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Risk management

for the six months ended 30 June 2009

Risk management

1. Overview

1.1 Introduction

Effective risk management is fundamental to the business activities of the Standard Bank Group (group). While we remain committed to increasing shareholder value by developing and growing our business within our board-determined risk appetite, we are mindful of achieving this objective in line with the interests of all stakeholders.

The capital and risk management information disclosed in this report fulfils Basel II Pillar 3 requirements, as stated in Regulation 43 of Regulations Relating to Banks, as governed by the Banks Act, 1990. Only banking operations are covered in terms of Pillar 3 requirements, and therefore, the insurance operations of the group's subsidiary, Liberty is excluded from this risk management report.

We seek to achieve an appropriate balance between risk and reward in our business, and continue to build and enhance the risk management capabilities that assist in delivering our growth plans in a controlled environment.

Our risk management processes have proven effective throughout the global financial crisis. Executive management has remained closely involved with important risk management initiatives which have focused more recently on the preservation of appropriate levels of liquidity and capital.

Risk management is at the core of the group's operating structures. We seek to limit adverse variations in earnings and equity by managing risk exposures and capital within agreed levels of risk appetite. Managing and controlling risks, minimising undue concentrations of exposure and limiting potential losses from stress events are all essential elements of the group's risk management and control framework. This framework ultimately ensures the protection of the group's reputation.

Responsibility and accountability for risk management resides at all levels in the group, from the executive down through the organisation to each business manager and risk specialist. The group uses the three lines of defence model:

- In the first line of defence, business unit management is primarily responsible for risk management. Their assessment, evaluation and measurement of risk is an ongoing process that is integrated into the day-to-day activities of the business. This process includes implementing the group's risk management framework, identifying issues and taking remedial action where required. Business unit management is also accountable for reporting to the governance bodies within the group.

- The second line of defence consists of group and business unit risk management functions which are appropriately independent of business management. The group risk management function is primarily accountable for setting the group's risk management framework and policy, providing oversight and independent reporting to executive management through the group risk oversight committee (GROC), and to the board through the group credit committee (GCC) and the group risk and capital management committee (GRCMC). The business unit risk management functions implement the group's risk management framework and policy in the business units, approving risks within specific mandates and providing an independent overview of the effectiveness of risk management by the first line of defence.

- The third line of defence consists of an internal audit function which provides an independent assessment of the adequacy and effectiveness of the overall risk management framework and risk governance structures, and reports to the board through the group audit committee (GAC).

Key components of the risk management control framework are the risk governance standards that have been developed for each risk type. These set out the principles for the governance, identification, measurement, management, control and reporting of each major risk type. Each standard is approved by the appropriate board risk committees and is supported by group and business unit risk policies and procedures.

Risks are controlled at the level of individual exposures and at portfolio level, as well as in aggregate across all businesses and risk types. Our approach to risk taking activities ensures an appropriate balance between the group's short- and long-term interests.

The specific sections that fulfil the Basel II Pillar 3 requirements as stated in Regulation 43 of Regulations Relating to Banks, as governed by the Banks Act, 1990 are:

- risk categories, page 4;
- capital management, pages 5 to 10;
- credit risk, pages 11 to 32;
- liquidity risk, pages 32 to 34;
- market risk, pages 34 to 40; and
- operational risk, pages 40 to 43.

All tables, diagrams and quantitative information in this risk management report are unaudited.

2. Risk management framework

2.1 Governance structure

There is strong independent oversight at all levels throughout the group.

Various committees, which are integral to the group's risk governance structure (set out in Figure 1 overleaf), allow executive management and the board to evaluate the risks faced by the group and the effectiveness of the group's management of these risks.

The responsibilities of GAC include:

- reviewing the group's financial position and making recommendations to the board on all financial matters including the assessment of the integrity and effectiveness of accounting, financial, compliance and other control systems; and
- ensuring effective communication between internal auditors, external auditors, the board, management and regulators.

The GRCMC and, in respect of credit risk and country risk, the GCC provides independent and objective oversight of risk and capital management across the group by:

- reviewing and assessing the adequacy and effectiveness of the group's risk management control framework;
- ensuring that risk and capital management standards and policies are appropriate and effective; and
- determining and monitoring the risk appetite of the group for each risk type under normal and potential stress conditions.

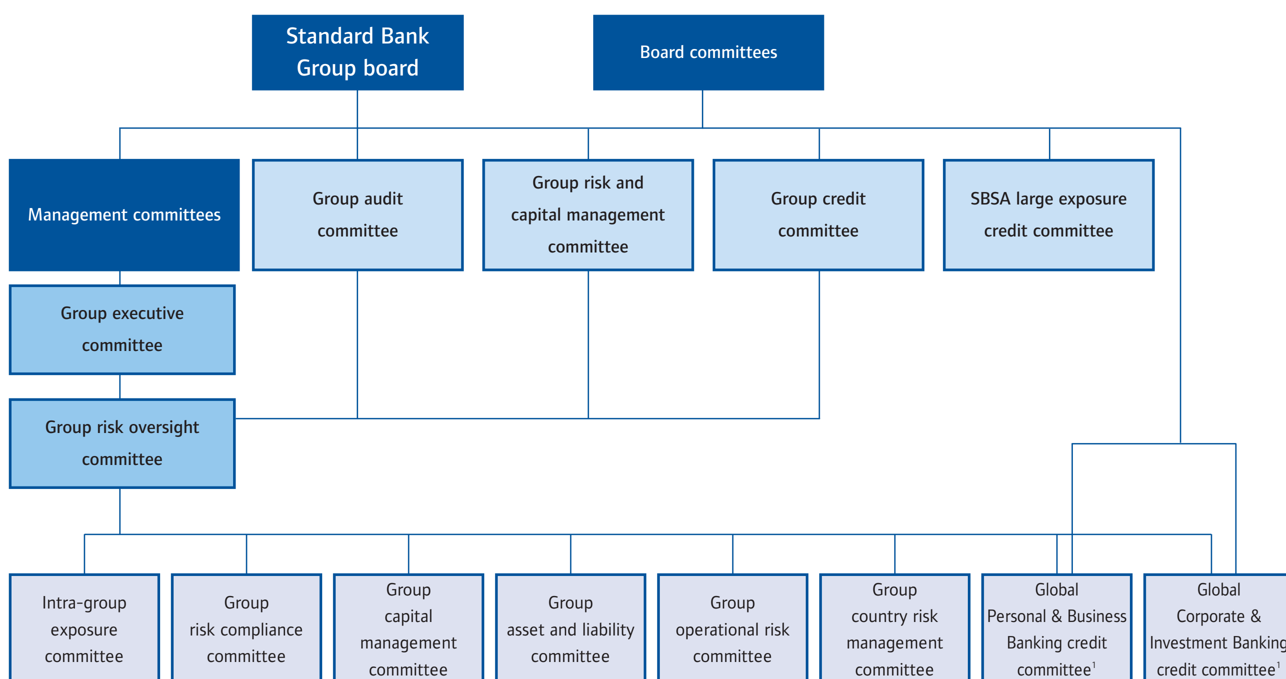
Group executive management delegates oversight of all risk types to GROC. This committee considers and, to the extent required, recommends for approval by the relevant board committees, in particular:

- levels of risk appetite and tolerance;
- risk governance standards and policies for each risk type;
- actions on the risk profile;
- risk strategy and key risk controls across the group;
- capital planning and capital funding activities;
- utilisation of risk appetite; and
- the usage and allocation of economic capital parameters for modelling, stress testing and scenario analysis.

