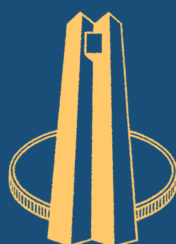
Annual Report 2005

Bank Supervision Department



South African Reserve Bank

Mission

To promote the soundness of banks through the effective application of international regulatory and supervisory standards

Business philosophy

Market principles underlie all activities and decisions, and we strive to act with professionalism, integrity, credibility and impartiality at all times. We liaise with each individual bank through a single point of entry – a relationship manager, assisted by a team with diverse competencies. We follow a risk-based management approach, not one of inspection, and our objective is to add value. Consequently, our role is that of a "watchdog", not that of a "bloodhound". We place emphasis on empowering our staff to ensure that all interaction and service delivery is characterised by professionalism, and a high premium is placed on ethical behaviour at all levels of activity. A relationship of mutual trust between the Department and all other key players is regarded as essential and is built up through regular open communication.

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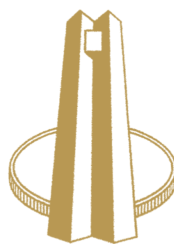


South African Reserve Bank

Message from the Registrar of Banks on the importance of information technology systems in banks

In recent years, continuous asset growth in the banking industry, rapid product development and the resultant new regulatory requirements have brought to the fore the importance of information technology (IT) systems.

Over the past five years, total bank assets in South Africa have more than doubled, from R820 billion as at December 2000 to R1 677,5 billion as at December 2005. Growth in the number of clients, in transaction sizes and in volumes has placed tremendous strain on IT systems that were sufficient only five years ago. In addition to the IT challenges arising from the enlarged balance sheets, mergers and acquisitions during the aforementioned five-year period have resulted in banks now having to operate a number of different systems. These are not necessarily compatible.

The trait of bankers continuously to explore new avenues to increase shareholder value, that is, the bottom line, and to improve risk management has resulted in ever more complex products being offered in the market. These products range from plain "vanilla-type" instruments used for hedging to very complicated securitisation structures and exotic derivatives. The question is whether the IT-system enhancements of the banking industry have been commensurate with the nature, size and complexity of the products with which banks are now dealing.

Regulators respond to such developments by setting risk-management guidelines and principles to ensure that banks are measuring, mitigating and monitoring their risk. A case in point is the new international framework to regulate bank capital adequacy, commonly referred to as Basel II. It has been reported that, thus far, some large South African banks have each spent over R100 million, the expenditure of one bank being closer to the R200 million mark, in readying themselves for Basel II. It is estimated that upon full compliance with Basel II, the large South African banks may have incurred a bill of between R100 million and R250 million each. Major European and North American banks are each expected to spend in excess of R360 million (€50 million).

These are high figures indeed, but we should note that *"Bankers implicitly accept risk as a consequence of providing services to customers and also take explicit risk positions that offer profitable returns relative to their risk appetites. The job of bank supervisors is to ensure that bank capital represents an adequate cushion against losses, especially during times of financial instability or stress. Basel II is yet another step to minimize the negative consequences of risk-taking by financial institutions, particularly those institutions that could contribute to financial instability."* (Speech by Governor Susan Schmidt Bies, US Federal Reserve System, May 2005.)

Another development that has gained pace over the past five years (in no small part as a result of the tragic events that occurred in the United States on 11 September 2001) is the fight against money laundering and terrorist financing. In most cases, this also requires additional IT-system investment. International guidance requiring banks to "know their customers" and monitor their transactions has been issued by both the Basel Committee on Banking Supervision and the Financial Action Task Force. South African banks are working towards full compliance with the requirements of the Financial Intelligence Centre Act, 2001, and effective implementation thereof has resulted in extensive adjustments to IT systems. In this regard, the reviews of the major South African banks discussed under banks' compliance with anti-money-laundering legislation, in chapter 2 of this annual report, have highlighted the need for and importance of systems being enhanced to attain the appropriate levels of sophistication not only to enable banks to fulfil their responsibilities in satisfying regulatory requirements, but also to aid the overall risk-management process.

It is recognised that banks are currently faced with enormous challenges and may have financial and human-resource constraints. The future viability and sustainability of banks, however, are dependent on banks having appropriate, reliable and robust IT systems, the sophistication of which does not lag behind the prevailing rapid progress and development of profit-driven products.

South African Reserve Bank

Bank Supervision Department

Annual report for the calendar year ended 31 December 2005 in terms of section 10 of the Banks Act, 1990, and section 8 of the Mutual Banks Act, 1993

This report presents an overview of the objectives and activities of the Bank Supervision Department of the South African Reserve Bank, with particular reference to the period from 1 January 2005 to 31 December 2005.

INDEX

Chapter		Page
1.	Registrar's review	4
2.	Current issues in banking supervision	16
3.	Developments related to banking legislation	39
4.	Trends in South African banks	50
	4.1 Balance-sheet structure	50
	4.2 Capital adequacy	58
	4.3 Profitability	61
	4.4 Liquidity risk	67
	4.5 Market risk	70
	4.6 Credit risk	72
	4.7 Currency risk	78

Appendices

1.	Organisational structure of the Bank Supervision Department	82
2.	Registered banks, mutual banks and local branches of foreign banks as at 31 December 2005	83
3.	Name changes and cancellation of registration of banks and branches of foreign banks during the period from 1 January 2005 to 31 December 2005	85
4.	Registered controlling companies as at 31 December 2005	86
5.	Foreign banks with approved local representative offices	87
6.	Trends in South African banks - list of tables	89
7.	Circulars sent to banking institutions during 2005	112
8.	Exemptions and exclusions from the application of the Banks Act, 1990	113
9.	Approval of acquisition or establishment of foreign banking interests in terms of section 52 of the Banks Act, 1990, from 1 January 2005 to 31 December 2005	114

Chapter 1

Registrar's review

banking system remained stable

During the year under review, the South African banking system remained stable, and banks were again adequately capitalised. It was also pleasing to note that the previous two years' downward trend in the banking sector's total gross overdues continued during 2005. There were, however, initial signs of a decline in banks' profitability indicators and efficiency, and concentration in the banking sector increased, as outlined below.

Other issues reviewed in this chapter include banks' progress with the implementation of the Financial Sector Charter, the acquisition of one of South Africa's big five banks by an international bank, progress with South Africa's economic-policy framework and the importance of succession planning for bank's senior executives.

During 2005, I was appointed as one of the four new executive general managers (EGMs) of the South African Reserve Bank (SARB), besides retaining my position as Registrar of Banks. The EGMs report to the Deputy Governors of the SARB, are responsible for the overall management of the SARB and, together with the Governor and the Deputy Governors, constitute the Governor's Executive Committee of the SARB. In this vein, it gives me great pleasure to state that three Deputy Registrars of Banks, namely, Mrs Yvette Singh and Messrs Madoda Petros and Michael Blackbeard, were appointed with effect from 1 April 2006.

Overview of the South African banking system

The South African banking system remained stable, and, in general, banks were sound and continued to benefit from and contribute to South Africa's economic health during 2005. Banks were well capitalised, and the average risk-weighted capital-adequacy ratio for the banking system as a whole was 13,3 per cent at the end of December 2005, compared to the required minimum ratio of 10 per cent.

banks were well capitalised

Growth in the total balance sheet remained strong throughout the year under review. By the end of December 2005, the total assets of banks – comprising, amongst other things, money, loans and advances, investment and trading positions and non-financial assets – had increased by 12 per cent (measured over a period of twelve months), to a level of R1 677,5 billion (December 2004: R1 489,4 billion). Mortgage advances showed the strongest growth of the various types of credit. At the end of 2005, the five largest banks (one of which is now internationally owned) represented about 89,6 per cent of the total assets of the banking sector, compared to 88,5 per cent at the end of December 2004. At the end of December 2005, small local banks constituted 2,2 per cent of total banking-sector assets (December 2004: 2,9 per cent), whereas other international banks constituted 8,6 per cent of the banking sector (December 2004: 8,2 per cent).

total assets of banks increased

Total non-bank deposits increased by 21,1 per cent over the 12-month period ended 31 December 2005 (December 2004: 20,5 per cent). The composition of non-bank deposits remained largely unchanged during the year under review.

profitability indicators declined somewhat

Profitability indicators, however, declined somewhat during 2005. By the end of December 2005, the average return on net qualifying capital and reserves (smoothed) was 14,4 per cent, down from 14,7 per cent in December 2004, whereas the return on assets (smoothed) decreased from 1,2 per cent in December 2004 to 1,1 per cent in December 2005. The efficiency (cost-to-income ratio) of the banking sector also started showing signs of a decline during the year under review, weakening from 63,9 per cent in December 2004 to 66,3 per cent in December 2005.

Throughout 2005, the average daily amount of liquid assets held by South African banks exceeded the statutory liquid-asset requirement. In December 2005, banks' liquid assets amounted to 119,7 per cent of the liquid assets required to be held, compared to a level of 116,8 per cent in December 2004.

Besides banks experiencing strong asset growth in their core products, gross amounts overdue also improved during 2005. Expressed as a percentage of total loans and advances, gross amounts overdue improved from 1,8 per cent in December 2004 to 1,5 per cent in December 2005. Banks' provisioning against these non-performing loans was adequate.

strong asset growth in core products

It is evident that banks benefited from and contributed positively to the solid and consistent performance of the South African economy. It remains important, however, for bankers to remain aware of the various stages of a banking cycle, as explained in detail in the previous annual report, and to prepare themselves for the effects of any future downturn. Despite benign conditions during the year under review, the banking sector for the first time saw not only profitability deteriorating, but also a decline in the all important international cost-to-income ratio, or the efficiency ratio.

decline in the efficiency ratio

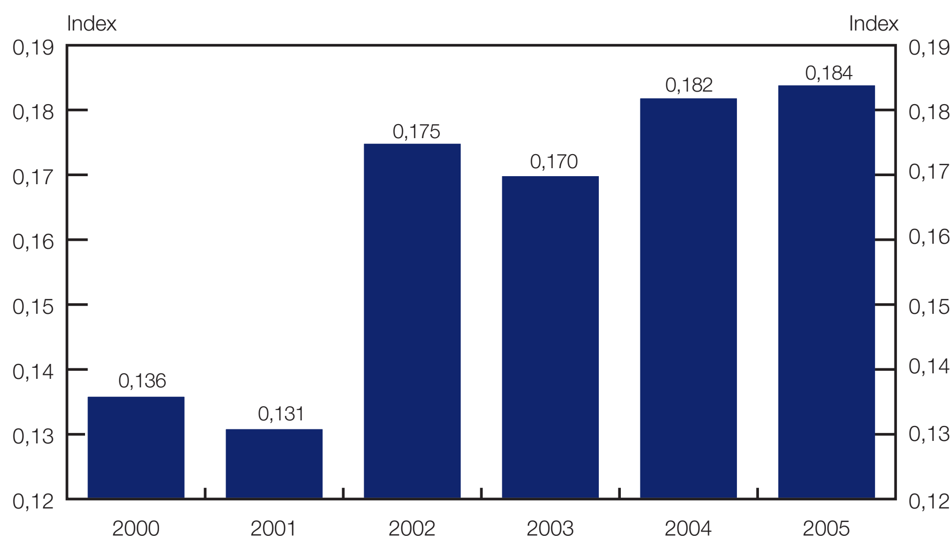
Concentration in the South African banking system

Several indices may be used to measure concentration and competition in a banking system. The most widely used index in the literature is the Herfindahl-Hirschman index, commonly referred to as the H-index. It is the sum of the squares of the percentages of market share held by the banks in the industry and ranges between 1 (for a monopoly) and 1/n, where n is the number of banks in the system. The H-index accounts for both the number and relative size of banks in the system and is therefore preferred to most other measures of concentration.

H-index

In South Africa, which had 34 banking institutions reporting data to the Bank Supervision Department (excluding two mutual banks, but including one institution doing banking business in terms of an exemption from the provisions of the Banks Act, namely, Ithala

Figure 1: H-index for the South African banking system (2000-2005)



H-index deteriorated

Limited) at the end of the year under review, the H-index deteriorated from 0,182 in 2004 to 0,184 in 2005, as illustrated in figure 1 below. Since the number of banks has decreased by only one bank since 2004, the deterioration in the H-index may be attributed mainly to the four largest banking groups constituting a larger proportion of the total banking system. These four banks constituted 83,8 per cent of the banking sector in December 2005, compared to 83,6 per cent in December 2004.

Progress with implementation of the Financial Sector Charter

In the previous annual report, it was noted that the Charter Council envisaged by the Financial Sector Charter had been established and that progress was being made with the creation of the structures necessary to ensure implementation of the Charter. During 2005, the Charter Council set up offices in Johannesburg, and the Charter Council Principal Officer, Mr Enoch Godongwana, was appointed in October 2005.

principal commitments

The principal commitments made in terms of the Charter include to:

- Improve access to financial services for low-income communities.
- Increase investment in housing for low-income households (target of R42 billion), small and medium black-owned enterprises (target of R5 billion), agriculture (target of R1,5 billion) and transformational infrastructure (target of R25 billion).
- Increase funding for black economic-empowerment (BEE) transactional financing.
- Accelerate employment equity and skills development within the financial sector.
- Increase procurement from BEE-accredited enterprises.
- Achieve BEE ownership and control targets.

The ten Charter Council committees tasked with addressing the challenges of implementing the commitments listed above met regularly throughout 2005, and most committees completed their work.

housing-finance target

With regard to targeted investment financing, the Charter Council will continue to work with Government to design risk-sharing and risk-mitigation measures. Charter participants committed themselves to achieving the housing-finance target of R42 billion for low-income households by 2008, and the negotiations for implementation took a new direction in 2005. As regards BEE transaction financing, it was agreed that R1 billion would go towards the funding of cooperatives. The Charter Council will facilitate discussions to define how to incentivise the financial sector to utilise black private-equity partners.

Access to and delivery of entry-level products

access standards for entry-level products

Access standards for entry-level products across all financial industries were finalised and approved by the Charter Council. Key indicators include physical access, appropriateness, affordability, fair value, simplicity and non-discrimination. The finalised standards give companies the opportunity to design new products to address access needs and contribute to their Charter commitments. The Access Committee also completed work on standards to measure consumer education. It was further agreed that the Charter Council would ensure that research on the needs of the target market and the impact of Charter initiatives would be undertaken on an ongoing basis.

Mzansi accounts

The banking industry is leading other financial industries as regards delivery of entry-level products. Almost two million Mzansi accounts have been opened since the launch of the new product by the four major banks and the PostBank in October 2004. The Mzansi account was launched prior to the development of the newly formulated access standards, but was designed with affordability and accessibility in mind. For that reason,

although the Mzansi account does not meet every aspect of the access standards, banks will be able to earn Charter points for Mzansi accounts in 2005. For 2006 and beyond, however, banks will be required to enhance the Mzansi offering by also providing affordable debit-order facilities.

Building on the success of the Mzansi national bank account, the four major banks and the PostBank launched the Mzansi money-transfer facility in September 2005, allowing for a convenient and safe method to transfer money. Customers without a bank account can send and receive up to R5 000 a day, in a secure and reliable way. Customers with bank accounts can transfer money to outlying areas by using the account-to-cash mechanism, and the recipient can collect the money immediately at a participating bank or a post office. In terms of the know-your-customer provisions of the Financial Intelligence Centre Act, 2001, both the sender and recipient will have to produce a bar-coded identity book when transferring or receiving money through the money-transfer facility.

Definitions, measurements and targets

The Charter Council announced in December 2005 that, for the most part, agreement had been reached on definitions, measurements and targets. All financial-sector companies are required to submit reports for the 2005 calendar year to the Charter Council by not later than 31 March 2006.

key elements

The Charter scorecard consists of the following key elements:

- Ownership and control.
- Human-resource development.
- Procurement and enterprise development.
- Empowerment financing.
- Access to financial services and consumer education.
- Corporate social investment.

Codes of Good Practice

The publication of the Codes of Good Practice by the Department of Trade and Industry (DTI) subsequent to publication of the Charter led to the Charter Council announcing that it had formally applied for the conversion of the Charter into a code, under section 9 of the Broad-based Black Economic Empowerment Act, 2003. The Charter may have to be realigned to the DTI Codes in terms of definition and measurement, which may pose far reaching challenges for banks that have already made significant progress in that qualifying criteria may be changed.

BEE in South African banks

In terms of the Charter, South African banks agreed to implement an agreed percentage of BEE shareholding, and all five big banks, as well as African Bank Investments Limited, entered into such transactions. The Bank Supervision Department took cognisance of the essence of these BEE transactions and, in particular, focused on the method whereby the transactions had been financed and whether any default might cause systemic risk.

structured finance and various hedging transactions

The BEE transactions were funded by means of structured finance, the collateral being the banks' shares, and various hedging transactions. The banks acquired the shares applicable to these transactions by either repurchasing their own shares in the market or by issuing shares. All the transactions in question were concluded at controlling-company level, and only the funding had an impact on the banks.

The debt incurred by the BEE participants in the transactions is to be repaid primarily from the share-dividend flow. Of importance in that regard are servicing of the debt and, in the event of default, the implications of the debt structure being unwound. In the view of the Department, it would be easy to mitigate default by a single party by the introduction of another party, and systemic risk is unlikely to arise, for the following reasons:

systemic risk is unlikely to arise

- The banks have recourse to their shares.
- Shares can be sold in the market.
- Shares can be cancelled.
- Various hedging mechanisms are in place.
- Transactions are ring fenced in separate special-purpose vehicles.
- Redemption of debt can be deferred.

Furthermore, the banks are adequately capitalised to absorb any loss that may arise, since their capital-adequacy ratios as at April 2005 were 13 per cent, as opposed to the regulatory requirement of 10 per cent. Default by any party would therefore have only a limited effect on a bank's capital-adequacy ratio.

Application in terms of section 37 of the Banks Act for the acquisition of shares in ABSA Group Limited, a bank controlling company

In 2005, the South African banking industry saw regulatory approval being granted on 9 May 2005 for the acquisition of a majority shareholding in ABSA Group Limited (ABSA), a bank controlling company, by Barclays Bank plc (UK) (Barclays). The transaction resulted not only in the first international ownership of a larger South African bank, but also in the receipt of the largest single foreign direct investment in South Africa to date. The transaction also affirmed South Africa's position as an attractive and stable financial centre.

largest single foreign direct investment

Background

Barclays applied to the Bank Supervision Department for approval in terms of section 37(2)(a)(iii) of the Banks Act, 1990, to acquire more than 49 per cent, but less than 74 per cent, of the issued shares in ABSA.

Approval in terms of section 37 of the Banks Act requires the consent of the Minister of Finance, through the Registrar of Banks. Such consent shall not be granted unless the Minister is satisfied that the proposed acquisition will not be contrary to the public interest, as well as the interests of the depositors, bank and bank controlling company concerned.

Owing to the importance of the transaction to the South African financial system, the Department consulted not only with other affected departments of the South African Reserve Bank, but also with other stakeholders, such as the Financial Services Authority in the United Kingdom, the Competition Commission and the Securities Regulatory Panel of South Africa. The purpose of the consultation process was to gather as much relevant information as possible, in order to enable the Department to give due consideration to the application. A recommendation was then submitted to the Minister, for his consideration, in accordance with the provisions of the Banks Act.

consultation process

Implications for the South African economy

The significant foreign direct investment in South Africa by Barclays confirms South Africa's political, economic and social progress and is evidence of the confidence that major international investors have in the country's regulatory environment.

Implications for the South African banking system

The combination of Barclays's financial strength and international exposure, on the one hand, and ABSA's local-market expertise, brand equity and retail-banking strength, on the other hand, represented a strong strategic fit. It is therefore foreseen that this will deliver significant value to ABSA's customer base.

strong strategic fit

Barclays had also stated its intention to enhance competition by developing access to banking services in South Africa amongst the historically underbanked low-income sector. In addition, Barclays has committed itself to matching or exceeding the broad-based black economic-empowerment (BEE) targets set for ABSA in terms of the Financial Sector Charter. Furthermore, Barclays's majority ownership of ABSA has the potential to strengthen the South African banking system by bringing substantial resources to bear in maintaining ABSA's sound financial position.

International ownership

Globally, the implications of international ownership of large, systemically significant banks have received much attention. It is commonly believed that internationally owned banks can strengthen a country's banking system, provided that a sufficient level of comfort can be provided in terms of supervisory arrangements and national-interest objectives.

Following the opening of South Africa's financial borders in 1994, international participation in the local banking industry increased, from 3 per cent as at the end of December 1994 to 8,2 per cent of total banking-sector assets by the end of December 2004.

Prior to the Barclays application, the South African banking sector included five internationally controlled banks - that is, banks in which international ownership constituted more than 50 per cent of the shares - and 15 local branches of international banks. The balance-sheet size of the five internationally controlled banks (subsidiaries) amounted to R5,9 billion as at the end of April 2005. Currently, after the successful application by Barclays, the South African banking sector includes six internationally controlled banks, the balance sheet of which amounted to R365,3 billion as at the end of December 2005.

six internationally controlled banks

Arguments for and against international ownership of domestic banks

Arguments in favour of opening domestic financial sectors to international ownership are, amongst others, the following:

arguments in favour

- Internationally owned banks provide stability in times of financial crises, since internationally owned banks are geographically more diversified than domestic banks and are therefore less affected by adverse shocks in the domestic economy.
- Internationally owned banks are expected to provide a "safe haven" in a troubled country, thereby potentially reducing the amount of funds flowing offshore.
- Internationally owned banks can provide a new source of funds to recapitalise troubled banks.
- Internationally owned banks may improve the efficiency of the domestic banking system through the transfer of technology and know-how and the exploitation of economies of scale.
- Entry of internationally owned banks may also support the development of financial markets in host countries and may result in increased integration with international capital markets.
- Internationally owned banks may also result in a higher degree of diversification of banking-systems assets and an increased presence of rating agencies and auditors.

- Studies found that the benefits of international entry seem to depend on the level of development of the host country. At least for developing nations, international entrants tend to be more efficient than existing domestic banks, and the increased competition appears to improve overall bank efficiency.
- International bank presence is argued to increase the amount of funding available to domestic projects by facilitating capital inflows.
- International banks are able to improve the quality, pricing and availability of financial services, either directly as providers of such enhanced services, or indirectly through competition.
- International bank presence is argued to improve accounting and transparency.
- An international presence may also enhance the ability of financial institutions to measure and manage risk effectively.

arguments against

Arguments against international bank participation are, amongst others, the following:

- Profits accruing to international owners, which may result in a financial loss to the domestic economy.
- Barriers to domestic bank entry, especially in times of uncertainty in the domestic market.
- Challenges with the regulation of international banks.
- Adverse shocks to international banks hurting the domestic economy.
- Despite a lack of firm empirical support for “cherry picking” by internationally owned banks, possible concerns about international banks serving the most profitable domestic markets or customers and leaving less competitive domestic banks to serve other, riskier customers.
- Uncertainty about internationally owned banks possibly limiting “flight-to-quality” events. Government action can vitiate this benefit, as in Argentina, where internationally owned banks initially received deposit inflows, but then experienced massive withdrawals once depositors became concerned that there might be discrimination against international banks.
- Internationally owned banks decreasing the stability of aggregate domestic bank credit, by providing additional channels for capital flight, or by more rapidly withdrawing from local markets in the face of a crisis (either in the host or the home country).
- Complex banks active in a number of jurisdictions raising multiple challenges to supervision.

Taking these factors and others issues into account, the Bank Supervision Department was of the opinion that the potential benefits of the proposed transaction would outweigh potential risks and disadvantages.

Four-pillar policy

aim of the four-pillar policy

Closely related to the consideration of the Barclays application was the debate on the existing four-pillar policy in the South African banking sector. The four-pillar policy relates to the minimum number of substantial banks - so-called pillars - on which the domestic banking industry relies, and the policy discourages a merger between any of the four large South African banks. The aim of the four-pillar policy is to ensure, amongst other things, effective competition in the interests of prudential and systemic stability. The optimal number of banks to be regarded as pillars within a country, as well as international ownership of any of these pillars, should be determined by an analysis of the circumstances prevailing in the country from time to time. The policy should therefore be subjected to a regular review, in line with market developments.

Provided all qualifying regulatory criteria can be satisfied, the Banks Act does not disqualify international ownership of a bank and/or a bank controlling company. As a result, the acquisition of a majority stake in ABSA, as one of the four pillars, by an international shareholder was not considered to impact negatively on the four-pillar policy in South Africa.

Conditions of approval

The ABSA/Barclays transaction required not only a recommendation by the Registrar of Banks, but also the approval of the Competition Commission and the Minister of Finance. The Competition Commission gave unconditional approval to the transaction, whereas the Minister consented to the transaction subject to a number of conditions. The purpose of imposing these conditions was to ensure ongoing maintenance of the soundness of the South African financial system and prevailing policy objectives. Barclays communicated its unequivocal agreement with these conditions, as well as a commitment to a long-term partnership with ABSA.

The above-mentioned conditions of approval encompass, amongst others, the following:

conditions of approval

- Barclays has confirmed that it supports ABSA's commitment to sound corporate governance and has undertaken to maintain a close ongoing relationship with ABSA's supervisors. The Bank Supervision Department will retain lead regulatory authority in respect of ABSA. Barclays has furthermore furnished the Department with a letter of comfort, committing itself to maintaining the financial soundness of ABSA and explicitly accepting the authority of the Department and the conditions applicable to the transaction.
- Barclays and ABSA have confirmed their commitment to matching or exceeding all appropriate broad-based BEE targets contained in the Financial Sector Charter.
- Barclays shall maintain a South African character in terms of ABSA's management and board composition, in the sense that the Chief Executive Officer of ABSA and the majority of the executive management team of ABSA shall be South African citizens, based locally. ABSA shall remain a South African incorporated company, with its primary listing on the JSE Limited.

Accordingly, after due consideration by the relevant authorities, regulatory approval for the acquisition by Barclays of more than 49 per cent, but less than 74 per cent, of the shares of ABSA was granted by the Minister of Finance in terms of section 37(2)(a)(iii) of the Banks Act.

Way forward

As noted above, the conditions imposed on the ABSA/Barclays acquisition by the Minister of Finance are specific to the transaction. Any future application by an international bank to acquire a majority shareholding in a major domestic bank would be considered on its own merits, taking into account the circumstances prevailing at that time.

any future application would be considered on its own merits

Finally, it is important to recognise that well-capitalised, well-managed and trusted domestic banks can be expected to exert a stabilising influence similar to that of international banks. Healthy banks are therefore essential for financial stability, and whether these banks are internationally or domestically owned is of secondary importance.

Evaluation of progress with South Africa's economic-policy framework

An Article IV consultation undertaken by the International Monetary Fund (IMF), during May 2005, involved an evaluation of progress made with various aspects of South Africa's economic-policy framework. The final report, presented to the Executive Board of the IMF on 2 September 2005, noted that South Africa had made significant progress during the first decade of democratic government. The South African authorities were commended for their continued sound implementation of macroeconomic and financial policies, as well as their increased focus on social spending and on addressing the many challenges facing the country.

significant progress

The IMF Executive Board noted that South Africa's growth performance had improved greatly over the past number of years. Since the growth performance, however, still fell short of addressing the widespread poverty in the country, the South African authorities were urged to continue with the structural reforms necessary to ensure that the country advanced to a higher growth plane. Higher growth in the country's gross domestic product would also be needed to address the high level of unemployment effectively. In that regard, the South African authorities were commended for their efforts to address unemployment through skills enhancement and a public-works programme.

growth performance had improved

The IMF directors welcomed the sound implementation of fiscal and debt-management policies and noted that South Africa had created sufficient leeway to increase expenditures for social and infrastructural purposes. South Africa was also commended for sound monetary-policy implementation, which had resulted in the lowest level of inflation in over three decades.

sound monetary-policy implementation

The IMF Board also welcomed the reassurance given by the South African authorities that a flexible exchange-rate regime would be maintained. In that regard, the Board welcomed the significant increase in the level of reserves during the year, which it regarded as contributing to a reduction in vulnerabilities.

flexible exchange-rate regime

The IMF directors further noted that indicators of the South African banking system's health were favourable and sound. In particular, it was noted that most of the recommendations of the IMF/World Bank Financial Sector Assessment Program, including legislation on anti-money laundering and countering of terrorist financing, had been implemented and that enhancements to the regulatory and supervisory framework would further strengthen the financial sector's resilience to adverse shocks. The South African authorities were encouraged to facilitate access to banking services for the whole population and to speed up implementation of the Financial Sector Charter, as well as the introduction of a regulatory framework for institutions providing basic banking services.

encouraged to facilitate access to banking services

On the social front, the IMF Board highlighted the prevalence of HIV/AIDS and its impact on economic development. The Board, however, noted that the South African authorities had intensified their campaign to reduce the incidence of HIV/AIDS, as well as other communicable and non-communicable diseases, and expressed its support for the South African Governments' efforts to address the problem.

Succession planning for senior executives and training of directors

Over the past decade, the importance of succession planning for senior executives and the training of directors of banks, non-executive directors in particular, have become an issue of great importance. The Bank Supervision Department, therefore, urges banks and their boards of directors to take note of the need for proper succession planning and ongoing director training.

need for proper succession planning

The Myburgh Report on the Standard of Corporate Governance in the Five Largest Banks, issued in 2003, recommended that banks in South Africa establish a directors' affairs committee, consisting of non-executive directors only and with responsibility for corporate governance and succession planning. The Banks Act, 1990, was therefore amended to incorporate such a requirement, and the majority of banks soon established the relevant committee.

Succession planning has consequently become more formalised and has remained on the agendas of banks' directors' affairs committees. Banks, however, have to remain focused on updating the succession plans for all senior executives.

Various articles have been written about the challenges facing bank boards when appropriate skills are scarce and not easily obtainable. Advocate J Myburgh also indicated that, although all the banks reviewed had an induction or orientation programme, they were advised to re-examine those programmes having regard to the banks' size and complexity and to introduce continuing education programmes. The objective of such continuing education programmes is to ensure that non-executive directors are sufficiently knowledgeable to be effective and efficient board members. During meetings held with banks as part of the supervisory process, the Department became aware of the efforts that banks were undertaking in that regard. It should be stressed, however, that directors of banks, especially non-executive directors, have to take responsibility for remaining abreast of developments in their bank as regards risks taken and management of these risks.

continuing education programmes

Banks are not paying sufficient attention to relevant training, as opposed to induction, to equip newly appointed non-executive directors properly to discharge their duties and responsibilities. Likewise in some instances, the Department is concerned about the level of new non-executive directors' commitment to attending board meetings.

The Department wishes to stress that its request for boards of directors to pay increased attention to succession planning and training is directed at the boards of all banks in South Africa, not only the boards of the five largest banks.

Human-resource issues

The objective of the Bank Supervision Department's employment plan is to accord with the aim of promoting equity through diversity, in line with the 2005 human-resource (HR) plan of the South African Reserve Bank. In essence, the main aims of the 2005 HR plan are to promote employment equity in the Bank and to ensure a competent and motivated workforce. The policy, as implemented, includes the accelerated development and promotion of employees with potential from the designated groups, that is, blacks (including Coloured and Asian persons), females and disabled persons.

value system

During 2005, the Department successfully implemented an agreed value system, pertaining to the conduct most appropriate for members of the Department within the business environment in which they operate. The six key areas addressed by the value system are:

- Mutual respect and trust.
- Personal ethics and conduct.
- Work ethics.
- Completed staff work.
- Teamwork.
- Personal growth and empowerment.

A key initiative of the Department in 2005 was to start filling vacancies in accordance with the new structure that had been approved during 2004. Good progress was made in that regard, and some key appointments were made. During the third quarter of 2005, however, the organisational structure had to be reviewed again to enable the Department to implement the new Capital Accord (Basel II) more effectively and efficiently. Once the revised structure had been approved, the Basel II Division was staffed accordingly at the beginning of September 2005.

In view of the uniqueness of some of the positions and the scarcity of resources in the industry, the Department's employment-equity objectives fell slightly below target during the year under review. At the end of 2005, 48 per cent, as opposed to the target of 50 per cent, of the Department's workforce was black, but, in terms of gender, 52 per cent, as opposed to the target of 50 per cent, of the employees were female.

Issues that will receive particular attention during 2006

During 2006, the Bank Supervision Department, besides fulfilling its normal supervisory and regulatory tasks, will place particular focus on the following issues, amongst others:

focal areas

- Further preparations towards implementation of the new Capital Accord (Basel II), including onsite visits to banks to assess their rating methodologies and models, ongoing monitoring of progress with banks' Basel II implementation plans, finalisation of amendments to the regulatory framework necessitated by Basel II and testing of the proposed amendments. Particular focus will also be placed on the training of staff members to enable them to meet the challenges posed by Basel II in their supervisory task.

- Continued review and updating of the regulatory framework and the Department's supervisory process and procedures to ensure that they reflect the latest local and international standards and developments.

- Ongoing engagement with banks to ensure that weaknesses in their corporate-governance processes and structures, including succession planning for senior executives and director training, are addressed.

- Continued participation in the initiatives and activities of international and regional bank-supervisory bodies, such as the Basel Committee on Banking Supervision and the Subcommittee of Bank Supervisors of the Southern African Development Community.

- Ongoing monitoring of banks' compliance with anti-money-laundering legislation.

- Continued combating and investigation of illegal deposit-taking by unregistered institutions and persons, and participation in consumer-education initiatives.

- Monitoring of bank's liquidity-risk management and market-risk modelling.

- Development and implementation of an upgraded database system for the capturing and processing of data submitted to the Department by banks.

Expression of thanks

I wish to extend my appreciation to the Minister and Deputy Minister of Finance for their valued inputs to requests in terms of statutory requirements. Sincere thanks also go to the Governor and Deputy Governors of the South African Reserve Bank – in particular Deputy Governor X P Guma, in his capacity as the Deputy Governor responsible for my Department - for their invaluable cooperation, guidance and support.

Countless individuals and organisations, locally and abroad, also continued to extend their cooperation to the Department. Among them, to name but a few, are the Chief Executive of the Financial Services Board and his staff, the senior executives of banking institutions and their external auditors, the Banking Association South Africa, the auditing profession, the staff of other departments of the South African Reserve Bank (during the year under review, the Financial Markets Department in particular), the Basel Committee on Banking Supervision, and the central bankers and bank supervisors, both in Southern Africa and elsewhere in the world, with whom the Department continues to interact.

My sincere thanks also go to my staff for their continued dedication, enthusiasm and professionalism in not only fulfilling their normal supervisory tasks, but dedicating much time and effort on equipping themselves to meet the challenges of implementing the new Capital Accord.

Errol M Kruger
Registrar of Banks and Executive General Manager: Bank Supervision Department

Chapter 2

Current issues in banking supervision

most important supervisory and regulatory developments

Some of the most important supervisory and regulatory developments during 2005 are addressed in this chapter. Preparations for the implementation of the new Capital Accord became an even more important focus area for the Bank Supervision Department than in previous years. Other issues discussed below include the findings of the Department's review of corporate governance in South African banks other than the big five banks, regional bank-supervisory activities, including training initiatives, monitoring of banks' compliance with anti-money-laundering legislation, issues relating to the establishment of a deposit-insurance scheme in South Africa, management of liquidity risk and market-risk modelling by South African banks, growth in mortgage loans, supervision of representative offices of foreign institutions and the Department's information and communication technology systems.

Progress towards implementation of the new Capital Accord

Good progress was made during 2005 with preparations for the implementation of the new Capital Accord (Basel II) on 1 January 2008.

During November 2005, the Basel Committee on Banking Supervision issued an updated version of the revised capital framework, incorporating the additional guidelines contained in the Committee's paper titled "The application of Basel II to trading activities and the treatment of double default effects". The changes introduced by the revised framework and the aforementioned document also resulted in the "Amendment to the Capital Accord to incorporate markets risks", originally issued in January 1996, being updated.

Basel II Project Team

dedicated project team

During 2005, the Department established a dedicated project team, which includes quantitative analysts and risk specialists, to drive the implementation of Basel II. Each risk specialist has been assigned dedicated responsibility for a specific risk area or aspect of a particular risk area. These responsibilities include, amongst other things, provision of technical guidance on model validation and minimum criteria for the use of more advanced approaches by banks. The risk specialists will also lead onsite visits to banks to assess the quality of banks' risk management and, in the case of banks intending to use an advanced approach, the models, methodologies and related controls used by such banks.

The Department's analysts are kept informed of the Basel II Project Team's work on an ongoing basis and, when possible, the relevant team of analysts accompanies the risk specialists during the above-mentioned visits to banks. In the case of banks that are intending to apply to use an advanced approach for capital-adequacy purposes, the lead analyst of each particular bank has a dedicated primary responsibility for Basel II implementation. This entails, amongst other things, ongoing monitoring of the particular bank's Basel II implementation plans and state of readiness.

ongoing monitoring of Basel II implementation plans and state of readiness

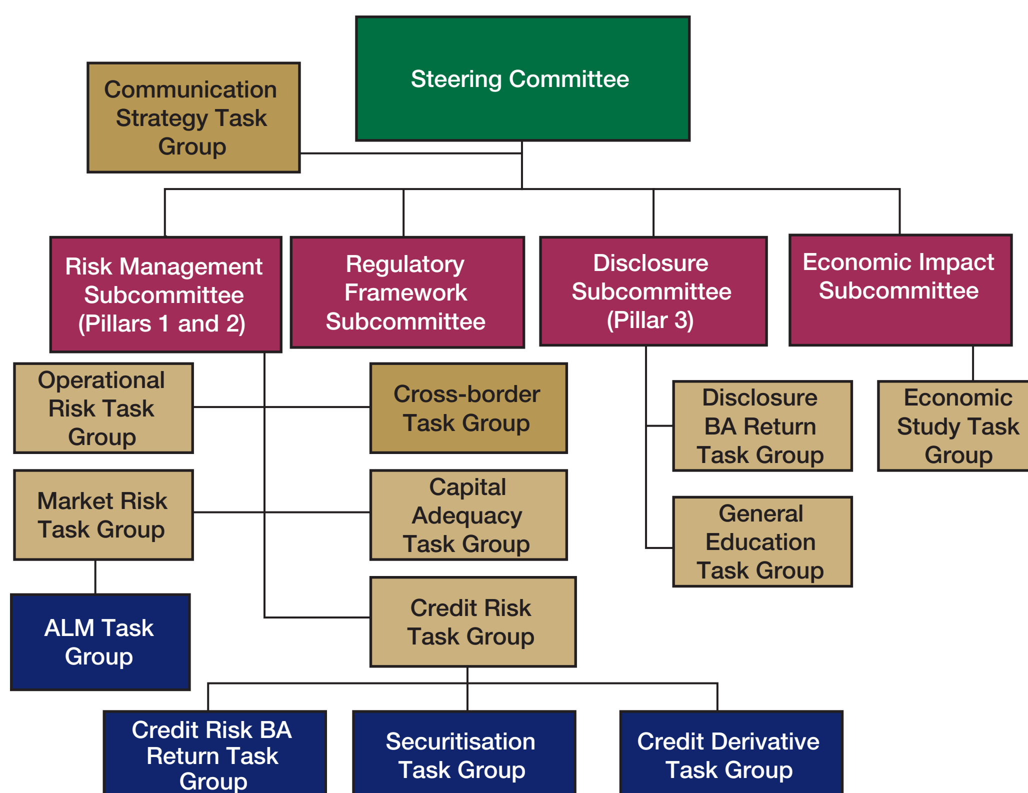
The Basel II Project Team's work will result in, amongst other things, input into an updated supervisory process.

