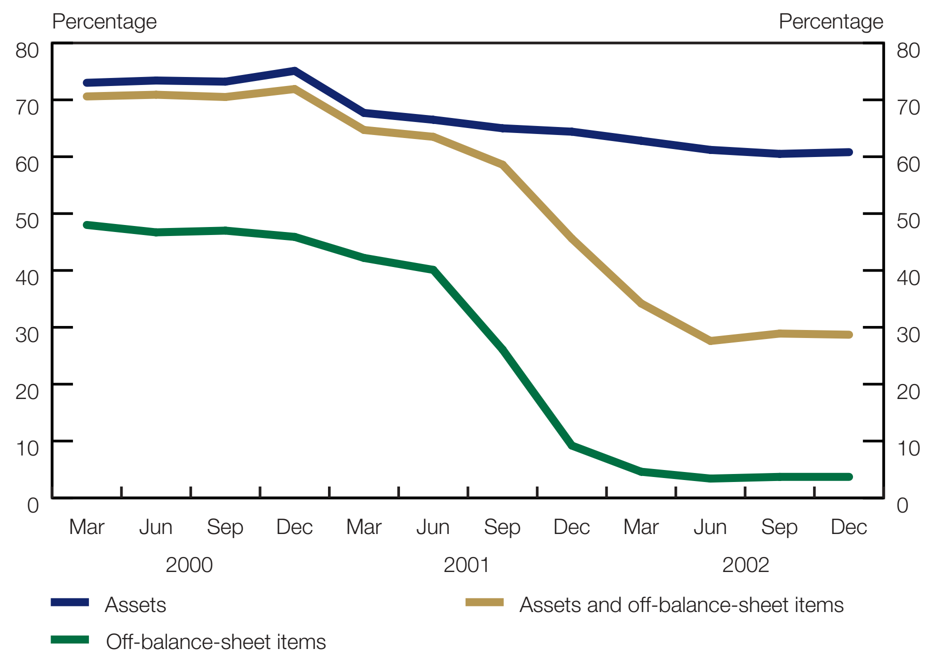


Risk profile of on- and-off-balance-sheet items

marked increase in off-balance-sheet items in 2001 and 2002

For the year ended 31 December 2002, total assets and off-balance-sheet items (figure 14) grew by 68,2 per cent (2001: 51,5 per cent), whereas total risk-weighted assets and off-balance-sheet items grew by 5,8 per cent (2001: 4,1 per cent). The marked increase in off-balance-sheet items in 2001 and 2002 compared to 2000 was due mainly to amendments to the Regulations relating to Banks that became effective on 1 January 2001. In terms of those amendments, banks have been required to report on central securities-depository participation, which, however, has not affected the average risk weighting of assets.

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



As a result of the composition of off-balance-sheet items, the average combined risk weighting for assets and off-balance-sheet items decreased from 58,1 per cent in 2001 to 29,9 per cent in 2002. At the end of December 2002, off-balance-sheet items accounted for approximately 56,3 per cent (December 2001: 34,1 per cent) of the combined total of assets and off-balance-sheet items. Figure 14 graphically illustrates the risk-weighted percentages of assets and off-balance-sheet items and of the combined total of assets and off-balance-sheet items.

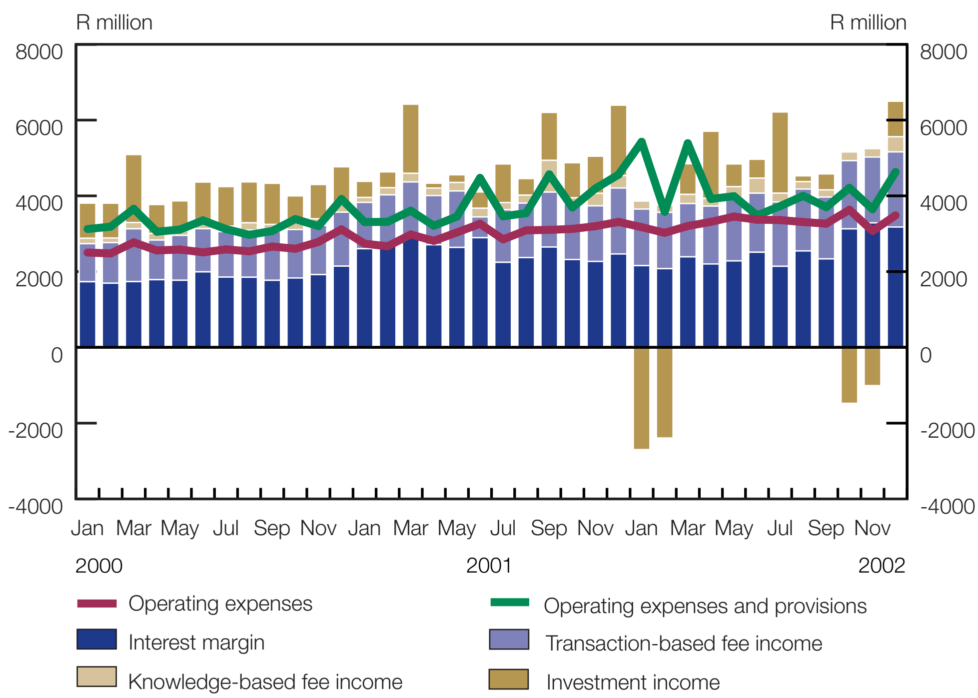
3.3 PROFITABILITY

analyses focus on the following aspects

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:

- 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).
- 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 2,8 per cent of total assets for the year, as opposed to 2,9 per cent in 2001) and transaction-based fee income (an average of 1,9 per cent of total assets for the year, as opposed to 1,8 per cent in 2001). As can be observed from figure 15, the income derived from the intermediation function (R49,9 billion) was generally just sufficient to cover the sum of operating expenses and provisions (R49,7 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 -0,02 per cent, respectively, of total assets (as opposed to 2,1 per cent and 1,1 per cent, respectively, during 2001).

interest margin decreased by 1,7 per cent

For the year, interest expense increased by about 39,8 per cent, which was 13,9 percentage points higher than the increase of 25,8 per cent in interest income. The net result thereof was that the interest margin decreased by 1,7 per cent, whereas it increased by 39 per cent in 2001. Interest derived from mortgage bonds and overdrafts and loans constituted 32,3 per cent and 30,3 per cent, respectively, of total interest income (as opposed to 33,3 per cent and 30,1 per cent, respectively, during 2001).

The main component of interest expense was interest on demand deposits and fixed and notice deposits. Interest paid in respect of demand deposits constituted 35,2 per cent (2001: 34,4 per cent) of the total interest expense, whereas interest paid on fixed and notice deposits constituted 27,7 per cent (2001: 29,2 per cent) of the total interest expense for the year.

FIGURE 16: INTEREST MARGIN

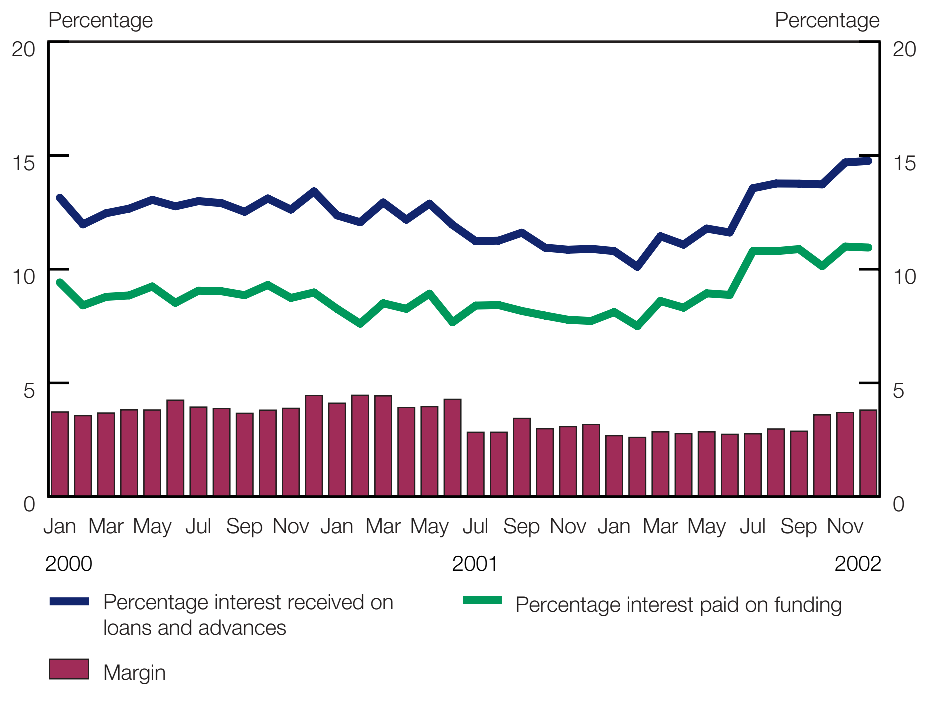


Figure 16 graphically displays the interest margin of the banking sector for the period from January 2000 to December 2002, whereas figure 17 represents the percentage-point change in the components of the interest margin for the aforementioned period. As can clear seasonal tendencies

clearly be seen from figure 16, the interest margin for the year was on average lower in 2002 than in 2001. By the end of December 2002, however, the interest margin was 3,8 per cent, compared to 3,2 per cent in 2001 and 4,5 per cent in 2000. 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