GROC meets quarterly with additional meetings when necessary.

The group risk management subcommittees set out below, report directly to GROC and through GROC to the GRCMC and the GCC.

Figure 1: Governance structure



[1] The board has delegated authority to these committees to act as nominated designated committees in respect of the regulations.

2.2 Approach and structure

The group's approach to risk management is based on well established governance processes and relies on both individual responsibility and collective oversight, supported by comprehensive reporting. This approach balances strong corporate oversight at group level that begins with proactive participation by the group chief executive and the group executive committee in all significant risk matters, with independent risk management structures within the business units.

Business unit heads are primarily responsible for the management of risk within each of their businesses and are responsible for ensuring that there are appropriate, adequately designed and effective risk management frameworks, in compliance with group standards. To ensure that there is independence and appropriate segregation of responsibilities between business and risk, business unit chief risk officer's report operationally to their respective business unit heads and functionally to either the group chief risk officer or the group chief credit officer.

2.3 Risk governance standards, policies and procedures

The group has developed a set of risk governance standards for each major risk type. The standards set out and ensure alignment and consistency in the manner in which the major risk types across the group are governed, identified, measured, managed, controlled and reported.

All standards are applied consistently across the group and approved by the GCC or the GRCMC. It is the responsibility of executive management in each business unit to ensure risk governance standards, policies and procedures are implemented and independently monitored by the risk management team in that business unit.

Each standard is supported by group and business unit policies and procedural documents.

Compliance with risk standards, policies and procedures is controlled through annual self assessments by the business units and group risk, supported by the group internal auditors as well as external auditors in terms of their statutory audit of financial statements.

2.4 Risk appetite

The group's risk appetite is an expression of the maximum level of residual risk that the group is prepared to accept to deliver its business objectives. Risk appetite is implemented in terms of various limits, economic capital usage and the risk adjusted performance measures expected to be achieved, recognising a range of possible outcomes.

The board establishes the parameters for the group's risk appetite by:

- providing strategic leadership and guidance;
- reviewing and approving annual budgets and forecasts for the group and each division; and
- regularly reviewing and monitoring the group's performance in relation to risk through quarterly board reports.

The board delegates the determination of risk appetite to the GRCMC and ensures that the risk appetite is in line with the strategy and the desired risk reward trade-off for the group. GROC recommends to the GRCMC, the GCC and the board the level of risk appetite for the group.

The group's risk appetite statements are defined by five broad metrics:

- headline earnings;
- liquidity;
- regulatory capital;
- economic capital; and
- target debt rating.

These metrics are then converted into tolerance levels and limits by analysing the risks that impact them.

2.5 Stress testing

Stress testing involves identifying possible events or future changes in economic conditions that could have an unfavourable impact on the group. Stress testing is used to assess and manage the adequacy of regulatory and economic capital and is an integral component to the group's internal capital adequacy assessment process (ICAAP). The group's stress testing framework guides the regular execution of stress tests at portfolio, business unit, legal entity and group levels.

Management reviews the outcomes of stress tests and selects appropriate mitigating actions to minimise and manage the risks to the group at the various levels. The appropriateness of the group-wide stress scenarios and the severity of the relevant scenarios are approved by the GRCMC based on GROC's recommendations.

The outcomes of stress scenarios are ultimately assessed against earnings, capital adequacy and liquidity requirements on a consolidated basis across all risk types and compared with the group's set risk appetite. Stress tests are used in proactively managing the risk profile of the group, capital planning and management, strategic business planning and setting capital buffers. Stress tests are regularly discussed with regulators.

During the year, the group performed group-wide stress tests based on a number of macroeconomic scenarios, each with different levels of severity. The outcome of these stress tests indicated that the group was well within its risk tolerance levels in all of the scenarios. In many scenarios, this was so even before applying relevant mitigating actions. Over the last 12 months, the group has performed its group-wide macroeconomic stress testing process on a bi-annual basis in line with changing economic conditions. Portfolio specific stress tests are conducted more frequently with many executed on a monthly basis. This enables early and proactive management of the potential impact of changes in economic conditions.

3. Risk categories

The group's principal risks are defined as follows:

3.1 Credit risk

The risk of loss to the group as a result of the failure by a client or counterparty to meet their contractual obligations to the group.

3.2 Country and cross-border risk

Country risk is the risk of loss arising when political or economic conditions, or events in a particular country reduce the ability of counterparties in that country to meet their financial obligations to the group.

Cross-border risk is the risk that actions taken by a government may restrict the transfer and convertibility of funds, of local currency into foreign currency, thereby impacting the ability to obtain payment from counterparties on their financial obligations to the group.

3.3 Liquidity risk

The risk that the group is unable to meet its payment obligations when they fall due. This may be caused by the group's inability to liquidate assets or to obtain funding to meet its liquidity needs.

3.4 Market risk

The risk of a change in the actual or effective market value or earnings of a portfolio of financial instruments caused by adverse movements in market variables such as equity, bond and commodity prices, currency exchange rates and interest rates, credit spreads, recovery rates, correlations and implied volatilities in all of the above.

3.5 Operational risk

The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This includes information and legal risk but excludes reputational and strategic risk.

3.6 Business risk

Business risk relates to the potential revenue shortfall compared to the cost base due to strategic and/or reputational reasons. From an economic capital perspective, business risk capital requirements are calculated as the potential loss arising over a one year time frame within a certain level of confidence as implied by the group's chosen target rating. The group's ability to generate revenue is impacted by, amongst other things, the external macroeconomic environment, its chosen strategy and reputation in the markets in which it operates.

3.7 Reputational risk

Reputational risk results from damage to the group's image which may impair its ability to retain and generate business. Such damage may result from a breakdown of trust, confidence or business relationships. Safeguarding the group's reputation is of paramount importance to its continued success and is the responsibility of every member of staff.

4. Scope of application

4.1 Basel II consolidation

Pillar 3 disclosures, as set out in the regulations, apply at group level and disclosures related to individual banks within the group are not required. Banking regulations view consolidation as including only those group companies (subsidiaries, joint ventures and voluntarily consolidated minority-owned entities) that conduct banking and other financial operations. This includes credit institutions, securities firms and financial entities, but no other companies. Basel II information has been disclosed in accordance with the following consolidation approaches:

- Consolidated

Includes the full risk-weighted exposure amounts of a subsidiary in the group consolidated risk-weighted exposures, for example, banking and financial entities.