Accord Implementation Forum

The Bank Supervision Department previously reported on the establishment and work of the Accord Implementation Forum (AIF) in pursuit of sound and robust implementation of Basel II and the significant contribution by banks that the structure facilitated. During 2005, the AIF met on a regular basis, and the extensive deliberations resulted in a substantial increase in the number of position papers issued. New task groups were created on an *ad hoc* basis when deemed necessary, and when the work allocated to a task group had been completed, the group was disbanded. The AIF structure is depicted in figure 1 below.

extensive deliberations

Figure 1: Structure of Accord Implementation Forum



Amendment of the South African regulatory framework

The South African regulatory framework has to be amended to provide for the requirements of Basel II. This entails amendments to both the Banks Act, 1990, and the Regulations thereto, discussed in more detail in chapter 3 of this annual report.

– ***Banks Act, 1990***

A first draft of proposed amendments to the Banks Act to enable implementation of Basel II was circulated to the AIF fora during November 2005, after having been approved by the Standing Committee for the Revision of the Banks Act, 1990. Banks were requested to submit their comments to the Bank Supervision Department by mid-January 2006, and a second draft of the proposed amendments was circulated at the end of January 2006. It is envisaged that the proposed Banks Act amendments will be promulgated during 2007.

proposed amendments

– *Regulations relating to Banks*

During May 2005, a first draft of the amendments to the Regulations proposed to cater for the requirements of Basel II, and constituting a complete revision of the Regulations, was issued to the AIF fora. A second draft of the proposed Regulations, which incorporated the extensive comments received from banks and the content of the numerous position papers generated by the AIF fora, was issued to the AIF fora, on a modular basis, from the end of November 2005.

variety of tests

During 2006, the Department will focus largely on finalisation of the regulatory framework. In order to improve the robustness of the proposed new statutory information returns contained in the proposed Regulations, banks will subject the proposed returns to a variety of tests, which should highlight areas in which improvements or further work may be required. This process should also be useful for banks in the specification of the systems and processes that will be required for the production of the proposed statutory information.

Assessment of banks' readiness for Basel II

gap analysis and self-assessment

In order to determine the readiness of all registered banks, branches of foreign banks and mutual banks in South Africa for the implementation of Basel II, they were requested to perform a gap analysis and self-assessment in terms of Banks Act Circular 15/2004, issued in September 2004. Banks were required to submit the results to the Bank Supervision Department, for analysis.

With a view to achieving some comparability between these assessments and to draw conclusions therefrom, all banks were furnished with a standardised set of templates for use in their gap analyses and readiness assessments. An international firm consulting on Basel II made available, free of charge, its internally developed high-level gap-analysis and readiness-assessment templates for this purpose.

Results of banks' self-assessments

identify banks' existing gaps

determine the extent of banks' compliance

The self-assessment by banks consisted of two parts. The purpose of the first part, the gap analysis, was to identify banks' existing gaps in the management and measurement of credit risk, market risk, asset-and-liability management (ALM) risk, operational risk and pillar 2 dimensions. The aim of the second part, the readiness assessment, was to determine the extent of banks' compliance with Basel II requirements.

The gap analysis revealed that smaller banks believed that they had larger gaps in their risk-management and measurement systems than their larger counterparts. For the big five banks, the analysis showed significant gaps in the management and measurement of credit risk, ALM risk and pillar II dimensions. The results of the gap analysis are summarised in figure 2 below.

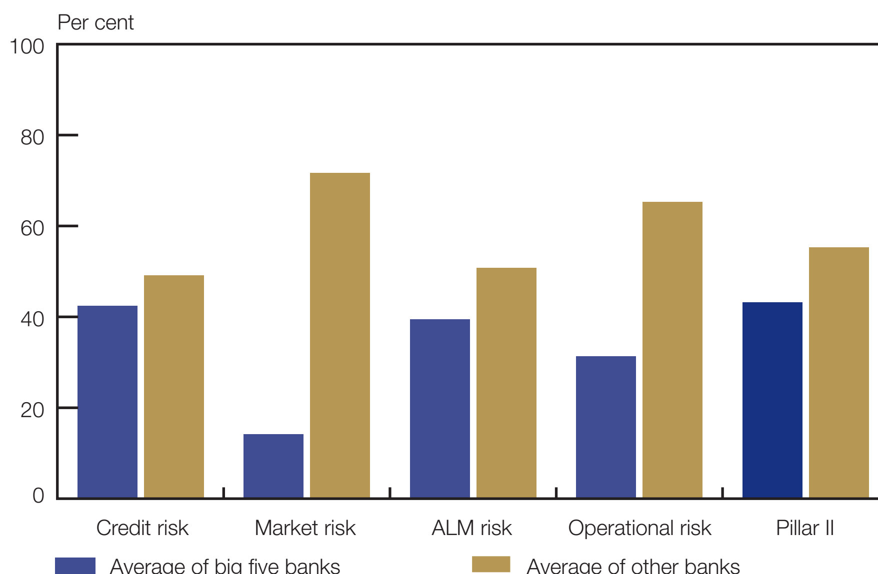
It should be noted that, in figure 2, "Average of big five banks" comprises Absa Bank Limited, The Standard Bank of South Africa Limited, FirstRand Bank Limited, Nedbank Limited and Investec Bank Limited.

The readiness assessment showed that banks still had to do much work in order to achieve full compliance with Basel II requirements. Although the areas of non-compliance with Basel II requirements varied from bank to bank, the following were identified as being common areas of concern:

common areas of concern:

- Basel II education of staff.
- Information technology systems.
- Building of Basel II-compliant models.
- Data management.
- Model validation and calibration.
- Management reporting and disclosure.
- Pillar 2 dimensions.

Figure 2: Summary of results of gap analysis



considerable progress

Since the performance of the self-assessments in 2004, considerable progress has been made on most fronts, as evidenced by the involvement of banks in the AIF fora and the output of the AIF fora.

Quantitative Impact Study 4

possible impact on the level of capital

In Banks Act Circular 2/2005, released early in January 2005, banks were requested to complete Quantitative Impact Study 4 (QIS 4). The aim of QIS 4 was to assess the possible impact of the implementation of Basel II on the level of capital in the banking industry.

The results of QIS 4 raised concerns about the quality of data, the dispersion of results and certain international issues. Accordingly, QIS 4 highlighted areas on which additional guidance is required to ensure consistent application of the Basel II framework by South African banks.

level of capital would not differ significantly

composition of the capital requirements would change

The QIS 4 results indicated that the level of capital that the banking industry would be required to hold in terms of Basel II would not differ significantly from the level that the banking industry was currently required to hold. In this regard, however, the benign economic conditions of the recent past have to be borne in mind. The QIS4 results further indicated that the composition of the capital requirements would change, owing to the introduction of a new capital charge for operational risk and a decrease in the credit-risk capital requirement.

The QIS 4 results were based on models in use at the time of the study. Since these models are expected to evolve over time, future results may differ from the QIS 4 results.

Consolidated supervision under Basel II

applied on a consolidated basis

Basel II will be applied on a consolidated basis to internationally active banks, in order to capture the risks faced by an entire banking group. In practice, supervisors have to perform supervision at every tier within a banking group, starting with the banking entity and progressing to the holding company of the particular banking group, including banking operations in all jurisdictions in which the group is active.

various items of national discretion

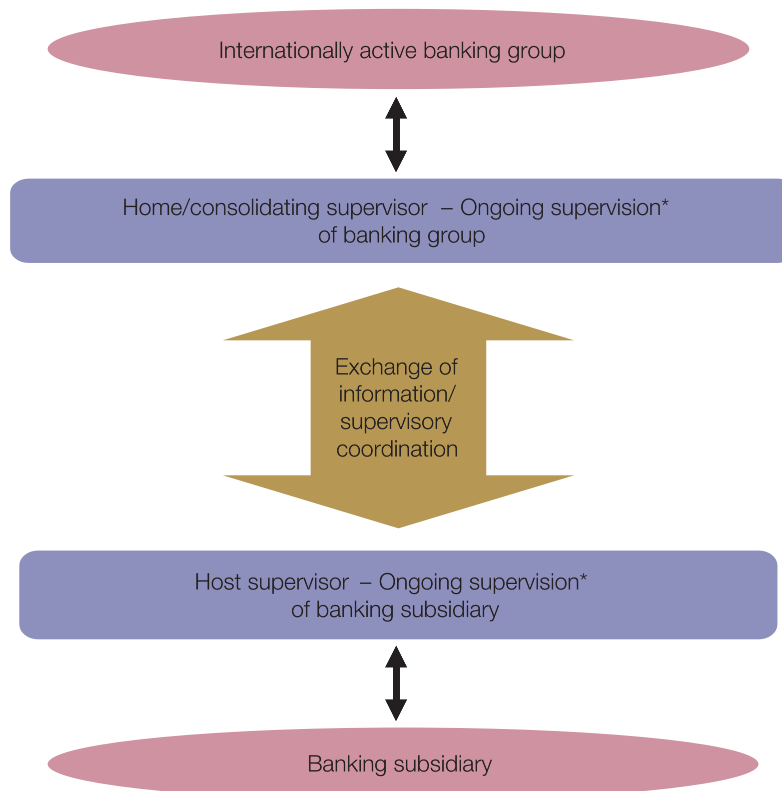
Basel II provides a menu of options for banks and makes provision for various items of national discretion. Furthermore, different jurisdictions are following timetables suited to their local conditions. It is widely recognised that this type of customisation between different jurisdictions may result in inconsistencies in the implementation of Basel II. The onus is on international regulators to coordinate their supervisory efforts, specifically when they have to supervise internationally active banks that operate in a number of jurisdictions, so as to promote the principles underpinning Basel II.

responsibilities of the consolidating supervisor

The responsibilities of the consolidating supervisor will encompass the supervision of the group-wide functions and the overall solvency of a consolidated group. Supervisory powers thus rest substantially with the authorities that license individual institutions, and consolidating supervisors will have to rely on their host peers for effective intervention at the level of a banking subsidiary, in many areas.

This may be illustrated as set out in figure 3.

Figure 3: Consolidated supervision



* Ongoing supervision may include risk identification, risk assessment, supervisory action and evaluation.

Practical concerns include:

- The need for increased supervisory transparency.
- Convergence of supervisory practices around common principles.
- Effective home/host coordination in respect of qualification and model validation.
- Avoidance of duplication of efforts or increasing regulatory burdens.
- Fostering commonality of pillar 2 approaches.

Internationally, consolidated supervision remains an area of ongoing research and debate. The Bank Supervision Department will continue to liaise with its international counterparts to assist internationally active banks in its jurisdiction.

Supervisory challenge

Migration from the existing Capital Accord to Basel II has necessitated significant amendments and refinements to the legal framework and supervisory review process followed by the Department. A major challenge will be to balance the supervisory requirements with the available resources.

challenge to balance the supervisory requirements with the available resources

The progress made thus far with the process of planning for and gearing up to the implementation of Basel II has benefited greatly from the active and enthusiastic involvement of the banking sector in the AIF fora. Personnel from the Banking Association South Africa who are dedicated to the Basel II planning and implementation process also continue to play a most valuable and an indispensable role.

efficient, effective and robust process

The combined efforts of all participants have contributed to an efficient, effective and robust process, from which the banking sector and the country as a whole is bound to benefit. This is in line with the Basel Committee on Banking Supervision's objective to strengthen the soundness and stability of the international banking system, whilst maintaining sufficient consistency to promote level playing-fields among banking institutions.

The Bank Supervision Department is of the view that Basel II is an interim point in striving towards the attainment of best practice.

Review of corporate governance in South African banks

review of 14 South African banks

In the second half of 2004, a four-person team of the Bank Supervision Department commenced with a corporate-governance review of 14 South African banks, including two mutual banks, but excluding the five big banks, which had been reviewed in 2003. The purpose was to assess these banks' compliance with sound corporate-governance practices, as laid down in the Banks Act, 1990, the Mutual Banks Act, 1993, the Regulations to these Acts, the recommendations of the Myburgh Report on the Standard of Corporate Governance in the Five Largest Banks and of the second King Committee on Corporate Governance. As in the case of the review of the five big banks undertaken by the Myburgh Working Group in 2003, the particular objective of the second review was to establish to which extent an adequate and effective process of corporate governance had been established and maintained within each bank and banking group, where applicable, and the extent to which the overall effectiveness of the process could be improved and enhanced.

objective of the second review

Scope of the review

adequacy of the following areas

The scope of the review, which was similar to that of the Myburgh Working Group's review, was to establish, describe and express an opinion on the adequacy of the following areas in the 14 banks reviewed:

- Structure, composition, role and functions of the board of directors.
- Role and functions of the:
  - Risk-management committee.
  - Audit committee.
  - Remuneration committee.
  - Directors' affairs committee.
  - Chief executive officer.
  - External auditors.
- Status, role and scope of the:
  - Risk function.
  - Internal audit function.
  - Compliance function.
  - Company-secretariat function.
- Director selection, career pathing and development.
- Independence of directors.
- Leadership.
- Management-accountability structure.
- Systems of control.
- Decision-making process and decision-making capability of the board.
- Reports from management to the board.
- Board monitoring of management activities reported to the board.
- Disclosure to stakeholders.
- Related-party lending, conflicts of interest and related matters.

Review process

The review process was very similar to that followed by the Myburgh Working Group and included the following:

analysis of various documents

- Analysis of various documents, including minutes of meetings of the following bodies:
  - Board of directors.
  - Audit committee.
  - Risk committee.
  - Remuneration committee.
  - Directors' affairs committee.

interviews

- Interviews, 191 in total, with the following:
  - All directors of the banks under review.
  - Heads of the following functions:
    - Risk management.
    - Compliance.
    - Internal audit.
    - Company secretariat.
    - External auditors of the banks under review.

consolidation of the information

- Consolidation of the information received and report writing.

The review was concluded by the release of a report titled "General report on the standard of corporate governance in South African registered banks and mutual banks (excluding the five major banking institutions and foreign branches)" on 1 September 2005. The report was distributed to all banking institutions under cover of Banks Act Circular 5/2005 of 7 September 2005.

General findings

The following general findings arose from the review:

general findings

- The banks reviewed were committed to adherence to and application of high standards of corporate governance.
- The banks' senior management and boards of directors were inclined to take seriously their responsibilities for ensuring effective corporate governance.
- The banks from time to time, at their own initiative, reviewed their corporate governance to ensure compliance with accepted corporate-governance principles.
- In general, the banks' corporate governance was sound.
- The banks reviewed were mindful of the need to improve continuously, especially in the light of ever evolving governance standards in South Africa and internationally.

Areas of concern

Certain areas of concern, however, were highlighted in the general report, as follows:

areas of concern

- ***Compliance function***

  allocation of resources

  It was found that the allocation of resources to the compliance function was a general problem, but that compliance officers had little choice but to accept that other departments, such as the internal audit department, enjoyed priority. Their limited resources resulted in compliance officers not being able to monitor effectively and test continuously the banks' compliance with legislation, including regulations, and supervisory requirements.

  In most of the banks reviewed, the compliance function was staffed by one person, even in banks with branches throughout the country. Consequently, the compliance officers often made an arrangement with the internal audit department to monitor and test compliance in branches.

  Tasks performed by the compliance officers were of limited duration, once off and, in some cases, periodic. The tasks included monitoring and testing for compliance in the bank's head office, drafting or updating compliance manuals, preparing reports for the attention of the audit and risk committees, assisting in raising awareness of compliance and inculcating a compliance culture within the banks. The compliance reports tabled at board meetings rarely elicited any response, discussion or action and, in general, were only noted.

  limited activity

  This limited activity, in turn, resulted in most compliance officers performing other, non-compliance functions – such as those of company secretary, finance director, risk manager, or head of the legal division - on a day-to-day basis, contrary to best practice. None of the compliance officers, however, performed revenue-generating functions, such as marketing or dealing. The compliance officers had generally become jacks/jills of all trades, resulting in the banks placing great reliance on these individuals and raising concerns about succession, there being little or no evidence of any transfer of skills taking place.

In some banks, compliance officers were distributed among the business units of the bank and reported to the heads of the business units. The problem is that, in such cases, compliance officers' independence is compromised, and they risk falling foul of the business-unit head manager should that person not be satisfied with what is reported about his or her unit.

compliance champion

In some of the banks in which the compliance function was staffed by one person, each business unit had a so-called compliance champion. The problem is that such a champion is usually the head of a business unit or a lower official. The champions, therefore, tend to be more occupied with business issues and operational duties than with the duty to monitor and test compliance with legislation and supervisory requirements.

– ***Director selection***

process tended to be informal

It was found that the director-selection process in the banks reviewed tended to be informal. Recruitment was based largely on personal contacts, friendships or industry referrals, and little or no use was made of independent recruitment agencies or advertisements for director positions. It was also found that, in some banks, there was no succession planning for non-executive directors to address replacement of outgoing directors. Generally, once a prospective director had been identified and had agreed to accept the position, appointment of the person was a *fait accompli*, resulting in the nomination committee being a mere rubber stamp.

It was found that the boards did not have any influence in the appointment of directors nominated by a shareholder of note. Such appointments were made at the discretion of the shareholder and usually disregarded whether the skills introduced were relevant or added value. It was also found that consideration was not given to the fitness and propriety of the shareholder company, as opposed to an individual director.

– ***Training***

banks did not have induction programmes

It was found that the banks did not have induction programmes for directors in place. Some banks, however, were addressing this deficiency at the time of the review.

some directors were not aware of critical regulatory requirements

It was also found that some directors were not aware of critical regulatory requirements that impacted on their banks. Board members generally did not inform themselves about the company or the legislation governing banks. In this regard, it should be noted that the effectiveness of directors is dependent less on their existing capability and more on their willingness to expand and update their knowledge and skills. Boards also tended to lack the courage to deal effectively with poorly performing members and did not develop or implement an exit strategy when necessary.

– ***Board monitoring of management and unresolved issues***

recurring matters

It was found, albeit in a few instances, that matters recurred at successive board meetings, without final resolution being reached. Common recurring matters included governance matters (such as an auditing firm providing both external and internal audit services to a bank, or a bank not having an in-house compliance function, but outsourcing it), strategic matters (such as a board's inability to reach finality on issues such as expanding the bank's branch network or introducing new products) and weak systems (such as unresolved internal control issues or unreconciled accounts). Recurring unresolved issues can undermine the effectiveness of a bank's corporate-governance framework and signify a weakness in a board's oversight and decision-making process.

– ***Transformation within boards***
  Issues relating to transformation within boards included demographic imbalances in terms of race and gender representation (given the weight that the banking sector places on the Financial Sector Charter) and the undesirability of any one individual being a member of all three principal committees, which might result in too much influence being concentrated in one individual.

demographic imbalances

– ***Effectiveness of directors' affairs committees***
  It was found that, in most of the banks reviewed, a director's affairs committee, which was introduced into legislation in 2003, had only recently been established. Therefore, the review team was unable to make a finding on the effectiveness of these committees.

unable to make a finding

– ***Segregation of duties***
  It was found that the extent to which a bank successfully managed segregation of duties depended on the size of its book. For example, when the credit book was still small in size, one person would handle all responsibilities pertaining to the book. As the book grew in size, however, the banks gradually introduced additional control measures, such as new staff to reduce overlaps or handle different functions.

segregation of duties depended on the size of book

The Department, as part of its ongoing supervision of the banking sector's commitment to sound corporate governance, will engage with the banks reviewed, in order to ensure that weaknesses identified in the review are addressed.

Interaction with other supervisors

As in the past, the Bank Supervision Department continued to interact with other supervisors, both locally and abroad, in fulfilling its regulatory and supervisory responsibilities. In view of the importance of the Basel Committee on Banking Supervision in the supervisory arena, coupled with the impending implementation of the new Capital Accord, interaction with the Basel Committee continued to be of particular importance.

Bank-supervisory activities at regional level

The Bank Supervision Department continued to participate in the activities of the SADC (Southern African Development Community) Subcommittee of Bank Supervisors (SSBS). The SSBS is the forum for bringing together the views of regional bank-supervisory bodies, the objective being to promote the overall standard of bank supervision in SADC member countries, in line with best international practice. The SSBS - through its Steering Committee, established to run day-to-day activities - actively promotes the harmonisation of bank-supervisory philosophies and practices in the SADC region.

SADC Subcommittee of Bank Supervisors

The objectives of the SSBS include:

objectives of the SSBS

- Enhancement of bank supervision, through adherence to and promotion of international supervisory standards.
- Harmonisation of banking legislation and supervisory systems and practices.
- Implementation of the Basel Core Principles for Effective Banking Supervision.
- Anti-money-laundering compliance and combating of terrorist financing.
- Formulation of training programmes in conjunction with regional and international bodies.

Projects of the SSBS Steering Committee

Projects of the SSBS Steering Committee include:

- Compliance with the Basel Core Principles.
- Financial-soundness indicators.
- Report on aggregated financial information.
- Bank-supervision information-technology application project.

During 2005, members of the Department attended two meetings of the SSBS Steering Committee to finalise a memorandum of understanding.

Courses in bank supervision

two regionally focused seminars

The Financial Stability Institute of the Bank for International Settlements presented two regionally focused seminars during 2005. The first seminar, which covered credit-risk management and the measurement of capital requirements for credit risk in the new Capital Accord (Basel II), was held at Victoria Falls, Zimbabwe, and was attended by 46 participants from 17 countries. The second seminar, which covered problem-bank resolution, was held in Maputo, Mozambique, and was attended by 34 participants from 11 countries. Both seminars were attended by staff members of the Bank Supervision Department.

objectives of the seminars

The objectives of the seminars were to:

- Provide an overview of the latest developments with Basel II.
- Update participants on current best practices in risk management and problem-bank resolution.
- Provide a forum for the exchange of ideas on common problems and the implementation of best supervisory practices, such as improving corporate governance in banks.
- Provide the Financial Stability Institute with useful information on the most important needs in the SADC region.

The Bank Supervision Department successfully hosted an intermediate course in banking supervision, attended by 25 participants from 10 SADC member countries.

Training of staff

objective

To ensure that the skills base of the Bank Supervision Department is constantly improved, considerable resources are allocated to training. The objective is to enable staff to:

- Implement sound global supervisory standards and practices.
- Share supervisory practices and experiences.
- Promote cross-sectoral and cross-border supervisory contacts and co-operation.

During 2005, staff members of the Department attended seminars and courses on banking supervision and financial topics not only in South Africa, but also in Austria, Hungary, Lesotho, Malaysia, Mozambique, Switzerland, the United Kingdom, the United States of America and Zimbabwe.

In order to overcome the Basel II skills shortage, the Department has subscribed to FSI Connect, a web-based information resource and learning tool for bank supervisors

worldwide, developed by the Financial Stability Institute. FSI Connect offers a comprehensive set of online tutorials directly related to banking and bank supervision. The tutorials reflect the most up-to-date information and cover capital adequacy and important risk-management topics, such as credit-risk, market-risk and operational-risk management.

FSI Connect

Alignment of South African Accounting Statements with International Financial Reporting Standards

For financial years commencing on or after 1 January 2005, listed banks have to prepare their consolidated financial statements in accordance with International Financial Reporting Standards (IFRS), which also includes International Accounting Standards. These financial statements also have to include comparative figures for 2004 prepared on an IFRS basis. Therefore, companies with a December year-end have an IFRS transition date of 1 January 2004 assuming the companies have only one year of comparative figures. The comparative figures are likely to differ from those published previously.

Since all European listed companies are required to prepare financial statements in terms of IFRS for years ending on or after 31 December 2005, the International Accounting Standards Board (IASB) revised many of its standards and interpretations and also issued a number of new standards. Although conversion to IFRS is compulsory for the consolidated financial statements of listed South African banks, the statements of other banks may continue to be prepared in accordance with South African Statements of Generally Accepted Accounting Practice (SA GAAP). As part of the process of bringing SA GAAP in line with IFRS, however, the Accounting Practices Board, which issues accounting standards in South Africa, has reissued all SA GAAP statements and interpretations when there were differences between these standards and those issued by the IASB. Consequently, all differences in wording between the affected statements and interpretations were removed, except when effective dates differed.

conversion to IFRS

The IFRS transition process is both complex and time consuming. The process, therefore, places significant demands on banks in areas such as staff training, data collection, and new or modified information system requirements. In order to compile the transition-date balance sheet to take into account both the optional and mandatory conversion exceptions of IFRS 1, companies have to make judgments and decisions about which options to apply in their first set of IFRS financial statements. IFRS 1 allows or requires companies to use options that might not be possible to use if companies continue to apply SA GAAP. Adaptations to existing accounting systems are required in order to produce and report financial information in terms of IFRS.

transition process is complex and time consuming

In South Africa, companies that continue to use SA GAAP and those that have changed to IFRS are required to apply the new and revised standards and interpretations. Most of the changes will affect years ending on or after 31 December 2005 year-ends. Because of the effect of different effective dates and the application of IFRS 1, the results of a bank that continues to apply SA GAAP are likely to differ from the results that would be obtained if the bank were to change to IFRS.

All listed banks in South Africa have spent a substantial amount of time and effort on ensuring that their figures accord with IFRS and have reported on the effect of conversion from “old” GAAP on their opening balance sheet.

Monitoring of banks' compliance with anti-money-laundering legislation

In June 2003, South Africa was admitted as a member of the Financial Action Task Force (FATF), established by the Group-of-seven summit in June 1989 to examine measures to combat money laundering, and retention of South Africa's membership will probably be assessed in the latter part of 2007. In terms of the FATF 40+9 Recommendations, countries are required to ensure that financial institutions in their jurisdictions are subject to adequate regulation and supervision and are effectively implementing the FATF Recommendations. Compliance with the FATF Recommendations on an ongoing basis is essential in order for a country to retain its FATF membership.

review of banks' compliance

In an attempt to ensure not only that banks complied with the FATF 40+9 Recommendations, but also that South Africa would retain its FATF membership, the Registrar of Banks instituted a review, in terms of section 7 of the Banks Act, of banks' compliance with section 21 of the Financial Intelligence Centre Act, 2001 (FICA), and the related exemptions, as outlined below.

The Bank Supervision Department also held a meeting with all banks during the earlier part of 2005 in order to obtain an update on their progress with the further implementation of know-your-client (KYC) procedures and the verification of clients. In particular, the banks gave feedback on their ability to comply with the 31 May 2005 deadline of the conditions of exemption from the provisions of section 21(2) of FICA, in terms of which the identity of 50 per cent of medium-risk clients had to be verified by 31 May 2005. All high-risk clients had to have been verified by 31 December 2004.

Review of the big banks in terms of section 7 of the Banks Act, 1990

auditors' terms of reference

The Registrar requested the five big banks to appoint an independent auditing firm to undertake physical verification of the client-verification data that the banks had submitted in terms of Banks Act Circular 10/2004. The auditors' terms of reference were to evaluate the banks' level of compliance with the requirements of the aforementioned circular. The Registrar wished to give the Director: Financial Intelligence Centre, Mr Murray Michell, and, thereafter, the Minister of Finance comfort from an external source that all data that had been submitted to the Bank Supervision Department in fulfilment of the requirements of Banks Act Circular 10/2004 were reliable.

In order to ensure a uniform view, a single firm of auditors was engaged in January 2005. The auditors had to evaluate and express an opinion on the banks' board-approved internal KYC policies and procedures. The auditors also had to evaluate and express an opinion on the capabilities of the banks' information systems to generate exception reports automatically, so as to identify non-cooperating client accounts and unauthorised unfreezing of accounts.

Upon conclusion of the review, the Department drew up a matrix of issues that were of concern to all five big banks. Many of the issues in the auditors' report were unresolved issues that had previously been referred to the Money Laundering Advisory Council.

Guidance provided by the Financial Intelligence Centre

Following the above-mentioned review, the Financial Intelligence Centre (FIC) provided guidance on a number of matters relating to compliance with the requirements of FICA.

Guidance Note 3 for banks on customer identification and verification and related matters was published on 18 July 2005, in *Government Gazette* No. 27803.

Supervisory process

The Department continued to supervise banks' compliance with the deadlines stipulated in the exemption from section 21(2) of FICA. Since the Department had observed that banks had encountered major difficulties in the re-identification of high-risk clients, as defined in the risk categories that banks had put in place, regular meetings were held with the FIC. There was also a concern that the number of clients in the high-risk categories would be far smaller than the number of clients in the medium-risk category.

In October 2005, a different firm of auditors was engaged to verify the big five banks' compliance with the next deadline of 30 September 2005, by which all medium-risk clients had to be re-identified. The specific terms of reference of the auditing firm were an expansion of the previous firm's terms of reference, and the improvement in findings was substantial. The Department is of the opinion that banks have made good progress with the implementation of anti-money-laundering measures and will continue to monitor and supervise banks' progress in this regard.

banks have made good progress

Combating of illegal deposit-taking

The Bank Supervision Department is responsible for the administration of the Banks Act, 1990, in terms of which the Registrar of Banks is tasked with, amongst other things, controlling certain activities of unregistered persons. During the year under review, the Department received a number of complaints, with supporting documentary evidence, about certain business activities of a number of institutions, which appeared to have accepted deposits from the general public as a regular feature of their business.

controlling certain activities of unregistered persons

The acceptance of deposits from members of the public as a regular feature of business is tantamount to conducting "the business of the bank", as defined in section 1 of the Banks Act. In terms of the Banks Act, it is an offence for any person to conduct the business of a bank unless such a person is a public company and is registered as a bank in terms of the Banks Act.

acceptance of deposits

Since the institutions in question were not registered as banks or mutual banks in terms of the Banks Act or Mutual Banks Act, 1993, respectively, they were in contravention of section 11 of the Banks Act. Forensic auditors from a number of auditing firms were appointed as temporary inspectors to investigate the institutions in question and to determine whether their activities were in contravention of the Banks Act. During 2005, three new inspections, together with 30 inspections carried over from the previous year, were undertaken. The inspection of 33 schemes has been delegated to eight forensic auditing firms.

When inspectors conclude that the activities of institutions are in contravention of the Banks Act, they are appointed as fund managers in terms of the Act. The purpose of such an appointment is to take control of the funds that were illegally solicited and taken and to liquidate the assets acquired by such an institution, in order to repay the investors in such an institution all or part of their funds.

fund managers

Sometimes, however, the Department is unable to appoint inspectors or funds managers, because an institution is liquidated before such an appointment has been made, whereas liquidators have already been appointed to deal with the estate of the

institution is liquidated

institution in terms of the Insolvency Act, 1936. Since the Insolvency Act, takes precedence over the Banks Act in such an instance, the fund managers are unable legally to conclude their mandate, and the involvement of the Department in the matter is thereby ended.

The activities of such unregistered persons are not only illegal, but in direct competition with the legitimate business of registered banks. In some cases, funds are illegally transferred off-shore in contravention of Exchange Control Regulations, 1961. Tax evasion by the operators of illegal deposit-taking schemes is also common. Such schemes are thus detrimental not only to the banking system, but also to the stability of the financial system and the economy in general. In order to ensure that all possible contraventions that may have been committed by the operators of illegal schemes are bought to book, the Department, therefore, forwards information on such schemes to other regulatory bodies and prosecuting authorities.

two types of investor

In the experience of the Department, illegal deposit-taking schemes generally attract two types of investor - less sophisticated persons and those who are driven by greed. The Department is therefore developing a policy on creating greater public awareness of illegal schemes. The aim is to reduce the level of unawareness amongst the most vulnerable segment of the population, including pensioners, people benefiting from hard-earned stokvel payouts and beneficiaries of death benefits, etc.

Deposit insurance in South Africa

South Africa does not have an explicit deposit-insurance scheme (DIS). Therefore, depositors with banks are currently dependent on the implied assurances in this regard provided by the policies and procedures of Government and the South African Reserve Bank, as the country's central bank.

South African DIS

During 2000, the Minister of Finance came to the conclusion that there was a need to establish a DIS in South Africa. The Minister requested the Bank Supervision Department to participate in a joint project with the National Treasury to investigate the requirements necessary to implement a South African DIS (SADIS). A work group, consisting of members of the National Treasury, the Department, the Banking Association South Africa and others, was established in order to research the issues and to make proposals on the establishment of SADIS.

The Work Group held numerous meetings and developed a number of discussion and position papers over the years. The Work Group has done comprehensive research on DISs in other jurisdictions and has come to the conclusion that each DIS was designed and implemented according to the specific needs and requirements of the particular jurisdiction. SADIS, therefore, is being developed to serve the purposes and interests of South Africa, as well as to incorporate the international best-practice principles and procedures available in order to attain that goal.

final proposal has not yet been submitted

Since a number of issues have remained unresolved, a final proposal has not yet been submitted to the Minister, for approval. The number of outstanding issues, as discussed later in this section, seems to be decreasing, however, and the Department is of the opinion that it should be possible to finalise a proposal, for submission to the Minister, during 2006.

Nature of a DIS

A central bank does not have a duty to compensate depositors of a bank that has failed. Even in the case of depositors with registered banks that are subject to the regulation

and supervision of the central bank, there is no general obligation to compensate stricken depositors. The provision of financial support to institutions in financial distress by the central bank is a matter of policy and should be aimed at preserving the stability of the banking system in general. In order to facilitate this role, however, attention has for some time been focused on the possibility of introducing some scheme whereby bank deposits are insured.

a DIS protects insured depositors

It is generally accepted that a DIS protects insured depositors against the consequences associated with the failure of a bank. A DIS, however, is not necessarily designed to protect banks from failing, or to address systemic banking crises.

public-policy objectives

Countries use a variety of public-policy objectives for their DISs. These may be classified into three broad categories:

- Contribution to financial system stability.
- Protection of less financially sophisticated depositors.
- Other public-policy objectives.

adverse effects

The introduction of a DIS, however, might have the following adverse effects:

- A DIS might promote moral hazard by encouraging banks to take more risk.
- Full depositor protection might make it difficult for supervisors to close banks, since it would be too costly to do so. This could result in a tendency to show forbearance, which, in turn, might lead to an increase in risk-taking by banks.
- Since depositors would have less incentive to discriminate between banks on the grounds of risk, competition between banks might be distorted, and the level of systemic risk might increase.
- Prudent banks may also argue that they are subsidising riskier banks.

possible advantages

In contrast, possible advantages of a well-designed DIS are that it may:

- Serve to protect the small and unsophisticated depositor.
- Contribute to financial stability.
- Reduce competitive inequalities between banks; without a DIS, banks that are regarded as being "too big to fail" would be favoured.
- Enable policy-makers to lower the entry barriers for special classes of deposit-taker and thereby, possibly, facilitate broader access to finance.
- Assist in inculcating a culture of savings through increased trust and confidence in the banking system in general.

Issues requiring resolution

issues still to be resolved

The issues still to be resolved by the Work Group are the following:

- ***Legal nature of SADIS***

insurance fund

If SADIS is to be an insurance fund in the true sense, the principles of insurance will dictate the nature of the fund. This means that there will have to be a specified transfer of risk from a member to the fund, that the concomitant premium paid by the member will have to reflect the individualised risk so transferred and that the fund will pay out only in the event of a specified insured event occurring.

aid fund

If SADIS is to be a protection/depositor-aid fund, the principles of an aid fund will dictate the nature of the fund. This means that the members will contribute an equal share to the expenses of the fund and that the fund will pay out only when specified events occur, or when an application for aid is received and approved.

resolution fund

If SADIS is to be a resolution fund, the principles of a resolution fund will dictate the nature of the fund. This means that the members will contribute a formula-based share, probably based on asset size or market-share size, to the fund and that the fund will be used mainly to resolve a liquidity or solvency crisis in a bank.

A combination of the principles listed above could also be applied.

– ***Functions, roles and responsibilities of SADIS***
  The legal nature of SADIS will dictate not only the above-mentioned differences in legal requirements, but also, amongst other things, SADIS's structure, processes and procedures, information requirements, powers and duties, agreements to be concluded and the skills and resources needed to operate the scheme.

  It will also be necessary to determine who would operate and manage the scheme. The various functions, roles and responsibilities of Government, the central bank and the banking supervisor will have to be determined and defined clearly, even if SADIS is to be operated by the private sector.

who would operate and manage

- ***Funding of SADIS***
  It will be necessary to determine how SADIS is to be funded, and which contributions, if any, will come from depositors themselves.

- ***Basis of participation in and membership of SADIS***
  It will be necessary to determine whether all banks will be required to participate in SADIS, or whether banks will have an option not to participate, and whether all bank deposits, or only a certain proportion or a certain category, will be covered by the scheme. An issue pertaining to membership is whether the scheme will include the envisaged dedicated and co-operative banks.

- ***Governance of SADIS***
  Appropriate structures and personnel to manage the scheme will have to be determined, implemented and appointed.