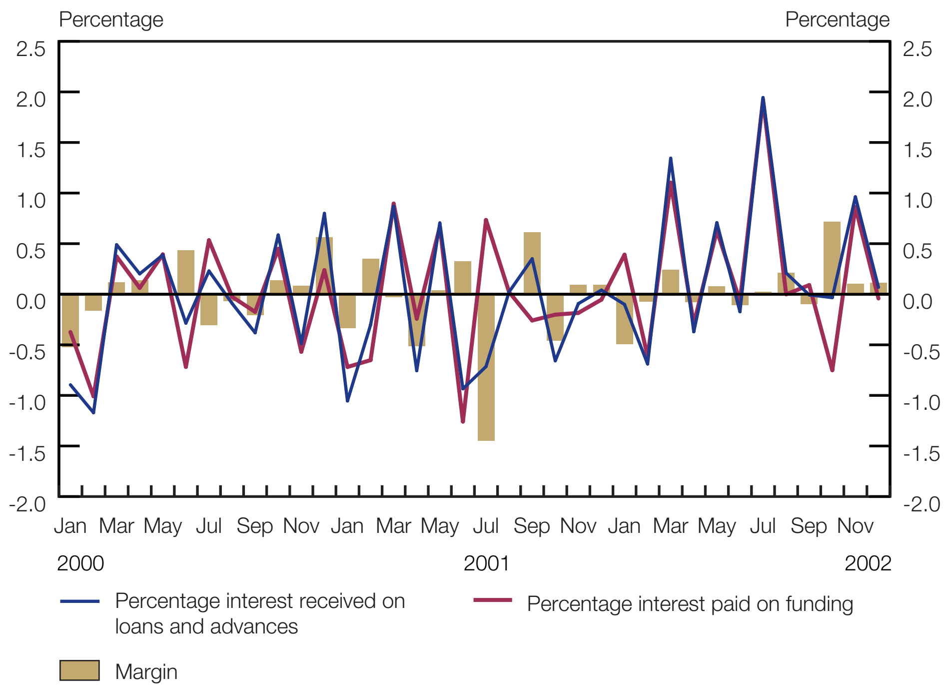
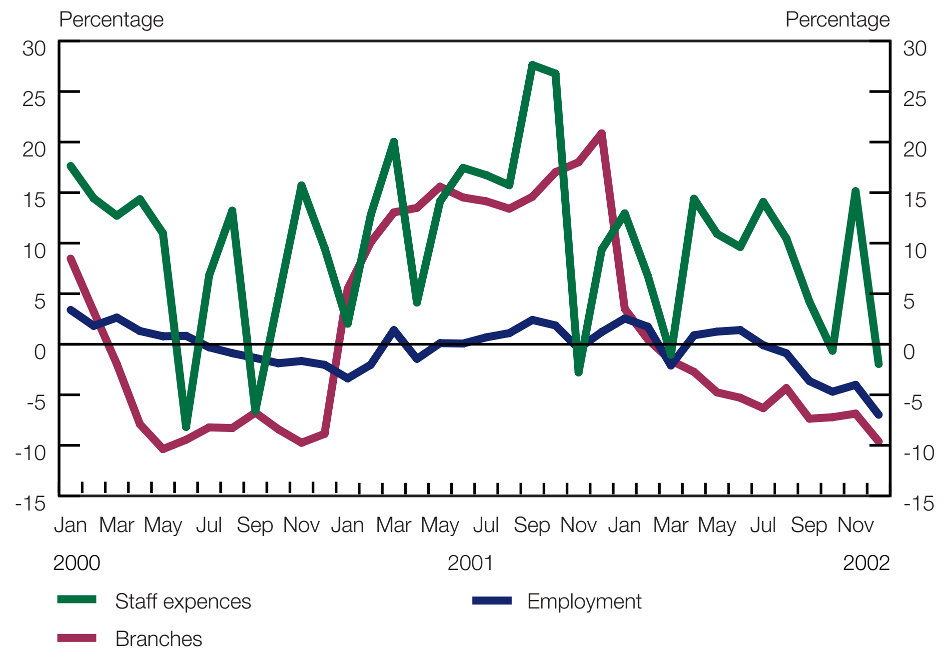


FIGURE 18: GROWTH IN STAFF EXPENSES, NUMBER OF EMPLOYEES AND NUMBER OF BRANCHES



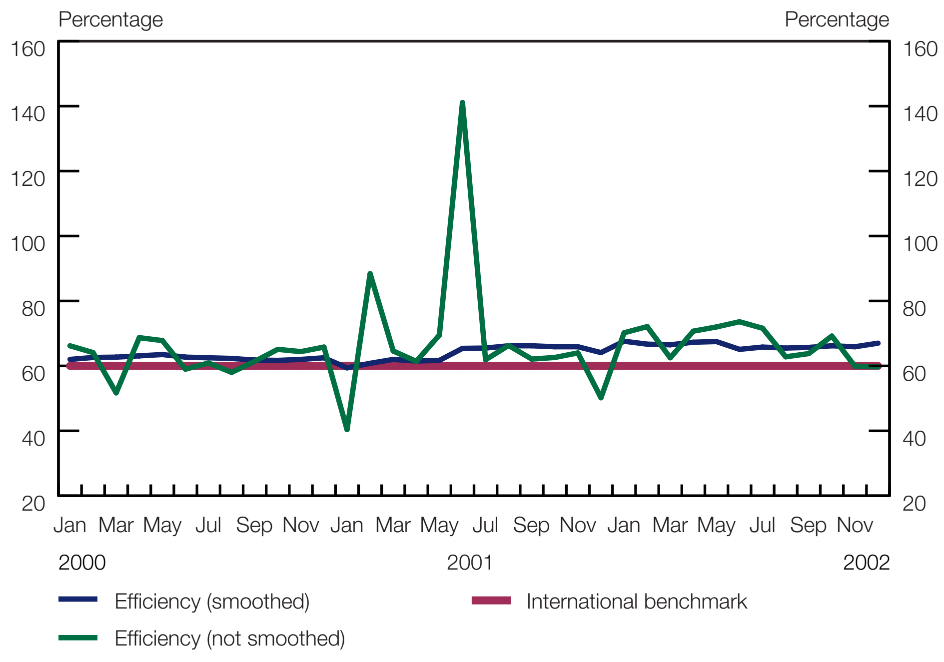
operating expenses increased by 9,6 per cent

The operating expenses of the total banking sector increased by 9,6 per cent (2001: 14,1 per cent) in 2002, mainly as a result of an increase of 7,6 per cent in total staff expenses, which accounted for about 47,2 per cent of total operating expenses. The increase in total staff expenses, however, was not due to an increase in the number of employees. This is confirmed by figure 18, which graphically displays the percentage change (measured over a 12-month period) in total staff expenses, the number of employees and the number of branches for the past three years. During 2002, both employment in the banking sector and the number of branches decreased by 1,2 per cent and 4,4 per cent respectively, as opposed to an increase of 0,1 per cent and 14,1 per cent, respectively, during 2001.

employment and number of branches decreased

Growth in operating expenses was also boosted by an increase in administrative expenses. Compared to the previous year, administrative expenses increased by 10,7 per cent and accounted for 42 per cent of total operating expenses.

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.

Figure 19 reflects the efficiency of the South African banking sector for the past three years. The high volatility in efficiency for 2001 was due mainly to some banks implementing Accounting Standard AC 133 in January 2001. In terms of the disclosure requirements of AC 133, banks were 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 book value or purchase price in terms of the equity accounting applied previously.

After reconsidering the implementation date of AC 133, however, the Accounting Practice Board announced that AC 133 would become effective for financial years commencing on or after 1 July 2002. As indicated in chapter 2 of this annual report, the objective of this delay was to enable companies to improve their business practices and systems and to efficiency was on average lower

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 2002, efficiency (67 per cent) was on average lower than in 2001 (64,1 per cent).

The actual values of, and the percentage growth in, the determinants of efficiency are graphically displayed in figure 20. Growth in total income of 5,1 per cent could not offset the increase in operating expenses (9,6 per cent), resulting in lower efficiency in the banking sector (as reflected in figure 19) during the year under review.