- Proportionately consolidated

Includes the pro rata portion of the risk-weighted exposure amounts of the entity in the group consolidated risk-weighted exposures, for example, banking and financial entities where joint control exists.

- Deduction

The respective investment in the entity is deducted from the consolidated capital and reserve funds and the related assets are removed from the consolidated balance sheet, for example, insurance and commercial entities or financial entities where no control exists.

Table 1: Treatment of legal entities under the consolidation approach as defined under Basel II

Type of treatment	Banks[1]	Securities firms[2]	Financial entities[3]	Commercial entities[4]	Insurance entities[5]
Consolidated	24	8	82		
Proportionately consolidated			8		
Deduction			11	110	6
Total	**24**	**8**	**101**	**110**	**6**

[1] Banks – public company's registered as banks in terms of the Banks Act, 1990.

[2] Securities firms – entities that conduct securities as envisaged in the Securities Services Act, 2004.

[3] Financial entities – entities that conduct financial activities, for example, lending business, financial leasing, consumer credit, mortgage credit, money transmission, portfolio management or money brokering.

[4] Commercial entities – entities primarily involved in the production of goods or non-financial services.

[5] Insurance entities – entities that conduct insurance business including any entity registered as an insurer in terms of the Short-term Insurance Act, 1998 or Long-term Insurance Act, 1998.

5. Approaches adopted

The Basel II approaches adopted by the group on 1 January 2008 are summarised below.

5.1 Credit risk

The group obtained approval from the South African Reserve Bank (SARB) to adopt the advanced internal ratings based (AIRB) approach for its credit portfolios. Certain portfolios in the group, for which the standardised and foundation internal ratings based (FIRB) approaches were initially adopted, are being migrated to the AIRB approach.

5.2 Operational risk

The group obtained approval from the SARB to adopt the standardised approach (TSA) for operational risk and at the same time implemented certain aspects of the advanced measurement approach (AMA) to bring the group in line with risk management best practice. The group has commenced with a formal programme to develop and implement an enhanced operational risk framework to support its target operational risk vision. The framework also aims to widely adopt best practices and will meet regulatory AMA requirements.

5.3 Market risk

The group obtained approval from the SARB to adopt the internal model approach for most trading product groups.

6. Capital management

The group's capital management framework is designed to ensure the group and its principal subsidiaries are capitalised in line with the group's risk profile, regulatory standards and economic capital standards. The group's capital management objectives are to:

- maintain sufficient capital resources to meet minimum regulatory capital requirements set by the SARB in accordance with Basel II requirements;
- maintain sufficient capital resources to support the group's risk appetite and economic capital requirements;
- support the group's credit rating;
- ensure that the group's foreign regulated subsidiaries meet their minimum capital requirements;
- allocate capital to businesses to support the group's strategic objectives, including optimising returns on economic regulatory capital; and
- ensure the group holds capital in excess of minimum requirements to achieve the target capital adequacy ratios set by management and debt rating objectives.

The GRCMC ensures compliance with the group's capital management objectives. The committee reviews actual and forecast capital adequacy on a quarterly basis. The processes in place for delivering the group's capital management objectives are:

- establishing internal targets for capital adequacy;
- managing capital ratio sensitivity to foreign exchange rate movements;
- ensuring regulatory capital adequacy requirements for foreign and local entities are met;
- allocating capital to support the group's strategic plans;
- applying stress tests to assess the group's capital adequacy under stress scenarios; and
- developing, reviewing and approving the ICAAP.

In addition to these processes, GROC and the board, through the GRCMC, annually review and set risk appetite, and analyse the impacts of stress scenarios to understand and manage the group's projected capital adequacy.

6.1 Capital adequacy

The group manages its capital base to achieve a prudent balance between maintaining capital ratios to support business growth and depositor confidence, and providing competitive returns to shareholders. The capital management process ensures that each group entity maintains sufficient capital levels for legal and regulatory compliance purposes. The group ensures that its actions do not compromise sound governance and appropriate business practices.

6.2 Regulatory capital

During the period under review the group complied with all externally imposed capital requirements to which its banking activities are subject, mainly, but not limited to, the relevant requirements of the Banks Act and Regulations relating to Banks, which are broadly consistent with the Basel II guidelines issued by the Bank for International Settlements, as well as those of the Financial Services Board (FSB) in South Africa.

In addition to the requirements of host country regulators, the group complies with the capital adequacy requirements of South African banking regulations. Regulatory capital adequacy is measured via two risk-based ratios, tier I and total capital adequacy ratios. Both these measures of capital are stated as a percentage of risk-weighted assets.

Tier I represents the permanent forms of capital such as share capital, share premium, retained earnings and

perpetual, non-cumulative preference shares whilst total capital also includes other items such as subordinated debt, impairments for performing loans and revaluation reserves.

Risk-weighted assets are determined on a granular basis by using risk weights calculated from internally derived risk parameters. Both on- and off-balance sheet exposures are included in the overall credit risk-weighted assets of the group. Notional risk-weighted assets for the market and operational risk components are determined using the risk drivers that impact on regulatory capital as inputs.

Tier I capital for the group was R71,2 billion as at 30 June 2009 (31 December 2008: R67,7 billion) and total capital for the group was R85,2 billion as at 30 June 2009 (31 December 2008: R81,6 billion). The change in the group's capital was primarily due to profits retained by the group in the first six months of the year and the issue of subordinated debt to the value of R1,9 billion.

The risk-weighted assets for the group reduced from R615 billion as at 31 December 2008 to R591,9 billion as at 30 June 2009. This reduction was mainly attributable to the impact of the strengthening of the rand on the group's offshore risk-weighted assets in the period under review.

The group maintained a well-capitalised position with strong core tier I, tier I and total capital ratios as set out in Table 2 overleaf.

6.3 Capital transferability

Subject to appropriate motivation and approval by exchange control authorities, no significant restrictions exist on the transfer of funds and regulatory capital within the group. The transfer of funds and regulatory capital within the group is conducted with due consideration given to the appropriateness of each action.