- ***Funding model***
  Issues pertaining to the funding model of the scheme include the possibility of requiring differential premiums and how foreign deposits are to be treated.

- ***Fund management***
  Issues pertaining to fund management include whether the scheme will offer line credit or a guarantee to its members and issues relating to the maintenance of adequate liquidity levels by the scheme.

- ***Reimbursement of depositors***
  Issues pertaining to the reimbursement of depositors include determination of the category of depositor that is to be reimbursed, as well as the coverage limit of such reimbursement.

- ***Failure resolution, claims and recoveries***
  Issues pertaining to failure resolution, claims and recoveries include whether SADIS should be afforded the legal power to facilitate bank resolutions and in which instances such resolutions would be appropriate. The Bank Supervision Department is not in favour of SADIS being afforded powers to resolve a crisis in a bank. Not only could such powers be in conflict with the powers afforded the Department in this regard, but they could also have an adverse impact on systemic risk.

Although the Work Group has reached consensus in principle on most of the issues listed above, the details have to be refined and finalised before a proposal is submitted to the Minister of Finance and before the proposal can be drafted into appropriate legislation.

Liquidity-risk and market-risk management

During 2005, the Bank Supervision Department undertook targeted reviews of some banks' management of liquidity risk and placed focus on the modelling of market risk by South African trading banks.

Management of liquidity risk

The objective of the management of liquidity risk is to ensure that a bank has sufficient funds on hand to meet its obligations.

As part of its ongoing supervisory review process, the Bank Supervision Department undertook targeted reviews of the management of liquidity during the year under review. The scope of the reviews covered the roles and responsibilities of the board of directors and senior management, asset-and-liability risk management, information systems and the quality of statutory reporting.

targeted reviews

It was found that, generally, liquidity strategies, policies and procedures, standards and limits were in place. Asset-and-liability committees convened on a monthly basis for an in-depth consideration of liquidity and balance-sheet management. Stress testing of assumptions, the techniques varying from rudimentary ones to more advanced risk measurement, were undertaken. The liquidity-risk contingency plans for handling a liquidity crisis ranged from basic event-risk management to more sophisticated contingency planning.

Weaknesses or concerns that the Department identified during the targeted reviews were communicated to the banks concerned. The Department is monitoring progress with the reviewed banks' action plans to rectify deficiencies on an ongoing basis.

Market-risk modelling

Market risk encapsulates the risks to which banks are exposed as a result of volatility in the market prices of their assets. The assets of banks that are subject to market risk include interest-rate related instruments, equities in the trading book, foreign exchange and commodities booked throughout the bank.

The Regulations relating to Capital Adequacy Requirements ("CAR") for Banks' Trading Activities in Financial Instruments require banks to report their market-risk exposure and to determine their capital adequacy using one of a number of methods, which vary in complexity. The simplified method is suited to banks with "vanilla-type" trading books and few systems supporting their trades. The building-block method is more suited to banks with significant exposures and which manage their risk internally with relatively manual processes and systems. The internal model (IM) approach permits banks that are using sophisticated risk-management systems not only to manage their risk and report their exposure, but to calculate their capital adequacy.

a number of methods

internal model (IM) approach

Before a bank may report in terms of the IM approach, the bank has to obtain approval from the Bank Supervision Department. The approval process is intensive, and the Department has to be satisfied both with the method whereby a bank calculates the capital required in relation to its market-risk exposure and with the robustness of the bank's risk-management processes to monitor its market-risk exposure. Following initial approval, the bank is granted a weighting (multiplication) factor, emanating from a statistical analysis of the volatility of the bank's portfolio exposure, known as its value at risk (VAR), which is used to determine its capital charge.

value at risk

sophisticated evaluation systems

As a result of increasing client demand for banks to trade in complex products and proprietary inclinations thereto, banks have to use progressively more sophisticated evaluation systems within both their treasuries and their risk-management departments. Complex instruments traded include non-linear products, such as structured equity options and credit derivatives. Sophisticated evaluation systems incorporate the measurement of risk using the VAR methodology, which is used within a bank as a management yardstick, on a daily basis. Such systems also permit banks to evaluate the impact of historical and hypothetical market-distress scenarios on their portfolio and to determine the worst losses that they can expect, as well as the adequacy of their capital to recover from such situations. Amongst other measures, the results of stress tests are a requirement for banks to obtain approval for use of the IM approach.

Currently, there are 12 trading banks in South Africa, two of which report to the Department in terms of the IM approach and three of which are in the process of applying therefor. Two more banks have indicated their intention to obtain approval for use of the IM approach in the near future. The greater sensitivity of the new Capital Accord to bank-wide risk is encouraging banks with significant market risk to pursue the IM approach.

onsite reviews of trading banks

In order to assess the operational risks associated with the IM approach and to review the multiplication factor more regularly, the Department is increasing the frequency of its onsite reviews of trading banks. This will enable the Department more rapidly to adjust the capital-charge requirements of banks using the IM approach via the multiplication factor under both adverse and favourable results.

Growth in mortgage loans

The South African mortgage market grew rapidly over the past number of years, a trend also evident in other mature markets. By the end of December 2005, South Africa had recorded mortgage-lending growth of 28,6 per cent (measured over a period of 12 months), compared to growth of 25,6 per cent in December 2004.

high mortgage growth

A number of developments, not only in South Africa but also in other international markets, led to high mortgage growth. These developments included, amongst other things, lower and variable mortgage-interest rates, a lower level of inflation, lower income-tax rates and an increase in the real disposable income of households. Real-estate prices reacted favourably to these positive developments. In a country report on selected issues in South Africa, issued in September 2005, the International Monetary Fund stated that, since 1997, the growth rate of housing prices in South Africa had been the highest in a large sample of economies, reaching a peak of 35,5 per cent in September 2004. According to the ABSA House Price Index, a declining trend, however, emerged during 2005, and housing prices eased year on year to 21,4 per cent in July 2005 and to 15,8 per cent in December 2005.

housing prices eased year on year

Another factor that promoted house-price appreciation, both domestically and internationally, was an increase in speculative buying, also known as the buy-to-let boom. In other words, investors purchased more property for profit than for use as their own residences. Many countries fear that a slowdown in the housing market will burst the so-called buy-to-let bubble. Research, however, has found that such fears are probably unfounded, owing to, amongst other things, the small scale of the buy-to-let market relative to the entire housing market.

lending innovations

As house prices have risen, lending innovations have allowed more borrowers to obtain larger mortgages than in the past. These innovations include, amongst other things, a

wider array of loan contracts being offered to borrowers, a greater reliance on capital-market funding by means of securitisation of home loans and high loan-to-value ratios. In view of the prevailing variety of innovative products, there has been some concern that banks' mortgage-loan portfolios may be vulnerable to a rise in interest rates and, in some markets, a decrease in house values. Although, no amount of banking regulation and supervision can prevent the occurrence of such problems in banks, the Bank Supervision Department continuously encourages the implementation and maintenance of sound risk-management practices by banks, in order for them to keep pace with such risks.

As the regulator of banks, the Bank Supervision Department is mindful of the high growth in mortgages over the past number of years and will continue to ensure that banks' risk-management processes are appropriate. In this regard, it should be noted that following a three-year period of significant growth in mortgage loans from the mid 1990s, the Bank Supervision Department issued Banks Act Circular 7/98 in August 1998, to amend the risk weighting of mortgage loans as from 1 October 1998. The circular provided, amongst other things, for a risk weighting of 50 per cent to be assigned to "loans fully secured by mortgage bonds on occupied urban residential dwellings or occupied individual sectional title dwellings, which loans are repayable in equal monthly instalments, where the monthly instalments are not overdue and to the extent that the capital amount outstanding does not exceed 80 per cent of the current market value of the mortgaged property", but for the risk weighting to be increased to 100 per cent in respect of any outstanding capital amount exceeding 80 per cent of the current market value of the mortgaged property. Furthermore, the minimum required capital-adequacy ratio of banking institutions was increased from 8 per cent to 10 per cent of risk-weighted assets in terms of Banks Act Circular 6/2001, issued by the Department in June 2001.

the Department will continue to ensure that banks' risk-management processes are appropriate

The Department's effort in the above regard will be enhanced by the implementation of the new Capital Accord on 1 January 2008, since it provides a more transparent and market-oriented regulatory framework.

Supervision of representative offices of foreign institutions

The Department subscribes to and fully endorses the Core Principles of Effective Banking Supervision of the Basel Committee on Banking Supervision. The Core Principles stipulate, amongst other things, that banking supervisors must have the authority to address compliance with banking legislation by banking institutions under their jurisdiction.

The Regulations relating to Representative Offices of Foreign Banking Institutions (the RO Regulations), issued under Government Notice No. 1370, in *Government Gazette* No. 22939 of 13 December 2001, seek to ensure continuous oversight, by the Department, of the activities of representative offices (ROs) of foreign banking institutions operating within the Republic of South Africa. The Department undertakes both onsite and offsite oversight, in order to establish whether an RO adheres to the applicable legislation.

onsite and offsite oversight

The onsite supervisory function entails annual visits to all registered ROs operating in the Republic. During such a visit, in-depth discussions are held with the chief representative officer (CRO) of an RO about the management of the RO and the extent of its operational activities, in order to determine whether the RO is functioning in accordance with the business plan approved by the board of the foreign institution concerned and whether the internal control measures of the RO are adequate and effective.

onsite supervisory function

offsite supervisory function

The offsite supervisory function includes analysis of the quarterly returns submitted by an RO in terms of the RO Regulations and evaluation of the internal control report (ICR) submitted by the CRO in terms of the requirements of Banks Act Circular 3/2004. The ICR has to be submitted annually, together with an application for renewal of the RO's licence to continue conducting its business in the Republic. In addition, a letter is required from the external auditors or the internal audit department of the RO's head office abroad, confirming concurrence, or otherwise, with the opinion that the CRO has expressed in the ICR.

Status of ROs during 2005

In view of the Department's stated policy that dormant ROs should be deregistered, two ROs were informed during 2005 that unless they could provide the Department with action plans to address their current or potential status as a dormant office, their registration as an RO would be withdrawn. One of these ROs was subsequently deregistered, whereas the other was granted permission to retain its licence in South Africa for another year, subject to compliance with the following conditions, to which the RO is adhering:

- The Department had to be furnished with the name and contact details of the officer at the institution's head office responsible for the RO.
- All regulatory returns prescribed by the RO Regulations had to be submitted, and the Department had to be informed on a quarterly basis of the progress made with the institution's strategic investigations into its continued representation in South Africa.

47 ROs from 23 countries

total of 135 staff members

total expenditure was US$12 000 000

As at 31 December 2005, 47 ROs from 23 countries were operating in South Africa, as opposed to 44 ROs as at 31 December 2004, and they employed a total of 135 staff members (2004: 120). Of these, 95 staff members or 70 per cent, were South African residents (2004: 90, or 70 per cent), and the remaining 40 staff members, or 30 per cent, were non-residents (2004: 30, or 25 per cent). The total expenditure of the ROs was US$12 000 000 as at 31 December 2005 (2004: US$10 971 000).

two institutions were deregistered

During 2005, the ROs of the following two institutions were deregistered:

- China Everbright Bank – 31 March 2005.
- Commerzbank – 19 October 2005.

five institutions were granted authorisation

The following five institutions were granted authorisation to establish an RO in South Africa during 2005:

- Barclays Bank plc - 14 December 2005.
- Barclays Private Clients International - 1 December 2005.
- HSBC Bank International Limited – 1 December 2005.
- ICICI Bank – 1 February 2005.
- Lloyds of London TSB - 27 June 2005.

Main areas of business

main areas of business

During the year under review, advisory services to network customers, advice on offshore private-banking investment and correspondent banking were the main areas of business of the ROs operating in South Africa.

In this regard, it should be noted that in terms of section 34 of the Banks Act, 1990, ROs are not permitted to conduct the "business of a bank", as defined in section 1 of the Act, and are therefore not permitted to take deposits. An analysis of the returns submitted

by the ROs during 2005 did not reveal any indication of possible contraventions of the Banks Act.

Information and communication systems

The information and communication systems currently used by the Bank Supervision Department were developed and implemented in 1996. Over the years, these systems have evolved into sophisticated and efficient analytical tools.

sophisticated and efficient analytical tools

Controls in the capturing and processing of banks' data

A number of controls are in place when the Department captures and processes the DI returns submitted by banks. All periods, present and future, in the Department's database are "locked". When banks have to submit their DI returns, the gateway is opened for a specific period. The system allows the Department to limit the submission per period, per bank and per set of DI returns. Each bank has been allocated a unique number, which makes it impossible for a bank to submit its DI returns by using another bank's unique number.

All banks submit their DI returns using the SARBDEX electronic data-interchange system. The system requires user identification, as well as a password, and uses SSL 128-bit encryption in order to ensure the secure submission of data.

When data are received from a bank, they are subjected to validation tests. Should the data fail the validation tests, the data are rejected, and a message, detailing the problem, is sent to the bank in question. The bank can then correct and resubmit the returns. When a bank's returns pass the validation tests, the data are accepted onto the database, and the gateway is automatically locked. Data are loaded into the database each evening, and data comparisons are done to ensure the correctness of the data that have been loaded.

validation tests

Each bank is required to submit a form DI 099, which contains the hash totals relating to the returns submitted. The form DI 099 of a bank has to be signed by its risk managers, as well as by its chief accounting officer (CAO) and chief executive officer (CEO). When a form DI 099 is received, the hash totals in the form are checked against the hash totals generated by the Department's systems. The objective is to ensure that the data submitted by a bank in its returns are the same as the data that have been signed off by the bank's risk managers, CAO and CEO.

Should a bank wish to resubmit data, it first has to submit an amended and signed form DI 099. This form is then used as a prompt to open the gateway for the particular bank, period and set of returns. After receipt of the resubmitted data, the gateway is automatically locked.

When a bank's external auditors request copies of the returns submitted by the bank for auditing purposes, an additional audit lock is applied. Should a bank wish to resubmit returns that are being audited, the Department requires a form DI 099 and a letter from the auditors agreeing to the resubmission of the said returns.

Reports and trend analysis

The Department has developed approximately 1 000 reports and graphs on the system, and these are used in the analysis of banks. All analysts of the Department can use the reports and change the way in which the data are viewed, or create their own reports and graphs.

used in the analysis of banks

A system was developed to take the data from the database and to create a set of approximately 200 graphs, for use in presentations. These graphs contain information on a bank, its peer group and the total banking sector.

Upgrading of database system

database and technology have to be upgraded

As a consequence of additional analytical requirements, resulting partly from the impending implementation of the new Capital Accord (Basel II), the Department's database and technology have to be upgraded. The Department is therefore acquiring a new database, together with an integrated suite of analytical tools. Development and implementation will take place in 2006, and the new BA returns, which will cater for the requirements of Basel II, will be developed on the new system.

Chapter 3

Developments related to banking legislation

A key responsibility of the Bank Supervision Department is to ensure that the legal framework for the regulation and supervision of banks and banking groups in South Africa remains relevant and current. The legal framework pertaining to banking regulation, therefore, has to take account of local and international developments in the markets and the regulatory standards applicable thereto. Consequently, the Department has to review the banking legislation – that is, the Banks Act, 1990, the Mutual Banks Act, 1993, the Regulations thereto and other pieces of related banking legislation – on an ongoing basis and make the necessary amendments.

During the past number of years, the Basel Committee on Banking Supervision and several international supervisory authorities published various documents that, amongst other things, address various cross-border matters, including matters relating to the roles and responsibilities of home and host supervisors and other relevant matters relating to the supervision of a bank or banking group on a solo basis and on a consolidated basis. Of particular importance to supervisors and the banking industry is the new Capital Accord, generally known as Basel II, which is to be implemented on 1 January 2008, in South Africa.

It is therefore imperative for the legal framework to be, amongst other things, sufficiently robust to enable the Registrar of Banks properly to discharge his/her role and responsibilities in respect of banks, controlling companies of banks and banking groups on a solo, consolidated and cross-border basis.

Based on the mission and philosophy of the Bank Supervision Department and in order to implement Basel II successfully in South Africa, in accordance with the latest international regulatory, supervisory and market best practices and standards, it has become necessary to make amendments to, amongst other things, the Banks Act, the regulatory framework (the Regulations), the supervisory process and related policies.

In particular, the legal framework pertaining to the supervision of banks requires amendment as regards the following aspects:

legal framework requires amendment as regards the following aspects

- Increased emphasis on the application of the Basel II requirements to all relevant banks and banking groups on a consolidated basis.
- Roles and responsibilities of home and host supervisors, respectively.
- Cooperation between supervisors.
- Sharing of information between supervisors.
- Responsibilities of banks and banking groups.
- Responsibilities of the management and boards of directors of banks and banking groups.
- Reporting requirements of banks and banking groups.
- Various options available to banks and banking groups in the calculation of minimum capital requirements in respect of credit-risk, market-risk and operational-risk exposures.
- Importance of the supervisory review process in order, amongst other things, to assess the capital adequacy and control environment of banks and banking groups.
- Comprehensive disclosure requirements for banks and banking groups.

Besides addressing proposed amendments to the Banks Act and the Regulations, this chapter also contains some comments on other legislation and draft legislation likely to affect the banking industry.

Proposed amendments to the Banks Act

The process of drafting amendments to the Banks Act in order to comply with the principles and standards outlined earlier in this chapter was developed further during the year under review. The first draft of the proposed amendments was approved by the Standing Committee for the Revision of the Banks Act, 1990, during November 2005 and was circulated to all banks, for comment. The second draft of the proposed amendments to the Banks Act was circulated at the end of January 2006. The proposed amendments to the Banks Act are the product of an assessment of the various prescriptions contained in Basel II, inputs received from the various subcommittees of the Basel II Accord Implementation Forum (AIF) and a number of discussions and debates on issues raised during meetings of the regulatory subcommittee of the AIF.

all proposed amendments are briefly outlined

Although the proposed amendments to the Banks Act are aimed mainly at addressing the prescriptions of Basel II, other necessary amendments are also proposed. In previous annual reports, reference was made to some of these amendments. Since these amendments have not yet been tabled in Parliament, however, all proposed amendments are briefly outlined hereunder, for the sake of completeness.

Definitions

Amendments to some definitions in, and insertion of certain definitions into, section 1 of the Banks Act are proposed, as follows:

– ***Consolidating supervisor***
  Basel II and all related documents emphasise, amongst other things, the importance of the respective roles and responsibilities of, as well as the need for cooperation between, home and host supervisors. Furthermore, the latest international practice is to refer to the home supervisor as the consolidating supervisor. It is therefore proposed that a definition of the term "consolidating supervisor" be inserted into the Banks Act.

– ***Deposit***
  The reference to the Insurance Act, 1943, in subparagraph (vi) of the definition of "deposit" has become outdated, since the aforementioned Act has been replaced by the Long-term Insurance Act, 1998, and the Short-term Insurance Act, 1998. The reference is to be amended accordingly.

– ***Division***
  It came to the attention of the Department that certain banks either established or proposed establishing divisions of the bank in conjunction with third parties that were not banks and that the word "bank" was being used together with the name of the third party. Although the said development was foreseen and addressed by an amendment to section 52 of the Banks Act during 2003, the provision could not be enforced effectively, since the term "division" had not been defined. It is therefore proposed that a definition of the term "division" be inserted into the Banks Act.

– ***Eligible institution***
  Basel II is a risk-sensitive framework, in terms of which external credit assessments or ratings issued by external credit-assessment institutions form an integral part of the calculation of a bank's minimum required capital and reserve funds. Based on the important role that external credit-assessment institutions or eligible institutions will play in determining a bank's minimum required capital and reserve funds, and in

view of the requirements of Basel II, it is proposed that a definition of the term "eligible institution" be inserted into the Banks Act.

– ***External credit assessment***
  For the same reasons as set out above, it is proposed that a definition of the term "external credit assessment" be inserted into the Banks Act.

– ***Host supervisor***
  Based on the same reasons as set out above, it is proposed that a definition of the term "host supervisor" be inserted into the Banks Act.

– ***Primary share capital***
  Basel II allows supervisors the discretion to take minority interests into account in the calculation of primary capital on a consolidated basis. It is proposed that the definition of "primary share capital" be augmented by enabling the percentage of minority interests that would qualify as primary capital to be prescribed by regulation.

– ***Primary and secondary unimpaired reserve funds***
  In terms of international best practice, home supervisors, amongst other things, need to keep certain matters in mind when they conduct consolidated supervision of a banking group. Currently, the definitions of primary and secondary unimpaired reserve funds include references only to "a/the bank". It is proposed that the definitions also make reference to a bank controlling company. Furthermore, the International Financial Reporting Standards adopted recently prescribe, amongst other things, the manner in which entities, including banks and banking groups, have to account for certain fair-value adjustments. It is proposed that these changes be reflected in the definition.

Sections 1 and 70 of the Banks Act – Deletion of references to the CAR Regulations

The provisions of the Regulations relating to Capital-adequacy Requirements ("CAR") for Banks' Trading Activities in Financial Instruments (the CAR Regulations) have been incorporated into the proposed amended Regulations relating to Banks. It is therefore proposed that references to the CAR Regulations be deleted.

Section 4 of the Banks Act – Written arrangements relating to the respective roles and responsibilities, as well as cooperation between, consolidating and host supervisors

Basel II clearly states, amongst other things, that in order to reduce the compliance burden and to avoid regulatory arbitrage, the methods and approval processes used by a bank at group level may be accepted by the host-country supervisor at the local level, provided that these methods and processes adequately meet the local supervisor's requirements. Whenever possible, supervisors should avoid performing redundant and uncoordinated approval and validation work, in order to reduce the implementation burden on banks and to conserve supervisory resources. It is proposed that section 4 of the Act be amended to provide therefor.

Section 4 of the Banks Act – Sharing of information

Sharing of information and cooperation between supervisors are prerequisites for the effective supervision of a banking group on a consolidated basis. Sharing of information relates not only to sharing of information between bank supervisors, but also to sharing

of information with securities or insurance supervisors. It is proposed that section 4 of the Banks Act be amended to provide therefor.

Section 4 of the Banks Act – Supervisory review process

Pillar 2 of Basel II deals comprehensively with the supervisory review process. It is proposed that section 4 of the Banks Act be amended to provide therefor.

Section 4 of the Banks Act – Mapping of external ratings

In terms of the requirements of Basel II, supervisors have to assign assessments of eligible external credit-assessment institutions to the risk weights available under the standardised risk-weighting framework. In other words, supervisors have to decide which assessment categories correspond to which risk weights. It is proposed that section 4 of the Banks Act be amended to make provision therefor.

Section 4 of the Banks Act – National discretion

Since Basel II recognises that the regulation and supervision of banks or banking groups are not an exact science and that discretionary elements within the supervisory review process are inevitable, the new framework contains various items of national discretion. It is proposed that section 4 of the Banks Act be amended to provide therefor.

Section 4 of the Banks Act – Disclosure of information

Basel II requires supervisors to make publicly available the criteria to be used in the review of banks' internal capital assessments. Basel II also states that, when supervisors choose to set target or trigger ratios, or to set categories of capital in excess of the regulatory minimum, factors that may be considered in doing so should be publicly available. Furthermore, Basel II requires the supervisory process for recognising eligible institutions to be made public and requires supervisors to make items of national discretion publicly available. It is proposed that section 4 of the Banks Act be amended to provide therefor.

Section 6(4) of the Banks Act – Circulars, guidance notes and directives

Currently, section 6(4) of the Banks Act states that "The Registrar may from time to time by means of a circular furnish banks with guidelines regarding the application and interpretation of the provisions of this Act or provide banks with any other information". It is proposed that the provisions of section 6(4) clearly distinguish between circulars, guidance notes and directives.

Section 7 of the Banks Act - Furnishing of information by banks

In order for the Registrar of Banks to discharge the respective roles and responsibilities as home and host supervisor successfully, it is essential, as a minimum, for the Registrar to be empowered to obtain information from banks, controlling companies and from a subsidiary or a branch of a parent bank. It is proposed that section 7 of the Banks Act be amended to provide therefor.

Section 30 of the Banks Act: Publication of information relating to banks, branches, controlling companies and representative offices of foreign institutions

Section 30 of the Banks Act requires the Registrar of Banks to keep a register of all registered banks and to publish such registrations in the *Government Gazette*. The Banks Act, however, does not require the Registrar to keep a register of registered controlling companies of banks and branches of foreign institutions. It is proposed that section 30 be amended to provide for such additional registers to be kept and for such registrations to be published in the *Government Gazette*.

additional registers

Section 37 of the Banks Act: Permission for acquisition of shares in bank or controlling company of a bank

Section 37 of the Banks Act places restrictions on the acquisition of shares in a bank or controlling company of a bank if such an acquisition will result in the person (and the associate/s of the person) holding in excess of certain threshold percentages of the "… total nominal value of all the issued shares of the bank or bank controlling company …". In future, various forms of hybrid instrument (shares with some debt characteristics) will be issued, further increasing the total nominal value of all issued shares of a bank or controlling company of a bank. It is therefore quite possible for a single shareholder to own less than the specified thresholds of 15 per cent, 24 per cent, 49 per cent, or 74 per cent of the total nominal value of all issued shares of a bank or bank controlling company, but to have voting rights attached to such shares in excess of the prescribed thresholds.

voting rights

Since section 37(5)(ii) of the Banks Act already refers to a limitation of voting rights, it would appear that the thresholds should relate not only to the nominal value of all shares in issue, but also voting rights. It is therefore recommended that section 37 be amended so that the thresholds also be made applicable to the voting rights attached to the shares.

Section 43 of the Banks Act: Registration of controlling companies of banks

Section 43(1) of the Banks Act provides that a public company that *desires* to exercise control over a bank *may* apply for registration as a controlling company of a bank. It is proposed that the section be amended to read that a public company that exercises control or that intends to exercise control over a bank *shall* apply for registration as a controlling company of a bank.

Section 50 of the Banks Act: Investments in controlling companies of banks

Section 50 of the Banks Act provides that a bank controlling company investing money in undertakings other than banks, or in fixed property not being used for the purpose of conducting the business of a bank, shall manage its transactions in such investments in such a way that the amount of such investments does not at any time exceed 40 per cent of the sum of its share capital and reserve funds. It is proposed that the section be amended to reflect the accounting standards in this regard properly and to provide that the amount of the said investments does not exceed 40 per cent of the share

calculated on a consolidated

capital and reserve funds of the bank controlling company *calculated on a consolidated basis, as prescribed*. The Regulations will then provide for the method of the calculation. It is also proposed that the same provisions be made applicable to loans and advances made by controlling companies of banks.

Section 52 of the Banks Act: Subsidiaries, branch offices, other interests and representative offices of banks and controlling companies

The enforcement and administration of section 52 of the Banks Act have become problematic, owing to certain issues relating to interpretation and the somewhat unclear wording of the section. It is proposed that section 52 be amended to clarify certain unclear provisions and to reflect the policy of the Bank Supervision Department in this regard adequately. It is furthermore proposed to regulate the establishment of divisions by banks, for the reasons set out earlier in this chapter, under the proposed amendments to the definitions in the Banks Act.

Section 54 of the Banks Act: Compromises, amalgamations, arrangements and affected transactions

As a result of the wording of section 54 of the Banks Act, as well as the various legal interpretations of the term “assets **and** liabilities”, enforcement of the provisions of the section has become somewhat problematic. It is proposed that section 54 be amended to address the difficulties in this regard.

Section 59 of the Banks Act – Returns regarding shareholders

Currently, section 59 of the Banks Act prescribes different reporting thresholds for domestic and foreign shareholders. It is proposed that the detailed provisions be contained in the Regulations and that section 59 be amended to enable such prescription by regulation.

Section 60 of the Banks Act – Directors of bank or controlling company of a bank

Section 60 of the Banks Act was substantially amended in 2003 to provide the Registrar of Banks with powers to object to the appointment of directors and executive officers. Since the promulgation of the amendments to section 60 and the establishment of a policy and procedure in this regard by the Bank Supervision Department, it has transpired that the provisions contain certain deficiencies. It is proposed that section 60 be amended to address these deficiencies.

Sections 64, 64A and 64B of the Banks Act – Audit, risk and directors’ affairs committee

Currently, the provisions of sections 64, 64A and 64B of the Banks Act relate only to banks. These sections, however, are equally relevant to controlling companies of banks and banking groups. Furthermore, Basel II clearly states that the scope of application of the framework will include, on a fully consolidated basis, any holding company that is the parent entity within a banking group, in order to ensure that the risk of the whole banking group is captured. It is therefore proposed that the aforementioned sections also be made applicable to controlling companies of banks and banking groups.

Section 70 of the Banks Act – Minimum share capital and unimpaired reserve funds

Currently, section 70 of the Banks Act provides that, in the calculation of the aggregate amount of capital that a bank is required to maintain, the sum of the bank's secondary capital and secondary unimpaired reserve funds shall be taken into account to an amount not exceeding the sum of the bank's allocated and qualifying primary share capital and allocated and qualifying primary unimpaired reserve funds. In order for the legislative framework to remain in line with international regulatory and supervisory requirements and developments, it is proposed that section 70 be amended.

Section 70A of the Banks Act - Minimum capital and reserve funds in respect of a controlling company of bank

Section 70A of the Banks Act currently provides that a controlling company of a bank has to maintain capital and reserve funds equal to the sum of the required capital amounts of the individually regulated entities, as determined by their respective regulators, plus a capital proxy amount in respect of unregulated entities. Neither the Banks Act nor the Regulations, however, require a banking group at any stage to calculate *consolidated or aggregated risk positions or exposures* before calculating a capital requirement for the banking group based on the consolidated or aggregated amount of risk exposure, not even in respect of a locally incorporated bank and its foreign branches.

consolidated or aggregated risk positions or exposures

The above position is, however, not sufficiently comprehensive, since Basel II clearly states that the framework will be *applied on a consolidated basis* to internationally active banks. It is therefore proposed that section 70A be amended accordingly.

applied on a consolidated basis

Section 73 of the Banks Act: Large exposures

Currently, section 73 of the Banks Act deals comprehensively with various matters relating to the exposure of a bank, bank controlling company, branch or branch of a bank to a single person. Basel II, however, clearly states that "… supervisors should assess the extent of a bank's credit risk concentrations, how they are managed, and the extent to which the bank considers them in its internal assessment of capital adequacy under Pillar 2. Such assessments should include reviews of the results of a bank's stress tests. Supervisors should take appropriate actions where the risks arising from a bank's credit risk concentrations are not adequately addressed by the bank …". Furthermore, concentration risk relates not only to counterparty exposure but also to exposure to an industry, sector or a geographical area. Therefore, it is proposed that section 73 of the Banks Act be amended to refer to concentration risk, instead of large exposures, and that the provisions address the difficulties within the South African market, on the one hand, and the Basel II prescription in that regard, on the other hand.

concentration risk

Section 74 of the Banks Act – failure or inability to comply with prudential requirements

Currently, section 74 of the Act provides only for the failure or inability of a bank to comply with prudential requirements. Basel II, however, clearly states that the scope of application of the framework will include, on a fully consolidated basis, any holding

company that is the parent entity within a banking group, in order to ensure that the risk of the whole banking group is captured. It is therefore proposed that the section also be made applicable to controlling companies of banks.

Sections 75 and 90 of the Banks Act – Returns and Regulations

The Banks Act and the Regulations contain various references to Statements of Generally Accepted Accounting Practice. Recently, however, South Africa adopted the International Financial Reporting Standards. It is therefore proposed that the terms "Generally Accepted Accounting Practice" in the Banks Act be replaced by a reference to the financial reporting standards issued by the Financial Reporting Standards Council, as set out in section 440S of the Companies Act.

Section 79 of the Banks Act – Shares, debentures and negotiable certificates of deposit

Currently, section 79(1)(c) of the Banks Act refers only to negotiable certificates of deposit that may not be issued otherwise than in accordance with prescribed conditions. Following certain amendments to the Income Tax Act, banks recently commenced issuing instruments such as promissory notes, instead of negotiable certificates of deposit. It is proposed that promissory notes and instruments with similar characteristics be included in section 79(1)(c).

Sections 81 to 84 of the Banks Act: Control of certain activities of unregistered persons

liquidation or sequestration

A practice that has emerged in enforcing sections 81 to 84 of the Banks Act is that once inspectors have been appointed to investigate a person operating an illegal scheme, such a person is invariably liquidated or sequestrated by the investors in the scheme or by a "friendly" creditor. Such a liquidation or sequestration negates the work done by the inspectors, and the higher fees charged by the appointed liquidator/trustee of the insolvent estate are to the detriment of depositors in such a scheme.

For various reasons, the Bank Supervision Department has been loathe to become involved in the liquidation process of unregistered persons. The Department's experience in the recent past, however, has made it imperative for the Registrar of Banks to become involved to some extent.

It is proposed that the relevant sections be amended to provide that whilst a person operating an illegal scheme is under investigation or management in terms of the provisions of the Banks Act, such a person may not be liquidated or sequestrated by any person, save with the leave of the court and only once the application has also been served on the Registrar.

It is also proposed that a duly appointed fund manager report to the Registrar on the solvency of the person operating the illegal scheme. In terms of the proposed amendment, should the person be found to be solvent, the manager will be permitted to repay depositors, in accordance with the provisions of section 84 of the Banks Act. When a person is found to be insolvent, however, the Registrar will be permitted to apply for the liquidation of the person and will be able to make a recommendation on the liquidator to be appointed, as well as agree to the liquidator's fee structure.

New section 85A of the Banks Act – Approval of eligible institutions

In terms of the requirements of paragraph 90 of Basel II, supervisors are responsible for determining whether or not an eligible institution meets the criteria listed in paragraph 91 of Basel II and, as such, may be regarded as an approved eligible institution. It is proposed that a new section in this regard be inserted into the Banks Act.

New section 85B of the Banks Act – Verification of information

In terms of international best practice, all information submitted to a consolidating or host supervisor in respect of a bank or bank controlling company and its foreign branches, subsidiaries or joint ventures should be verified in one of three ways, namely, by the host supervisory authority, by external auditors appointed by either the host or consolidating supervisory authority, or by the consolidating supervisory authority. It is proposed that a new section in this regard be inserted into the Banks Act.

Possible amendments under consideration or being researched

Other possible amendments to the Banks Act that are currently under consideration, or on which research is being done, relate to the following:

– ***Liquid assets***
  The Land Bank has submitted a proposal for the revision of the definition of "liquid assets", in order to accommodate the issue of Land Bank development bills, with a maturity of six months, for the funding of short-term production loans to emerging farmers. The Land Bank argues that whereas the definition currently refers to these bills as being issued to fund mutual co-operatives, many of these co-operatives may in fact have been converted to companies. The Land Bank, therefore, proposes that the definition of liquid assets include a reference to companies. The proposal is currently being considered.

– ***Sanctions or fines for non-compliance***
  Although the Banks Act provides for the imposition of fines on banks in certain prescribed instances, as set out in sections 74 and 91 of the Banks Act, it has become clear that the provisions of the aforementioned sections are inadequate. It is proposed that the Registrar of Banks be afforded the power to impose substantial fines or sanctions on banks for non-compliance with certain provisions of the Banks Act or with certain directives issued by the Registrar. In order for such power to be exercised judiciously and fairly, it is proposed that the decision to impose a fine or sanction on a bank be taken by a panel. The following issues will be considered in this regard:

  following issues will be considered

  - Sanctions on banks that are in non-compliance with the Banks Act or a directive should include non-financial options, such as prohibiting a delinquent bank from submitting any further application in terms of the Banks Act until the transgression has been addressed.
  - There is a view that financial penalties imposed on banks are likely to be passed on to the client/consumer in some way. A contrary view, however, is that, owing to competition between banks, the passing-on of a fine to consumers will be curtailed, especially when such a bank is also "named and shamed" for its non-compliance.

- The public might regard penalties and sanctions imposed on a bank as a sign of problems in that bank and, consequently, lose trust in that bank, which could result in a run on the bank, as well as the associated systemic implications of such a run.

– ***Amendments to the Basel Core Principles***
The Core Principles for Effective Banking Supervision, generally known as the Basel Core Principles, which were issued by the Basel Committee on Banking Supervision during September 1997, are currently being reviewed. It is proposed that the revised version of the Basel Core Principles be scrutinised once it has been published, in order to identify amendments to the legal and regulatory framework that may become necessary.

– ***Amendments to the Companies Act***
Consideration will also be given to the impact on and applicability to the Banks Act of recent amendments to the Companies Act, as indicated later in this chapter.

Regulations relating to Banks

The prescriptions contained in Basel II have necessitated a complete revision of the Regulations. The process of drafting amendments to the Regulations has been managed via the AIF and its various subcommittees. The second draft of the Regulations has been circulated to all banks, for comment, to reach the Department by 31 March 2006.

Legislation and draft legislation likely to affect the banking industry

Several other pieces of legislation and draft legislation are likely to affect the banking industry, as well as the ongoing regulation and supervision of banks by the Bank Supervision Department.

National Credit Act, 2005

The National Credit Act, 2005 (NCA), which came into force on 1 June 2006, repeals the Usury Act and the Credit Agreements Act, whereby consumer credit is regulated, and replaces both of the aforementioned Acts. Since the NCA regulates all credit extension, it applies to all banks, as credit providers.

applies to all banks

Some of the Bank Supervision Department's concerns about certain provisions of the National Credit Bill, 2005, as previously provided to the Department of Trade and Industry, have been addressed by subsequent amendments. The Department, however, remains concerned about the practical implementation of the NCA and its possible effects on not only the business of banks, but also the regulation and supervision of banks.

Second-tier and third-tier banks

During the year under review, the Bank Supervision Department cooperated with the National Treasury in proposing solutions to difficulties relating to the establishment of second-tier and third-tier banks. The Department expects further progress to be made with the Dedicated Banks Bill, 2004, and the Co-operative Banks Bill, 2004.

expects further progress

Companies Amendment Bill, 2005

The Companies Amendment Bill, 2005, aims in section 269A to insert provisions that would require audit committees for public-interest companies. The proposed amendment stipulates that an audit committee appointed by the board of directors should consist of not less than three independent non-executive directors. Currently, section 64 of the Banks Act prescribes, amongst other things, that the chairperson and the majority of the members of a bank's audit committee shall be non-executive directors, whilst allowing a minority of executive directors to serve on an audit committee.

audit committee

The Bank Supervision Department is of the opinion that the specialised nature and business of a bank necessitates the accommodation of an executive director on the audit committee. The Department is therefore of the view that the proposed new legislation should make provision for such specialised business.