FIGURE 20: DETERMINANTS OF EFFICIENCY

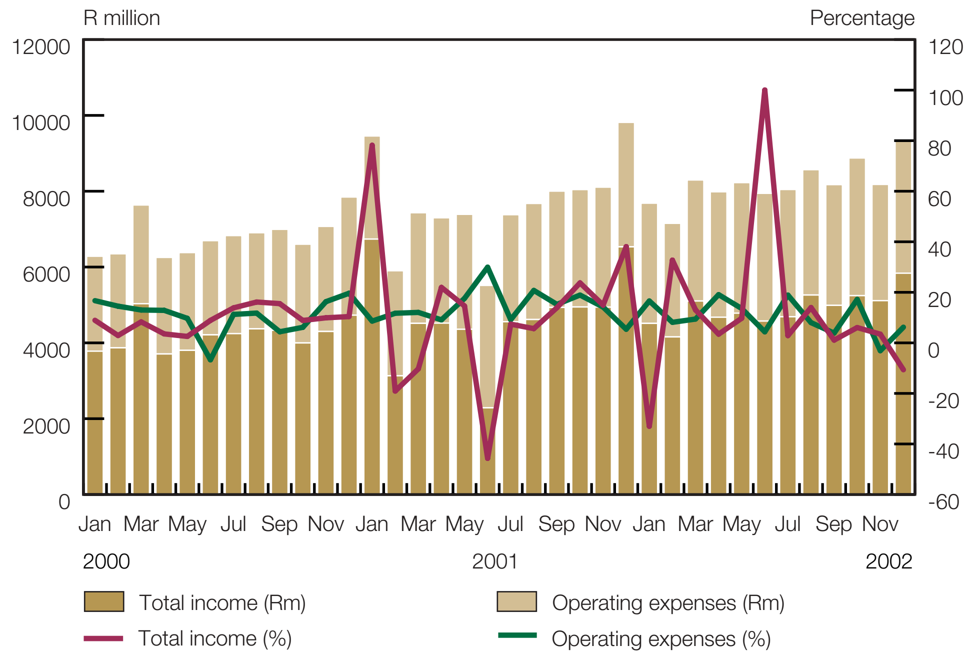


FIGURE 21: EFFICIENCY OF BANKING INSTITUTIONS ACCORDING TO ASSET SIZE – DECEMBER 2002

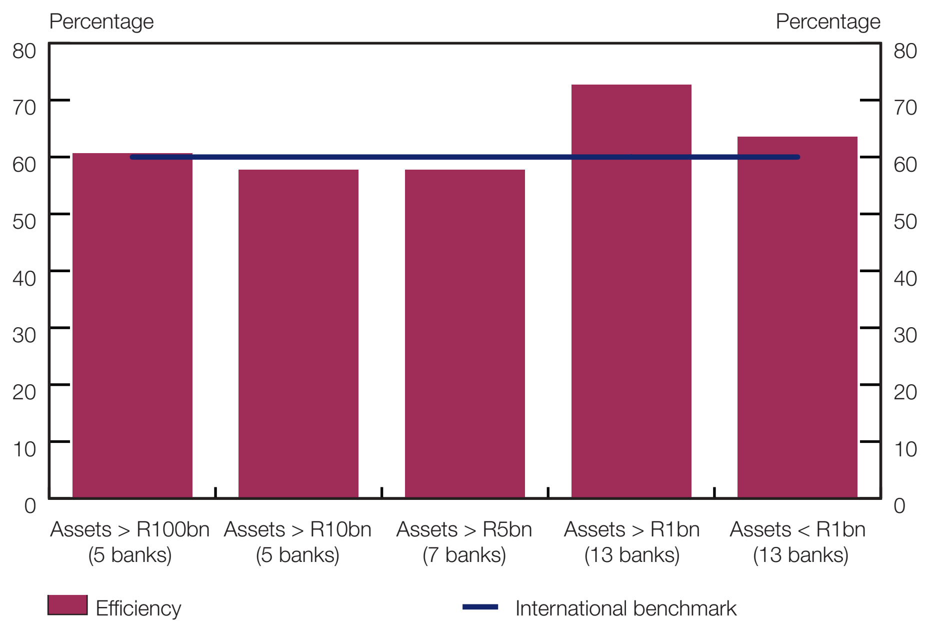
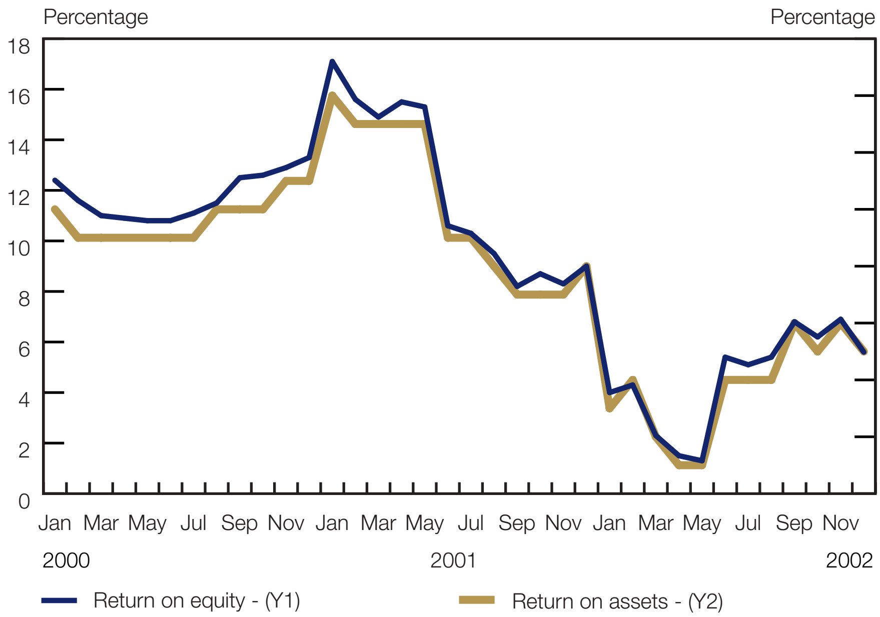


Figure 21 graphically displays the efficiency of the various categories (according to asset size) of banking institution for the year under review. The figure clearly shows that banks with asset values of above R5 billion, but below R50 billion, were the most efficient, at an efficiency ratio of 57,7 per cent, in December 2002. The next most efficient, at an efficiency ratio of 60,7 per cent, were banks with asset values of above R100 billion. Banks with asset values of above R1 billion, but below R5 billion, were the least efficient. It should be borne in mind, however, 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.

FIGURE 22: PROFITABILITY (12-month smoothed average)



The banking sector achieved a before-tax return equivalent to approximately 0,8 per cent of total assets (2001: 1,0 per cent). An after-tax return equivalent to approximately 0,4 per cent of total assets (2001: 0,7 per cent) was reported for 2002, whereas an after-tax return equivalent to approximately 5,6 per cent on net qualifying capital and reserves was reported (2001: 9,0 per cent).

marked deterioration in both the ROA and the ROE

The trends (calculated on the basis of a 12-month moving average) in the return on equity (ROE) and the return on assets (ROA) for the past three years are graphically displayed in figure 22. From January 2001 until May 2002, a marked deterioration in both the ROA and the ROE can clearly be detected from figure 22. This deterioration was due mainly to higher operating expenses, as discussed earlier in this chapter.

productivity of employees improved

Productivity can be measured by comparing the expenditure on employees with the amount of income generated. Figure 23 graphically displays the productivity of the banking sector for the past three years. During the year under review, the total income generated per employee was on average equivalent to R40 699, as opposed to R38 162 in 2001. Staff expenses per employee, on the other hand, were on average R12 893 in 2002, as opposed to R11 828 during 2001. 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 R26 334 in 2001 to R27 806 in 2002, indicating that the productivity of employees in the banking sector improved during the year under review.