Table 2: Basel II regulatory capital

	June 2009 Rm	December 2008[1] Rm	June 2008[1] Rm
Tier I			
Issued primary capital and unimpaired reserve funds	**84 128**	87 225	83 783
Ordinary share capital and premium	**17 100**	16 997	17 301
Ordinary shareholders' reserves[2]	**63 070**	64 612	61 944
Minority interest	**3 958**	5 616	4 538
Regulatory deductions	**15 079**	14 432	12 344
Goodwill and other intangible assets	**7 651**	8 364	7 681
Investment in regulated non-banking entities not consolidated	**126**	110	132
Investment in banks not consolidated	**1 436**		
Other – 50% deducted from tier I and II respectively	**5 866**	5 958	4 531
Expected loss exceeding eligible provision	**821**	970	1 489
Investment in insurance and financial entities not consolidated	**4 822**	4 757	2 813
Other	**223**	231	229
Regulatory exclusions	**3 391**	10 562	10 173
Non-qualifying entities' ordinary shareholders' reserves[3]	**2 465**	3 642	3 512
Foreign currency translation reserves	**10**	6 168	4 932
Other reserves[4]	**916**	752	1 729
Preference share capital and premium	**5 495**	5 495	5 495
	71 153	67 726	66 761
Tier II			
Issued secondary capital and reserves	**17 899**	17 436	18 546
Preference share capital and premium	**8**	8	8
Subordinated debt	**17 059**	16 027	17 558
Impairments for performing loans	**832**	1 165	772
Revaluation reserves		236	208
Regulatory deductions – 50% deducted from tier I and II respectively	**5 866**	5 958	4 531
Expected loss exceeding eligible provision	**821**	970	1 489
Investment in insurance and financial entities not consolidated	**4 822**	4 757	2 813
Other	**223**	231	229
	12 033	11 478	14 015
Tier III			
Issued tertiary capital			
Subordinated debt	**2 040**	2 393	2 196
Total eligible capital	**85 226**	81 597	82 972
Total capital requirement	**57 711**	59 959	56 853
Total risk-weighted assets	**591 906**	614 960	583 104
Capital adequacy ratio (%)	**14,4**	13,3	14,2
Tier I capital adequacy ratio (%)	**12,0**	11,0	11,4
Core tier I capital adequacy ratio (%)	**11,1**	10,1	10,5

[1] *June and December 2008 comparatives have been restated.*

[2] *Unappropriated profits have been included in tier I capital.*

[3] *Mainly insurance and commercial entities.*

[4] *Mainly the share-based payment reserve, cash flow hedge reserve and available-for-sale revaluation reserve.*

Table 3: Capital adequacy ratio

	Minimum regulatory requirement %	Target ratio %	June 2009 %	December 2008[1] %	June 2008[1] %
Total capital adequacy ratio	9,75	11 – 12	**14,4**	13,3	14,2
Total tier I capital adequacy ratio	7,0	9	**12,0**	11,0	11,4
Core tier I capital adequacy ratio	5,25		**11,1**	10,1	10,5

[1] June and December 2008 comparatives have been restated.

Table 4: Basel II risk-weighted assets

	June 2009 Rm	December 2008[1] Rm	June 2008[1] Rm
Credit risk	**462 989**	496 323	462 275
Portfolios subject to the standardised approach	**108 576**	123 175	121 603
Corporate	**45 459**	54 179	61 518
Sovereigns	**20 098**	21 954	22 846
Banks	**16 817**	15 844	14 154
Residential mortgages	**3 281**	3 136	1 710
Retail – other[2]	**22 728**	27 868	21 181
Securitisation exposure	**193**	194	194
Portfolios subject to the FIRB approach	**86 730**	106 245	95 142
Corporate	**70 672**	87 864	79 858
Sovereigns	**494**	1 584	375
Banks	**15 297**	16 797	14 909
Securitisation exposure	**267**		
Portfolios subject to the AIRB approach	**231 768**	229 770	209 658
Corporate	**87 195**	88 481	73 209
Sovereigns	**3 349**	3 226	2 702
Banks	**10 062**	11 191	8 420
Retail mortgages	**61 383**	61 000	61 365
Qualifying retail revolving credit	**43 511**	37 991	34 521
Retail – other[2]	**24 183**	26 342	27 638
Securitisation exposure	**2 085**	1 539	1 803
Other assets	**19 684**	22 642	22 279
Equity risk	**16 231**	14 491	13 593
Portfolios subject to the market-based approach	**4 425**	7 074	6 657
Listed	**43**	1 485	2 057
Unlisted	**4 382**	5 589	4 600
Portfolios subject to the probability of default/loss given default approach	**11 806**	7 417	6 936
Market risk	**37 907**	40 442	46 956
Portfolios subject to the standardised approach	**26 765**	29 560	38 767
Portfolios subject to the internal models approach	**11 142**	10 882	8 189
Operational risk			
Portfolios subject to the standardised approach	**91 010**	78 195	73 873
Total risk-weighted assets	**591 906**	614 960	583 104

[1] June and December 2008 comparatives restated due to the re-calculation of credit risk and equity risk on a group level, resulting in risk-weighted assets decreasing by R19,1 billion (December 2008) and R1,4 billion (June 2008) respectively.

[2] Retail – other includes retail small and medium enterprises (SME), vehicle and asset finance and term lending.

6.4 Economic capital

Economic capital is the basis for measuring and reporting quantifiable economic risks faced by the group. The group assesses its economic capital requirements by measuring the group's risk profile using both internally and externally developed models. Economic capital is used for risk management, capital management, capital planning, capital allocation, evaluation of new business and performance measurement.

The group's economic capital management framework provides the governance and the methodology for the quantification of economic capital, and assigns roles and responsibilities for the management and allocation of economic capital across the group. Economic capital underpins the group's disciplined approach to risk and return decisions.

The methodologies used to govern the quantification of economic capital have evolved rapidly over the past two years. These methodologies are subject to regular reviews to ensure that the economic capital results are a true reflection of the underlying portfolios and risk drivers that impact the group.

Economic capital is the amount of permanent capital that a transaction, or business unit or risk type must hold in order to support the economic risk. For potential losses arising from risk types that are statistically quantifiable, economic capital reflects the worst case loss commensurate with the group's targeted financial strength. The group currently targets a rating of A-.

Economic capital is calculated for each of the following quantifiable risk types as defined in the group's risk taxonomy:

- credit risk;
- market risk;
- operational risk;
- business risk; and
- interest rate risk in the banking book (IRRBB).

The board, through the GRCMC, and senior executive management review economic capital results regularly, which facilitates improved risk management across the group.

The group has refined its ICAAP over the period under review to incorporate the impact of residual risk, risk concentrations, correlation of risk, diversification impacts and stress tests to ensure the group is adequately capitalised on an economic basis.

A key component of the ICAAP is the assessment of the group's capital adequacy using economic capital. The ICAAP was approved by the board, through the GRCMC, and formed the basis for discussion with the SARB on the group's risk profile and capital adequacy.

Table 5: Economic capital by risk type

	June 2009 Rm	December 2008 Rm	June 2008[1] Rm
Credit risk	**29 879**	32 891	27 440
Market risk	**1 433**	1 458	1 287
Operational risk	**5 219**	4 245	3 945
Business risk	**1 742**	1 225	1 225
Interest rate risk in the banking book	**3 173**	2 943	2 575
Banking activities – Economic capital	**41 446**	42 762	36 472
Available financial resources	**81 113**	82 699	81 483
Economic capital coverage ratio	**1,96**	1,93	2,23

[1] *June 2008 comparatives have been restated.*

Credit risk economic capital of R29,9 billion for June 2009 (December 2008: R32,9 billion) represents the largest source of risk faced by banking entities in the group and as such accounts for the majority of total economic capital. The decline of 9% in credit risk is mainly attributable to the impact of the appreciation of the rand on the group's offshore risk exposures.