The Companies Amendment Bill also aims to provide in section 274A for the rotation of auditors of companies. The proposed amendment stipulates that an auditor may not serve for more than four consecutive financial years.

rotation of auditors

After consultation with the banking industry and auditing profession, and in line with international best practice, the Department, however, during 2004 issued Banks Act Circular 16/2004, regarding the rotation of auditors of banks. The said circular distinguishes between a lead, an engagement and a concurring partner. In terms of the said circular, lead partners and engagement partners have to be rotated after five years. Concurring partners, used to provide another level of objectivity on the work done by lead and engagements partners, however, are excluded from the rotation process.

In the view of the Department, the legislature should take note of the international best practice, as set out in Banks Act Circular 16/2004, and should consider either extending the proposed period to five years, or excluding banks (public-interest companies registered as such) from the four-year period of rotation proposed by the Companies Amendment Bill.

Chapter 4

Trends in South African banks

comparative figures may differ from those reported in the 2004 annual report

This chapter reflects the main trends apparent from the information received from registered banks during the year under review. Certain comparative figures in respect of 2004 may differ from those reported in the 2004 annual report, because some banking institutions subsequently submitted amended returns.

The reports and graphs in sections 4.1 to 4.7 below are affected largely by the position of the "big four" banks, which constituted 83,8 per cent of the banking sector in December 2005 (December 2004: 83,6 per cent). The five largest banks constituted 89,6 per cent of the banking sector as at the end of December 2005 (December 2004: 88,5 per cent).

4.1 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 changes thereto on the risk profile of the banking sector. The aggregated balance sheet of the banking sector in South Africa equalled R1 677,5 billion as at 31 December 2005, as opposed to R1 498,4 billion as at 31 December 2004 and R1 379,8 billion as at 31 December 2003.

Figure 1: Aggregated balance sheet

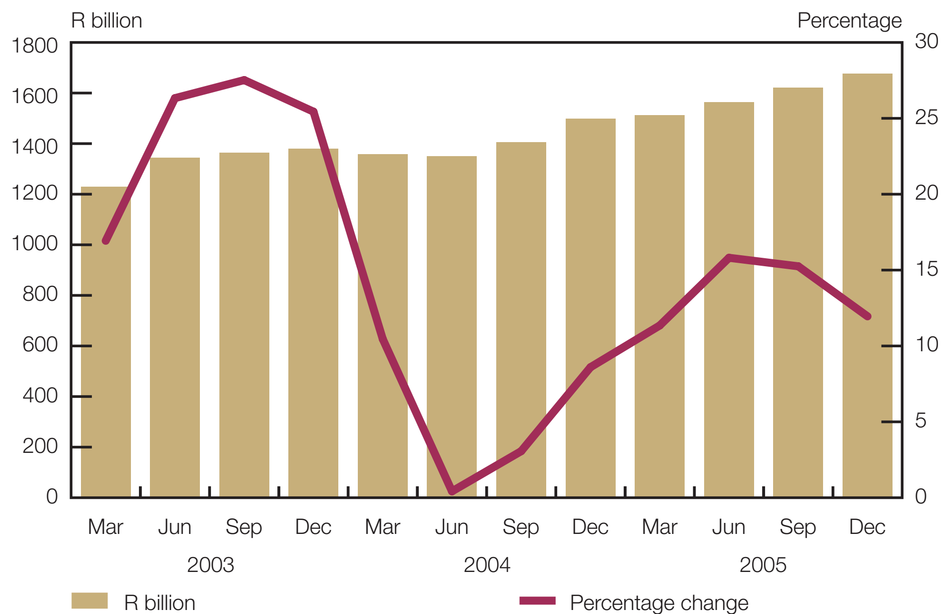


Figure 1 graphically depicts the quarter-end value of, and percentage growth (measured over 12 months) in, the aggregated balance sheet of the banking sector for the period from March 2003 to December 2005. From December 2003, when a growth rate of 25,4 per cent was recorded, growth in the aggregated balance sheet decreased uninterruptedly until June 2004 (0,4 per cent), to end 2004 at 8,6 per cent. The sharp decrease in total assets during the first two quarters of 2004 was due mainly to the deregistration of two A-2 rated banks (being banks other than the five largest banks) and a decrease in the total assets of some local branches of international banks. During

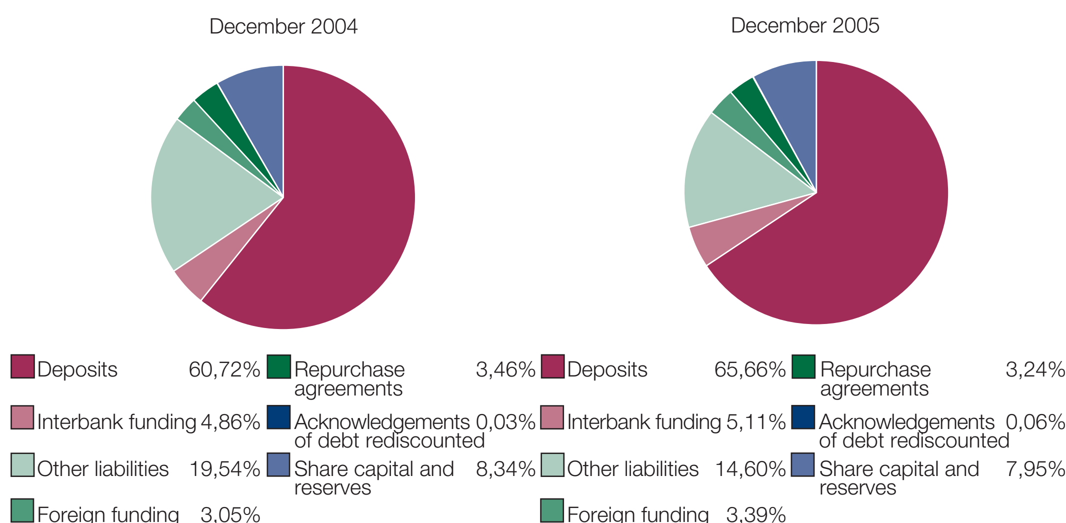
2005, growth in the aggregated balance sheet accelerated until June 2005 (15,8 per cent), but moderated to 15,3 per cent in September 2005. By the end of 2005, a growth rate of 12 per cent had been recorded. The increase during the first two quarters of 2005 relates to generally strong growth in the core products of A1-rated banks (that is, the five largest banks), the main products being mortgages, instalments and overdrafts. The moderation from the third quarter of 2005 until the end of the year was due mainly to a decrease in derivative activities.

growth rate of 12 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



Total liabilities as at the end of December 2005 equalled R1 677,5 billion, as opposed to R1 498,4 billion as at the end of December 2004. Domestic deposits from the public, in the amount of R1 101,5 billion, remained the main source of funding for the banking sector and constituted 65,7 per cent of total liabilities in December 2005, compared to 60,7 per cent in December 2004. Share capital and reserves and other liabilities as a percentage of total liabilities, on the other hand, decreased from 8,3 per cent and 19,5 per cent, respectively, in December 2004 to 8,0 per cent and 14,6 per cent, respectively, in December 2005. The decrease in other liabilities was due mainly to a revaluation of derivatives. Foreign funding and interbank funding, on the other hand, increased from 3,1 per cent and 4,9 per cent, respectively, in December 2004 to 3,4 per cent and 5,1 per cent, respectively, in December 2005. The increase in interbank funding was due mainly to excess funds being available in the market. Repurchase agreements decreased from 3,5 per cent in December 2004 to 3,2 per cent in December 2005.

domestic deposits from the public remained the main source of funding

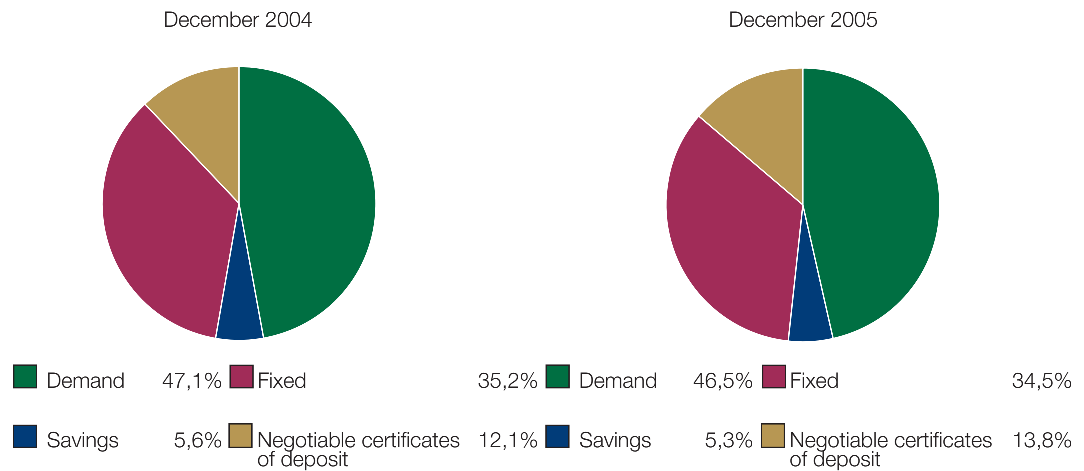
Composition of non-bank deposits

Total non-banks deposits as at the end of December 2005 equalled R1 101,5 billion, as opposed to R909,9 billion as at the end of December 2004. Figure 3 reflects a year-on-year comparison of the composition of non-bank deposits. Demand deposits and fixed and notice deposits as a percentage of total non-bank deposits constituted the

largest portion of total non-bank deposits, followed by negotiable certificates of deposit (NCDs). Demand deposits and fixed and notice deposits as a percentage of total non-bank deposits decreased from 47,1 per cent and 35,2 per cent, respectively, in December 2004 to 46,5 per cent and 34,5 per cent, respectively, in December 2005. The share of non-bank deposits represented by NCDs increased from 12,1 per cent at the end of December 2004 to 13,8 per cent at the end of December 2005. As noted in the previous annual report, the growth in NCDs during the past two years was due to the removal of stamp duties on NCDs in the 2004 budget speech, consequently decreasing the cost of NCDs.

growth in NCDs

Figure 3: Composition of non-bank deposits



Maturity structure of non-bank deposits

Figure 4: Composition of non-bank funding according to maturity

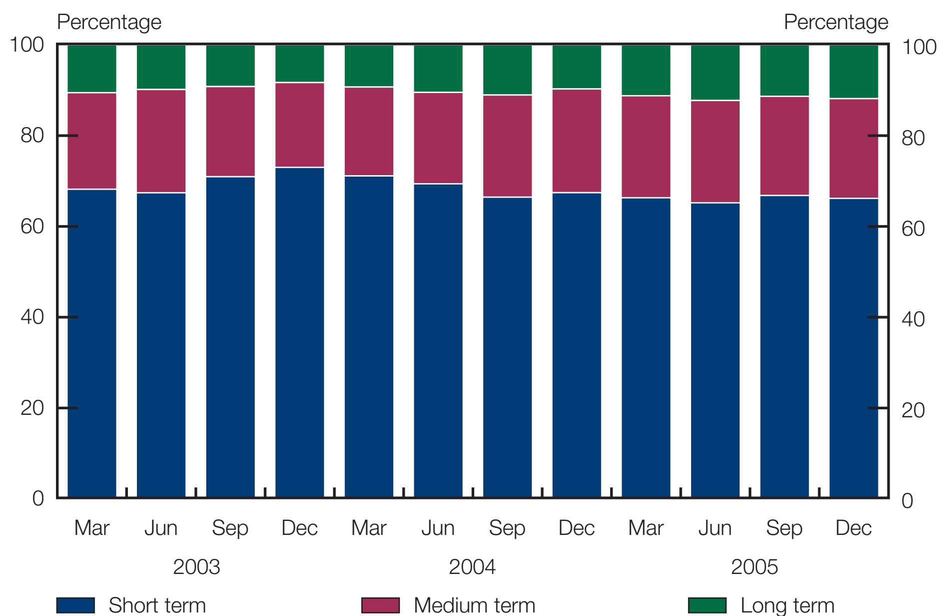


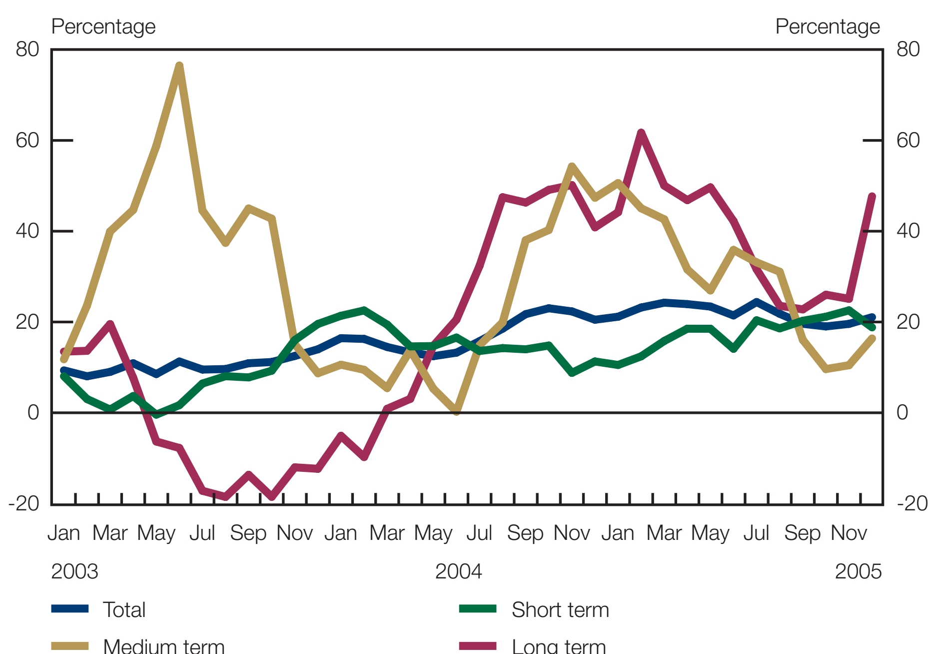
Figure 4 reflects the composition of non-bank deposits (according to maturity) for the period from March 2003 to December 2005. Short-term deposits remained the largest component of total non-bank funding and accounted for 66,2 per cent of total non-bank funding as at 31 December 2005, compared to 67,4 per cent as at the end of December 2004 and 73 per cent as at the end of December 2003. Medium-term deposits accounted for 22 per cent as at 31 December 2005, compared to 22,9 per cent and 18,7 per cent as at the end of December 2004 and the end of December 2003, respectively. Although long-term deposits remained the smallest component of total non-bank funding and accounted for 11,9 per cent of total non-bank funding as at 31 December 2005, they showed some steady growth when compared to 9,7 per cent and 8,3 per cent as at the end of December 2004 and the end of December 2003, respectively.

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

long-term deposits showed some steady growth

The high percentage of 66,2 per cent represented by short-term deposits during 2005 was due mainly to a combination of banks' pricing policy and depositors' view on interest rates. Although the aforementioned percentage appears to be high, it has proved to be stable over the past number of years.

Figure 5: Growth in non-bank funding according to maturity (percentage change over 12 months)



Growth in short-term deposits remained relatively stable over the past three years and decreased from 19,6 per cent in December 2003 to 11,3 per cent in December 2004 and, by the end of December 2005, had increased to 18,8 per cent (measured over a period of 12 months).

Growth in medium-term deposits increased substantially, from 0,2 per cent in June 2004 to 54,3 per cent in November 2004, whereas growth in long-term deposits increased from 0,9 per cent in March 2004 to 61,7 per cent in February 2005. The increase in growth in both medium-term deposits and long-term deposits during the above-mentioned periods was due mainly to some A1-rated banks deciding to lengthen

their medium-term and long-term funding books, in line with the accelerated growth in banks' mortgage books resulting from the lower interest-rate environment in South Africa.

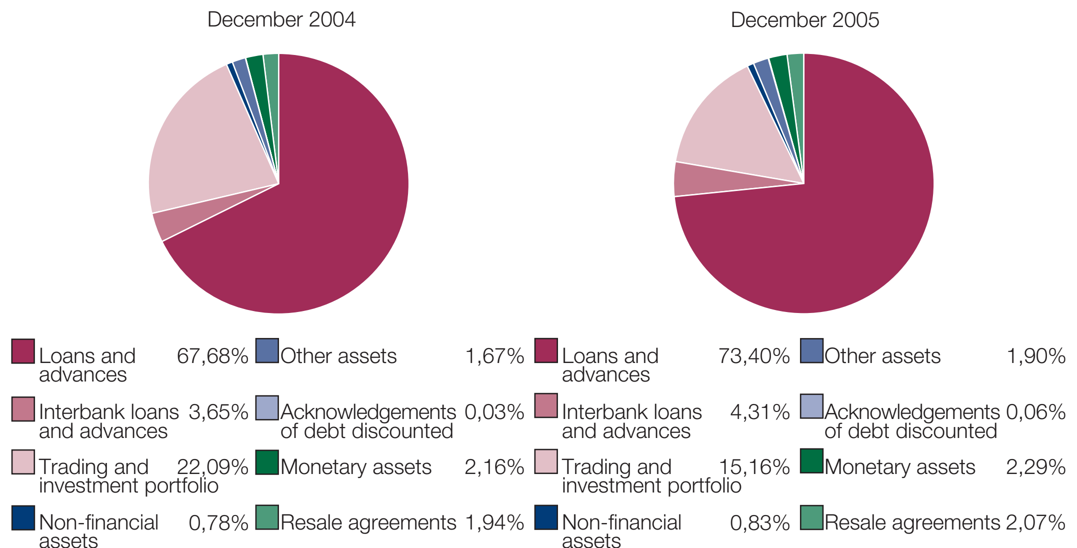
growth in both medium-term deposits and long-term deposits decreased

During 2005, however, growth in both medium-term deposits and long-term deposits decreased. Growth in medium-term deposits decreased from 54,3 per cent in November 2004 to 9,6 per cent in October 2005, whereas growth in long-term deposits decreased from 61,7 per cent in February 2005 to 25,1 per cent in November 2005. The decrease in growth in both medium-term and long-term deposits during the aforementioned periods was due mainly to customers being uncertain about possible interest-rate cuts during 2005 and, consequently, not wanting to be tied into long-term funding positions. By the end of December 2005, however, growth rates of 16,4 per cent and 47,7 per cent had been recorded for medium-term deposits and long-term deposits, respectively.

Other major liabilities of the banking sector as at 31 December 2005 included foreign funding of R56,8 billion (which increased by 24,2 per cent when compared to the December 2004 level of R45,8 billion), capital and reserves of R133,3 billion (which increased by 6,7 per cent when compared to the December 2004 level of R124,9 billion) and interbank funding of R85,6 billion (representing a growth rate of 17,7 per cent when compared to the December 2004 level of R72,8 billion). Other liabilities, on the other hand, decreased to R244,9 billion as at 31 December 2005 (a decrease of 16,3 per cent when compared to the level of R292,8 billion as at the end of December 2004).

Assets

Figure 6: Assets – year-on-year comparison

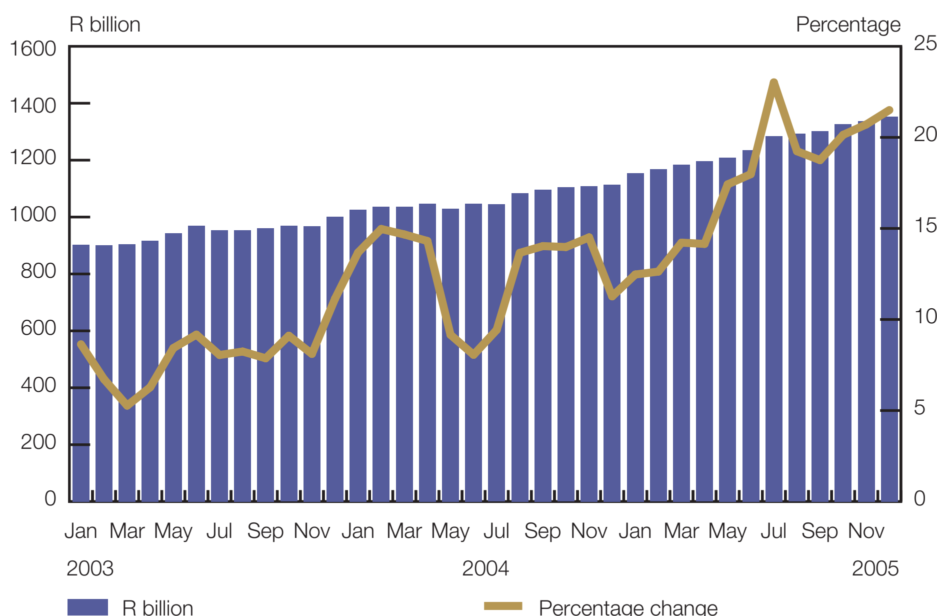


banking sector's assets increased by R179,1 billion

Figure 6 graphically reflects a year-on-year comparison of the composition of assets as at 31 December 2004 and 31 December 2005. The banking sector's assets increased by R179,1 billion (representing a growth rate of 12 per cent) during 2005, to a total of R1 677,5 billion as at the end of December 2005. Factors contributing to this growth were the following:

- Monetary assets (which refer to legal tender in the Republic of South Africa, gold coin, bullion and non-South African currency holdings, and deposits with the South African Reserve Bank) grew by 18,6 per cent, from R32,3 billion as at 31 December 2004 to R38,3 billion as at 31 December 2005.
- Non-bank advances grew by 21,4 per cent, from R1 014,1 billion as at the end of December 2004 to R1 231,4 billion as at the end of December 2005. Growth in non-bank advances was due, amongst other things, to sharp growth in mortgage loans, credit cards and instalments.
- Loans granted under resale agreements increased by 19,2 per cent, from R29,1 billion as at the end of December 2004 to R34,6 billion as at the end of December 2005.
- Trading and investment assets decreased by 23,2 per cent, from R331 billion as at the end of December 2004 to R254,3 billion as at 31 December 2005. The decrease in trading and investment assets was due mainly to marking to market of derivatives.
- Non-financial assets increased by 18,9 per cent, from R11,6 billion as at the end of December 2004 to R13,8 billion as at the end of December 2005.
- Other assets increased by 27,3 per cent, from R25 billion as at the end of December 2004 to R31,8 billion as at the end of December 2005.

Figure 7: Total loans and advances

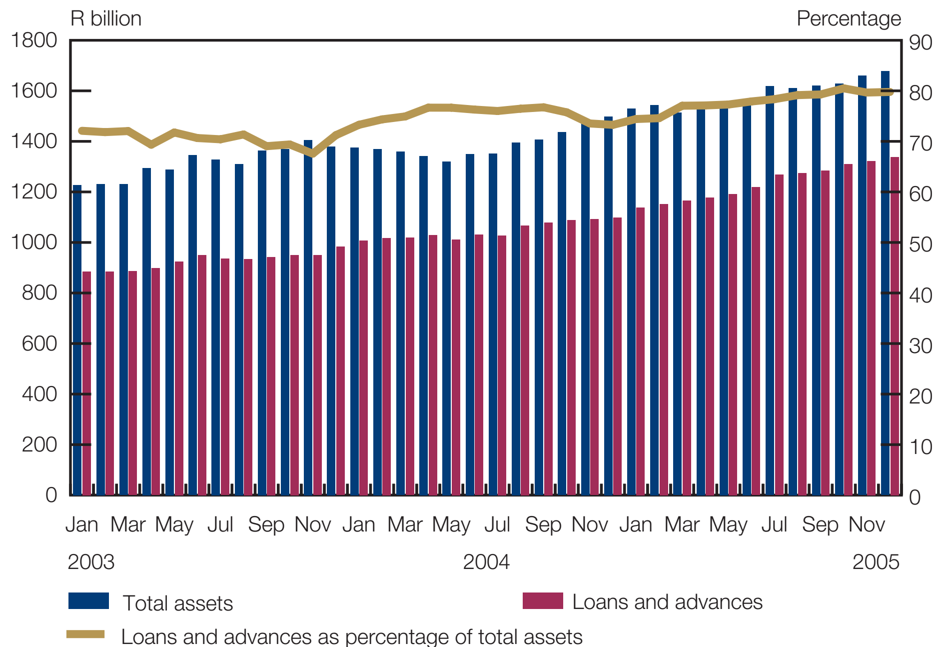


Total loans and advances as at the end of December 2005 equalled R1 353,6 billion, as opposed to R1 114,13 billion as at the end of December 2004. Figure 7 graphically depicts the month-end value of, and percentage growth (measured over 12 months) in, total loans and advances of the banking sector for the past three years. During 2005, growth in total loans and advances increased strongly, from 12,5 per cent in January 2005 to 23 per cent in July 2005, before decreasing slightly, to 18,8 per cent in September 2005. The strong growth in total loans and advances during the first seven months of 2005 was due mainly to growth in mortgage loans, followed by growth in overdrafts and loans and instalment debtors, the peak in July 2005 being due to an increase in the interbank advances, mortgage loans and foreign-currency loans of two A1-rated banks. By the end of 2005, a growth rate of 21,5 per cent had been recorded.

strong growth in total loans and advances during the first seven months of 2005

The gross amounts overdue for the different asset classes during 2005 are depicted in figure 33, in section 4.6.

Figure 8: Loans and advances as a percentage of total assets



Loans and advances as a percentage of total assets increased from 71,2 per cent in December 2003 to 73,3 per cent in December 2004, before increasing throughout 2005 to 80,5 per cent in October 2005. Loans and advances as a percentage of total assets decreased somewhat during the last two months of 2005, to end the year at 79,8 per cent (see figure 8).

Composition of loans and advances

mortgage loans constituted the biggest portion of total loans and advances

The composition of loans and advances is depicted graphically in figure 9. A comparison of the composition of loans and advances in 2004 and 2005 clearly shows that mortgage loans constituted the biggest portion of total loans and advances, followed by overdrafts and loans.

As at the end of December 2005, non-bank loans and advances constituted 73,4 per cent (December 2004: 67,7 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 R217,3 billion (2004: R138,2 billion), representing a growth rate of 21,4 per cent (2004: 15,8 per cent), achieved in respect of non-bank advances during 2005 can be attributed to the following areas (see also figure 10):

– Mortgage loans increased by R116,2 billion, to a level of R522,4 billion, representing an increase of 28,6 per cent. The sharp increase in mortgages during 2005 was due, amongst other things, to South Africa having experienced a lower interest-rate environment from June 2003, as well as increased demand for housing

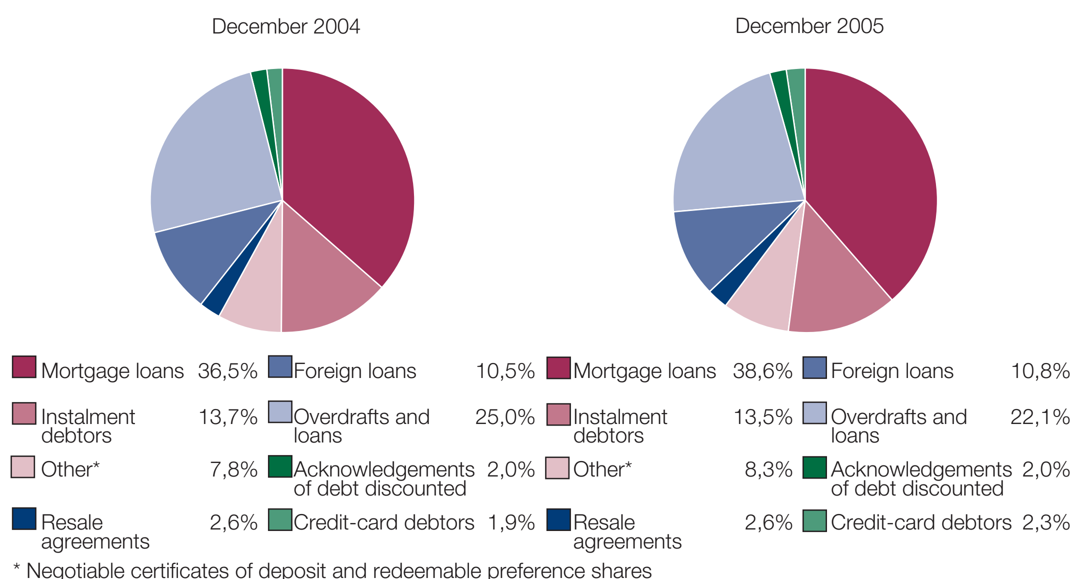
by the previously disadvantaged sector of the population. The strong growth in mortgages from 2003 is clearly depicted in figure 10.

- Overdrafts and loans increased by R19,6 billion, to a level of R298,5 billion, representing a growth rate of 7 per cent. It can be noted from figure 10 that growth in overdrafts and loans was on an increasing trend from September 2004 (2,1 per cent), before declining from 16,3 per cent in July 2005 to 4,2 per cent at the end of November 2005. The initial increase in overdrafts and loans was due mainly to increased demand by customers for overdrafts in view of lower interest rates, whereas the decrease during the latter part of 2005 was due to various corporates' lower appetite for borrowing. The lower utilisation of funding by corporates was due to corporates funding themselves by the issue of their own paper.

lower utilisation of funding by corporates

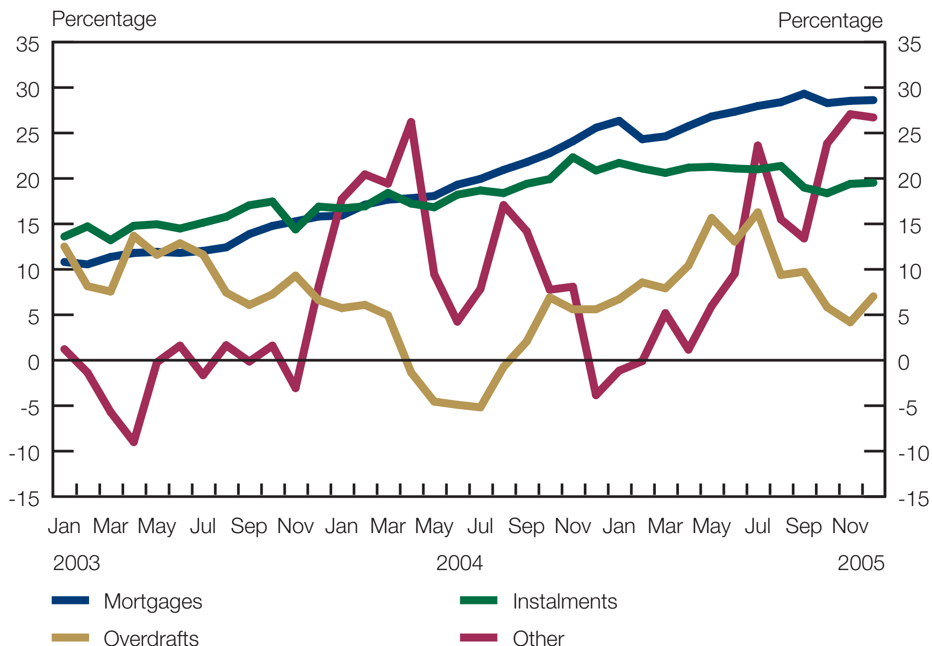
- Instalment debtors increased by R29,8 billion, to a level of R182,2 billion, representing an increase of 19,5 per cent. The strong growth in instalment debtors, which was due mainly to lower interest rates, is clearly depicted in figure 10.
- Foreign-currency loans and advances increased by R28,8 billion, to a level of R145,5 billion, representing an increase of 24,7 per cent. The increased growth in foreign-currency loans and advances was due, amongst other things, to an increased flow of funds between South Africa and foreign centres and factors such as fluctuating and more volatile market conditions.
- Credit cards increased by R10 billion, to a level of R31,2 billion, representing an increase of 47,4 per cent. The sharp growth in credit cards was evidence of the growing borrowing demand by customers resulting from the lower interest-rate environment in South Africa.
- Acknowledgements of debt discounted increased by R5 billion, to a level of R27,5 billion, representing an increase of 22,1 per cent.
- Redeemable preference shares increased by R2,6 billion, to a level of R18,3 billion, representing an increase of 16,2 per cent. An increase in redeemable preference shares was noticeable from May 2005, when an A1-rated bank reported an investment in preference shares as part of a black economic-empowerment transaction.

Figure 9: Composition of loans and advances



* Negotiable certificates of deposit and redeemable preference shares

Figure 10: Growth in selected loans and advances



4.2 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.

For the year under review, the average capital and reserves held by the banking sector amounted to R130,7 billion (R116,5 billion in December 2004), and R122,5 billion (R107,5 billion in December 2004) thereof constituted qualifying capital and reserves for purposes of assessing capital adequacy. The capital-adequacy ratio for the banking sector in total as at the end of December 2005 was 13,3 per cent (2004: 12,7 per cent).

only one bank did not meet the minimum capital-adequacy ratio

An analysis of the percentage distribution of banks in terms of capital adequacy at the end of December 2005 (see figure 11) reveals that only 2,9 per cent (2004: 2,9 per cent) of the total number of banking institutions – in fact, only one bank – did not meet the minimum capital-adequacy ratio of 10 per cent, whereas 37,1 per cent of banking institutions (2004: 45,7 per cent) had capital-adequacy ratios that exceeded 20 per cent.

Banking institutions that reported capital-adequacy ratios of above 20 per cent (that is, 37,1 per cent of institutions) represented only 3,3 per cent of total banking-sector assets (see figure 12). Banking institutions with a capital-adequacy ratio of between 12 per cent and 20 per cent (40 per cent of banking institutions) represented 29 per cent of total banking sector assets, whereas banking institutions with a capital-adequacy ratio of between 10 per cent and 12 per cent (20 per cent of banking institutions) represented the largest portion of total banking sector assets, namely, 67,7 per cent.

Figure 11: Distribution of banks in terms of capital adequacy

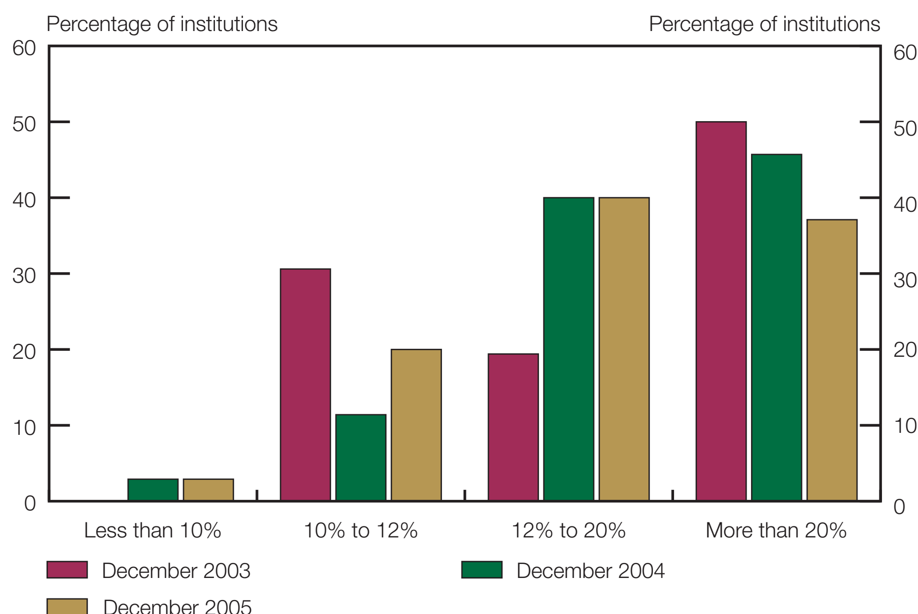


Figure 12: Banks' capital adequacy in terms of total asset value

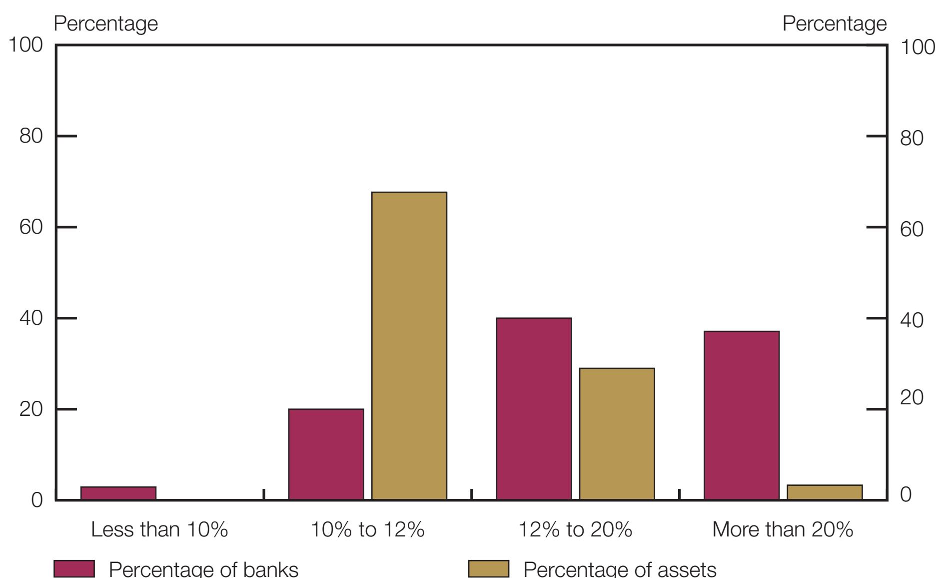
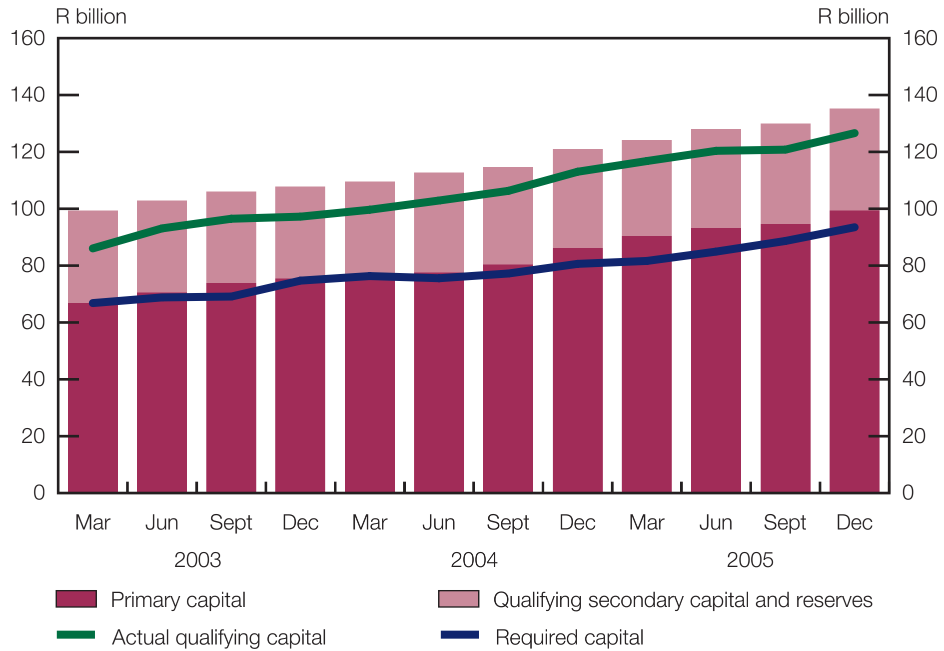


Figure 13 reflects the rand values of the split, over time, between primary and secondary capital, as well as required capital and actual qualifying capital. At the end of December 2005, primary capital and reserves constituted 73,4 per cent (2004: 71,2 per cent) of qualifying capital and reserves before deduction of impairments amounting to R8,7 billion (2004: R8,0 billion). Primary capital and reserves grew by 9,8 per cent (2004: 23,9 per cent) during 2005, to R99,2 billion as at the end of December 2005. The increase in the growth of primary capital and reserves was due to the issue of non-redeemable non-cumulative preference shares and the appropriation of profits by some banks. Secondary capital and reserves increased by 1,4 per cent (2004: 3,3 per cent),

increase in the growth of primary capital and reserves

to R36 billion as at the end of December 2005. Banks continued to hold a buffer in excess of the required capital during 2005.