FIGURE 23: PRODUCTIVITY

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 the 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

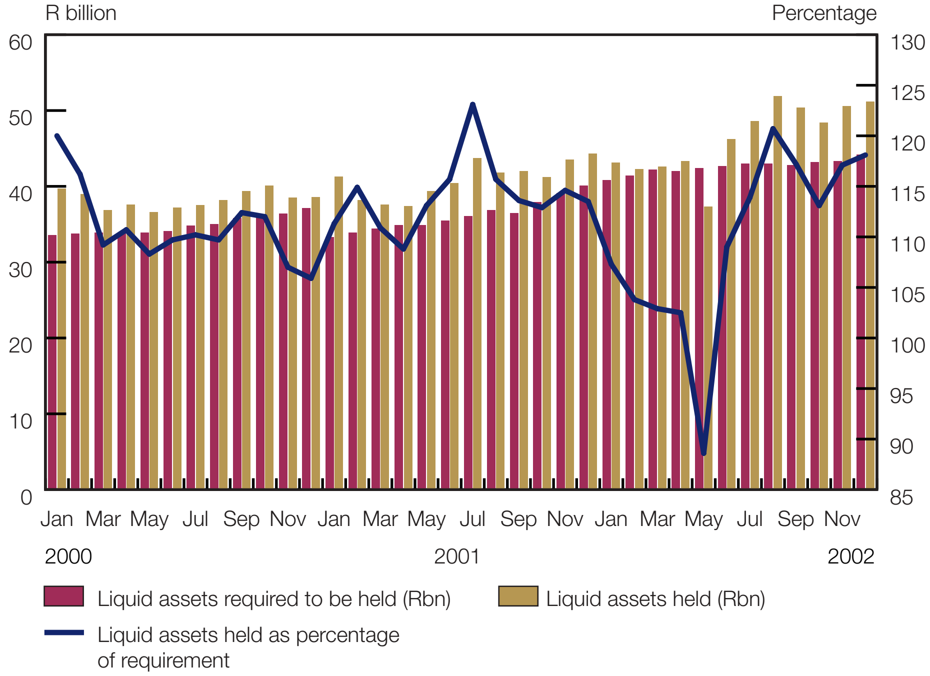
average daily amount of liquid assets held exceeded statutory liquid-asset requirement

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.

adjusted liabilities were reduced by 12,2 per cent

Approximately 56,1 per cent (2001: 57,4 per cent) of the average daily amount of liquid assets held during December 2002 consisted of securities issued by virtue of section 66 of the Public Finance Management Act, 1999, whereas 29,5 per cent (2001: 34,4 per cent) consisted of Treasury bills of the Republic of South Africa and 2,3 per cent (2001: 4,3 per cent) consisted of short-term bills issued by the Land Bank. Cash-management schemes managed on behalf of banks' clients increased by about 7,7 per cent (2001: 20,5 per cent). Set-off had decreased by 25,1 per cent (measured over 12 months) by the end of December 2002 and represented approximately 10 per cent (2001: 11,3 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 12,2 per cent (2001: 15,5 per cent), or R108,3 billion (2001: R124,7 billion), because of the use of cash-management schemes by banks' clients and the setting off of some asset balances against liabilities.

FIGURE 24: STATUTORY LIQUID ASSETS – ACTUAL VERSUS REQUIRED



Volatility of funding

As at 31 December 2002, total wholesale deposits constituted 81,2 per cent (2001: 84,1 per cent) of total wholesale and retail deposits. As can be seen in figure 25, wholesale deposits shorter than three months represented 50,1 per cent of total funding for December 2002. The sharp decrease, from R364,2 billion in December 2000 to R281,6 billion in January 2001, in wholesale deposits shorter than three months was due mainly to the inability of some banks to report in terms of the amended Regulations relating to Banks as from the effective date of 1 January 2001. Because of an amendment to the definition of wholesale deposits, however, comparisons over time should be made with caution.

comparisons over time should be made with caution

The aggregate amount of the 10 largest depositors of individual banks averaged R167,4 billion (2001: R115,4 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 18 per cent (2001: 13,8 per cent) at the end of December 2002 (see figure 25).

Short-term wholesale deposits (0-31 days) represented 39,6 per cent of total funding in December 2002, as opposed to 37,5 per cent for December 2001 (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' inability to report some information in terms of the amended Regulations relating to Banks as from the effective date. 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 2002, wholesale deposits shorter than seven days and wholesale deposits between eight and 31 days represented 23 per cent and 16,6 per cent, respectively, of total funding.