Operational risk economic capital was higher in June 2009 at R5,2 billion (December 2008: R4,2 billion) due to the inclusion of 2008 audited gross income figures in the calculation of operational risk economic capital.

Business risk economic capital at R1,7 billion in June 2009 (December 2008: R1,2 billion) was higher due to a refinement in the quantification methodology.

The group's total economic capital requirement of R41,4 billion for June 2009 (December 2008: R42,8 billion) is reflective of the capital requirement to cover the risk profile of the group.

Available financial resources (AFR) is the capital supply defined on an economic basis, which essentially comprises permanent capital and is broadly equivalent to equity capital. The reduction in AFR to R81,1 billion as at June 2009 (December 2008: R82,7 billion) of R1,6 billion is largely due to the impact of the appreciation of the rand on the foreign currency translation reserve of the group, offset by profits earned in the first half of the year. The AFR covers the minimum economic capital requirement of R41,4 billion for June 2009 (December 2008: R42,8 billion) by a factor of 1,96 times (December 2008: 1,93 times), indicating a substantially higher capital position relative to risks assumed on banking activities.

Table 6: Capital adequacy of banking subsidiaries

	June 2009				December[1] 2008	June[1] 2008	
	Tier I capital %	**Tier II capital %**	**Tier III capital %**	**Total capital %**	Total capital %	Total capital %	**Host regulatory requirement %**
Standard Bank Group	12,0	2,1	0,3	14,4	13,3	14,2	9,75
The Standard Bank of South Africa (SBSA)	9,9	3,2	0,1	13,2	12,2	12,2	9,75
Rest of Africa							
CfC Stanbic Bank Kenya	11,2	4,3		15,5	13,0	17,2	12
Stanbic Bank Botswana	8,8	8,9		17,7	18,2	15,2	15
Stanbic Bank Congo	13,2	6,6		19,8	10,8	13,6	10
Stanbic Bank Ghana	12,7	3,2		15,9	18,4	13,4	10
Stanbic Bank Tanzania	17,3	2,0		19,3	14,0	17,1	12
Stanbic Bank Uganda	15,4	0,1		15,5	13,2	12,6	12
Stanbic Bank Zambia	12,8	4,3		17,1	15,5	18,7	10
Stanbic Bank Zimbabwe	34,2	1,2		35,4	58,5	15,9	10
Stanbic IBTC Bank Nigeria	37,9	0,5		38,4	29,9	23,0	10
Standard Bank Malawi	20,2	6,4		26,6	22,1	17,7	10
Standard Bank Mauritius	15,5	6,5		22,0	23,9	13,3	10
Standard Bank Mozambique	10,5	3,2		13,7	11,1	11,1	8
Standard Bank Namibia	14,3	3,2		17,5	14,5	14,5	10
Standard Bank Swaziland	11,8	3,6		15,4	17,5	12,9	8
Standard Lesotho Bank	13,6	1,3		14,9	8,9	17,2	8
Standard International Holdings, incorporating	10,1	2,1	1,1	13,3	13,7	12,6	10,6
– Banco Standard de Investimentos (Brazil)							
– Standard Bank Argentina							
– Standard Bank Asia (Hong Kong)							
– Standard Bank Plc (United Kingdom)							
– Standard Merchant Bank (Asia) (Singapore)							
– ZAO Standard Bank (Russia)							
Standard Bank Isle of Man	9,2	3,9		13,1	11,2	11,8	10
Standard Bank Jersey	9,2	2,7		11,9	11,1	12,1	10
Aggregate regulatory capital requirement for banking operations				10,1	10,4	10,1	

[1] *June and December 2008 comparatives have been restated.*

7. Credit risk

7.1 Definition

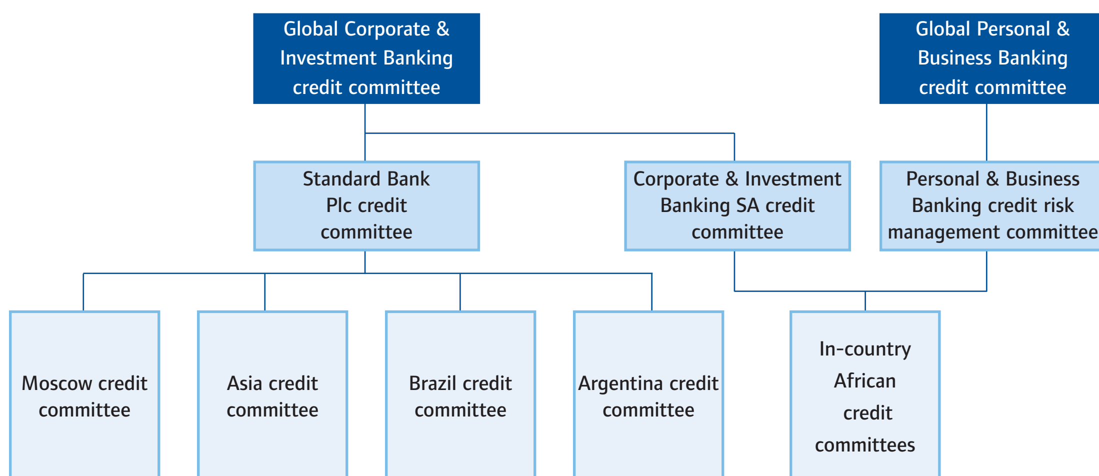
Credit risk arises mostly from lending and related banking activities, including underwriting and traded products such as derivative contracts, and securities borrowing and lending products. It may also arise when fair values fall due to credit risk of the group's exposure to financial instruments.

7.2 Framework and governance

Credit risk is the group's most material risk. It is managed in accordance with the group's comprehensive risk management control framework. A group credit standard sets out the principles under which the group is prepared to assume credit risk. Functional responsibility for credit risk resides within the group's business units while the group chief credit officer has responsibility for the oversight of credit risk across the group.

The principal executive management committee responsible for credit risk is GROC. The senior business unit credit committees, the global credit committees for both Personal & Business Banking and Corporate & Investment Banking, report directly to GROC and indirectly through GROC to the GCC. The global credit committees have been approved by the board as the designated committees for approving key aspects of the credit rating systems for Personal & Business Banking and Corporate & Investment Banking as required by the SARB, the Banks Act and the Regulations relating to Banks under the Banks Act, 1990. The GCC is the principal board committee responsible for credit risk, with GAC being responsible for reviewing credit impairment adequacy. The structure of the senior credit committees is illustrated in Figure 2 below.

Figure 2: Group senior credit committees



The committees have clearly defined mandates and delegated authorities, which are regularly reviewed. Membership of the regional committees includes senior credit officers of Standard Bank Plc. Credit committee responsibilities include: governance oversight; risk appetite; model performance, development and validation; counterparty and portfolio risk limits and approvals; country, industry, market, product, customer segment and maturity concentration risk; risk mitigation; impairments; stress testing; and risk usage and optimisation of regulatory and economic capital.