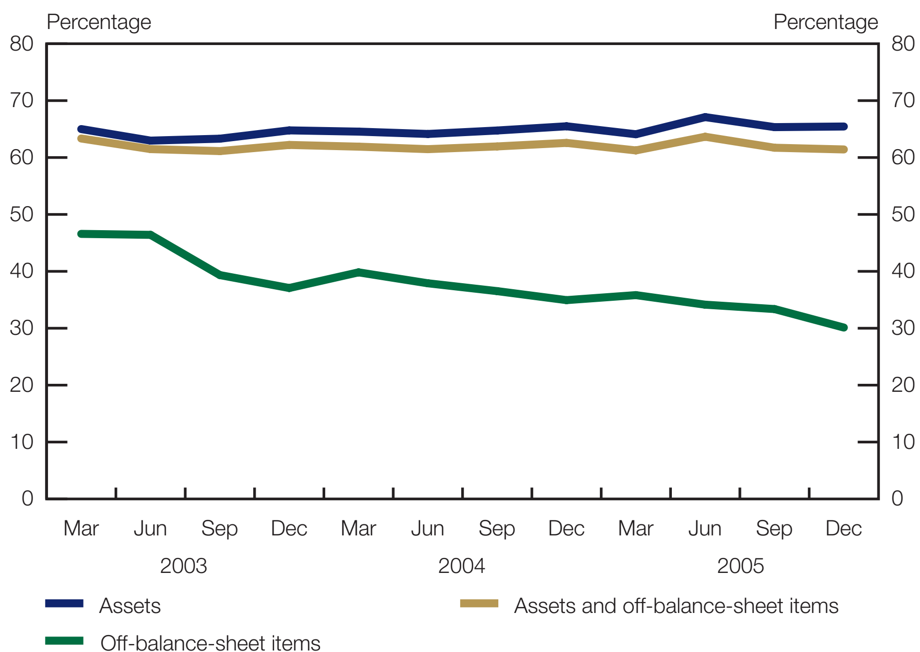
Figure 13: Qualifying capital and reserves



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

Figure 14 graphically depicts the risk-weighted percentages of assets and off-balance-sheet items and of the combined total of assets and off-balance-sheet items. The risk

Figure 14: Risk profile of on- and off-balance-sheet items



weighting of the banking sector's assets decreased slightly, from 65,49 per cent as at the end of December 2004 to 65,45 per cent as at the end of December 2005. The risk weighting of off-balance-sheet items decreased from 34,9 per cent as at the end of December 2004 to 30,1 per cent as at the end of December 2005, owing to strong growth in indemnities and guarantees, together with unutilised facilities, which were assigned to a lower risk-weighting category. As a result of the change in the composition of off-balance-sheet-items, the combined risk weighting of assets and off-balance-sheet items decreased slightly, from 62,6 per cent in 2004 to 61,4 per cent in 2005.

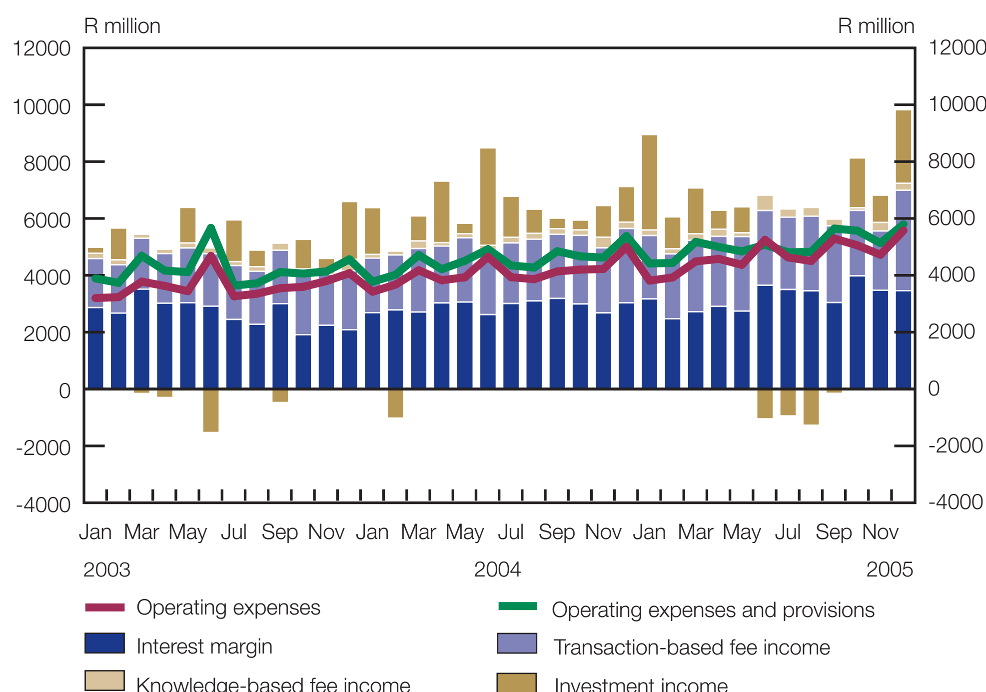
4.3 Profitability

An evaluation of the profitability of banks focuses on an assessment of the quality of income and the long-term sustainability of the activities that generate the income. For this reason, the Bank Supervision Department focuses on the following aspects in its analysis of a bank's profitability:

analysis focuses on the following aspects of a bank's profitability

- Quality of earnings (nature of earnings, that is, whether or not recurring, and the risk sensitivity of earnings).
- Sources of income (such as a fair spread of interest income and non-interest income).
- Nature of income (such as the intermediation function, or trading and advisory activities).
- Integrity of the information.
- Profitability of assets and effectiveness of activities.
- Cost control and cost optimisation.
- Balance between the effort expended on activities and the income generated therefrom.

Figure 15: Composition of the income statement



The total income, that is, net interest turn (that is, interest income less interest expense) plus non-interest income, of the banking sector amounted to R84,4 billion at the end of December 2005, as opposed to R76,6 billion at the end of December 2004. As can be

the intermediation function again constituted the main source of income

seen from figure 15, the intermediation function again constituted the main source of income for banks. The intermediation function generates interest margin (an average of 2,3 per cent of total assets for 2005) and transaction-based fee income (an average of 1,8 per cent of total assets for 2005). The income of R69,1 billion derived from the intermediation function during 2005 was generally sufficient to cover the sum of operating expenses and provisions, which amounted to R60,7 billion. The generation of additional income from investments, including Government stock and Treasury bonds, knowledge-based fee income and income derived from trading and advisory activities, also contributed to the continued profitability of banks. Fee income and investment and trading income as a percentage of total assets were equivalent to 2,0 per cent and 0,6 per cent, respectively, during 2005, as opposed to 1,9 per cent and 0,9 per cent, respectively, during 2004.

interest margin increased by 10,6 per cent

For the year 2005, interest expense increased by about 9,8 per cent, whereas interest income increased by 10,1 per cent. The net result thereof was that the interest margin increased by 10,6 per cent, whereas it increased by 9,1 per cent in 2004. The main components of interest expense were interest in respect of demand deposits at 27,4 per cent of the total interest expense (2004: 28,2 per cent) and interest in respect of fixed and notice deposits at 31,7 per cent of the total interest expense (2004: 34 per cent). Interest derived from mortgage bonds and overdrafts and loans constituted 36,5 per cent and 25,1 per cent, respectively, of total interest income during 2005, as opposed to 35,4 per cent and 26,5 per cent, respectively, during 2004.

Figure 16: Interest margin

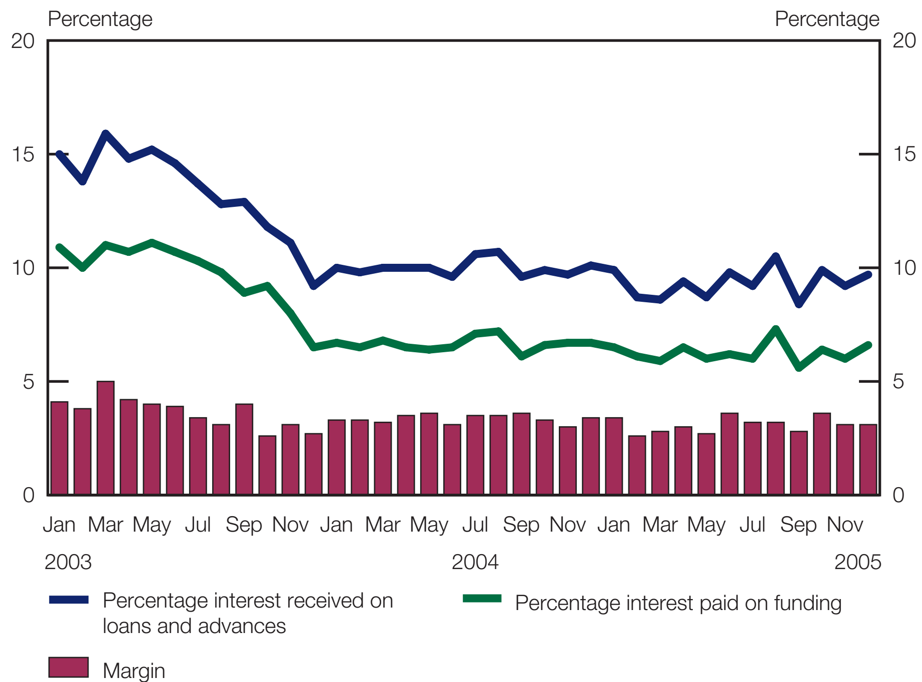


Figure 16 graphically depicts the interest margin of the banking sector for the period from January 2003 to December 2005, whereas figure 17 depicts the percentage-point change in the components of the interest margin for the aforementioned period. The interest margin for the year was on average lower in 2005 than in 2004. By the end of December 2005, the interest margin was 3,1 per cent, compared to 3,4 per cent in 2004 and 2,7 per cent in 2003. The margin of 2,6 per cent at the end of February

2005 was affected mainly by February being a short month. The margin of 2,8 per cent at the end of September 2005 was affected by the refinement of reporting by an A1-rated bank. An analysis of the relative monthly percentage-point change in the underlying components, as well as in the interest margin (see figure 17), displayed clear cyclical tendencies.

Figure 17: Percentage-point change in interest margin

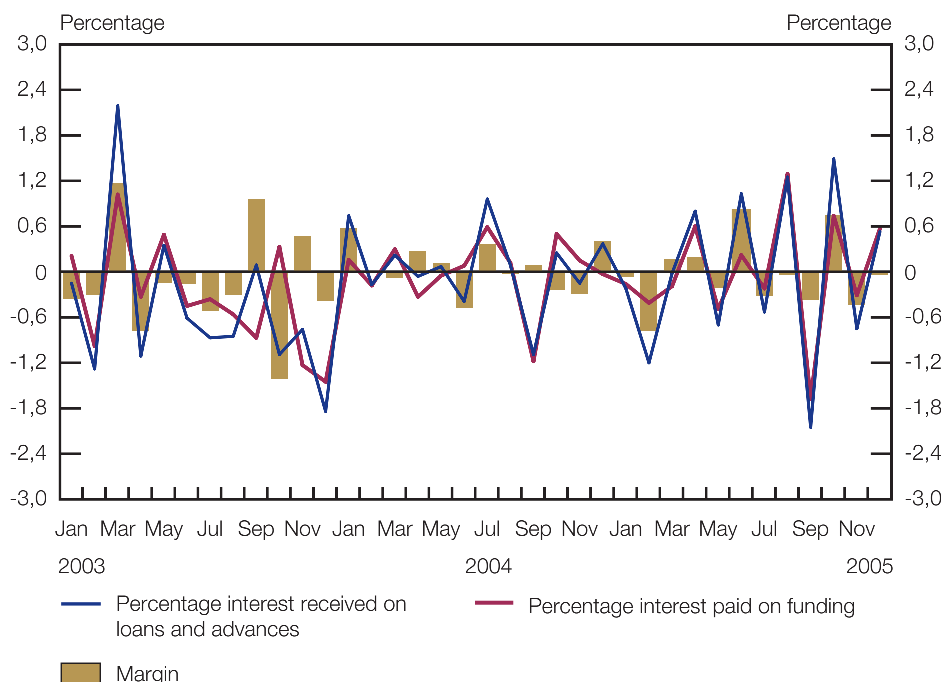
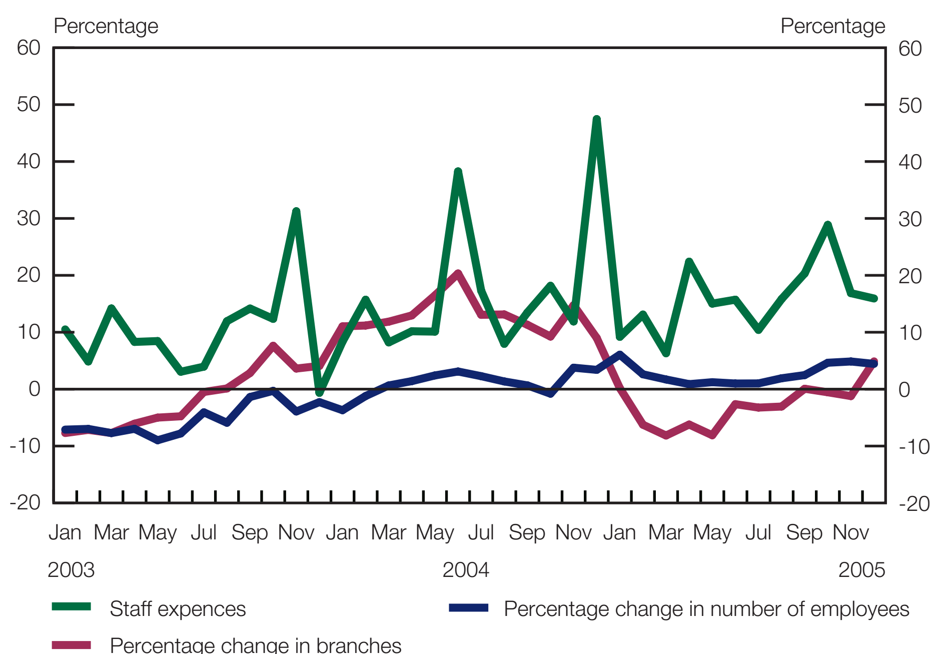


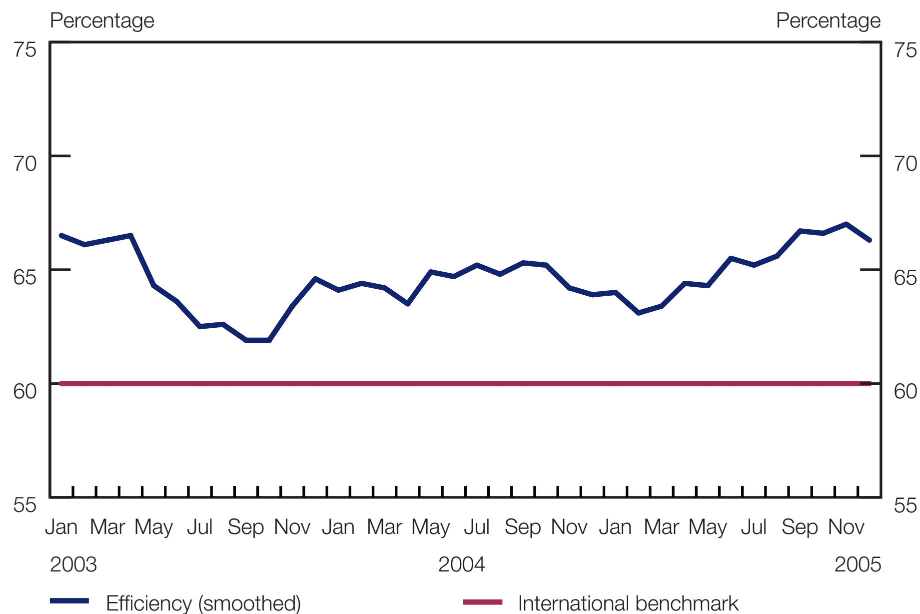
Figure 18: Growth in staff expenses, number of employees and number of branches



operating expenses increased

The operating expenses of the total banking sector increased by 14,6 per cent in 2005 (12,5 per cent in 2004), mainly as a result of an increase of 16 per cent in total staff expenses, which accounted for about 57,1 per cent (2004: 55,4 per cent) of total operating expenses. The increase in staff expenses was due mainly to, amongst other things, bonuses paid out during the year and an increase in the number of specialised personnel in some banks. Figure 18, graphically depicts 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 2005, the number of employees in the banking sector increased by 2,7 per cent, whereas the number of branches decreased by 2,8 per cent, as opposed to an increase of 1,1 per cent in the number of employees and an increase of 12,8 per cent in the number of branches during 2004. An increase in administrative expenses also contributed to the growth in operating expenses. In 2005, administrative expenses increased by 14,1 per cent and accounted for 40,4 per cent (2004: 40,6 per cent) of total operating expenses.

Figure 19: Efficiency ratio of South African banking sector

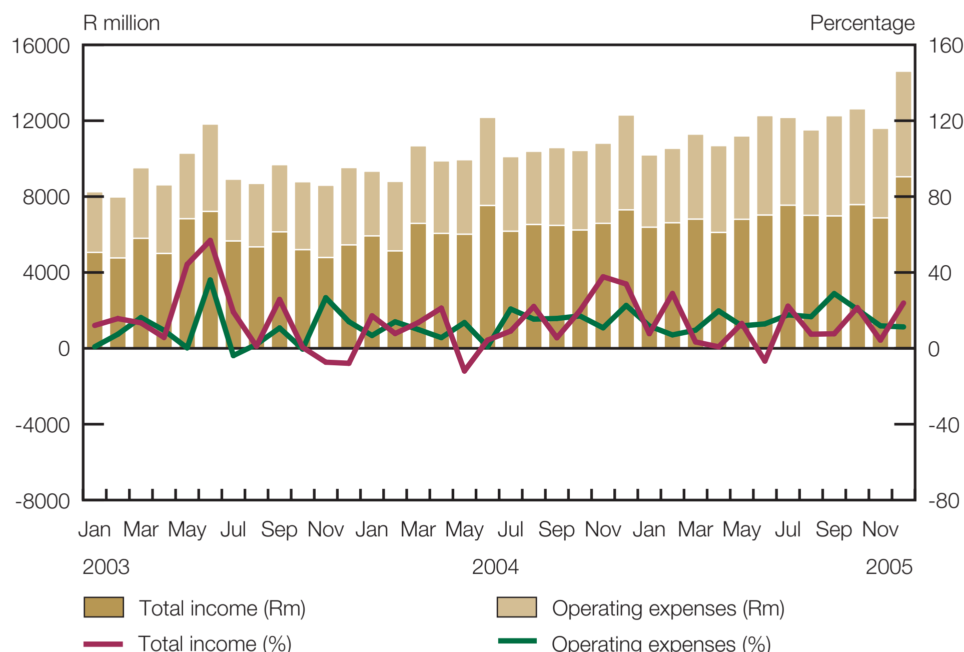


A widely used indicator of the efficiency of the banking sector is the ratio, expressed as a percentage, of operating expenses to total income. The lower the ratio is, the more efficient a bank is considered to be. Currently, it is considered desirable for the ratio to be 60 per cent, and a ratio of below 50 per cent is considered to indicate a highly efficient institution.

the efficiency ratio deteriorated

Figure 19 reflects the efficiency ratio of the South African banking sector for the past three years. Smoothed over a 12-month period, the efficiency ratio of the banking sector deteriorated from 63,9 per cent in December 2004 to 66,3 per cent in December 2005. The deterioration in the efficiency ratio in December 2005, compared to December 2004, can be attributed to the increased operating expenses of some banks relating to, amongst other things, information-technology system changes and personnel costs. Operating expenses increased from R5 billion at the end of December 2004 to R5,6 billion at the end of December 2005.

Figure 20: Determinants of efficiency ratio



The actual values of, and the percentage growth (smoothed over a 12-month period) in, the determinants of the efficiency ratio are graphically illustrated in figure 20. Growth of 14,6 per cent in operating expenses offset the increase of 10,7 per cent in total income, resulting in a decline in the efficiency ratio for the banking sector (see figure 19) during 2005.

Figure 21: Efficiency ratio of banking institutions according to asset size – December 2005

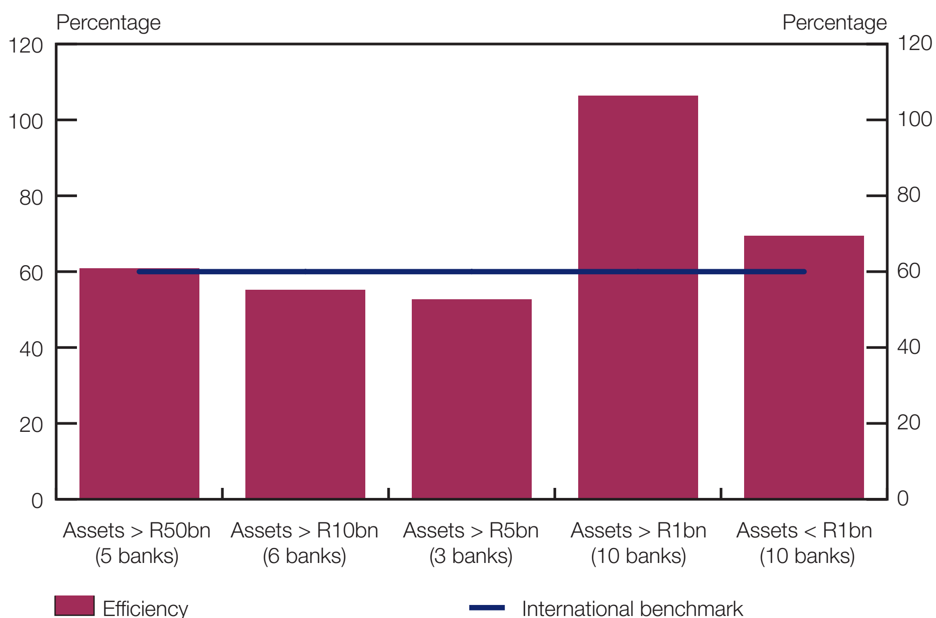
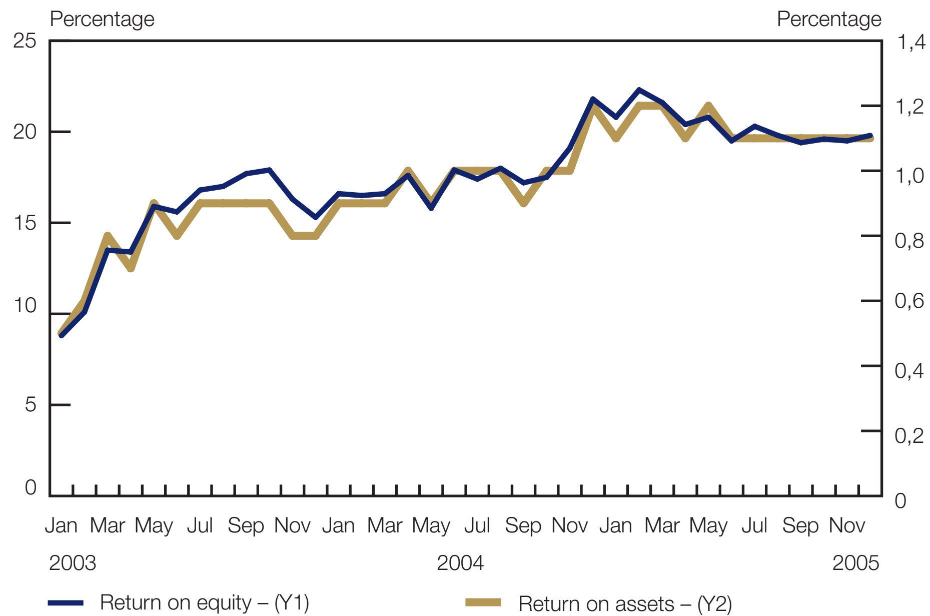


Figure 21 graphically depicts the efficiency ratio of the various categories (according to asset size) of banking institution for the year ended December 2005. The graph shows that, in December 2005, banks with assets of above R5 billion, but below R10 billion, were the most efficient, with an efficiency ratio of 52,7 per cent, followed by banks with assets above R10 billion, but below R50 billion (55,2 per cent). The least efficient were banks with asset values of above R1 billion, but below R5 billion (106,4 per cent), mainly as a result of continuing high costs relating to start-up operations having been reported by some banks. 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 will fluctuate accordingly.

Figure 22: Profitability (12-month smoothed average)

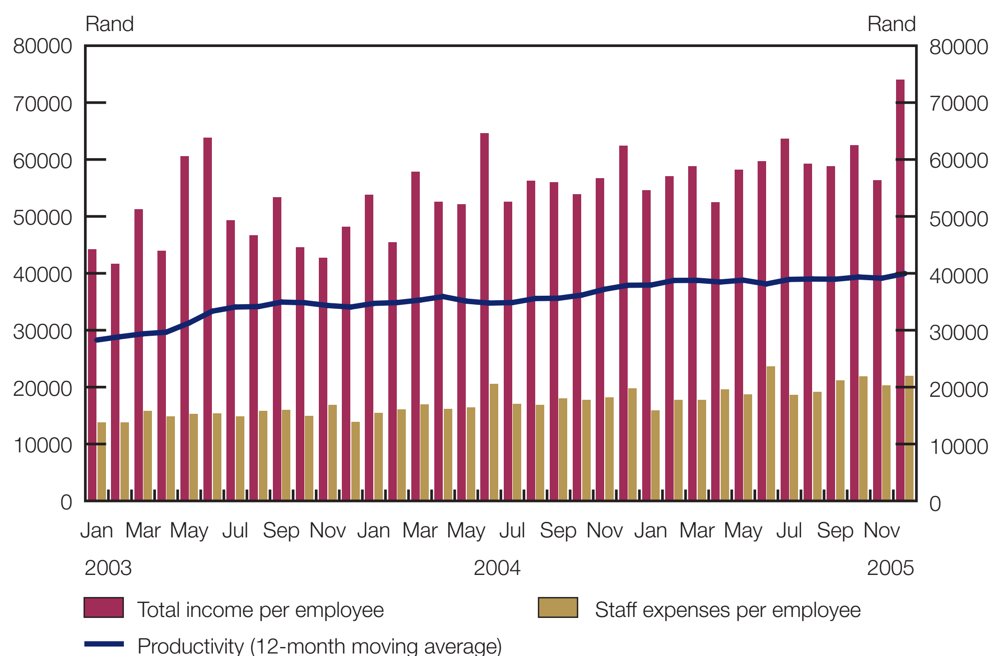


gradual decrease in both the ROE and the ROA

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 depicted graphically in figure 22. The gradual decrease in both the ROE and the ROA during 2005 resulted from a decrease in net income after tax having been recorded during 2005. The said decrease resulted mainly from higher operating expenses having been recorded during 2005, as mentioned earlier. For 2005, an after-tax return of approximately 1,1 per cent on total assets (2004: 1,2 per cent) was reported, whereas an after-tax return of approximately 14,5 per cent on net qualifying capital and reserves (2004: 14,7 per cent) was reported. The banking sector achieved a before-tax return of approximately 1,48 per cent on total assets (2004: 1,5 per cent).

Productivity can be measured by comparing the expenditure on employees with the amount of income generated. Figure 23 graphically depicts the productivity of the banking sector for the past three years. During 2005, the total income generated per employee was on average R59 679, as opposed to R55 362 in 2004. In 2005, the average staff expenses per employee, on the other hand, were R19 715 (2004: R17 461). Also reflected in figure 23 is the average (smoothed over a 12-month period) net income generated per employee. The net income generated per employee was R39 964 in 2005, as opposed to R37 900 in 2004.

Figure 23: Productivity



4.4 Liquidity risk

Liquidity risk is the risk that an entity will not have sufficient liquid resources available to meet commitments as they become due or the risk that an entity will encounter difficulty in liquidating assets.

An evaluation of liquidity-risk management involves an analysis of the short-term liquidity mismatch in relation to total funding and the trend thereof, an assessment of the sources of liquid funds available for funding such mismatches and a consideration of the volatility of the funding sources available.

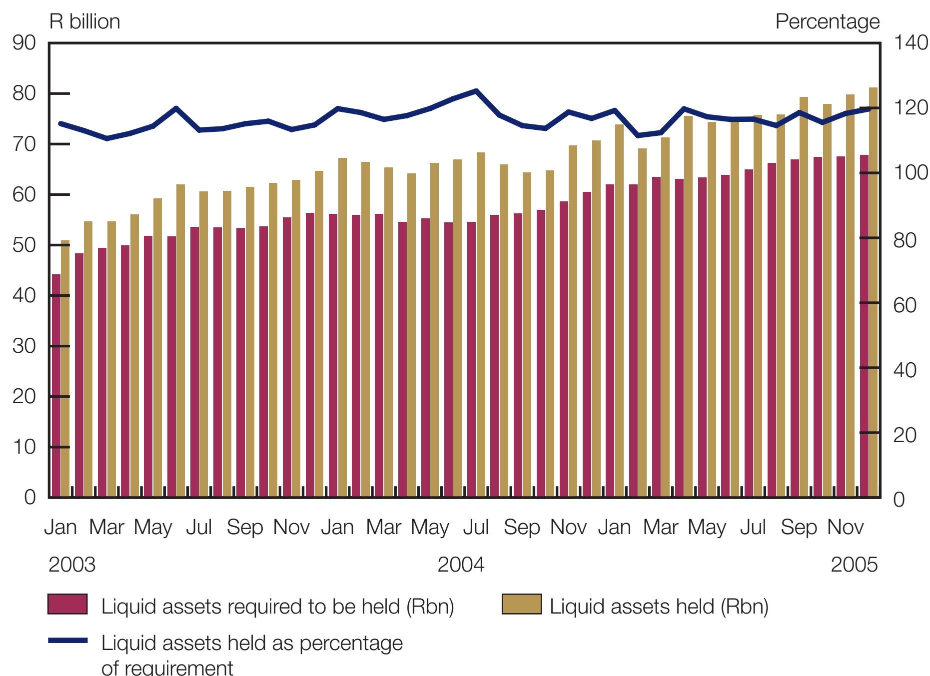
Statutory liquidity

The liquid-asset requirement is calculated on total liabilities less capital and reserves (referred to as adjusted liabilities). The total liabilities are adjusted, owing to the use of cash-management schemes by banks' clients and the setting off of some asset balances against liability balances. Figure 24 shows that the average daily amount of liquid assets held by banks exceeded the statutory liquid-asset requirement throughout 2005. For the month of December 2005, the average daily amount of liquid assets held represented 119,7 per cent of the statutory liquid-asset requirement, compared to 116,8 per cent for December 2004.

liquid assets held exceeded the statutory liquid-asset requirement

Approximately 46,8 per cent (2004: 54,4 per cent) of the average daily amount of liquid assets held during December 2005 consisted of securities issued by virtue of section 66 of the Public Finance Management Act, 1999, whereas 32,3 per cent (2004: 28,4 per cent) consisted of Treasury bills of the Republic of South Africa, and 1 per cent (2004: 1,1 per cent) consisted of short-term bills issued by the Land Bank. Cash-management schemes managed on behalf of banks' clients decreased by about 13,2 per cent (2004: 18,1 per cent). Set-off decreased by 48,8 per cent (2004: 50,4 per cent), measured over a 12-month period, as at the end of December 2005 and represented approximately 11 per cent (2004: 11,2 per cent) of adjusted liabilities.

Figure 24: Statutory liquid assets – actual versus required



Volatility of funding

total wholesale deposits constituted 93,2 per cent of total wholesale and retail deposits

As at 31 December 2005, total wholesale deposits constituted 93,2 per cent (2004: 94,8 per cent) of total wholesale and retail deposits. As can be seen from figure 25, wholesale deposits shorter than three months as a percentage of total funding decreased substantially, from 57,5 per cent in March 2005 to 46,8 per cent in April 2005 and from 41,7 per cent in September 2005 to 37,4 per cent in October 2005. The decreases were due mainly to a change in the reporting of wholesale deposits from a contractual to an anticipated basis, in line with the regulatory requirements, by two A1-rated banks. By the end of December 2005, wholesale deposits shorter than three months represented 37,8 per cent of total funding.

During 2005, the aggregate amount of the funding provided by the 10 largest depositors of individual banks averaged R244,5 billion (2004: R194,2 billion). The 10 large depositors constituted 18 per cent (2004: 17,1 per cent) of the aggregate amount of total funding-related liabilities to the public at the end of December 2005.

Short-term wholesale deposits (nil to 31 days) represented 24,5 per cent of total funding in December 2005, as opposed to 43,9 per cent for December 2004 (see figure 26). As at the end of December 2005, wholesale deposits shorter than seven days and wholesale deposits between eight and 31 days represented 16,8 per cent and 7,7 per cent, respectively, of total funding. As can be seen in figure 26, wholesale deposits shorter than three months, categorised according to sight to seven days, eight to 31 days and nil to 31 days as a percentage of total funding decreased substantially in April 2005 and October 2005. The decreases were due mainly to a change in reporting from a contractual to an anticipated basis by two A1-rated banks, as mentioned previously.