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

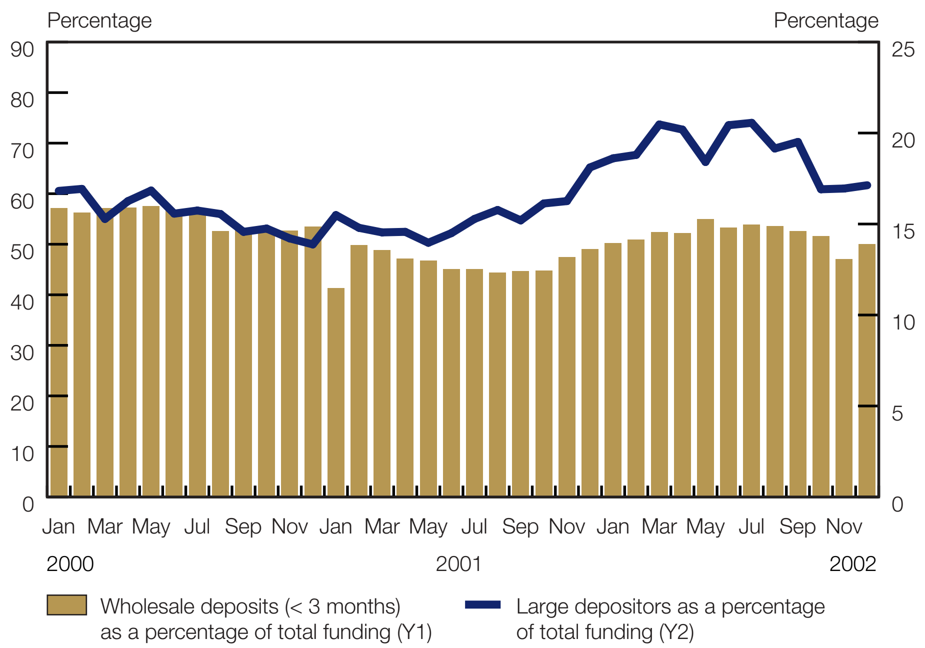


FIGURE 26: SHORT-TERM WHOLESALE DEPOSITS

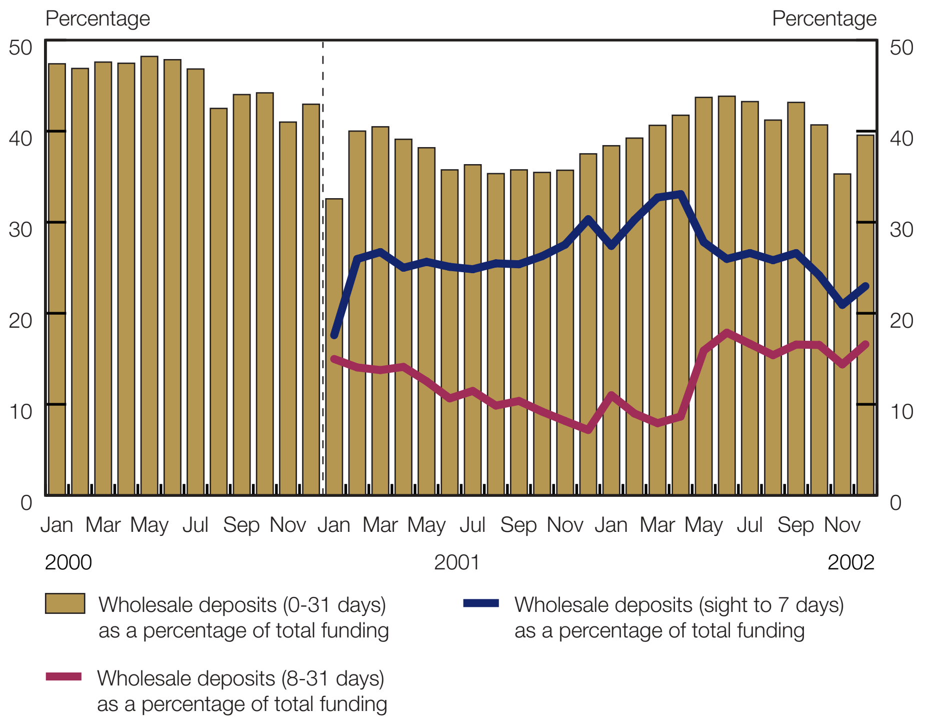


FIGURE 27: COMPOSITION OF WHOLESALE DEPOSITS ACCORDING TO MATURITY

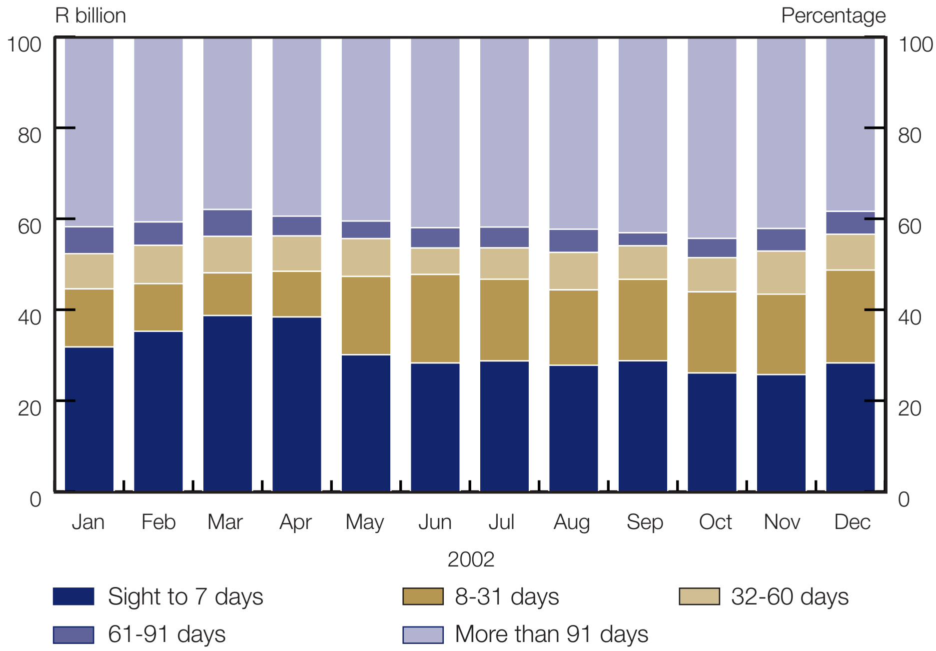


Figure 27 displays the composition (measured over a period of 12 months) of wholesale deposits according to maturity for the year under review. Wholesale deposits with a maturity shorter than seven days and wholesale deposits with a maturity greater than 91 days constituted the biggest portion of wholesale deposits in December 2002, namely, 28 per cent and 38 per cent, respectively. Wholesale deposits with a maturity of 32 to 60 days constituted only a small portion of total wholesale deposits, namely, 8 per cent, followed by deposits with a maturity of eight to 31 days (20 per cent of total wholesale deposits).

3.5 MARKET RISK

turnover in derivatives fluctuated widely

Turnover in derivatives fluctuated widely during the year under review, from approximately R1,329 billion in January 2002, to R438,4 million in June 2002 and to R545,8 million in October 2002 (see figure 28). In terms of the amended Regulations relating to Banks, banks have also been required to report on forward contracts, which decreased from R1,790 billion in January 2002 to R896,1 million in December 2002.

total unexpired derivative contracts decreased by 4,5 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 R586,5 million in December 2002 (December 2001: R1,2 billion), or 53,3 per cent of the banking sector's total assets (December 2001: 115,9 per cent). Average monthly balances, computed on a quarterly basis, were reported as R1,120 billion, R1,096 billion, R922,3 million and R634,4 million for the quarters ended March 2002, June 2002, September 2002 and December 2002, respectively. Compared to the previous year, total unexpired derivative contracts decreased by 4,5 per cent. As at 31 December 2002, the total value of unexpired derivative contracts was R6,891 billion (December 2001: R7,214 billion), representing 626,1 per cent of total assets (December 2001: 686,9 per cent of total assets). As at 31 December 2002, over-the-counter traded derivatives accounted for 91,5 per cent (2001: 83,1 per cent) of all unexpired derivative contracts.

FIGURE 28: TURNOVER IN DERIVATIVE CONTRACTS

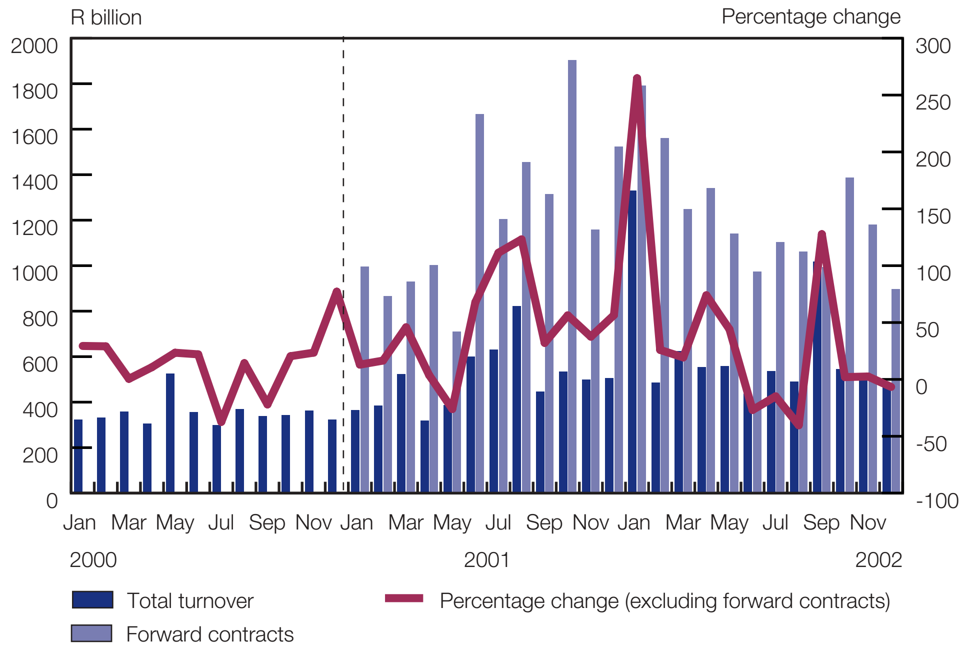
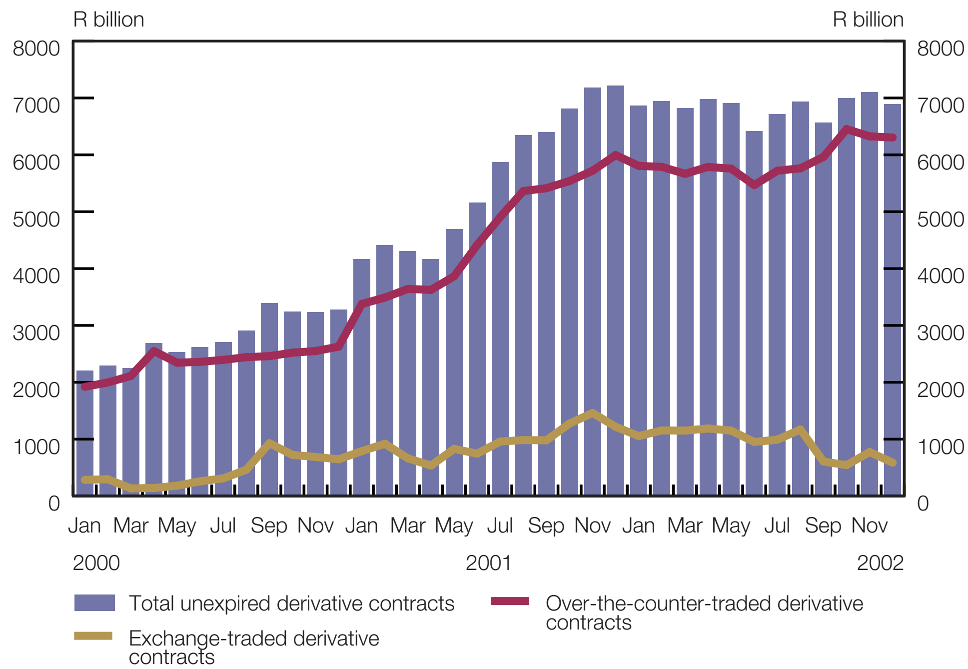


FIGURE 29: TOTAL UNEXPIRED DERIVATIVE CONTRACTS

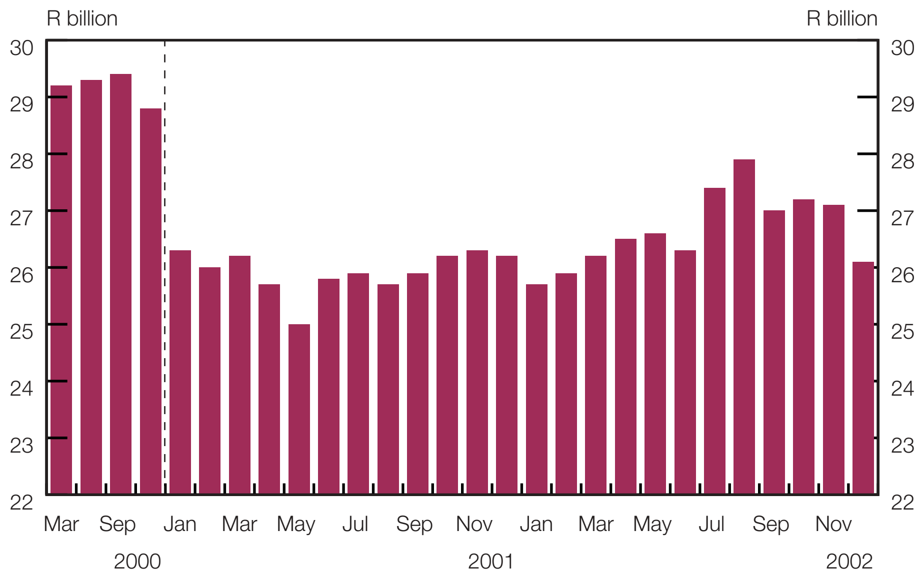


3.6 CREDIT RISK

Analysis of overdue amounts

Figure 30 graphically displays the level of total overdues for the banking sector for 2000 (in terms of the previous Regulations relating to Banks) and from March 2001 to December 2002 (in terms of the amended Regulations effective from 1 January 2001).