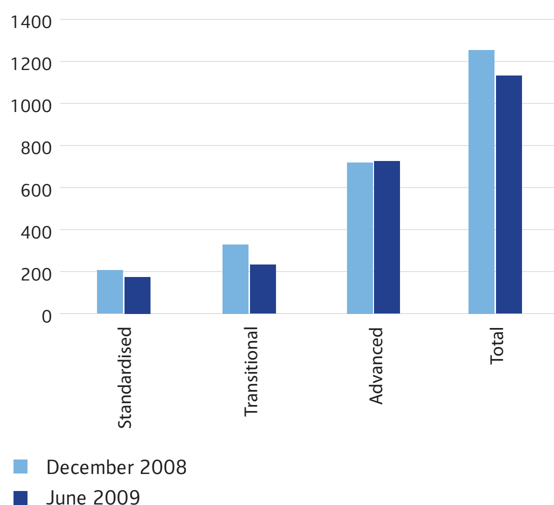
7.3 Basel II approaches adopted

The group has adopted the AIRB approach for credit risk. This is being consistently implemented across the group. Certain subsidiaries and portfolios that are not currently on the AIRB approach are in the process of migrating to this approach.

Due to the turmoil in the global economy since June 2008, December 2008 was deemed to be a more appropriate comparison for all risk types.

In certain instances, comparatives have been restated due to the refinement of methodology and/or in line with international best practice.

Graph 1: Group Basel II exposure by approach (Rbn)



7.4 Standardised approach

The group has adopted the standardised approach for some of its non-material subsidiaries and portfolios for which the calculation of regulatory capital is based on net counterparty exposures after recognising a limited set of qualifying collateral. A prescribed percentage, the risk weighting of which is based on the perceived credit rating of each counterparty, is then applied to the net exposure.

Table 7: External credit assessment institutions

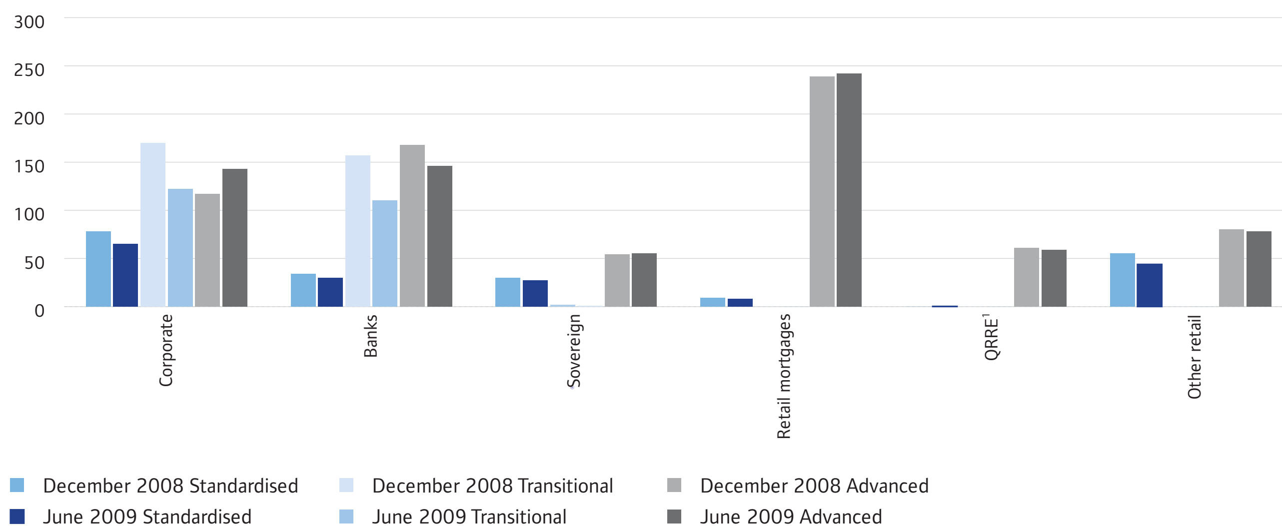
Asset class	Moody's Investor Services	Standard & Poor's	Fitch
Corporate		√	
Sovereign	√	√	
Banks		√	
SMEs			√

For exposures that have been rated by approved credit assessment institutions, the process prescribed by the SARB is used to ascribe public issue ratings into comparable assets in the banking book. For counterparties for which there are no credit ratings available, exposures are classified as unrated and a 100% risk weighting is applied for determining regulatory capital usage.

7.4.1 Analysis of exposures by risk weighting

Summarised in Table 8 below are the group's exposures subject to the standardised approach per risk weighting as at 30 June 2009 and 31 December 2008.

Graph 2: Group Basel II exposure by approach and asset class (Rbn)



[1] *QRRE – Qualifying revolving retail exposures*

Table 8: Exposure subject to the standardised approach per risk weighting

	June 2009			December 2008
	Exposure Rm	Mitigation Rm	Exposure after mitigation Rm	Exposure after mitigation Rm
Based on risk weights				
0% – 35%	23 307	145	23 162	22 191
50%	33 048	755	32 293	31 569
Rated	6 263	181	6 082	1 448
Unrated	26 785	574	26 211	30 121
75%	33 488	356	33 132	45 342
100% and above	84 019	1 556	82 463	102 963
Rated	9 061	912	8 149	1 772
Unrated	74 958	644	74 314	101 191
Total	173 862	2 812	171 050	202 065

7.4.2 Specialised lending exposures subject to the slotting approach

For certain specialised lending asset classes, the slotting approach under the standardised approach has been adopted.

Table 9: Specialised lending exposures

	June 2009 Rm	December 2008 Rm
Based on risk weight		
0% - 50%	**510**	602
70% - 95%	**767**	3 677
115% - 250%	**1 071**	841
Total	**2 348**	5 120

Specialised lending portfolios using the IRB approach, incorporated under the corporate asset class, are disclosed in the IRB analysis.

7.4.3 Equity exposures subject to the standardised approach

Equity exposures under the standardised approach as at 30 June 2009 and 31 December 2008 are set out in Table 10. Under this approach unlisted and listed equity exposures are ascribed a 100% risk weighting respectively.

Table 10: Equity exposures based on the standardised approach

	June 2009 Rm	December 2008 Rm
Categories		
Listed	**45**	51
Unlisted	**599**	499
Total	**644**	550

7.5 Internal ratings based (IRB) approach

Measuring credit risk under the IRB approach requires the assessment of its core components, which are probability of default (PD), exposure at default (EAD) and loss given default (LGD). The way in which the group measures these components for specific asset classes is described below.

7.5.1 Corporate, sovereign and bank exposures

Corporate, sovereign and bank exposures include South African and international companies, sovereigns (government entities), local and provincial government entities, pure bank financial institutions and public sector entities. Corporate entities include large corporate companies as well as small and medium corporate enterprises that are managed on a relationship basis or have a combined exposure to the group of more than R7,5 million.

A risk grade is assigned to each borrower using an appropriate rating model. Rating models are used to achieve objectivity, comparability, transparency and consistency in assigning ratings.