Figure 25: Wholesale deposits shorter than three months and large depositors

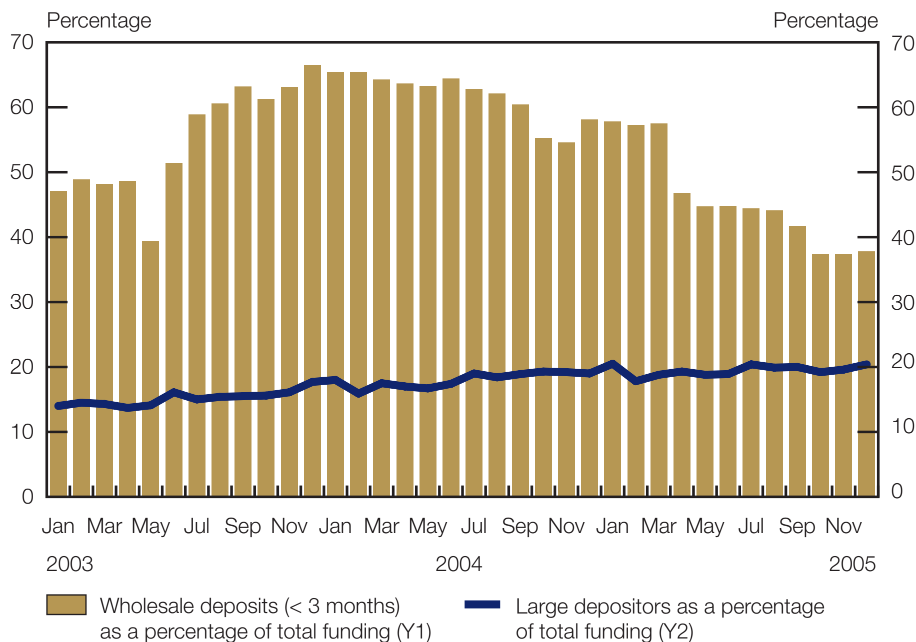


Figure 26: Short-term wholesale deposits

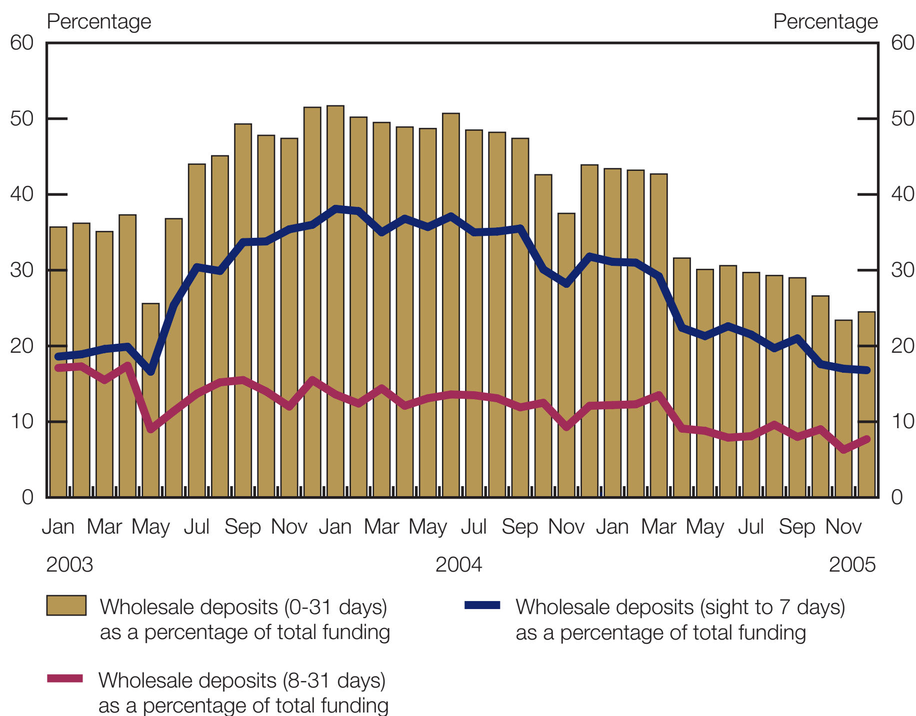
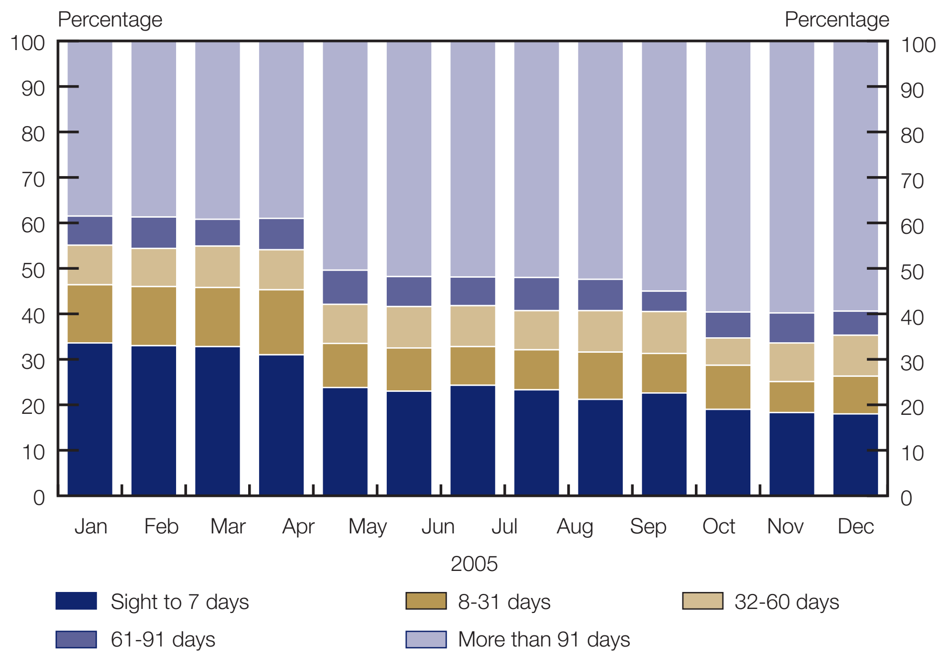


Figure 27 depicts the composition (measured over a 12-month period) of wholesale deposits according to maturity for 2005. Wholesale deposits with a maturity greater than 91 days and wholesale deposits with a maturity shorter than seven days

constituted the largest portion of wholesale deposits in December 2005, namely, 59,5 per cent and 18 per cent, respectively. Wholesale deposits with a maturity of 32 to 60 days constituted only a small portion of total wholesale deposits, namely 9 per cent, followed by deposits with a maturity of eight to 31 days, which constituted 8,3 per cent of total wholesale deposits. Wholesale deposits with a maturity of 61 to 91 days constituted the smallest portion of total wholesale deposits, namely, 5,3 per cent. The noticeable decrease in wholesale deposits (sight to seven days) relates to a change in the reporting of wholesale deposits from a contractual to an anticipated basis by two A1-rated banks, as mentioned previously.

Figure 27: Composition of wholesale deposits according to maturity



4.5 Market risk

Market risk is the risk of loss arising from movements in market prices or rates away from the rates or prices set out in a transaction or agreement. This section, however focuses on derivatives, which derive much of their value from an underlying product.

turnover in derivatives generally fluctuated

Turnover in derivatives, excluding forward contracts, generally fluctuated during 2005. Total actual turnover in derivative contracts, excluding forward contracts, increased from R475,8 billion for the month of January 2005 to R840,7 billion for the month of August 2005, before declining to R728,9 billion for the month of December 2005. The increase in August 2005 was mainly driven by, amongst other things, high market expectations of a rate increase, market opportunities and increased customer flows. The decrease in December 2005 was due largely to the general year-end slowdown in activity in the derivative markets.

As can clearly be seen from figure 28, forward contracts contributed to the largest portion of total turnover in derivative instruments and increased from R1 442,5 billion in January 2005 to R2 172,5 billion in August 2005, but decreased to R1 346 billion in December 2005.

Figure 28: Turnover in derivative contracts

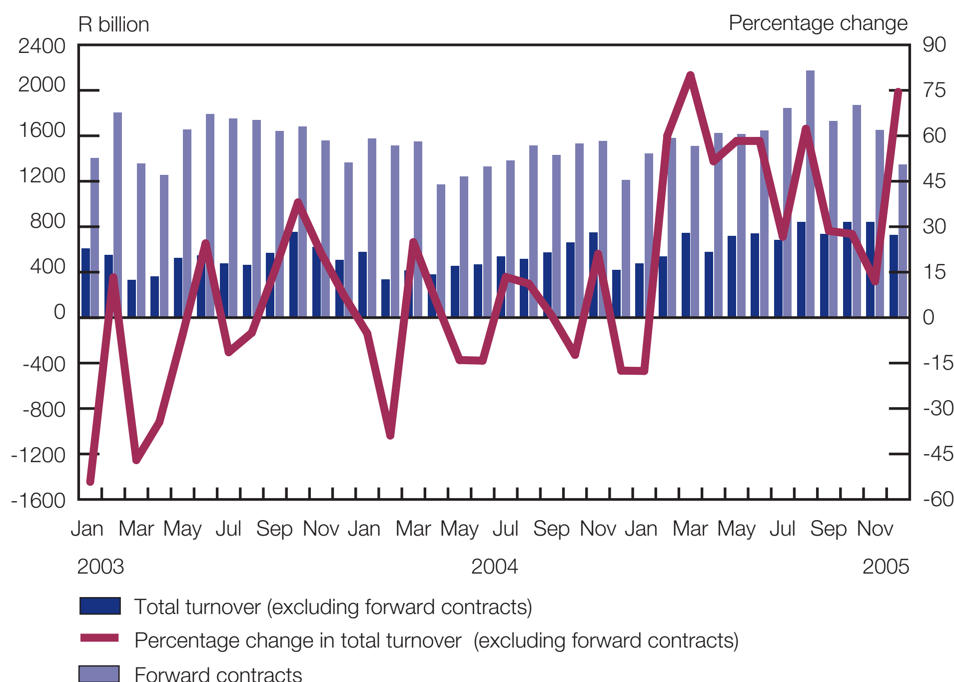
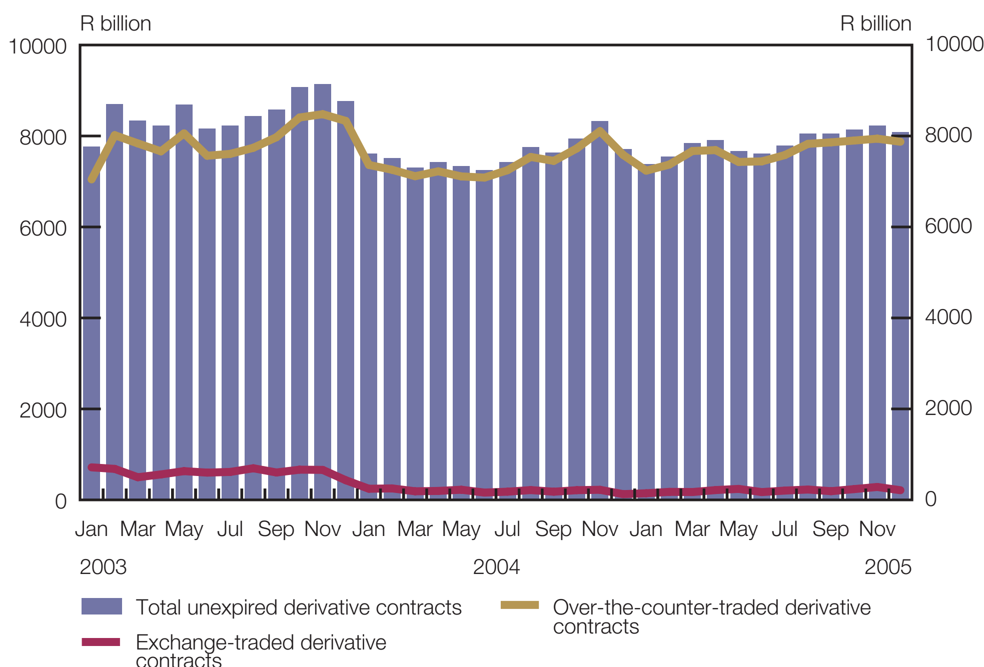


Figure 29 reflects the gross nominal value of and growth in total unexpired derivative contracts. Total unexpired contracts consist mainly of over-the-counter(OTC)-traded derivative contracts and a small amount of exchange-traded derivative contracts.

Figure 29: Total unexpired derivative contracts



During 2005, total unexpired derivative contacts increased from R7 383,3 billion in January 2005 to R8 086 billion in December 2005, as a direct result of the growth in unexpired OTC-traded derivative contracts, which increased from R7 237,8 billion in

January 2005 to R7 873,4 billion in December 2005. Unexpired exchange-traded derivative contracts increased from R145,5 billion in January 2005 to R212,6 billion in December 2005.

As at the end of December 2005, unexpired OTC-traded derivative contracts accounted for 97,4 per cent (2004: 98,4 per cent) of total unexpired derivative contracts, whereas unexpired exchange-traded contracts accounted for 2,6 per cent (2004: 1,6 per cent) of total unexpired derivative contracts. The total value of unexpired derivative contracts represented 482 per cent of total assets as at the end of December 2005 (December 2004: 514,7 per cent).

4.6 Credit risk

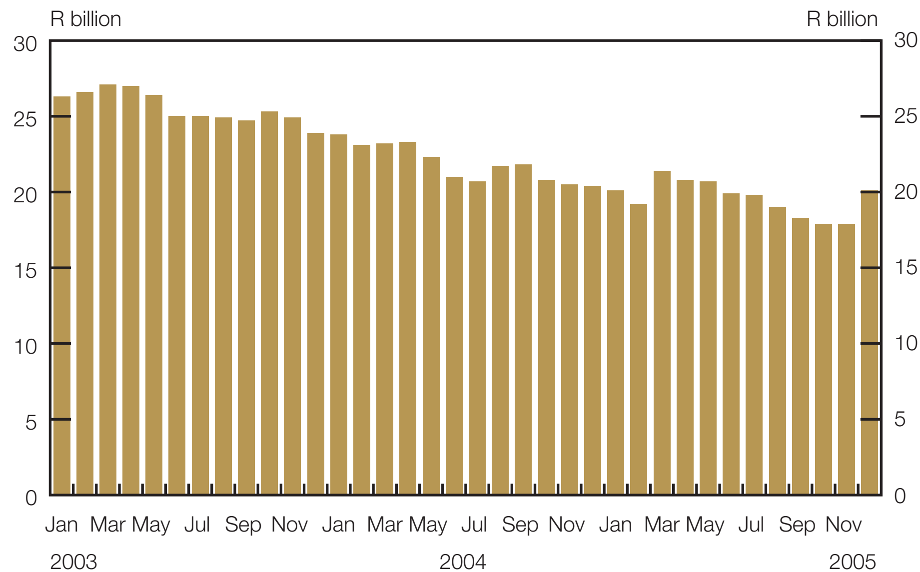
Credit risk is the risk that a party to a contractual agreement or transaction will be unable to meet its obligations or will default on commitments.

enhanced asset growth in core products

As mentioned in section 4.1 above, banks experienced enhanced asset growth in their core products during 2005, mortgages, instalments and overdrafts being the main products, owing mainly to favourable economic conditions. These growing credit portfolios were generally well managed by banks, as evidenced by the level of total overdues.

Analysis of overdue amounts

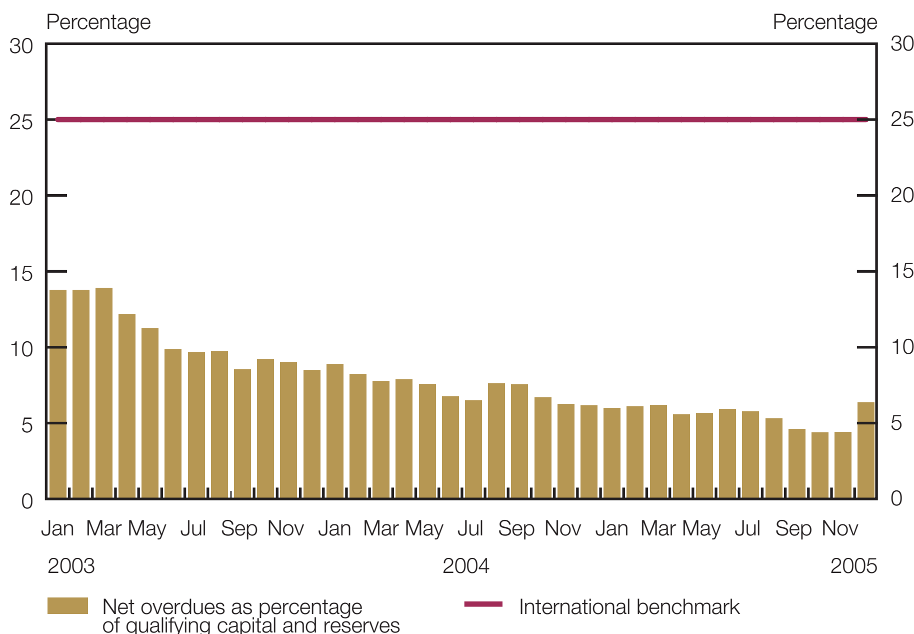
Figure 30: Total banking-sector overdues



total gross overdues continued to decrease

Figure 30 graphically depicts the level of total gross overdues of the banking sector for the period from January 2003 to December 2005. During 2005, total gross overdues continued to decrease, from R20,4 billion in December 2004 to R20,1 billion in December 2005, although total gross overdues increased noticeably during March 2005 and December 2005. The increase in March 2005 was due to a reporting correction by a large bank, whereas the increase in December 2005 was due mainly to a change in reporting, resulting from system developments to reflect a consolidated “per person” classification of credit risk, replacing “per account” reporting, in line with the requirements of regulation 28 of the Regulations relating to Banks.

Figure 31: Net overdues as a percentage of net qualifying capital and reserves



The ratio of net overdues (that is, gross overdues less specific provisions) to net qualifying capital and reserves is an indicator of the extent to which credit risk has materialised. As at the end of December 2005, net overdues amounted to R8,2 billion (2004: R7,3 billion), and specific provisions amounted to R11,9 billion (2004: R13,1 billion).

Figure 31, which depicts this ratio for the past three years, indicates that net overdues as a percentage of net qualifying capital and reserves decreased from 6,2 per cent in December 2004 to 4,4 per cent in November 2005. By the end of December 2005, however, this ratio had increased to 6,4 per cent, owing to the above-mentioned increase in total overdues in that month resulting from the change in reporting to reflect the regulatory “per person” credit-risk classification.

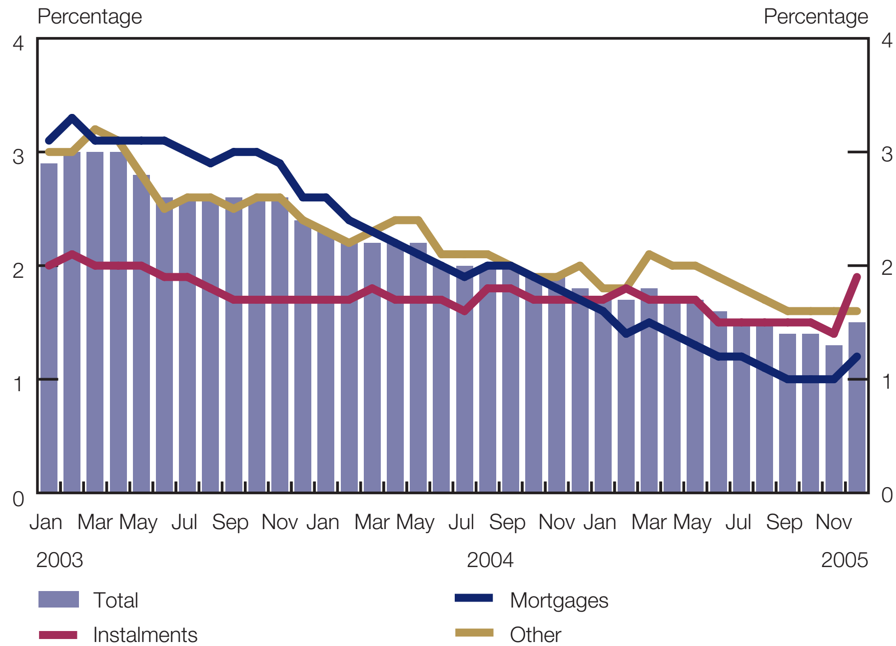
Expressed as a percentage of total loans and advances, gross amounts overdue improved from 1,8 per cent in December 2004 to 1,3 per cent in November 2005, before increasing to 1,5 per cent in December 2005 as a result of the previously mentioned change in reporting to reflect the regulatory “per person” credit-risk classification. The increase in March 2005 (1,8 per cent) was due to a reporting correction by a large bank, as mentioned previously.

mortgage loans overdue improved substantially

From December 2004 to November 2005, mortgage loans overdue (as a percentage of total mortgage loans) improved substantially, from 1,7 per cent to 1 per cent. During March 2005 and December 2005, however, mortgage loans overdue (as a percentage of total mortgage loans) increased to 1,5 per cent and 1,2 per cent, respectively, for the reasons mentioned previously.

Other loans and advances overdue (as a percentage of total other loans and advances) increased from 2 per cent in December 2004 to 2,1 per cent in March 2005, before decreasing to 1,6 per cent in December 2005. The sharp increase in March 2005 was due to a reporting correction by a large bank.

Figure 32: Composition of overdues (as a percentage of loans and advances)



Instalment sales overdue (as a percentage of total instalment sales) improved from 1,7 per cent in December 2004 to 1,4 per cent in November 2005, before increasing significantly to 1,9 per cent in December 2005. The sharp increase during December 2005 was due to the previously mentioned change in reporting to reflect the regulatory "per person" credit-risk classification.

Figure 33: Analysis of overdue accounts

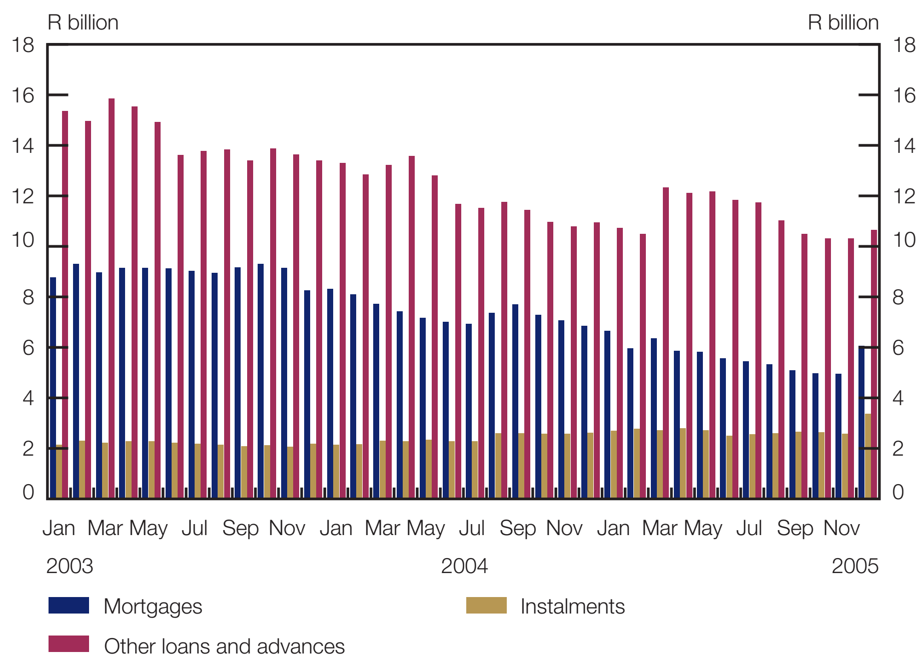
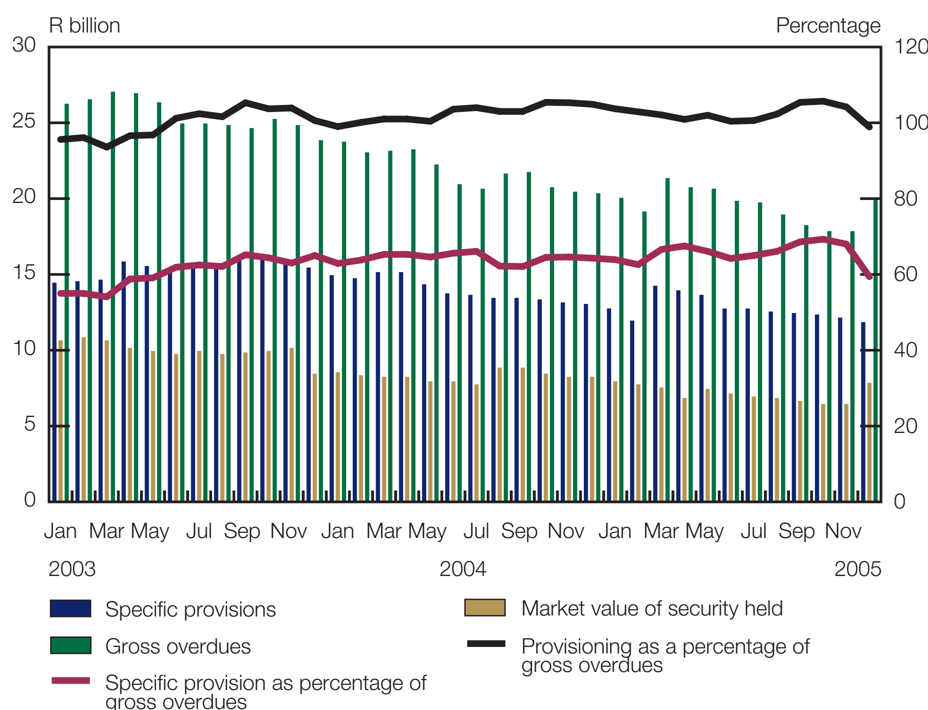


Figure 33 graphically depicts an analysis of the gross amounts overdue for the different asset classes from January 2003 to December 2005. The gross overdues in respect of other loans and advances decreased from R11 billion in December 2004 to R10,7 billion in December 2005. The noticeable increases during March 2005 (R12,3 billion) and December 2005 were due to the reasons mentioned previously. Mortgage accounts overdue decreased from R6,9 billion in December 2004 to R5 billion in November 2005, before increasing to R6,1 billion in December 2005, whereas instalment accounts overdue remained fairly stable, at approximately R2,6 billion, from December 2004 to November 2005, before increasing to R3,4 billion in December 2005. The increases in mortgage accounts overdue and instalments accounts overdue were due mainly to the reasons mentioned previously.

Provisioning policy for bad and doubtful loans and advances

Figure 34: Adequacy of provisions



provisions remained adequate

Figure 34 indicates that provisions by banks remained adequate throughout 2005. By the end of December 2005, specific provisions amounted to 59,4 per cent of all overdues (December 2004: 64,3 per cent). Total specific provisions and the market value of security held as a percentage of total overdues decreased from 104,9 per cent in December 2004 to 98,9 per cent in December 2005. The decrease in December 2005 was due to an increase in total overdues in December 2005, resulting from a change in reporting, as explained previously, which ultimately resulted in the ratio decreasing.

As at the end of December 2005, specific provisions per asset class, expressed as a percentage of overdue amounts, were as follows:

- Mortgages - 31,5 per cent (36 per cent on 31 December 2004).
- Instalment sales - 56,8 per cent (56,8 per cent on 31 December 2004).
- Other loans and advances - 76,1 per cent (83,7 per cent on 31 December 2004).

Figure 35: Specific provisions as percentage of total overdues

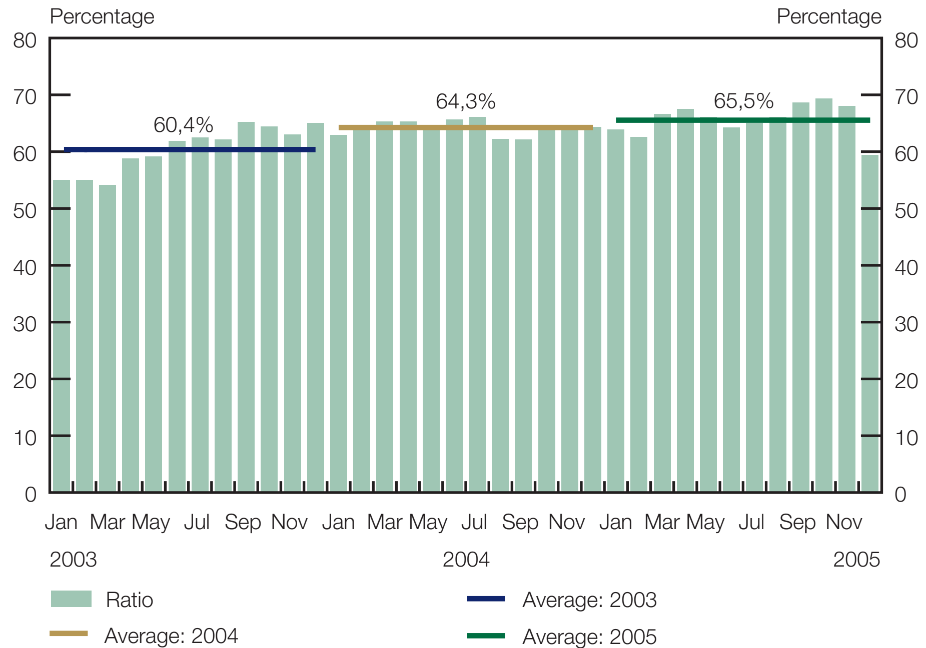
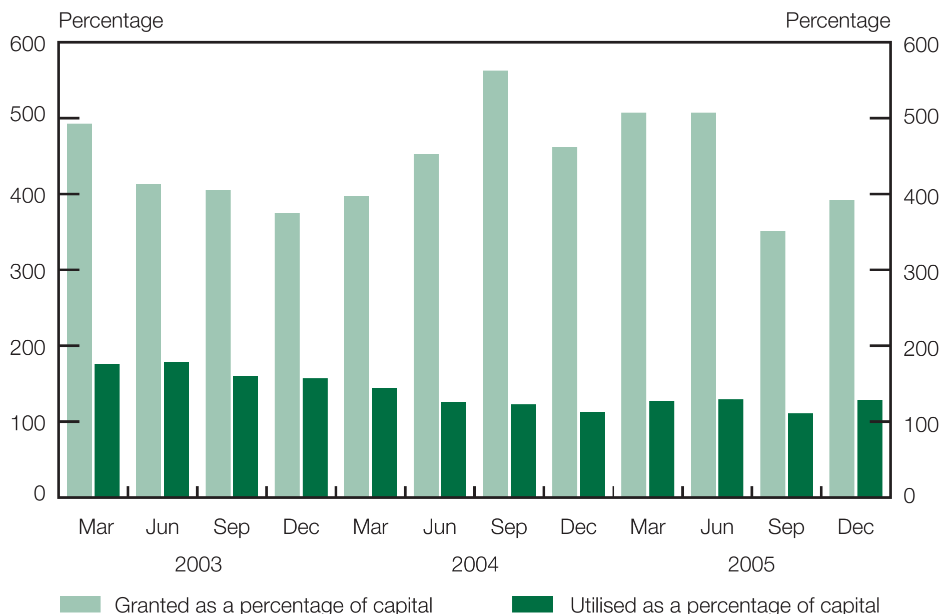


Figure 35 graphically depicts the relationship of specific provisions to total gross overdues from January 2003. On average, specific provisions amounted to 65,7 per cent of overdues during 2005 (2004: 64,3 per cent). Specific provisions as a percentage of total overdues, however, decreased from 68 per cent in November 2005 to 59,4 per cent in December 2005, owing to an increase in total overdues in December 2005, which ultimately resulted in the ratio decreasing.

Figure 36: Large exposures granted and utilised as a percentage of capital



Large exposures

In terms of section 73(1)(b) of the Banks Act, 1990, exposures granted that exceed 10 per cent of capital and reserves (referred to as large exposures) should not exceed, in total, 800 per cent of net qualifying capital and reserves, and any single exposure granted and exceeding 25 per cent should be an impairment against the capital of the bank. 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 other things, exposures to Government and other banks.

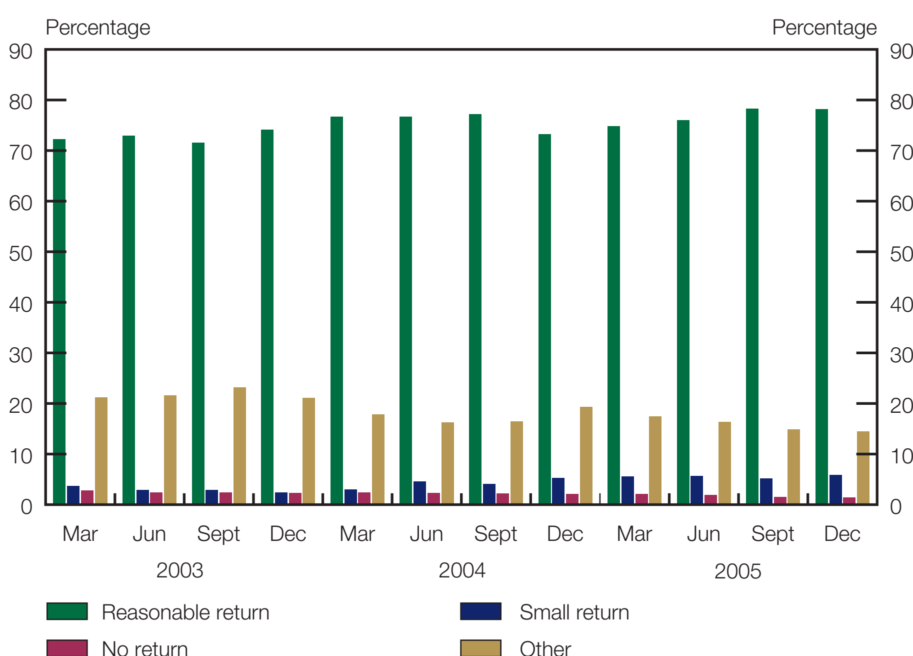
The large exposures granted and utilised during the period from March 2003 to December 2005 are depicted graphically in figure 36. Large exposures granted decreased from 461,8 per cent of net qualifying capital and reserves in December 2004 to 391,7 per cent in December 2005. The decrease in large exposures granted from June 2005 to September 2005 was due mainly to banks aligning unutilised facilities with utilised facilities. Large exposures utilised increased from 113 per cent of net qualifying capital and reserves in December 2004 to 128,8 per cent in December 2005.

decrease in large exposures granted

Quality of assets

Figure 37 graphically depicts that about 78,2 per cent of the banking sector's assets (December 2004: 73,3 per cent) earned a reasonable return, whereas 5,8 per cent (December 2004: 5,3 per cent) earned a small return, and the remaining 16 per cent (December 2004: 21,4 per cent) earned no return. The increase in the reasonable-return category and the decrease in the no-return category were due mainly to a general improvement in credit-risk ratios during 2005. Although favourable economic conditions, such as lower interest rates and improved economic growth, will impact positively on asset quality, the challenge remains to maintain asset quality when economic conditions deteriorate.

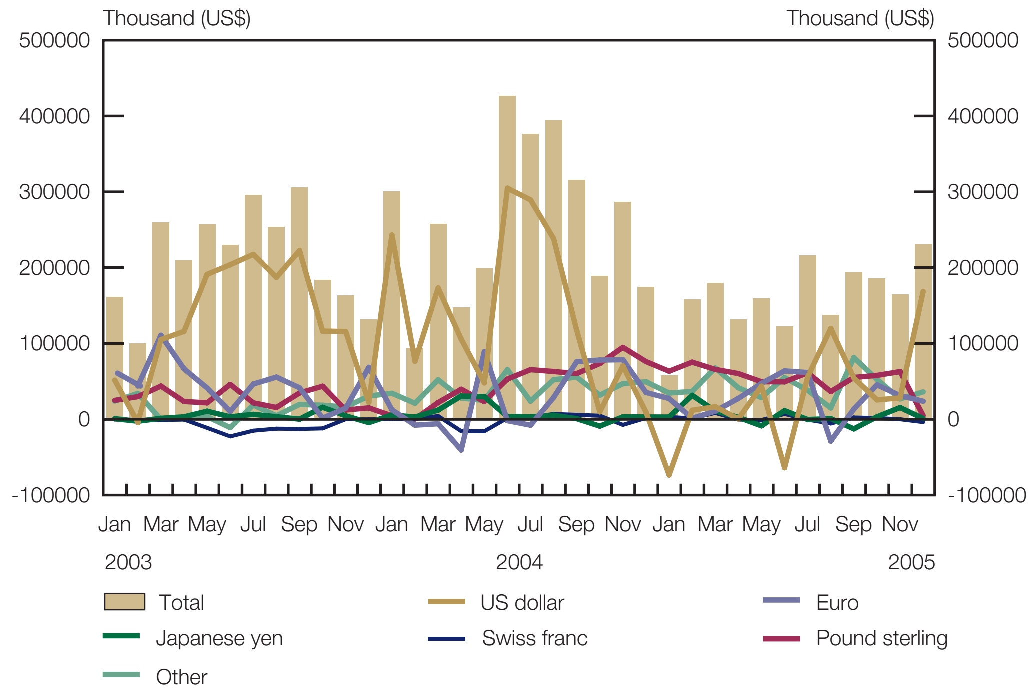
Figure 37: Asset performance



4.7 Currency risk

During 2005, the aggregated net open foreign-currency position after hedging fluctuated, but remained safely within the statutory limit of 10 per cent of net qualifying capital and reserves.

Figure 38: Aggregated effective net open foreign-currency position (all currencies converted to US dollars)



decrease in the aggregated net effective open foreign-currency position

As depicted in figure 38, the size and extent of the fluctuations in the aggregated net effective open foreign-currency position of the total banking sector on average decreased during 2005 when compared with 2003 and 2004. The decrease in the aggregated net effective open foreign-currency position was due mainly to the US dollar-aggregated net effective open position, which was lower in value than in 2003 and 2004. The aggregated net effective open foreign-currency position of the total banking sector increased from US$174,7 million in December 2004 to US$230,6 million in December 2005. Expressed as a percentage of net qualifying capital and reserves, the aggregated net effective open foreign-currency position of individual banks amounted to 1,1 per cent in December 2005, as opposed to 0,9 per cent in December 2004.

From December 2004 to December 2005, the maximum net open position in foreign currency after hedging increased from 0,8 per cent to 1,7 per cent, but remained well within the statutory limit of 10 per cent of net qualifying capital and reserves (see figure 39).