FIGURE 30: TOTAL BANKING-SECTOR OVERDUES



In terms of the amended Regulations relating to Banks, banks also have 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 clearly be seen in figure 30. A dotted line separates the overdues in terms of the previous Regulations from the overdues in terms of the amended Regulations. Because of the amended definition of overdues, comparisons over time should therefore be made with caution.

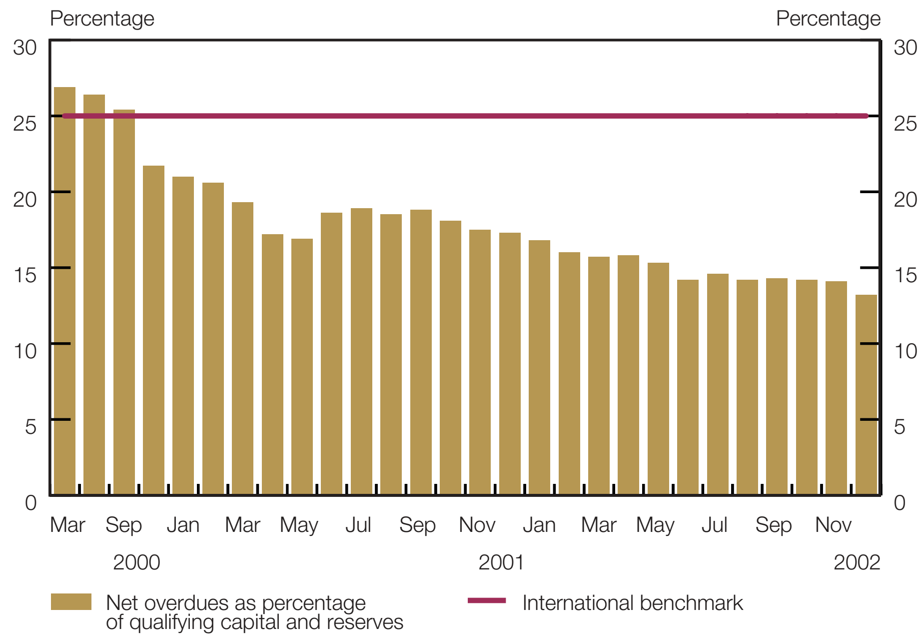
comparisons over time should be made with caution

Gross overdues increased from R26,3 billion in June 2002 to R27,4 billion in July 2002 (that is, by R1,1 billion), mainly as a result of the reclassification of loans and advances by a smaller bank. From January 2001 to the end of December 2002, the net decrease in gross overdues of the total banking sector amounted to R117,4 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. As can be clearly noted from this figure, net overdues as percentage of net qualifying capital and reserves decreased almost uninterruptedly during 2002. Net overdues as a percentage of net qualifying capital and reserves decreased from 17,3 per cent in December 2001 to 16,8 per cent in January 2002. By the end of December 2002, this ratio had improved to 13,2 per cent, which was well below the international benchmark of 25 per cent.

net overdues decreased almost uninterruptedly

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



Expressed as a percentage of total loans and advances (see figure 32), gross amounts overdue improved from 3,2 per cent in December 2001 to 3,1 per cent in January 2002. By the end of December 2002, the gross amount overdue (as a percentage of total loans and advances) had improved to 2,9 per cent. From January 2002 to December 2002, mortgage loans overdue (as a percentage of total mortgage loans and advances) and instalment sales overdue (as a percentage of total instalment sales) improved from 3,4 per cent to 3 per cent and from 3 per cent to 1,9 per cent, respectively. Other loans and advances overdue (as a percentage of total other loans and advances), however, increased from 2,9 per cent to 3 per cent.

FIGURE 32: COMPOSITION OF OVERDUES (as a percentage of loans and advances)

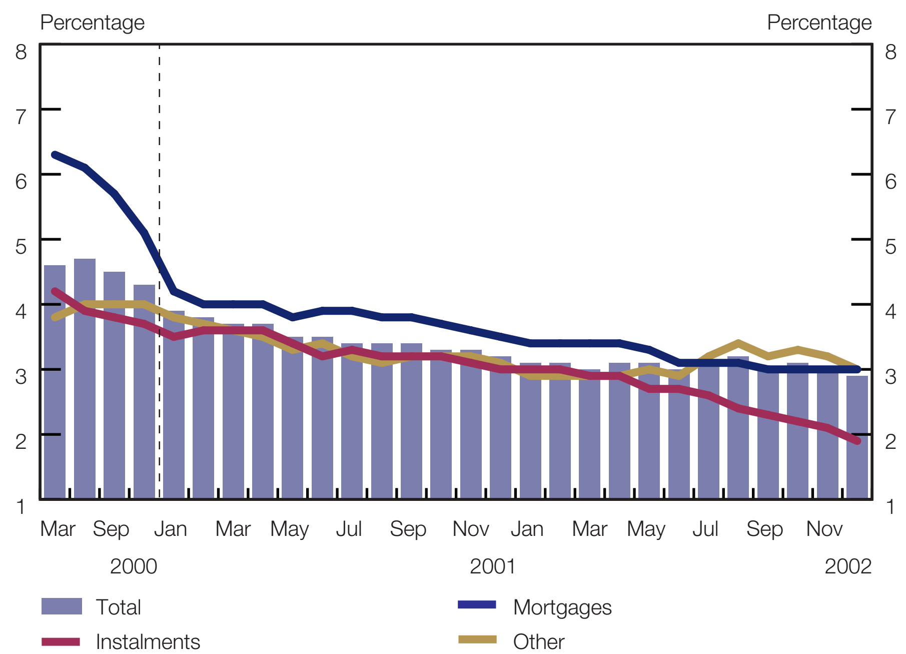
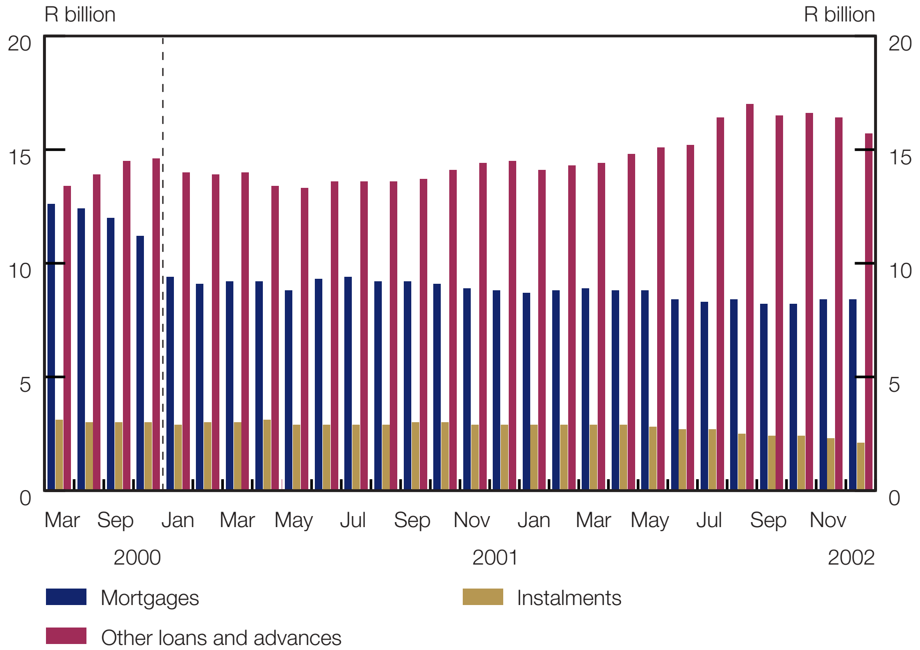


Figure 33 graphically displays an analysis of overdue amounts for the period from March 2000 to December 2002. The gross amount overdue in respect of other loans and advances, which constituted the biggest portion of amounts overdue, increased from R14,1 billion to R15,7 billion during the year under review and, by the end of December 2002, exceeded overdues in respect of mortgages by R7,2 billion. Overdues in respect of mortgages decreased from R8,8 billion in December 2001 to R8,7 billion in January 2002 and to R8,4 billion in December 2002, and overdues in respect of instalment sales decreased from R2,9 billion to R2,1 billion during the year under review.