Most rating models take quantitative and qualitative factors as well as financial statements into account, which are combined to produce a stand-alone rating. The models also factor in geographic differences as well as support, both explicit and implicit, to determine the final risk grade.

The group uses an internationally comparable 25-point master rating scale for counterparties. Each performing risk grade is mapped to a PD that is used to quantify the credit risk for each borrower. The mapping of the master rating scale to the SARB risk buckets, external credit assessment institutions' alphanumerical rating scales and grading categories is shown in Table 11.

Table 11: Relationship between the group master rating scale & external ratings

Group master rating scale	SARB risk bucket	Moody's Investors Services	Standard & Poors	Fitch	Grading	Credit quality
1-4	AAA to AA-	Aaa, Aa1, Aa2, Aa3	AAA, AA+, AA, AA-	AAA, AA+, AA, AA-	Investment grade	Normal monitoring
5-7	A+ to A-	A1, A2, A3	A+, A, A-	A+, A, A-		
8-12	BBB+ to BBB-	Baa1, Baa2, Baa3	BBB+, BBB, BBB-	BBB+, BBB, BBB-		
13-21	BB+ to B-	Ba1, Ba2, Ba3, B1, B2, B3	BB+, BB, BB-, B+, B, B-	BB+, BB, BB-, B+, B, B-	Sub-investment grade	
22-25	Below B-	Caa1, Caa2, Caa3, Ca	CCC+, CCC, CCC-	CCC+, CCC, CCC-		Close monitoring
Default	Default		D	D	Default	Default

Absolute default probabilities are assigned to risk grades so that the long-run average default rate predicted by a model provides the best estimate of the population default rate over the economic cycle. This is done through a calibration process that uses historical default rates and other data from the applicable portfolio. In low default portfolios, such as the sovereign and bank asset classes, the group uses internal data where available and external benchmarks and studies, particularly from rating agencies.

EAD and LGD parameters are derived using approved methodologies and are based on a combination of internal and external historical default and recovery data. EAD is the exposure amount that the group estimates will be outstanding at the time of default. This estimation is most relevant for the group's revolving or working capital facilities and the methodology used is based on the borrower's risk grade or other factors. LGD is measured as a percentage of the EAD that the group estimates it will lose as a result of a default. It is based largely on the customer type, seniority of the loan and level of collateralisation.

7.5.2 Specialised lending exposures

Specialised lending exposures include project, object and commodity finance as well as real estate finance. Creditworthiness is assessed on a transactional level as the group relies on repayment from the cash flows generated by the underlying asset, as opposed to the financial strength of the borrower. The models used to rate project, object and commodity finance transactions are scorecards combining quantitative and qualitative factors to generate a PD and LGD for each transaction.

LGD per facility is calculated per loan tranche net of collateral. Since a characteristic of specialised lending is that the financed asset (project, commodity or object) forms an essential component of the recovery calculation, a realisable value is first calculated for the underlying asset. Additional forms of loss mitigation such as additional collateral (for example cash pledges, mortgages, bonds or equity), third or related party guarantees and insurance policies are then taken into account to derive the total value of all collateral held.

A blended scorecard approach is used to derive the credit risk grade of project, object and commodity finance deals, which is then converted to a unique PD. The property finance developer model is used to generate risk parameters for developer transactions originated by the property finance division of Corporate & Investment Banking and is only used in South Africa. The model applies a scorecard approach which combines quantitative and qualitative factors to calculate PD and LGD.

7.5.3 Retail mortgages

Retail mortgage exposures relate to mortgage loans to individuals. Credit behaviour in this instance is measured using internally developed scorecards. The PDs are calculated from behaviour scores using statistical calibration of internal historical default experience for the residential mortgage portfolio.

The LGDs per product are estimated using historic recovery data. The EAD is estimated per segment using internal historic data on limit utilisation.

7.5.4 Qualifying revolving retail exposures (QRRE)

QRRE relates to cheque accounts, credit cards and revolving personal loans. The credit behaviour of each portfolio is measured using internally developed scorecards specific to each portfolio. Mapping the behaviour score to a PD is performed for each portfolio using a statistical calibration of portfolio specific historical default experience.

The LGDs are estimated for portfolio specific segments using historic recovery data. The EAD is estimated per portfolio and per portfolio specific segment using internal historic data on limit utilisation.

7.5.5 Other retail

Other retail covers other branch lending and vehicle finance. The credit behaviour of each portfolio is measured using internally developed scorecards specific to each portfolio. Mapping the behaviour score to a PD is performed for each portfolio using a statistical calibration of portfolio specific historical default experience. As with QRRE portfolios, the LGDs are estimated for portfolio specific segments using historic recovery data and the EAD is estimated per portfolio and per portfolio specific segment using internal historic data on limit utilisation.

7.5.6 Equity exposures subject to the simple risk-weight method

Most equity exposures are treated under the PD/LGD approach described in Table 13 on the next page.

However, a portion of equity exposures are still measured using the simple risk-weighted method. These exposures as at 30 June 2009 and 31 December 2008 are set out in Table 12. Under this approach, unlisted and listed equity exposures are ascribed a 400% and 300% risk weighting respectively.

Table 12: Equity exposures based on the simple risk-weighted approach

	June 2009 Rm	December 2008 Rm
Categories		
Listed	**1**	1 337
Unlisted	**261**	260
Total	**262**	1 597

The group's international operations have migrated from the simple risk-weighted approach to the PD/LGD approach for equity exposures. Due to the adoption of this approach, there has been a reduction in listed equity exposures on the simple risk-weighted approach for June 2009 as seen in Table 12 below.

The PD/LGD approach is used to model the credit risk and capital requirement for equities excluding strategic investments in the banking portfolio. The group's standard approved risk grade models, described earlier, are used in this process together with the regulatory prescribed LGD of 90% and a maturity factor of five years.

The PD/LGD approach is used for most of the group's South African equity investment portfolios. Where no suitable model exists for the equity investment, the fall-back capital calculation is the simple risk-weighted approach.

7.5.7 Analysis of PDs, EADs and LGDs by asset class and risk grade under the IRB approach

Table 13 overleaf sets out the group's PDs, EADs and LGDs for specific Basel II asset classes under the IRB approach by risk grade bands as at 30 June 2009 and 31 December 2008.

Approximately 44% of the asset class exposures fall within the investment grade category. As per the group master rating scale, investment grade is represented by risk grades 1-12. The group monitors rating migration on an ongoing basis.