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)

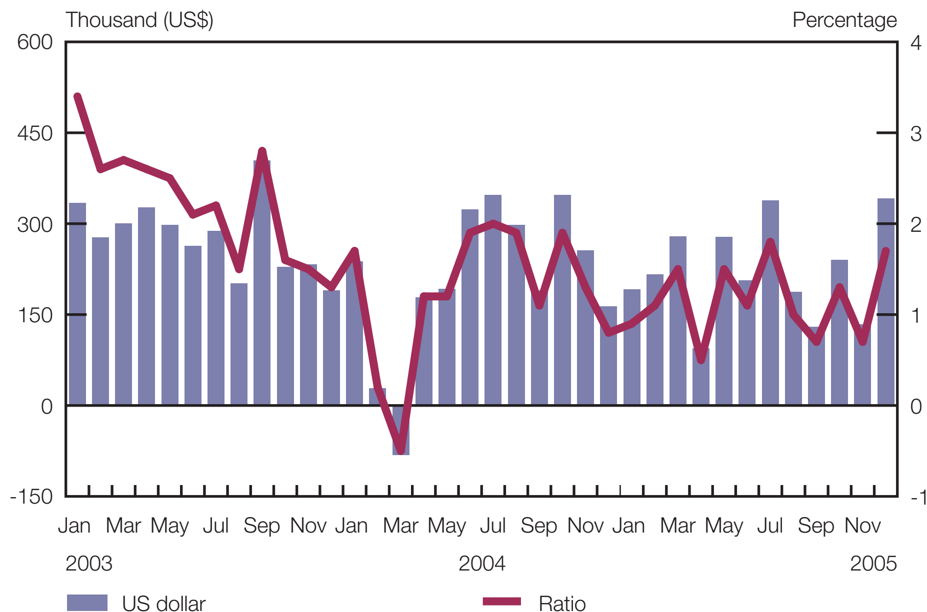


Figure 40: Position in foreign-currency instruments

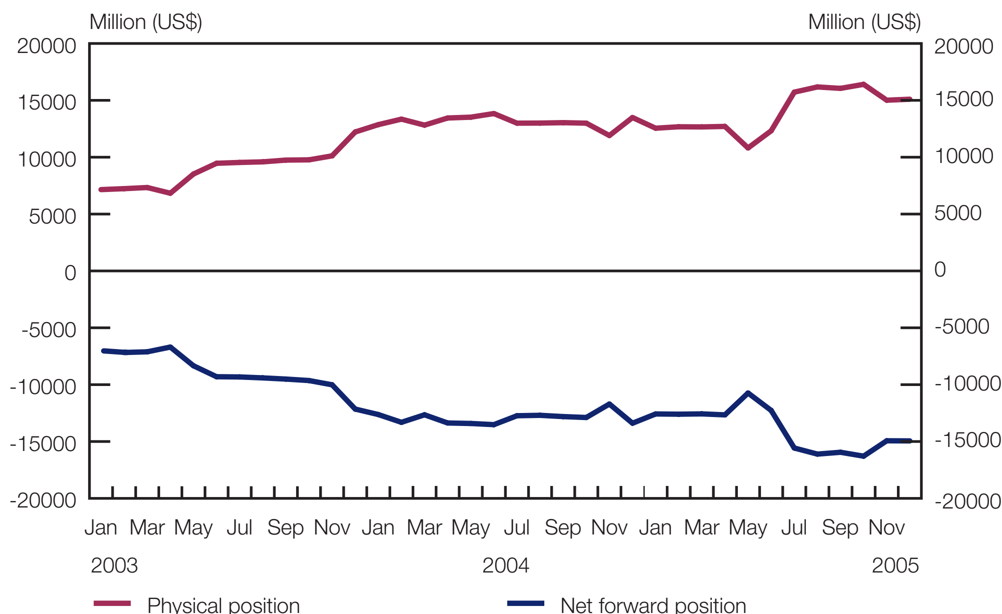
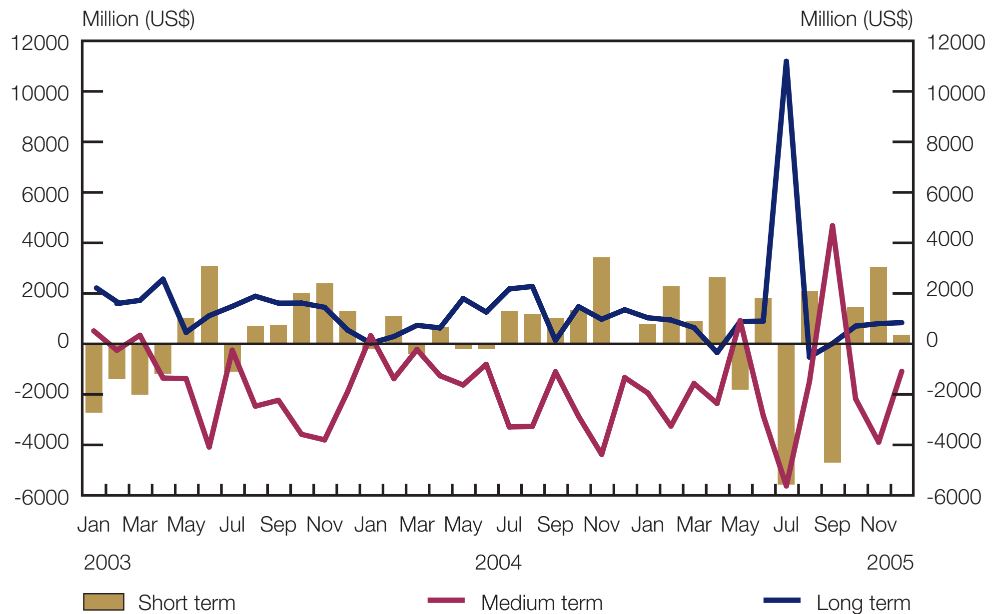


Figure 40 graphically depicts the position in foreign-currency instruments for the period from January 2003 to December 2005. The physical position equals the difference between the foreign assets and foreign liabilities, whereas the net forward position is the difference between commitments to sell foreign currency and commitments to purchase foreign currency. The physical position increased from US$13,5 billion in December 2004 to US$15,1 billion in December 2005, whereas the net forward position increased from -US$13,4 billion in December 2004 to -US$14,9 billion in December 2005. The increase in the physical position mirrored the widening forward position in order to maintain the overall net open position within the regulatory limit of 10 per cent of qualifying capital.

Figure 41 depicts the liquidity-maturity structure of foreign assets, liabilities and commitments from January 2003 to December 2005. An analysis of the liquidity-maturity structure of foreign assets, liabilities and commitments indicates that banks maintained a small net open foreign-currency position during the past three years. The net impact of the maturity ladder was minimal.

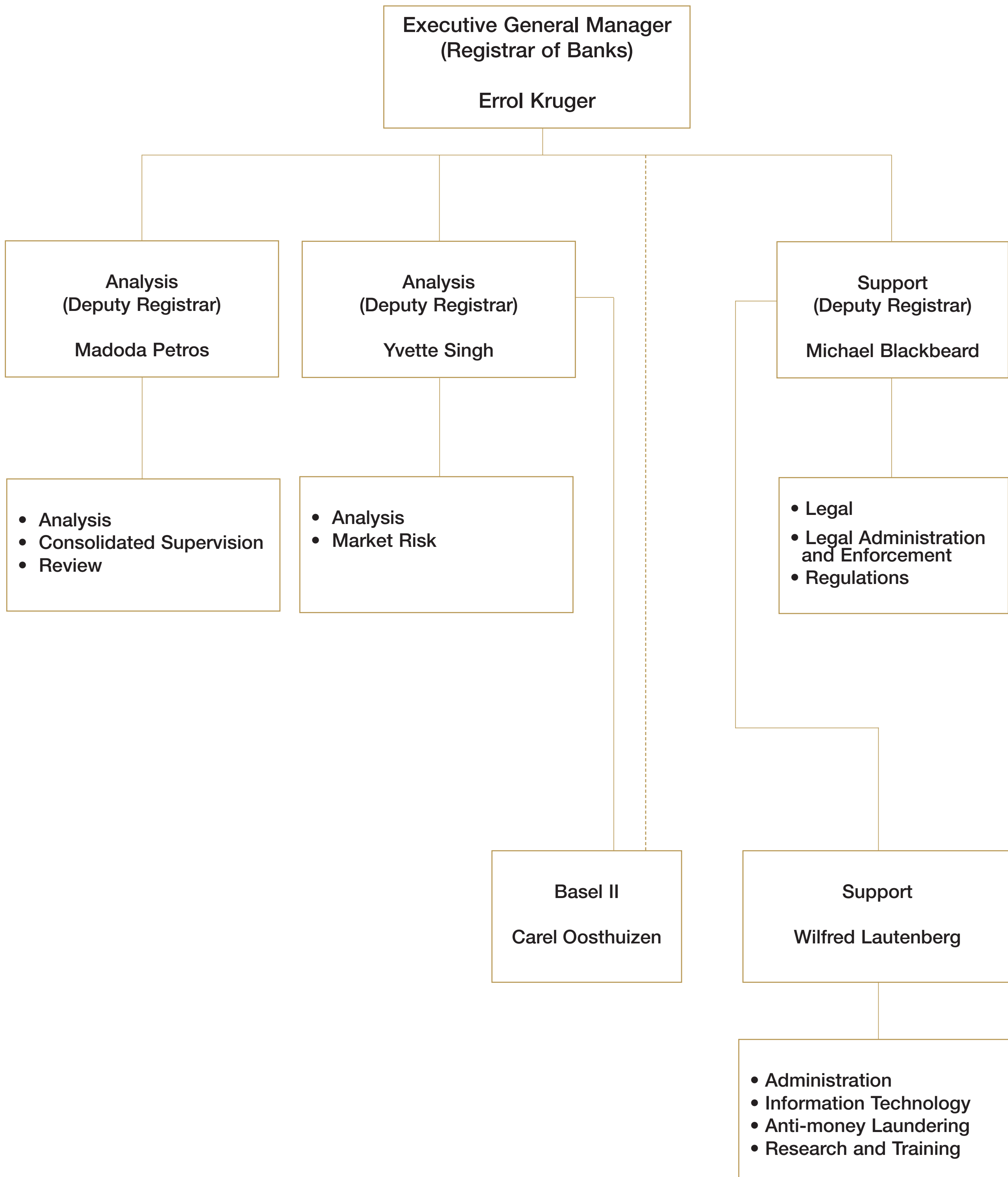
Figure 41: Liquidity-maturity structure (US dollars)



Appendices

Appendix 1

Organisational structure of the Bank Supervision Department



Appendix 2

Registered banks, mutual banks and local branches of foreign banks as at 31 December 2005

Registered banks

Institution		Address	Total assets at 31 December		Percentage annual growth
			2004 R million	2005 R million	
1.	ABSA Bank Limited	P O Box 7735, Johannesburg, 2000	295 803	358 607	21,2
2.	African Bank Limited	Private Bag X170, Halfway House, 1685	7 332	7 462	1,8
3.	Albaraka Bank Limited	P O Box 4395, Durban, 4000	983	1 146	16,6
4.	Capitec Bank Limited	P O Box 12451, Die Boord, Stellenbosch, 7613	728	1 170	60,9
5.	FirstRand Bank Limited	P O Box 786273, Sandton, 2146	263 262	307 310	16,7
6.	Habib Overseas Bank Limited	P O Box 62369, Marshalltown, 2107	344	422	22,8
7.	HBZ Bank Limited	P O Box 1536, Wandsbeck, 3631	793	1 023	29,0
8.	Imperial Bank Limited	P O Box 6093, Rivonia, 2128	16 897	22 290	31,9
9.	Investec Bank Limited	P O Box 785700, Sandton, 2146	72 396	97 129	34,2
10.	Marriott Corporate Property Bank Limited	P O Box 3211, Durban, 4000	737	771	4,7
11.	Mercantile Bank Limited	P O Box 782699, Sandton, 2146	2 734	3 431	25,5
12.	Nedbank Limited	P O Box 1144, Johannesburg, 2000	308 955	303 225	-1,9
13.	Rennies Bank Limited	P O Box 185, Johannesburg, 2000	335	378	13,0
14.	Sasfin Bank Limited	P O Box 95104, Grant Park, 2051	752	948	26,1
15.	TEBA Bank Limited	Private Bag X174, Halfway House, 1685	2 219	2 257	1,7
16.	The South African Bank of Athens Limited	P O Box 7781, Johannesburg, 2000	618	666	7,8
17.	The Standard Bank of South Africa Limited	P O Box 7725, Johannesburg, 2000	385 197	436 281	13,3

Appendix 2

Registered banks, mutual banks and local branches of foreign banks as at 31 December 2005 (continued)

Bank (with effect from 1 July 1996) in terms of the Supervision of Financial Institutions Rationalisation Act, 1996 (Act No. 32 of 1996)

Institution	Address	Total assets at 31 December		Percentage annual growth
		2004 R million	2005 R million	
1. MEEG Bank Limited	P O Box 429, East London, 5200	801	952	18,9

Registered mutual banks

Institution	Address	Total assets at 31 December		Percentage annual growth
		2004 R million	2005 R million	
1. GBS Mutual Bank	P O Box 114, Grahamstown, 6140	421	500	18,8
2. VBS Mutual Bank	P O Box 3618, Makhado, 0920	209	222	6,2

Registered local branches of foreign banks

Institution	Address	Total assets at 31 December		Percentage annual growth
		2004 R million	2005 R million	
1. ABN AMRO Bank N.V.	P O Box 78769, Sandton, 2146	7 063	12 792	81,1
2. Bank of Baroda	91/121 Cowey Road, Cowey Park, Berea, Durban, 4001	166	150	-9,6
3. Bank of China Limited Johannesburg Branch (trading as Bank of China Johannesburg Branch)	P O Box 782616, Sandton, 2146	381	437	14,5
4. Bank of Taiwan South Africa Branch	P O Box 1999, Parklands, 2121	1 142	639	-44,0
5. Barclays Bank Plc, South Africa Branch	P O Box 1542, Saxonwold, 2132	7 681	9 401	22,4
6. Calyon (trading as Calyon Corporate and Investment Bank)	P O Box 527, Melrose Arch, 2076	22 746	20 646	-9,2
7. China Construction Bank Corporation – Johannesburg Branch	Private Bag X10007, Sandton, 2146	816	703	-13,8
8. Citibank N.A.	P O Box 1800, Saxonwold, 2132	29 391	26 572	-9,6
9. Commerzbank Aktiengesellschaft	P O Box 860, Parklands, 2121	6 095	6 912	13,4
10. Deutsche Bank AG	Private Bag X9933, Sandton, 2146	13 494	19 166	42,0
11. HSBC Bank Plc – Johannesburg Branch	Private Bag X951, Houghton, 2041	2 851	4 102	43,9
12. JPMorgan Chase Bank, N.A. (Johannesburg Branch)	Private Bag X9936, Sandton, 2146	24 724	22 225	-10,1
13. Société Générale	P O Box 6872, Johannesburg, 2000	2 796	2 701	3,4
14. Standard Chartered Bank – Johannesburg Branch	P O Box 782080, Sandton, 2146	3 382	3 493	3,3
15. State Bank of India	P O Box 2538, Saxonwold, 2132	497	650	30,7

Appendix 2

Registered banks, mutual banks and local branches of foreign banks as at 31 December 2005 (continued)

Banks in final liquidation

Institution		Liquidator	Date of order
1.	Islamic Bank Limited	Mr A D Wilkins of Deloitte & Touche	13 January 1998
2.	Regal Treasury Private Bank Limited	Mr T A P du Plessis of D & N Trust and Mr J Pema of Sekela Antrust (Pty) Limited	10 February 2004

Appendix 3

Name changes and cancellation of registration of banks and branches of foreign banks during the period from 1 January 2005 to 31 December 2005

Name changes

Previous name		New name	Date of change
1.	JP Morgan Chase Bank (Johannesburg Branch)	JP Morgan Chase Bank, N.A. (Johannesburg Branch)	13 September 2005
2.	Marriott Merchant Bank Limited	Marriott Corporate Property Bank Limited	9 March 2005

Cancellation of registration

Institution		Date of cancellation
1.	Peoples Bank Limited	1 February 2005

Appendix 4

Registered controlling companies as at 31 December 2005

	Institution	Address
1.	ABSA Group Limited	P O Box 7735, Johannesburg, 2000
2.	African Bank Investments Limited	P O Box X170 Halfway House, 1685
3.	Capitec Bank Holdings Limited	P O Box 12451, Die Boord, Stellenbosch, 7613
4.	FirstRand Bank Holdings Limited	P O Box 786273, Sandton, 2146
5.	Investec Limited	P O Box 785700, Sandton, 2146
6.	Marriott Holdings Limited	P O Box 3211, Durban, 4000
7.	Mercantile Bank Holdings Limited	P O Box 782699, Sandton, 2146
8.	Nedbank Group Limited	P O Box 1144, Johannesburg, 2000
9.	Rennies Bank Holdings Limited	P O Box 185, Johannesburg, 2000
10.	Sasfin Holdings Limited	P O Box 95104, Grant Park, 2051
11.	Standard Bank Group Limited	P O Box 7725, Johannesburg, 2000
12.	TEBA Bank Controlling Company Limited	Private Bag X174, Halfway House, 1685

The following institutions are deemed to be controlling companies in terms of section 42 of the Banks Act, 1990:

	Institution	Address
1.	Albaraka Investment and Development Company (in respect of Albaraka Bank Limited)	P O Box 6854, Jeddah, 21452, Saudi Arabia
2.	National Bank of Greece (in respect of The South African Bank of Athens Limited)	86 Eolou Street, Athens TT 121, Greece
3.	Pitcairns Finance (in respect of Habib Bank Limited)	21, Avenue de la Faiencerie, L-1511 Luxemburg, RCS Luxemburg, B nr 33-106

Appendix 5

Foreign banks with approved local representative offices

	Institution	Address
1.	American Express Bank Limited	P O Box 651, Parklands, 2121
2.	Banca di Roma	P O Box 787018, Sandton, 2146
3.	Banco BPI, SA	P O Box 303, Bruma, 2026
4.	Banco Espirito Santo e Comercial de Lisboa	P O Box 749, Bruma, 2026
5.	Banco Privado Português, SA	P O Box 78407, Sandton, 2146
6.	Banco Totta & Açores SA	P O Box 309, Bruma, 2026
7.	Bank Leumi Le-Israel BM	Private Bag X41, Saxonwold, 2132
8.	Bank of Cyprus Group	P O Box 652176, Benmore, 2010
9.	BNP Paribas Johannesburg	P O Box 653002, Benmore, 2010
10.	Barclays Bank Plc	P O Box 1542, Saxonwold, 2132
11.	Barclays Private Bank Limited	P O Box 1542, Saxonwold, 2132
12.	Barclays Private Clients International Limited	P O Box 1542, Saxonwold, 2132
13.	Bayerische Hypo- und Vereinsbank AG	P O Box 1483, Parklands, 2121
14.	Belgolaise Bank	P O Box 652065, Benmore, 2010
15.	Crédit Industriel et Commercial	302 Portofino, 30 9th Street, Killarney, 2193
16.	Credit Suisse (South Africa) (Pty) Limited	P O Box 458, Green Point, 8051
17.	Credit Suisse First Boston (Europe) Limited	Private Bag X9911, Sandton, 2146
18.	Dresdner Bank AG	P O Box 413355, Craighall, 2024
19.	Dresdner Kleinwort Wasserstein Limited	P O Box 413355, Craighall, 2146
20.	Export-Import Bank of India	P O Box 2018, Saxonwold, 2132
21.	Fairbairn Private Bank (Isle of Man) Limited	P O Box 787549, Sandton, 2146
22.	Fairbairn Private Bank (Jersey) Limited	P O Box 787549, Sandton, 2146
23.	First Bank of Nigeria	P O Box 784796, Sandton, 2146
24.	Fortis Bank (Nederland) N.V.	P O Box 652065, Benmore, 2010
25.	Hellenic Bank Public Company Limited	P O Box 783392, Sandton, 2146
26.	HSBC Bank International Limited	P O Box 51037, Waterfront, 8002
27.	Icici Limited	P O Box785553, Sandton, 2146
28.	ING Bank (Switzerland) Limited	P O Box 65660, Benmore, 2010
29.	Kredietbank SA Luxembourgeoise	P O Box 1163, Stellenbosch, 7599
30.	Laiki Banking Group	Suite #199, Private Bag X9916, Village Walk, Sandton, 2146
31.	Lloyds TSB Offshore Limited	P O Box 785553, Sandton, 2146
32.	Millenium BCP	P O Box 273, Bruma, 2026
33.	N M Rothschild & Sons (CI) Limited	P O Box 411332, Craighall, 2024
34.	Natexis Banques Populaires	P O Box 1414, Morningside, 2057
35.	National Bank of Egypt	P O Box 55402, Nolrthlands, 2116
36.	Royal Bank of Canada Europe Limited	P O Box 784568, Sandton, 2146
37.	Société Générale Representative Office for Southern Africa	P O Box 2805, Saxonwold, 2132
38.	Sumitomo Mitsui Banking Corporation	Private Bag X134, Bryanston, 2021
39.	The Bank of New York, Johannesburg Representative Office	Postnet Suite 100, Private Bag X43, Sunninghill, 2157

Appendix 5

Foreign banks with approved local representative offices (continued)

	Institution	Address
40.	The Bank of Tokyo-Mitsubishi, Ltd	P O Box 78519, Sandton, 2146
41.	The Representative Office for Southern and Eastern Africa of the Export-Import Bank of China	Private Bag X91, Benmore, 2010
42.	The Royal Bank of Scotland	P O Box 678, 23 Broad Street, St Helier, Jersey, J E 4 8PD Channel Islands
43.	UBS AG	P O Box 652863, Benmore, 2010
44.	Union Bank of Nigeria Plc	P O Box 653125, Benmore, 2010
45.	Vnesheconombank	P O Box 413742, Craighall, 2024
46.	Wachovia Bank, NA	P O Box 3009, Parklands, 2121
47.	WestLB AG	P O Box 786126, Sandton, 2146

Appendix 6

Trends in South African banks

The following tables have been selected for publication because they disclose:

- The most important industry trends.
- Industry statistics that facilitate banks' evaluation of their own positions.

Note: Certain of the comparative figures in respect of 2003 and 2004 may differ from those reported in the 2003 and 2004 Annual Reports owing to the submission of amended returns by banks after publication of those reports.

TABLE	PAGE
1. Composition of balance sheet – liabilities	90
2. Composition of balance sheet – assets	91
3. Composition of selected liabilities	92
4. Composition of loans and advances to non-banks	93
5. Funding maturity structure	94
6. Analysis of capital and reserves	95
7. Risk profile of assets	96
8. Risk profile of off-balance-sheet items	97
9. Risk profile of loans and advances	98
10. Capital adequacy	100
11. Composition of income statement	101
12. Profitability: operating ratios	102
13. Profitability ratios	103
14. Percentage composition of interest income	104
15. Percentage composition of interest expense	105
16. Calculation of liquid-asset requirement	106
17. Analysis of overdue accounts	107
18. Analysis of overdue accounts: selected ratios	108
19. Large credit exposures	109
20. Profitability of assets	110
21. Open position in foreign currency	111

Table 1

Composition of balance sheet – liabilities

	Interbank funding R million	Non-bank funding R million	Foreign funding R million	Loans received under repurchase agreements R million	Other liabilities R million	Acknow-ledge-ment of debt R million	Capital and reserves R million	Total liabilities R million
Average month-end balance for quarter								
2003:01	80 560	661 461	54 746	37 366	293 267	1 972	100 381	1 229 752
2003:02	72 337	706 333	47 214	44 672	332 977	2 394	103 490	1 309 416
2003:03	69 733	716 181	43 599	46 266	351 035	1 893	105 720	1 334 426
2003:04	68 000	737 015	38 446	51 949	377 669	1 574	109 988	1 384 640
2004:01	75 299	765 467	44 947	45 696	321 756	1 844	112 894	1 367 904
2004:02	68 613	798 164	43 577	48 130	262 532	945	115 877	1 337 838
2004:03	69 907	849 980	45 116	57 062	244 028	682	117 603	1 384 377
2004:04	70 793	898 640	43 872	54 554	282 581	528	122 213	1 473 181
2005:01	83 317	940 484	46 996	53 429	278 443	270	125 927	1 528 867
2005:02	80 915	980 976	49 743	54 801	251 398	255	126 296	1 544 385
2005:03	86 348	1 036 035	53 665	48 564	262 387	173	129 626	1 616 798
2005:04	82 645	1 077 420	55 740	57 010	248 947	597	132 693	1 655 053
Month-end balance for year								
December 2003	68 082	755 135	38 785	57 015	349 203	1 415	110 188	1 379 823
December 2004	72 765	909 918	45 762	51 806	292 756	481	124 945	1 498 434
December 2005	85 645	1 101 495	56 832	54 307	244 928	1 004	133 331	1 677 543
Average for 12 months								
2003	72 657	705 247	46 001	45 063	338 737	1 958	104 895	1 314 558
2004	71 153	828 063	44 378	51 361	277 724	1 000	117 147	1 390 825
2005	83 307	1 008 729	51 536	53 451	260 294	324	128 635	1 586 276
Percentage annual growth	%	%	%	%	%	%	%	%
2003	-16,8	14,0	-33,6	15,3	145,3	-33,6	6,6	25,4
2004	6,9	20,5	18,0	-9,1	-16,2	-66,0	13,4	8,6
2005	17,7	21,1	24,2	4,8	-16,3	108,7	6,7	12,0

Table 2

Composition of balance sheet – assets

	Money R million	Interbank advances R million	Non-bank advances R million	Loans granted under resale agreements R million	Invest-ment portfolio R million	Non-financial assets R million	Acknow-ledgement of debt outstanding R million	Other assets R million	Total assets R million
Average month-end balance for quarter									
2003:01	22 869	50 086	802 870	32 286	256 087	12 543	1 972	51 038	1 229 752
2003:02	23 332	54 203	835 243	34 781	311 348	12 188	2 394	35 927	1 309 416
2003:03	24 244	55 849	847 578	34 155	325 323	12 363	1 539	33 374	1 334 426
2003:04	26 371	59 729	861 084	39 912	353 192	12 310	1 217	30 825	1 384 640
2004:01	25 143	67 790	907 024	39 934	283 870	12 051	1 769	30 323	1 367 904
2004:02	26 145	64 920	916 222	42 847	242 165	11 685	945	32 910	1 337 838
2004:03	27 664	68 094	945 310	44 323	254 257	11 383	682	32 664	1 384 377
2004:04	30 650	57 879	998 105	36 603	308 306	11 541	531	29 566	1 473 181
2005:01	31 475	69 229	1 047 284	35 409	298 967	11 582	270	34 651	1 528 867
2005:02	33 010	62 112	1 095 289	38 529	272 285	11 948	255	30 956	1 544 385
2005:03	33 659	73 193	1 168 549	34 397	262 368	12 125	173	32 334	1 616 798
2005:04	37 350	68 069	1 217 211	38 306	247 044	13 262	571	33 239	1 655 053
Month-end balance for year									
December 2003	28 846	60 402	875 965	46 417	328 061	12 271	1 207	26 654	1 379 823
December 2004	32 319	54 767	1 014 122	29 076	331 015	11 641	481	25 013	1 498 434
December 2005	38 338	72 255	1 231 379	34 648	254 284	13 840	962	31 836	1 677 543
Average for 12 months									
2003	24 204	54 967	836 694	35 284	311 488	12 351	1 781	37 791	1 314 558
2004	27 401	64 671	941 665	40 927	272 150	11 665	982	31 366	1 390 825
2005	33 874	68 151	1 132 083	36 660	270 166	12 229	318	32 795	1 586 276
Percentage annual growth	%	%	%	%	%	%	%	%	%
2003	8,7	27,7	9,5	28,4	147,6	-2,0	-43,4	-37,4	25,4
2004	12,0	-9,3	15,8	-37,4	0,9	-5,1	-60,1	-6,2	8,6
2005	18,6	31,9	21,4	19,2	-23,2	18,9	99,8	27,3	12,0

Table 3

Composition of selected liabilities

	Deposits					Loans under repurchase agreement				Foreign funding		
	Demand R million	Savings R million	Fixed and notice R million	Negotiable certificates of deposit R million	Total R million	SARB and Corp for Public Deposits R million	Banks R million	Non-banks R million	Total R million	Banks R million	Non-banks R million	Total R million
Average month-end balance for quarter												
2003:01	328 751	37 095	248 879	46 735	661 461	11 486	13 745	12 134	37 366	28 098	26 647	54 746
2003:02	328 936	39 803	280 977	56 617	706 333	11 569	20 734	12 368	44 672	22 877	24 336	47 214
2003:03	340 181	42 492	297 239	36 269	716 181	12 085	19 308	14 873	46 266	20 592	23 006	43 599
2003:04	368 865	44 953	298 989	24 208	737 015	13 190	24 577	14 182	51 949	18 713	19 733	38 446
2004:01	391 119	45 377	306 963	22 008	765 467	13 383	23 380	8 932	45 696	25 860	19 087	44 947
2004:02	383 028	46 880	315 041	53 214	798 164	13 676	25 864	8 590	48 130	25 949	17 628	43 577
2004:03	393 411	48 308	321 775	86 486	849 980	13 551	30 132	13 380	57 062	24 965	20 151	45 116
2004:04	415 640	50 552	325 880	106 568	898 640	13 631	26 898	14 025	54 554	21 542	22 329	43 872
2005:01	431 912	50 518	333 830	124 224	940 484	13 934	27 079	12 416	53 429	24 955	22 040	46 996
2005:02	443 557	51 933	355 450	130 035	980 976	14 118	26 987	13 697	54 801	26 530	23 213	49 743
2005:03	475 021	53 934	364 538	142 541	1 036 035	14 085	19 790	14 688	48 564	27 415	26 250	53 665
2005:04	499 575	57 070	371 517	149 258	1 077 420	12 225	24 996	19 789	57 010	26 920	28 820	55 740
Month-end balance for year												
Dec 2003	392 482	45 573	294 449	22 631	755 135	13 006	27 465	16 545	57 015	21 077	17 708	38 785
Dec 2004	428 740	51 095	320 224	109 859	909 918	13 444	24 286	14 075	51 806	20 616	25 146	45 762
Dec 2005	511 693	57 870	380 351	151 581	1 101 495	11 909	23 465	18 934	54 307	27 110	29 722	56 832
Average for 12 months												
2003	341 683	41 086	281 521	40 957	705 247	12 083	19 591	13 390	45 063	22 570	23 431	46 001
2004	395 800	47 780	317 415	67 069	828 063	13 560	26 568	11 232	51 361	24 579	19 799	44 378
2005	462 517	53 364	356 334	136 515	1 008 729	13 591	24 713	15 148	53 451	26 455	25 081	51 536
Percentage annual growth	%	%	%	%	%	%	%	%	%	%	%	%
2003	17,5	22,9	25,5	-60,0	14,0	8,1	32,3	-0,8	15,3	-36,3	-30,0	-33,6
2004	9,2	12,1	8,8	385,4	20,5	3,4	-11,6	-14,9	-9,1	-2,2	42,0	18,0
2005	19,3	13,3	18,8	38,0	21,1	-11,4	-3,4	34,5	4,8	31,5	18,2	24,2

Table 4

Composition of loans and advances to non-banks

	Negotiable certificates of deposit R million	Instalment debtors R million	Mortgage loans R million	Credit cards R million	Acknow-ledgement of debt discounted R million	Redeem-able preference shares R million	Overdrafts and loans R million	Foreign-currency loans and advances R million	Less: Specific provisions R million	Total R million
Average month-end balance for quarter										
2003:01	15 051	110 218	285 208	15 119	18 906	16 574	252 573	106 718	17 498	802 870
2003:02	16 878	115 337	296 033	15 715	22 361	15 638	266 806	105 324	18 849	835 243
2003:03	15 737	120 091	307 008	16 173	19 992	16 168	260 891	110 260	18 742	847 578
2003:04	10 571	124 340	319 678	16 721	23 951	16 278	263 826	104 328	18 612	861 084
2004:01	7 663	129 346	333 431	17 713	29 160	15 408	266 697	125 977	18 370	907 024
2004:02	4 903	135 440	350 523	18 584	25 609	15 219	257 246	126 349	17 649	916 222
2004:03	10 224	142 705	371 183	19 460	22 305	14 517	257 489	124 382	16 957	945 310
2004:04	15 672	150 500	396 923	20 697	21 129	15 258	279 744	114 480	16 297	998 105
2005:01	21 230	156 678	417 061	23 531	24 212	15 396	287 312	118 521	16 656	1 047 284
2005:02	22 564	164 133	443 934	25 427	25 135	17 817	290 663	123 323	17 707	1 095 289
2005:03	24 793	171 876	477 237	27 289	24 924	18 275	287 709	153 143	16 698	1 168 549
2005:04	22 477	179 251	509 983	29 969	26 370	17 767	295 615	151 558	15 779	1 217 211
Month-end balance for year										
December 2003	9 205	126 087	323 444	16 950	24 914	15 397	264 069	114 418	18 519	875 965
December 2004	16 716	152 406	406 174	21 169	22 499	15 707	278 893	116 723	16 164	1 014 122
December 2005	21 225	182 165	522 413	31 207	27 461	18 258	298 506	145 501	15 358	1 231 379
Average for 12 months										
2003	14 559	117 497	301 982	15 932	21 302	16 165	261 024	106 658	18 425	836 694
2004	9 616	139 498	363 015	19 113	24 551	15 100	265 294	122 797	17 318	941 665
2005	22 766	167 985	462 054	26 554	25 160	17 314	290 325	136 636	16 710	1 132 083
Percentage annual growth	%	%	%	%	%	%	%	%	%	%
2003	-31,3	16,9	15,8	15,8	24,8	-8,8	6,6	-2,8	7,7	9,5
2004	81,6	20,9	25,6	24,9	-9,7	2,0	5,6	2,0	-12,7	15,8
2005	27,0	19,5	28,6	47,4	22,1	16,2	7,0	24,7	-5,0	21,4

Table 5

Funding maturity structure

	Short-term %	Medium-term %	Long-term %
Quarter			
2003:01	62,2	22,6	15,2
2003:02	63,5	22,8	13,7
2003:03	64,8	21,8	13,3
2003:04	66,1	21,3	12,6
2004:01	66,9	20,1	13,0
2004:02	66,1	19,8	14,1
2004:03	64,8	20,7	14,4
2004:04	63,4	22,9	13,6
2005:01	64,7	21,7	13,6
2005:02	63,9	21,4	14,6
2005:03	64,0	20,7	15,3
2005:04	64,3	20,5	15,2
Month-end for year			
December 2003	68,4	19,5	12,0
December 2004	65,7	21,1	13,2
December 2005	64,6	20,6	14,8
Average for 12 months			
2003	64,2	22,1	13,7
2004	65,3	20,9	13,8
2005	64,2	21,1	14,7

Table 6

Analysis of capital and reserves

	Primary capital R million	Qualifying secondary capital R million	Tertiary qualifying capital R million	Total qualifying capital R million	Less: Impairments R million	Net qualifying capital R million	As percentage of total risk exposure: Primary capital %	Impairments %	Secondary capital %
Average month-end balance for quarter									
2003:01	66 771	32 611	1 449	100 831	13 336	87 495	10,0	2,0	4,9
2003:02	70 517	32 354	1 318	104 189	9 783	94 406	10,3	1,4	4,7
2003:03	73 865	32 121	1 634	107 620	9 508	98 112	10,7	1,4	4,7
2003:04	75 459	32 207	2 166	109 833	10 449	99 384	10,6	1,5	4,5
2004:01	75 136	34 366	2 160	111 662	9 847	101 814	10,2	1,3	4,6
2004:02	77 439	35 186	2 110	114 736	9 738	104 998	10,5	1,3	4,7
2004:03	80 259	34 412	2 241	116 911	8 378	108 534	10,7	1,1	4,5
2004:04	86 120	34 883	2 131	123 135	7 991	115 144	11,0	1,0	4,4
2005:01	90 371	33 690	1 891	125 951	7 277	118 674	11,1	0,9	4,1
2005:02	93 087	34 869	1 602	129 558	7 582	121 977	11,0	0,9	4,1
2005:03	94 505	35 490	1 499	131 494	9 219	122 274	10,6	1,0	4,0
2005:04	99 240	36 028	1 434	136 701	8 670	128 031	10,6	0,9	3,8
Average for 12 months									
2003	71 653	32 323	1 642	105 618	10 769	94 849	10,4	1,6	4,7
2004	79 739	34 712	2 160	116 611	8 988	107 623	10,6	1,2	4,6
2005	94 301	35 019	1 607	130 926	8 187	122 739	10,8	0,9	4,0
Percentage annual growth	%	%	%	%	%	%			
2003	2,9	1,4	49,3	3,1	-31,7	8,8			
2004	23,9	3,3	-12,5	16,8	-21,9	20,8			
2005	9,8	1,4	-22,2	7,0	-8,5	8,0			

Table 7

Risk profile of assets

	Risk category							Total	Risk-weighted assets	Risk-weighted assets as percentage of total average assets
	0% R million	10% R million	20% R million	50% R million	100% R million	150% R million	Impairments R million	R million	R million	%
Average month-end balance for quarter										
2003:01	235 719	11 263	65 271	192 272	522 889	0	3 800	1 031 215	671 207	65,1
2003:02	239 928	10 897	82 593	202 440	534 037	0	3 042	1 072 936	683 288	63,7
2003:03	248 156	9 700	84 017	211 404	535 881	1	2 929	1 092 088	688 643	63,0
2003:04	239 161	11 542	89 496	223 285	554 472	0	3 468	1 121 423	719 844	64,2
2004:01	245 981	12 066	100 473	232 806	567 848	1	3 911	1 163 086	744 664	64,1
2004:02	238 262	11 407	100 150	245 753	561 912	16	3 972	1 161 473	745 707	64,2
2004:03	235 518	9 838	99 479	261 961	570 183	6	4 119	1 181 104	763 242	64,6
2004:04	234 497	8 574	97 394	279 203	603 737	0	4 548	1 227 954	809 160	65,9
2005:01	246 907	9 782	101 453	292 385	621 312	93	3 532	1 275 464	824 233	64,6
2005:02	241 379	8 472	102 953	307 861	648 896	0	4 294	1 313 855	867 203	66,0
2005:03	254 692	8 193	120 576	331 319	666 436	3	5 120	1 386 339	908 237	65,5
2005:04	251 526	9 705	133 066	351 122	704 410	30	4 976	1 454 836	957 365	65,8
Month-end balance for year										
Dec 2003	235 587	12 697	93 488	226 308	560 603	0	3 994	1 132 676	733 661	64,8
Dec 2004	242 411	8 297	95 383	285 788	609 174	0	4 360	1 245 412	815 570	65,5
Dec 2005	261 372	9 470	125 490	360 454	717 982	61	4 380	1 479 209	968 142	65,4
Average for 12 months										
2003	240 741	10 850	80 344	207 350	536 820	0	3 310	1 079 416	690 746	64,0
2004	238 565	10 471	99 374	254 931	575 920	6	4 138	1 183 404	765 693	64,7
2005	248 626	9 038	114 512	320 672	660 264	32	4 481	1 357 624	889 260	65,5
Percentage annual growth	%	%	%	%	%	%	%	%	%	
2003	1,5	25,7	40,9	19,1	10,1	-100,0	4,3	12,0	11,7	
2004	2,9	-34,7	2,0	26,3	8,7	-100,0	9,2	10,0	11,2	
2005	7,8	14,1	31,6	26,1	17,9	-100,0	0,5	18,8	18,7	