FIGURE 33: ANALYSIS OF OVERDUE ACCOUNTS



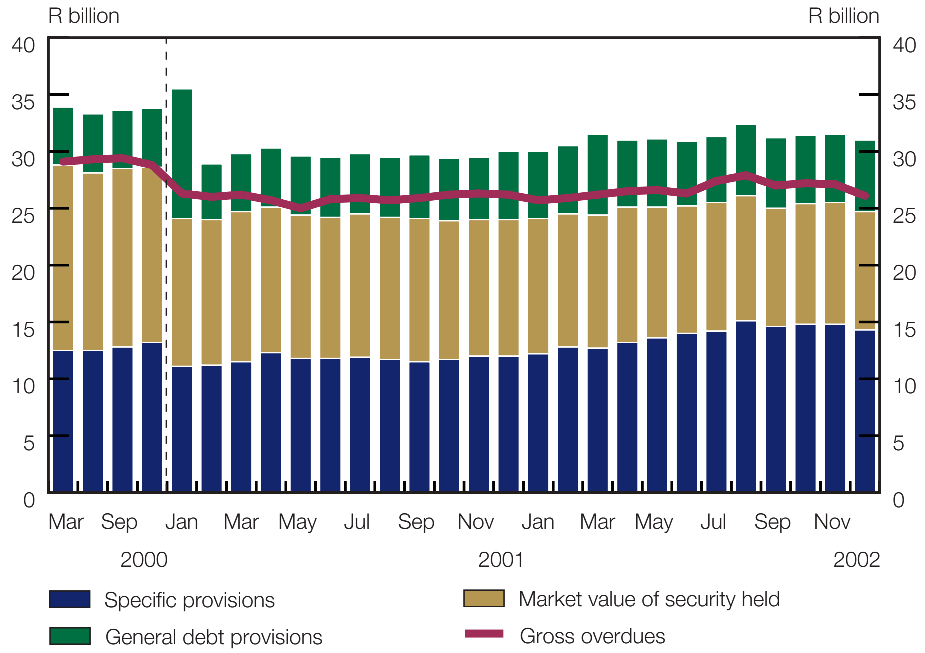
Provisioning policy for bad and doubtful loans and advances

As indicated in the previous annual report, the implementation of the amended Regulations relating to Banks on 1 January 2001 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, despite the marked increase in overdues between June and August 2002. By the end of December 2002, specific provisions covered about 54,5 per cent (December 2001: 45,9 per cent) of all overdues. At the end of December 2002, provisioning (that is, specific provisioning plus security) covered about 94,4 per cent of overdues, compared to 91,7 per cent in December 2001.

FIGURE 34: ADEQUACY OF PROVISIONS

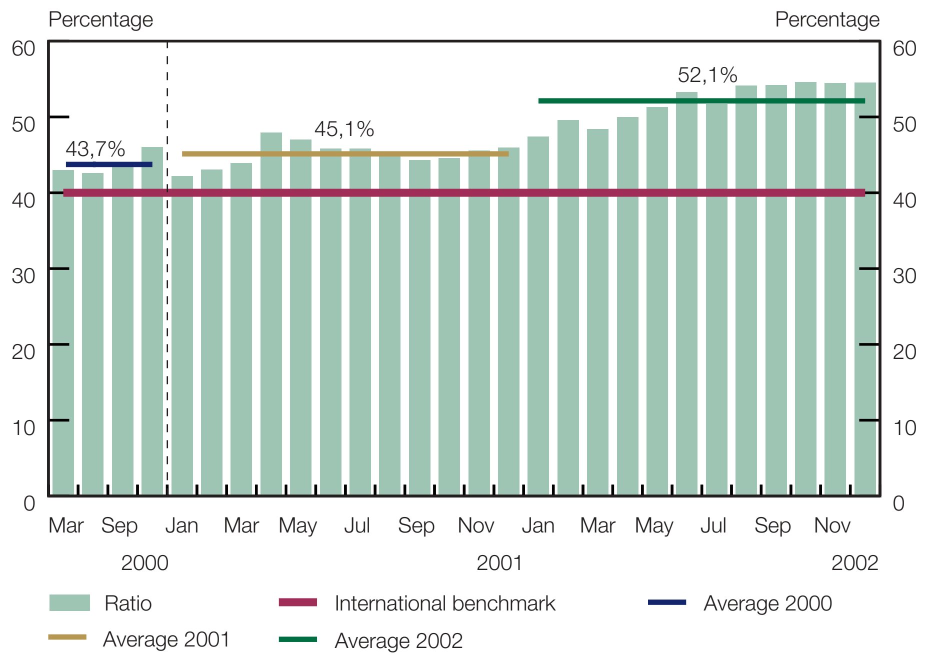


specific provisions by loan type

Specific provisions made at the end of December 2002, by loan type and expressed as a percentage of overdue amounts, were as follows:

- Mortgages - 26,1 per cent (2001: 27,4 per cent).
- Instalment sales - 66,5 per cent (2001: 52,3 per cent).
- Other loans and advances - 68,3 per cent (2001: 56 per cent).

FIGURE 35: SPECIFIC PROVISIONS AS PERCENTAGE OF TOTAL OVERDUES



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 52,1 per cent of overdues were covered by specific provisioning during 2002 (2001: 45,1 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

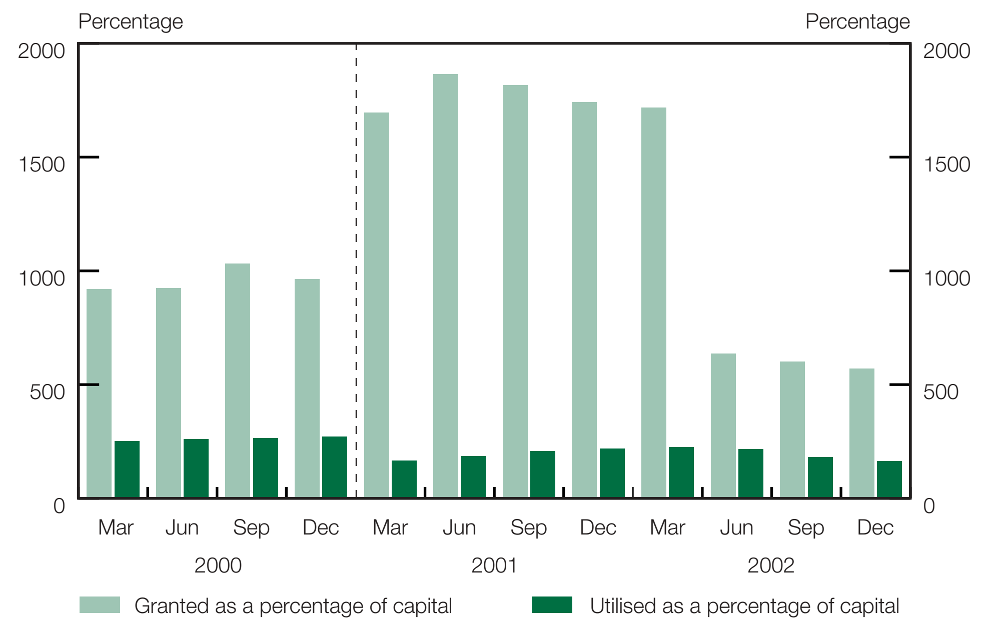
As from January 2001, the Regulations relating to Banks have required large exposures granted not to exceed 800 per cent of capital and reserves, in line with the guidelines of the European Economic Community. In terms of these guidelines, those large exposures granted that exceed 15 per cent of capital 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 2000 to December 2002 is illustrated graphically in figure 36

overdues in respect of large exposures decreased

Large exposures granted increased by R50,8 million, to a level of R1,5 billion in January 2002 (representing 1 718,5 per cent of net qualifying capital and reserves), as opposed to R1,4 billion (representing 1 743,3 per cent of net qualifying capital and reserves) in December 2001. By the end of December 2002, large exposures granted had decreased to a level of R514,2 million (representing 570,2 per cent of net qualifying capital and reserves). Overdues in respect of large exposures decreased from R216,7 million in December 2001 to R214,2 million in January 2002. By the end of December 2002, overdues in respect of large exposures had decreased marginally to R32,5 million, and specific provisions covered about 2 per cent of overdues. The value of the security held by banks covered the remaining overdues.