Table 8

Risk profile of off-balance-sheet items

	Risk category									Risk-weighted off-balance-sheet items	Risk-weighted items as percentage of total average off-balance-sheet items
	0%[1] R million	5% R million	10% R million	20% R million	50% R million	100% R million	150% R million	Impairments R million	Total R million	R million	%
Average month-end balance for quarter											
2003:01	21 325	489	1 520	6 048	57 264	16 792	0	0	1 240 838	46 810	3,8
2003:02	20 652	283	1 889	6 035	58 309	17 498	0	0	1 220 494	48 062	3,9
2003:03	26 185	387	2 332	11 035	56 210	15 187	0	31	1 325 144	46 061	3,5
2003:04	27 524	1 030	5 580	11 717	55 895	10 330	0	110	1 380 600	42 331	3,1
2004:01	29 953	1 085	12 604	6 560	68 200	14 137	0	165	1 527 308	52 513	3,4
2004:02	35 000	1 154	11 314	8 572	68 051	15 274	0	165	1 572 653	53 852	3,4
2004:03	37 062	302	9 348	9 795	62 280	13 447	0	269	1 711 245	50 186	2,9
2004:04	41 963	159	8 872	10 316	56 982	11 405	0	338	1 971 627	46 238	2,3
2005:01	49 762	248	9 290	8 929	57 259	13 739	16	547	2 082 625	50 590	2,4
2005:02	54 155	401	10 106	11 982	61 245	10 708	0	750	2 113 880	52 254	2,5
2005:03	61 431	479	14 655	12 878	68 064	11 202	0	683	2 459 051	56 133	2,3
2005:04	72 930	321	17 188	11 294	71 282	11 975	0	590	2 689 927	57 506	2,1
Month-end balance for year											
Dec 2003	29 280	677	11 682	5 879	57 938	9 778	0	165	1 437 695	42 775	3,0
Dec 2004	44 441	169	8 459	10 422	56 739	10 906	0	373	2 006 856	45 944	2,3
Dec 2005	75 595	279	19 806	11 706	70 714	11 865	0	583	2 849 477	57 388	2,0
Average for 12 months											
2003	23 922	547	2 830	8 709	56 920	14 952	0	35	1 291 769	45 816	3,6
2004	35 995	675	10 535	8 811	63 878	13 566	0	234	1 695 708	50 697	3,0
2005	59 570	362	12 810	11 271	64 463	11 906	4	642	2 336 371	54 121	2,3
Percentage annual growth	%	%	%	%	%	%	%	%	%	%	
2003	30,7	189,3	580,8	-5,8	0,9	-43,4	-100,0	-100,0	10,7	-9,8	
2004	51,8	-75,1	-27,6	77,3	-2,1	11,5	-100,0	126,1	39,6	7,4	
2005	70,1	64,9	134,1	12,3	24,6	8,8	-100,0	56,3	42,0	24,9	

1. 0% risk category = Total off-balance-sheet activities minus central securities depository participation

Table 9(a)

Risk profile of loans and advances

	0% R million	10% R million	20% R million	50% R million	100% R million	150% R million	1000% R million	Total R million	Risk-weighted loans and advances R million	Risk-weighted loans and advances as percentage of total loans and advances %
Month-end balance for year 2003										
Intragroup bank advances	26 277	38	0	0	3 569	0	0	29 884	3 573	12,0
Interbank advances	0	0	27 388	0	0	0	0	27 388	5 478	20,0
Negotiable certificates of deposits	0	0	3 636	0	2	0	0	3 638	729	20,0
Instalment debtors	27	384	131	0	121 952	0	0	122 495	122 017	99,6
Mortgage loans	0	0	25	222 255	99 723	0	0	322 003	210 855	65,5
Credit-card debtors	0	0	0	0	16 868	0	0	16 868	16 868	100,0
Acknowledgements of debt discounted	12 169	61	7 996	12	5 746	0	0	25 984	7 357	28,3
Redeemable preference shares	679	0	325	0	14 446	0	135	15 585	15 862	101,8
Overdrafts and loans	4 006	6 287	1 805	0	244 793	0	1 086	257 978	256 641	99,5
Foreign-currency loans and advances	58 680	925	37 596	0	6 496	0	0	103 696	14 107	13,6
Loans granted under resale agreements	1 000	2 333	6 371	0	8 154	0	0	17 859	9 662	54,1
S A Reserve Bank and Corporation for Public Deposits	259	0	0	0	0	0	0	259	0	0
Banks	741	0	6 371	0	0	0	0	7 113	1 274	17,9
Non-banks	0	2 333	0	0	8 154	0	0	10 487	8 388	80,0
Total loans and advances	102 838	10 029	85 273	222 267	521 749	0	1 221	943 378	663 150	70,3
Less: Specific provisions	0	57	0	32	18 481	0	0	18 569	18 503	99,6

Table 9(b)

Risk profile of loans and advances

	0% R million	10% R million	20% R million	50% R million	100% R million	150% R million	1000% R million	Total R million	Risk-weighted loans and advances R million	Risk-weighted loans and advances as percentage of total loans and advances %
Month-end balance for year 2004										
Intragroup bank advances	24 223	0	0	0	3 648	0	0	27 872	3 648	13,1
Interbank advances	267	0	27 545	0	0	0	7	27 819	5 580	20,1
Negotiable certificates of deposits	0	0	16 154	0	0	0	0	16 154	3 231	20,0
Instalment debtors	30	727	130	0	149 006	0	0	149 893	149 105	99,5
Mortgage loans	0	0	71	281 541	121 094	0	0	402 706	261 879	65,0
Credit-card debtors	0	0	0	0	21 336	0	0	21 336	21 336	100,0
Acknowledgements of debt discounted	14 961	145	1 121	10	5 465	0	0	21 702	5 708	26,3
Redeemable preference shares	534	0	325	0	14 522	0	135	15 516	15 938	102,7
Overdrafts and loans	10 684	4 798	1 473	127	252 195	0	1 704	270 982	270 077	99,7
Foreign-currency loans and advances	66 301	144	40 136	32	7 820	0	0	114 434	15 878	13,9
Loans granted under resale agreements	2 562	1 052	3 865	0	1 224	0	0	8 703	2 102	24,2
S A Reserve Bank and Corporation for Public Deposits	2 118	0	0	0	0	0	0	2 118	0	0
Banks	444	0	3 865	0	0	0	0	4 309	773	17,9
Non-banks	0	1 052	0	0	1 224	0	0	2 276	1 329	58,4
Total loans and advances	119 564	6 866	90 821	281 711	576 310	0	1 847	1 077 118	754 481	70,0
Less: Specific provisions	7	124	0	26	15 997	0	0	16 154	16 022	99,2

Table 9(c)

Risk profile of loans and advances

	0% R million	10% R million	20% R million	50% R million	100% R million	150% R million	1000% R million	Total R million	Risk-weighted loans and advances R million	Risk-weighted loans and advances as percentage of total loans and advances %
Month-end balance for year 2005										
Intragroup bank advances	28 784	0	0	0	1 674	0	0	30 458	1 674	5,5
Interbank advances	3	0	35 499	0	0	0	1	35 504	7 113	20,0
Negotiable certificates of deposits	0	0	18 702	0	204	0	0	18 906	3 945	20,9
Instalment debtors	13	1 059	9	0	177 803	0	0	178 884	177 911	99,5
Mortgage loans	2	0	0	357 800	160 636	0	0	518 438	339 536	65,5
Credit-cards debtors	0	0	0	0	30 634	0	0	30 634	30 634	100,0
Acknowledgements of debt discounted	20 106	38	822	385	4 549	61	16	25 976	5 157	19,9
Redeemable preference shares	0	0	1 277	0	16 516	0	54	17 847	17 311	97,0
Overdrafts and loans	8 455	4 752	404	0	274 163	0	1 802	289 576	292 739	101,1
Foreign-currency loans and advances	71 700	74	59 092	0	9 925	0	519	141 311	26 945	19,1
Loans granted under resale agreements	1 608	1 883	5 800	0	6 603	0	0	15 893	7 951	50,0
S A Reserve Bank and Corporation for Public Deposits	51	0	0	0	0	0	0	51	0	0
Banks	1 199	0	5 800	0	0	0	0	6 998	1 160	16,6
Non-banks	358	1 883	0	0	6 603	0	0	8 844	6 791	76,8
Total loans and advances	130 670	7 805	121 605	358 186	682 706	61	2 392	1 303 426	910 915	69,9
Less: Specific provisions	7	166	0	0	15 086	0	0	15 259	15 102	99,0

Table 10

Capital adequacy

	Risk-weighted assets and off-balance-sheet items R million	Counterparty-risk exposure R million	Total risk exposure R million	Required capital R million	Net qualifying capital R million	Net qualifying capital Percentage
Quarter						
2003:01	668 973	17 541	651 432	67 009	56 529	8,5
2003:02	691 279	17 035	674 244	69 191	63 822	9,2
2003:03	690 628	16 066	674 562	69 123	68 055	9,9
2003:04	713 243	16 658	696 585	71 379	63 343	8,9
2004:01	748 016	12 762	735 254	74 867	66 456	8,9
2004:02	734 053	8 125	725 929	73 476	71 435	9,7
2004:03	761 747	8 333	753 414	76 250	73 633	9,7
2004:04	793 667	10 760	782 907	79 446	83 117	10,5
2005:01	821 662	8 969	812 693	82 273	82 382	10,0
2005:02	859 434	8 126	851 308	86 054	84 607	9,8
2005:03	896 670	8 697	887 973	89 798	87 072	9,7
2005:04	949 689	9 296	940 394	95 121	92 191	9,7
Average for 12 months						
2003	688 164	16 882	671 282	69 865	61 708	9,0
2004	753 466	10 450	743 016	77 427	71 414	9,5
2005	870 525	8 916	861 609	89 992	86 726	10,0
Percentage annual growth	%	%	%	%	%	
2003	9,2	-2,5	9,5	9,0	10,9	
2004	11,3	-35,4	12,4	11,3	31,2	
2005	19,7	-13,6	20,1	19,7	10,9	

Table 11(a)

Composition of income statement

	Average monthly balance for quarter 2003				Average monthly balance for quarter 2004			
	March R million	June R million	September R million	December R million	March R million	June R million	September R million	December R million
Interest income	11 215	11 672	10 480	8 732	8 558	8 579	9 219	9 132
Interest expense	8 198	8 682	7 904	6 651	5 832	5 677	6 121	6 229
Interest margin	3 017	2 990	2 576	2 081	2 726	2 903	3 098	2 903
Less: Specific provisions on loans and advances	722	770	564	482	466	348	609	522
Less: General debt provisions	20	26	-65	27	37	186	-4	-3
Other	12	13	1	7	-2	-10	-5	6
Adjusted interest margin	2 262	2 181	2 077	1 564	2 225	2 379	2 499	2 377
Add: Transaction-based fee income	1 738	1 838	1 878	2 004	2 028	2 143	2 185	2 436
Income from management of funds	4 000	4 019	3 954	3 569	4 253	4 522	4 684	4 813
Less: Operational expenses	3 404	3 916	3 388	3 824	3 758	4 136	3 978	4 476
Net income from management of funds	596	103	567	-255	494	386	706	337
Add: Investment and trading income	393	-191	525	1 168	502	1 985	888	903
Less: Specific provisions - investment	0	9	1	4	-9	-2	2	3
Add: Knowledge-based fee income	167	177	184	231	177	178	200	264
Net income before tax	1 169	1 653	1 884	776	1 731	2 013	1 916	1 831
Taxation	228	516	440	646	354	461	555	315
Net income after tax	941	1 137	1 444	130	1 377	1 552	1 361	1 516

Table 11(b)

Composition of income statement

	Average monthly balance for quarter 2005				Results for 12 months			Average for year		
	March R million	June R million	September R million	December R million	2003 R million	2004 R million	2005 R million	2003 R million	2004 R million	2005 R million
Interest income	8 811	9 422	10 105	10 718	126 295	106 461	117 170	10 525	8 872	9 764
Interest expense	6 023	6 322	6 772	7 080	94 306	71 574	78 593	7 859	5 965	6 549
Interest margin	2 788	3 100	3 333	3 638	31 989	34 887	38 576	2 666	2 907	3 215
Less: Specific provisions on loans and advances	617	347	335	420	7 614	5 836	5 159	635	486	430
Less: General debt provisions	68	3	57	77	24	647	614	2	54	51
Other	-5	-5	0	-5	98	-34	-44	8	-3	-4
Adjusted interest margin	2 108	2 755	2 941	3 146	24 252	28 439	32 848	2 021	2 370	2 737
Add: Transaction-based fee income	2 340	2 570	2 623	2 639	22 374	26 376	30 515	1 865	2 198	2 543
Income from management of funds	4 447	5 325	5 564	5 785	18 967	25 642	31 718	1 581	2 137	2 643
Less: Operational expenses	4 076	4 732	4 809	5 120	43 593	49 046	56 211	3 633	4 087	4 684
Net income from management of funds	371	593	755	665	3 033	5 769	7 152	253	481	596
Add: Investment and trading income	2 031	178	-787	1 767	5 682	12 832	9 566	474	1 069	797
Less: Specific provisions - investment	-1	0	9	-5	41	-17	10	3	-1	1
Add: Knowledge-based fee income	202	308	276	213	2 277	2 457	2 996	190	205	250
Net income before tax	2 021	1 689	2 126	2 449	16 448	22 473	24 856	1 371	1 873	2 071
Taxation	444	454	563	620	5 492	5 055	6 242	458	421	520
Net income after tax	1 577	1 235	1 563	1 829	10 956	17 419	18 614	913	1 452	1 551

Table 12

Profitability: operating ratios

	Interest income to loans and advances %	Interest expense to funding %	Interest margin %	Provisions to loans and advances %
Average monthly balance for quarter				
2003:01	14,5	10,6	3,8	1,0
2003:02	14,0	10,8	3,2	1,0
2003:03	12,8	9,7	3,1	0,6
2003:04	10,9	7,9	3,0	0,5
2004:01	9,9	6,7	3,2	0,5
2004:02	9,7	6,5	3,2	0,5
2004:03	10,0	6,8	3,2	0,6
2004:04	9,5	6,6	2,9	0,5
2005:01	8,7	6,2	2,5	0,6
2005:02	9,1	6,2	2,9	0,2
2005:03	9,3	6,3	3,0	0,3
2005:04	9,5	6,3	3,1	0,3
Average for the 12 months ended				
December 2003	12,2	9,1	3,1	0,7
December 2004	9,3	6,3	3,0	0,5
December 2005	8,5	5,8	2,7	0,3

Table 13

Profitability ratios

	Net income after tax to total assets %	Net income after tax to net qualifying capital equity and reserves %	Stated as percentage of total assets: Interest income %	Interest expense %	Interest margin %	Operating expenses %	Fee income %	Investment and trading income %
Average month-end balance for quarter								
2003:01	0,9	12,9	10,9	8,0	2,9	3,3	1,9	0,4
2003:02	1,0	14,4	10,7	8,0	2,7	3,6	1,8	-0,2
2003:03	1,3	17,7	9,4	7,1	2,3	3,0	1,9	0,5
2003:04	0,1	1,6	7,6	5,8	1,8	3,3	1,9	1,0
2004:01	1,2	16,3	7,5	5,1	2,4	3,3	1,9	0,4
2004:02	1,4	17,8	7,7	5,1	2,6	3,7	2,1	1,8
2004:03	1,2	15,1	8,0	5,3	2,7	3,4	2,1	0,8
2004:04	1,2	15,8	7,4	5,1	2,4	3,6	2,2	0,7
2005:01	1,2	16,0	6,9	4,7	2,2	3,2	2,0	1,6
2005:02	1,0	12,2	7,3	4,9	2,4	3,7	2,2	0,1
2005:03	1,2	15,4	7,5	5,0	2,5	3,6	2,2	-0,6
2005:04	1,3	17,2	7,8	5,1	2,6	3,7	2,1	1,3
Average for the 12 months ended								
December 2003	0,8	11,2	9,2	6,8	2,3	3,2	1,8	0,4
December 2004	1,2	14,7	7,1	4,8	2,3	3,3	1,9	0,9
December 2005	1,1	14,5	7,0	4,7	2,3	3,4	2,0	0,6

Table 14

Percentage composition of interest income

	Interbank loans %	Instal-ment debtors %	Mortgage loans %	Credit cards %	Acknow-ledge-ment of debt dis-counted %	Redeem-able pref-erence shares %	Over-drafts and loans %	Foreign-currency loans and advances %	Loans under resale agree-ments %	Negoti-able certi-ficates of deposit %	Interest income from invest-ments %
Average month-end balance for quarter											
2003:01	10,1	12,9	32,5	2,1	2,0	1,2	29,3	2,4	1,2	1,4	4,9
2003:02	8,0	12,8	33,4	2,1	2,3	1,4	27,0	2,2	1,5	1,6	7,7
2003:03	6,1	13,6	33,8	2,3	2,6	1,4	28,6	2,1	3	1,6	4,9
2003:04	6,8	15,0	35,1	2,6	2,8	1,5	29,0	2,1	3,6	1,1	0,4
2004:01	8,9	14,4	33,9	2,5	2,8	1,0	27,6	2,5	3,2	0,6	2,5
2004:02	8,1	15,1	35,7	2,6	2,8	1,4	25,8	1,3	3,2	0,3	3,7
2004:03	7,3	14,4	35,0	2,6	2,4	1,2	26,9	2,3	2,7	0,8	4,4
2004:04	5,2	14,8	37,1	2,7	2,1	1,6	25,7	2,6	2,3	1,0	4,9
2005:01	5,9	15,6	36,2	2,9	2,2	1,0	24,6	3,0	1,9	1,4	5,3
2005:02	6,0	15,0	36,7	3,0	2,0	1,3	25,3	3,5	1,9	1,5	3,8
2005:03	9,0	14,5	35,7	3,1	1,8	1,3	25,5	4,4	1,6	1,3	1,7
2005:04	5,3	15,8	37,3	3,4	1,8	1,3	24,8	4,9	1,8	1,3	2,4
Average for the 12 months ended											
December 2003	7,9	13,5	33,6	2,2	2,4	1,4	28,4	2,2	2,2	1,4	4,7
December 2004	7,3	14,7	35,4	2,6	2,5	1,3	26,5	2,2	2,8	0,7	3,9
December 2005	6,6	15,2	36,5	3,1	1,9	1,2	25,1	4,0	1,8	1,4	3,2

Table 15

Percentage composition of interest expense

	Intra-group funding %	Interbank funding %	Demand deposits %	Savings deposits %	Fixed and notice deposits %	Nego-tiable certifi-cates of deposit %	Loans under re-purchase agree-ments %	Other funding %	Foreign funding %	Transfer cost of trading activities %	Debt instru-ments %
Average month-end balance for quarter											
2003:01	9,7	6,9	33,3	2,5	29,5	5,2	2,5	8,8	1,1	-3,4	4,0
2003:02	10,2	5,1	29,7	2,5	31,1	6,1	3,5	10,4	0,7	-3,3	4,1
2003:03	3,8	5,1	29,7	2,3	35,4	5,2	4,9	12,0	0,6	-2,9	3,9
2003:04	3,9	4,2	28,2	2,0	33,8	3,4	4,9	13,5	0,7	0,4	4,9
2004:01	4,3	4,3	29,9	2,0	33,5	2,6	4,4	13,5	1,0	-1,2	5,7
2004:02	4,0	4,6	29,3	2,2	35,6	5,6	4,4	9,2	10,	-1,8	5,9
2004:03	3,7	3,8	26,6	2,0	34,7	10,2	4,7	9,1	0,9	-1,0	5,2
2004:04	3,9	4,4	27,0	1,9	32,4	11,0	4,7	8,4	1,2	-0,8	5,8
2005:01	3,9	4,8	29,0	2,0	31,2	12,3	4,7	5,4	1,5	-0,5	5,7
2005:02	3,9	4,8	26,1	1,9	33,5	13,0	4,0	6,5	1,6	-0,3	5,0
2005:03	4,1	4,2	25,6	1,9	30,5	12,2	3,2	12,1	1,8	-0,2	4,6
2005:04	2,7	3,9	29,0	1,9	31,8	12,9	3,8	7,1	2,2	0	4,7
Average for the 12 months ended											
December 2003	7,1	5,4	30,3	2,3	32,3	5,0	3,9	11,1	0,8	-2,5	4,2
December 2004	4,0	4,3	28,2	2,0	34,0	7,5	4,6	10,0	1,0	-1,2	5,6
December 2005	3,6	4,4	27,4	1,9	31,7	12,6	3,9	7,9	1,8	-0,2	5,0

Table 16(a)

Calculation of liquid-asset requirement

	Average month-end balance for quarter 2003				Average month-end balance for quarter 2004			
	March R million	June R million	September R million	December R million	March R million	June R million	September R million	December R million
Liabilities including capital and reserves	1 215 145	1 288 005	1 314 487	1 376 314	1 367 284	1 331 174	1 360 564	1 446 501
Less: Capital and reserves	100 978	104 214	105 902	109 118	113 756	115 065	116 141	119 363
- average daily amount of funding from head office or branches	12 307	8 459	6 926	7 508	9 896	11 463	8 988	7 890
- average daily amount owing by banks, branches and mutual banks	117 484	128 821	131 511	140 535	132 701	109 482	107 814	111 704
Liabilities as adjusted	984 375	1 046 511	1 070 148	1 119 256	1 110 966	1 095 164	1 127 621	1 207 543
Liquid-asset requirement	49 219	52 325	53 508	55 963	55 548	54 758	56 381	60 377
Liquid assets held	53 392	59 067	60 926	63 259	66 323	65 789	66 197	68 367
SARB notes and coins	4 114	3 960	4 632	5 985	6 680	6 488	6 835	7 900
Gold coin and bullion	8	7	4	5	5	21	7	0
Clearing-account balances	2 140	0	0	1	1	2	-2	5
Treasury bills of the Republic	15 212	17 288	15 790	17 383	21 152	19 555	16 841	18 181
Stock issued - Exchequer Act, 1975								
Securities issued - Public Finance	26 808	26 589	33 255	36 383	35 089	34 615	37 719	37 539
Management Act, 1999	4 527	10 523	6 590	2 812	2 634	4 445	4 193	3 978
Securities of the SARB	583	700	656	689	762	663	604	764
Land Bank bills								
Memorandum items								
Cash-management schemes	47 952	50 269	50 971	54 162	56 379	61 118	63 437	65 173
Set-off	59 355	66 214	67 330	74 338	79 825	83 548	93 674	109 068
Ratios	%	%	%	%	%	%	%	%
Liquid assets held to liquid assets required	113,0	115,5	114,0	114,7	118,3	120,1	119,2	116,4

Table 16(b)

Calculation of liquid-asset requirement

	Average month-end balance for quarter 2005				Month-end for year			Percentage annual growth		
	March R million	June R million	September R million	December R million	2003 R million	2004 R million	2005 R million	2003 %	2004 %	2005 %
Liabilities including capital and reserves	1 499 696	1 521 030	1 589 575	1 633 592	1 384 542	1 482 832	1 654 418	26,7	7,1	11,6
Less: Capital and reserves	124 193	124 221	128 628	131 495	109 004	122 315	131 766	7,1	12,2	7,7
- average daily amount of funding from head office or branches	8 674	9 940	10 714	8 726	9 087	7 716	11 695	-43,7	-15,1	51,6
- average daily amount owing by banks, branches and mutual banks	110 106	106 054	113 441	132 071	144 531	113 492	132 974	60,2	-21,5	17,2
Liabilities as adjusted	1 256 724	1 280 816	1 336 791	1 361 300	1 122 068	1 239 309	1 377 982	26,9	10,4	11,2
Liquid-asset requirement	62 836	64 041	66 839	68 065	56 103	61 965	68 899	26,9	10,4	11,2
Liquid assets held	71 437	74 732	76 962	79 636	64 696	70 656	81 176	26,0	9,2	14,9
SARB notes and coins	8 882	8 686	8 223	8 480	6 204	7 970	8 728	73,3	28,5	9,5
Gold coin and bullion	0	0	0	0	6	0	0	-45,1	-96,4	0
Clearing-account balances	4	10	7	1	1	5	-45	1 200,00	300,0	-959,6
Treasury bills of the Republic	21 967	24 841	24 668	26 169	18 082	19 318	27 496	12,8	6,8	42,3
Stock issued - Exchequer Act, 1975										
Securities issued - Public Finance										
Management Act, 1999	33 634	34 563	36 094	37 476	37 051	37 415	38 661	38,5	1,0	3,3
Securities of the SARB	6 137	5 872	7 274	6 779	2 656	5 139	5 650	-34,4	93,5	9,9
Land Bank bills	812	760	696	731	696	808	684	-24,9	16,1	-15,3
Memorandum items										
Cash-management schemes	53 708	51 006	50 719	54 014	57 111	67 467	58 534	17,3	18,1	-13,2
Set-off	117 238	125 384	130 896	52 262	75 732	113 864	58 289	27,3	50,4	-48,8
Ratios	%	%	%	%	%	%	%			
Liquid assets held to liquid assets required	114,4	117,8	116,6	117,9	114,8	116,8	119,7			

Table 17

Analysis of overdue accounts

	Mortgage loans R million	Instalment finance R million	Other loans R million	Total R million	Specific provisions R million	Market value of security held R million
Average month-end balance for quarter						
2003:01	9 017	2 223	15 397	26 636	14 570	10 754
2003:02	9 151	2 265	14 702	26 119	15 640	9 987
2003:03	9 056	2 132	13 675	24 863	15 723	9 905
2003:04	8 909	2 129	13 638	24 676	15 817	9 537
2004:01	8 049	2 209	13 126	23 384	14 958	8 435
2004:02	7 203	2 303	12 697	22 202	14 461	8 098
2004:03	7 332	2 496	11 581	21 409	13 582	8 540
2004:04	7 072	2 590	10 910	20 571	13 257	8 382
2005:01	6 330	2 732	11 183	20 245	13 041	7 788
2005:02	5 751	2 678	12 044	20 473	13 503	7 192
2005:03	5 299	2 612	11 093	19 003	12 637	6 878
2005:04	5 330	2 865	10 428	18 623	12 165	6 968
Month-end balance for year						
December 2003	8 265	2 188	13 396	23 849	15 501	8 485
December 2004	6 848	2 616	10 962	20 425	13 126	8 302
December 2005	6 061	3 373	10 657	20 090	11 934	7 926
Average for 12 months						
2003	9 034	2 187	14 353	25 573	15 438	10 046
2004	7 414	2 400	12 078	21 892	14 065	8 364
2005	5 677	2 722	11 187	19 586	12 837	7 206
Percentage annual growth	%	%	%	%	%	%
2003	-1,7	5,6	-14,4	-8,7	8,7	-18,5
2004	-17,1	19,5	-18,2	-14,4	-15,3	-2,2
2005	-11,5	28,9	-2,8	-1,6	-9,1	-4,5

Table 18

Analysis of overdue accounts: selected ratios

	Specific provisions as a percentage of total overdues %	Specific provisions and securities held as percentage of total overdues %	Overdues as percentage of advances %	Specific provisions as a percentage of advances %	Net overdues[1] as percentage of net qualifying capital and reserves %
End of quarter					
2003:01	54,1	93,6	3,0	1,6	13,9
2003:02	61,9	101,1	2,6	1,6	9,9
2003:03	65,1	105,3	2,6	1,7	8,5
2003:04	65,0	100,6	2,4	1,5	8,5
2004:01	65,3	101,0	2,2	1,5	7,8
2004:02	65,6	103,6	2,0	1,3	6,7
2004:03	62,1	103,0	2,0	1,2	7,6
2004:04	64,3	104,9	1,8	1,2	6,2
2005:01	66,6	102,1	1,8	1,2	6,2
2005:02	64,2	100,4	1,6	1,0	5,9
2005:03	68,6	105,4	1,4	1,0	4,6
2005:04	59,4	98,9	1,5	0,9	6,4
Average for 12 months					
2003	61,3	100,0	2,6	1,6	10,1
2004	64,3	103,1	2,0	1,3	7,0
2005	64,6	101,6	1,6	1,0	5,8

1. Net overdues = gross overdues less specific provisions.

Table 19

Large credit exposures

	Granted R million	Utilised R million	Utilised as a percentage of advances %	Utilised as a percentage of net qualifying capital and reserves %	Granted as a percentage of net qualifying capital and reserves %
Average month-end balance for quarter					
2003:01	439 848	157 027	17,4	175,9	492,8
2003:02	397 579	171 909	17,7	178,5	412,8
2003:03	408 862	161 629	16,8	160,1	405,1
2003:04	367 694	154 243	15,4	157,1	374,6
2004:01	413 167	150 000	14,5	144,1	396,9
2004:02	484 959	135 257	12,9	126,3	452,7
2004:03	614 652	134 078	12,2	122,8	562,8
2004:04	547 096	133 909	12,0	113,0	461,8
2005:01	587 373	147 696	12,5	127,4	506,8
2005:02	611 373	155 481	12,6	128,9	507,0
2005:03	435 380	137 477	10,6	110,7	350,5
2005:04	501 417	164 832	12,2	128,8	391,7
Average for 12 months					
2003	403 496	161 202	16,8	167,6	419,6
2004	514 969	138 311	12,9	126,0	469,3
2005	533 886	151 371	11,9	123,9	437,0
Percentage annual growth	%	%			
2003	-29,2	4,4			
2004	48,8	-13,2			
2005	-8,3	23,1			

Table 20

Profitability of assets

	Money R million	Advances: Reasonable margin R million	Advances: Small margin R million	Advances: No yield R million	Investments: Profitable R million	Investments: Not profitable R million	Infra-structure R million	Total R million
Average month-end balance for quarter								
2003:01	22 835	879 340	49 474	32 158	154 075	13 854	65 248	1 216 983
2003:02	23 453	942 047	35 578	32 062	205 307	11 639	50 391	1 300 475
2003:03	24 244	969 372	38 931	31 677	210 967	11 824	47 260	1 334 275
2003:04	26 349	991 225	40 672	33 776	233 706	11 758	44 119	1 381 605
2004:01	25 083	1 046 582	37 023	33 522	172 034	11 739	44 105	1 370 089
2004:02	26 125	1 026 329	58 241	31 311	133 113	13 213	45 366	1 333 697
2004:03	27 664	1 070 514	55 779	30 554	141 750	13 400	44 696	1 384 356
2004:04	30 641	1 098 533	67 526	31 760	188 946	13 999	41 655	1 473 060
2005:01	31 475	1 141 819	80 052	30 776	185 311	12 908	46 502	1 528 844
2005:02	33 494	1 163 140	89 418	33 486	165 938	16 453	42 678	1 544 607
2005:03	33 659	1 250 480	91 926	26 082	153 520	16 699	44 623	1 616 987
2005:04	37 350	1 302 392	89 942	26 088	129 703	22 524	46 991	1 654 991
Month-end balance for year								
December 2003	28 845	1 022 663	33 054	32 494	211 344	11 232	40 130	1 379 762
December 2004	32 291	1 097 918	79 218	31 251	207 967	12 625	37 121	1 498 391
December 2005	38 338	1 311 654	98 015	24 659	124 139	34 168	46 632	1 677 605
Average for 12 months								
2003	24 220	945 496	41 164	32 418	201 014	12 269	51 755	1 308 335
2004	27 378	1 060 490	54 642	31 787	158 961	13 088	43 956	1 390 301
2005	33 995	1 214 458	87 835	29 108	158 618	17 146	45 199	1 586 357
Percentage annual growth	%	%	%	%	%	%	%	%
2003	8,7	21,3	-63,5	-9,6	457,8	47,3	-29,8	25,5
2004	11,9	7,4	139,7	-3,8	-1,6	12,4	-7,5	8,6
2005	18,7	19,5	23,7	-21,1	-40,3	170,6	25,6	12,0

Table 21

Open position in foreign currency

	Total foreign-exchange assets USA$ million	Total foreign-exchange liabilities USA$ million	Net spot position USA$ million	Commit-ments to purchase foreign currency USA$ million	Commit-ments to sell foreign currency USA$ million	Mismatched forward commit-ments USA$ million	Foreign branches USA$ million
Average month-end balance for quarter							
2003:01	13 808	6 568	7 240	130 506	137 611	-7 106	39
2003:02	14 635	6 364	8 272	152 492	160 604	-8 112	72
2003:03	16 260	6 634	9 626	164 472	173 885	-9 413	73
2003:04	16 711	6 010	10 702	152 259	162 859	-10 600	57
2004:01	19 825	6 815	13 010	135 650	148 514	-12 864	70
2004:02	20 290	6 688	13 603	133 827	147 261	-13 434	89
2004:03	20 206	7 195	13 011	133 731	146 477	-12 746	98
2004:04	20 646	7 850	12 796	143 956	156 617	-12 661	82
2005:01	20 724	8 094	12 630	149 700	162 282	-12 582	84
2005:02	19 859	7 912	11 947	163 656	175 543	-11 887	78
2005:03	24 531	8 548	15 983	177 178	193 053	-15 874	74
2005:04	24 384	8 877	15 506	189 805	205 194	-15 390	77
Month-end balance for year							
December 2003	18 363	6 146	12 217	141 197	153 344	-12 147	61
December 2004	21 964	8 475	13 489	141 855	155 246	-13 392	78
December 2005	24 462	9 363	15 098	184 287	199 232	-14 946	78
Average for 12 months							
2003	15 354	6 394	8 960	149 932	158 740	-8 808	60
2004	20 242	7 137	13 105	136 791	149 717	-12 926	85
2005	22 374	8 358	14 017	170 085	184 018	-13 933	78
Percentage annual growth	%	%	%	%	%	%	%
2003	33,7	-8,6	74,1	20,9	24,1	78,9	40,4
2004	19,6	37,9	10,4	0,5	1,2	10,2	26,3
2005	11,4	10,5	11,9	29,9	28,3	11,6	0,5

Appendix 7

Circulars sent to banking institutions during 2005

Banks Act Circular 1/2005	Annual withdrawal and retention of circulars
Banks Act Circular 2/2005	New Capital Accord (Basel II): impact study and related requirements
Banks Act Circular 3/2005	Enforcement of the 31 May 2005 deadline for client identification and verification in terms of the Financial Intelligence Centre Act, 2001 (FICA)
Banks Act Circular 4/2005	Issue of a guidance note by the Financial Intelligence Centre (FIC) in terms of section 4(c) of the Financial Intelligence Centre Act, 2001 (the FIC Act)
Banks Act Circular 5/2005	Report on the standard of corporate governance in banking institutions
Banks Act Circular 6/2005	Enforcement of the 30 September 2005 deadline for client identification and verification in terms of the Financial Intelligence Centre Act, 2001 (FICA)

Appendix 8

Exemptions and exclusions from the application of the Banks Act, 1990

Section 1(cc): Exemptions by the Registrar of Banks

Government Gazette		Topic	Expiry
Date	Number		
1994/12/14	16167	A group of persons between which a common bond exists	Indefinite
1994/12/14	16167	Commercial paper	Indefinite
2006/01/27	28414	"Ithala Limited" A wholly owned subsidiary of Ithala Development Finance Corporation Limited	2008/12/31
1994/12/14	16167	Mining houses	Indefinite
1994/12/14	16167	Trade in securities and financial instruments	Indefinite
2004/06/04	26415	Securitisation schemes	Indefinite

Section 1(dd): Exemptions by the Minister of Finance

Government Gazette		Topic	Subparagrph	Expiry
Date	Number			
2006/01/27	28414	Financial service co-operative	(dd)(i)	2006/12/31
1991/01/31	13003	Participation bond schemes	(dd)(ii)	Indefinite
1991/01/31	13003	Unit trust schemes	(dd)(ii)	Indefinite

Section 1(gg): Exemptions by the Registrar of Banks

Government Gazette		Topic	Expiry
Date	Number		
1998/09/22	19283	Members of the Johannesburg Stock Exchange as persons authorised to accept money as mandataries and to deposit such money into banking accounts maintained by them	Indefinite

Section 2(vii): Exclusions by the Minister of Finance

Government Gazette		Topic	Expiry
Date	Number		
1992/01/24	13744	Post Office Savings Bank	Indefinite
1994/12/14	16167	Industrial Development Corporation of SA Limited	Indefinite

SECTION 78(1)(d)(iii): Exemptions by the Registrar of Banks

Government Gazette		Topic	Expiry
Date	Number		
1997/05/02	17949	Category of assets of a bank held in the name of a person other than the bank concerned	Indefinite

Appendix 9

Approval of acquisition or establishment of foreign banking interests in terms of section 52 of the Banks Act, 1990, from 1 January 2005 to 31 December 2005

Name of bank/ controlling company	Date of approval	Name of interest (and percentage interest held, if not 100 per cent)	Country
FirstRand Bank Holdings Limited*	2005-01-24	Africa International Financial Holdings LLC	Mauritius
FirstRand Bank Holdings Limited	2005-03-04	RMB Resources Limited	Australia
FirstRand Bank Holdings Limited	2005-03-16	Hastie Holdings (Pty) Limited	Australia
FirstRand Bank Holdings Limited*	2005-03-18	UBS Management (Pty) Limited	Australia
FirstRand Bank Holdings Limited	2005-04-13	RMB Resources Incorporated	United States of America
FirstRand Bank Holdings Limited	2005-06-23	Celpay Holdings B Celpay Zambia Celpay Democratic Republic of Congo (DRC)	Netherlands Zambia DRC
FirstRand Bank Holdings Limited	2005-11-30	Quantum Asset Management (Pty) Limited	Australia
Investec Plc**	2005-03-11	Silversmart Hong Kong Limited	Hong Kong
Investec Plc**	2005-03-17	Thalberg Limited	Ireland
Investec Plc**	2005-03-17	Boi-If Services Number 1 Company	Ireland
Investec Plc**	2005-03-17	Newco Perosa 1 Newco Perosa 2 Newco Perosa 3	British Virgin Islands
Investec Limited	2005-08-23	African Lion 2 Limited	Mauritius
Investec Limited	2005-12-06	Acia Investments Limited Islands	British Virgin
Standard Bank Group Limited	28-06-2005	Standard Bank London Dubai Branch Emirates	United Arab
Standard Bank Group Limited	29-08-2005	Standard Bank Global Services Limited	Isle of Man
Standard Bank Group Limited	10-11-2005	The Standard Bank of South Africa Limited – Representative Office Luanda	Angola
Standard Bank Group Limited	10-11-2005	Standard Bank Argentina	Argentina
Standard Bank Group Limited	21-12-2005	Standard Bank Plc Sydney Branch	Australia

* Applications for the acquisition of indirect interests were noted in terms of Banks Act Circular 8/2004.
** Applications in respect of Investec Plc to establish or acquire foreign interests or subsidiaries were noted in terms of the conditions of approval of the Investec dually listed company structure.