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

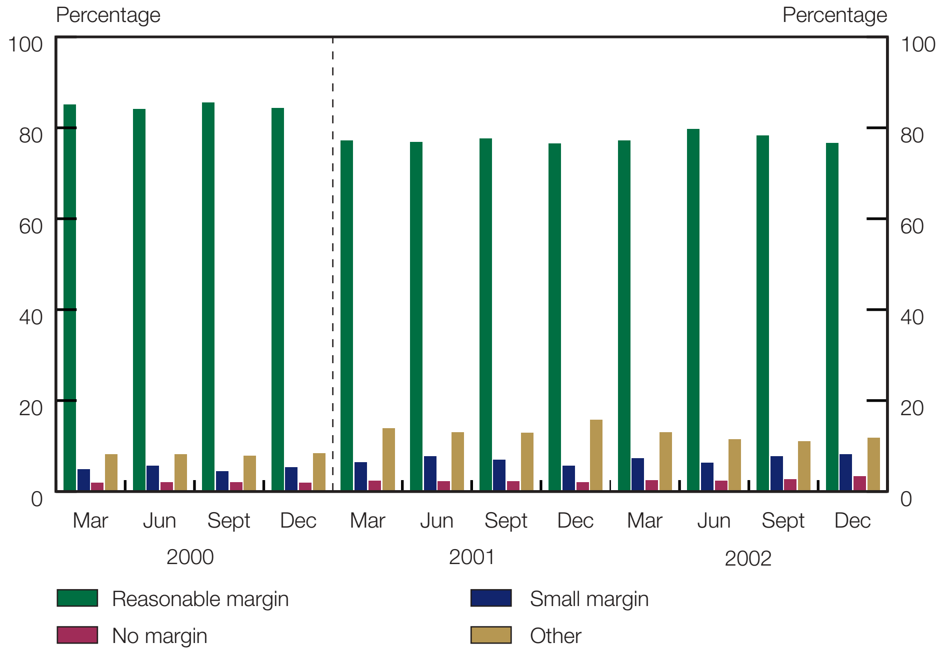


Quality of assets

76,7 per cent of assets earned a reasonable margin

Figure 37 shows that, by the end of December 2002, about 76,7 per cent of the banking sector's assets (December 2001: 76,5 per cent) earned a reasonable margin and 8,2 per cent (December 2001: 5,7 per cent) earned a small margin, whereas the remaining 15,1 per cent of assets (December 2001: 17,8 per cent), including infrastructure, earned no margin.

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 0,1 per cent in January 2002 and, by the end of December 2002, the ratio had increased to 0,3 per cent. The aggregated net effective open foreign-currency position of the total banking sector is displayed in figure 38.

During the year under review, the maximum net open position in foreign currency after hedging decreased from 4,6 per cent to 3,6 per cent and remained safely within the limit of 10 per cent of net qualifying capital and reserves (see figure 39).

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

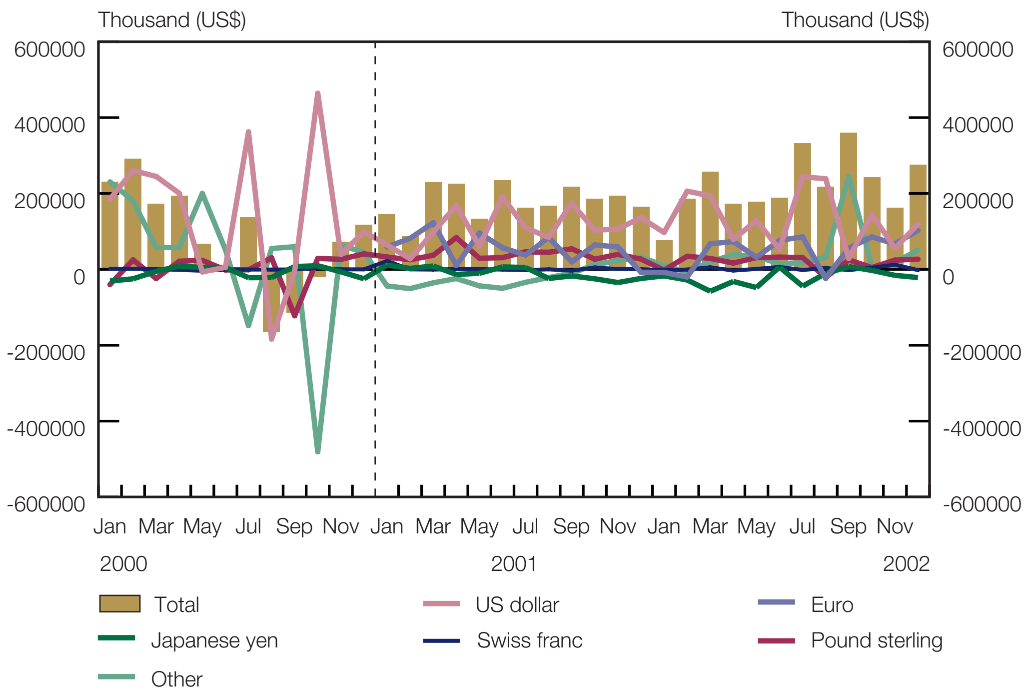
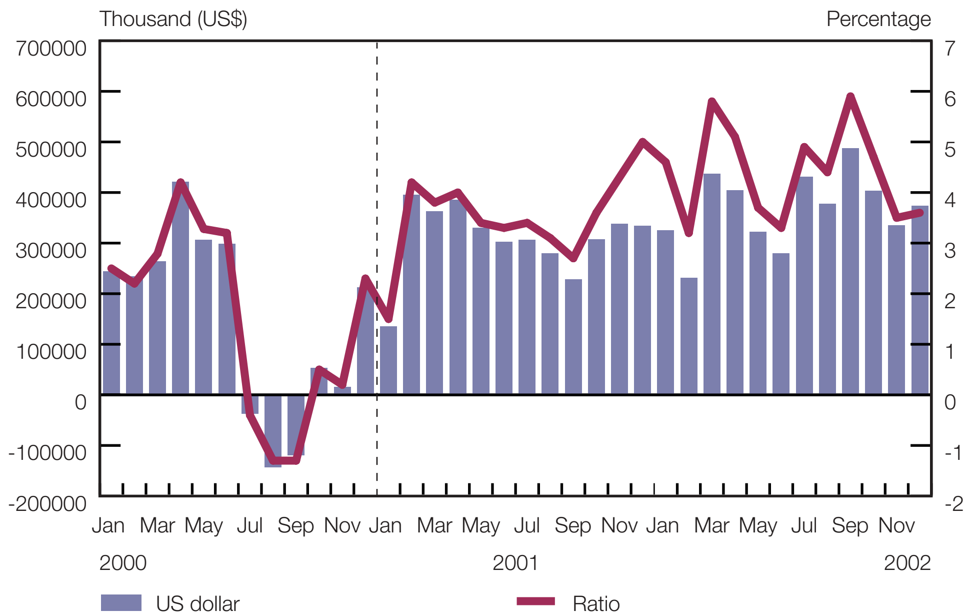


FIGURE 39: MAXIMUM EFFECTIVE NET OPEN FOREIGN-CURRENCY POSITION AS A PERCENTAGE OF NET QUALIFYING CAPITAL AND RESERVES (compliance with limit of 10 per cent)



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

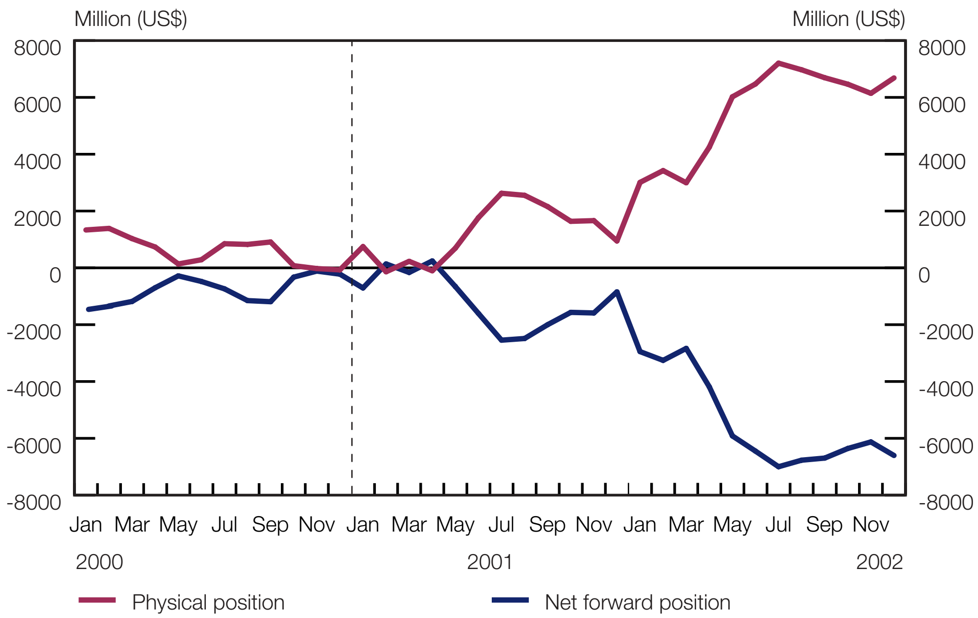


FIGURE 41: LIQUIDITY-MATURITY STRUCTURE (US dollars)