Table 13: Analysis of PDs, EADs and LGDs by risk grade

	Average PD %	Corporate EAD Rm	Corporate LGD %	Corporate Exposure weighted average risk weight %	Sovereign EAD Rm	Sovereign LGD %	Sovereign Exposure weighted average risk weight %	Banks EAD Rm	Banks LGD %	Banks Exposure weighted average risk weight %
June 2009										
Non-default		254 511			53 565			119 782		
1-4	0,03	6 389	36,76		4 137	31,51		44 324	39,32	
5-7	0,05	3 825	44,70					31 880	37,86	0,01
8-12	0,26	104 353	34,57	0,03	48 697	12,61	0,03	35 318	35,76	0,03
13-21	2,18	136 817	34,20	0,39	731	36,86	0,01	8 260	44,16	0,07
22-25	33,03	3 127	31,63	0,12					38,39	
Default	100,00	8 870	41,43	1,40	582	45,00	0,48	600		
Total		263 381	34,77		54 147	14,73		120 382	38,03	
December 2008										
Non-default		298 748			52 794			129 119		
1-4	0,03	4 790	31,51		2 436	25,09		49 828	37,53	
5-7	0,05	4 123	44,26		3	24,08		30 648	39,42	
8-12	0,26	140 422	32,16	0,04	48 869	12,52	0,03	38 832	36,35	0,03
13-21	2,53	143 585	31,66	0,38	1 486	42,49	0,03	9 774	42,33	0,08
22-25	33,16	5 828	36,31	0,23				37	0,84	
Default	100,00	3 969	43,79	0,57	13	45,00	0,01	2 281	11,67	0,20
Total		302 717	32,31		52 807	13,95		131 400	37,52	

7.6 Analysis of credit loss experience for the six months ended 30 June 2009

Given the difficult macroeconomic conditions in all the jurisdictions in which the group operates, credit quality deteriorated across all portfolios in the six months ended June 2009, albeit at a slowing rate.

The group's credit loss ratio was 1,84% for the period, reflecting a decline from the 1,86% recorded in the six months ending December 2008, in comparison to the increase from 1,31% recorded at end of June 2008.

In Personal & Business Banking, the credit loss ratio was 2,80% for the period (six months ending December 2008: 2,77%; six months ending June 2008: 2,18%). Non-performing loans as a percentage of the total book were 7,7% at the end of June 2009, 5,7% at the end of December 2008 and 4,0% at the end of June 2008. Despite the severity and duration of the economic downturn, early arrears have improved, and there are tentative signs that the rate of growth in impaired loans is slowing. Impaired loans increased by 49% between June 2008 and December 2008, and by 35% from December 2008 to June 2009.

Retail mortgages EAD Rm	Retail mortgages LGD %	Retail mortgages Exposure weighted average risk weight %	QRRE EAD Rm	QRRE LGD %	QRRE Exposure weighted average risk weight %	Retail other EAD Rm	Retail other LGD %	Retail other Exposure weighted average risk weight %	Equity Exposure Rm	Equity PD %
207 337			**47 384**			**74 146**			**3 072**	
1 038	**15,20**		**107**	**39,83**		**1 610**				
1 325	**15.14**		**1 279**	**45,62**		**2 773**				
33 705	**15,23**	**0,01**	**6 439**	**50,09**	**0,02**	**7 569**	**33,02**	**0,01**	**1 405**	**0,05**
148 699	**15,51**	**0,22**	**33 111**	**64,88**	**0,92**	**56 006**	**36,19**	**0,57**	**1 545**	**0,19**
22 570	**15,71**	**0,52**	**6 448**	**68,80**	**2,88**	**6 188**	**35,65**	**0,93**	**122**	**2,50**
19 324	**15,69**	**1,34**	**3 477**	**67,36**	**4,60**	**3 818**	**37,18**	**1,82**		
226 661	**15,50**		**50 861**	**63,13**		**77 964**	**33,85**		**3 072**	
218 988			49 011			76 948			2 855	
			40	44,90		870				
			1 271	43,05		2 625				
65 227	14,48	0,01	7 421	46,89	0,02	6 973	30,50	0,01	1 138	0,04
138 345	14,89	0,22	33 297	62,26	1,01	60 573	35,46	0,68	1 696	0,17
15 416	15,01	0,33	6 982	65,72	2,94	5 907	34,32	0,85	21	2,50
15 539	15,08	1,00	2 789	64,72	3,48	2 534	36,01	1,15		
234 527	14,80		51 800	60,17		79 482	33,40		2 855	

The credit loss ratio in Corporate & Investment Banking deteriorated to 1,15% (six months ending December 2008: 0,64%; six months ending June 2008: 0,31%). Global financial stress caused by falling commodity prices and suppressed demand for exports, and the significant slowdown in consumer spending, among other factors, heightened corporate default risk. Credit impairment charges rose 89% from the six months ended December 2008 to the six months ending June 2009, and 353% from the end of June 2008.

Targeted strategies will remain in place to proactively contain and manage credit risk and losses. Measures include appropriate credit extension criteria, close monitoring of troubled accounts, active management of early delinquencies and an ongoing improvement in collection capabilities.

7.7 Credit portfolio analysis

7.7.1 Analysis by asset class

Table 14 sets out the group's total Basel II exposures and EADs by approach and asset class as at 30 June 2009 and 31 December 2008. The two most material asset classes, corporate and retail mortgages, have significant levels of collateralisation in place.

Table 14: Asset class exposure by Basel II approach

	On-balance sheet			Off-balance sheet			Repurchase and resale agreements		
	Standardised Rm	Transitional Rm	Advanced Rm	Standardised Rm	Transitional Rm	Advanced Rm	Standardised Rm	Transitional Rm	Advanced Rm
June 2009									
Corporate	59 425	79 990	46 121	5 047	6 705	57 134	297	14 016	24 130
Sovereign	24 164	1 147	52 610	2 178	114	192	962		2 504
Banks	26 601	24 603	50 468	2 937	3 029	5 090	30	36 647	18 613
Retail exposure	43 982		303 221	8 076		76 788			
Retail mortgages	7 719		209 587			32 824			
QRRE	366		32 571			26 887			
Other retail	35 897		61 063	8 076		17 077			
Total	154 172	105 740	452 420	18 238	9 848	139 204	1 289	50 663	45 247
December 2008									
Corporate	69 777	101 175	36 124	7 589	9 897	46 284	60	15 677	21 339
Sovereign	27 867	1 309	51 305	41	286	30	1 679		2 751
Banks	29 120	24 822	53 789	4 445	2 982	5 770	615	40 339	17 741
Retail exposure	51 549		303 271	12 441		76 408			
Retail mortgages	9 052		207 780			31 252			
QRRE			33 177			27 577			
Other retail	42 497		62 314	12 441		17 579			
Total	178 313	127 306	444 489	24 516	13 165	128 492	2 354	56 016	41 831

Derivative instruments			Total by approach			Total	Gross defaulted exposures	EAD		Impairment of exposures	
Standardised Rm	Transitional Rm	Advanced Rm	Standardised Rm	Transitional Rm	Advanced Rm	Rm	Rm	Transitional Rm	Advanced Rm	Specific Rm	Portfolio Rm
143	21 203	15 999	64 912	121 914	143 384	330 210	11 353	100 170	165 697	2 232	
	23	8	27 304	1 284	55 314	83 902	13	1 272	52 875	7	
18	45 277	72 032	29 586	109 556	146 203	285 345	710	47 511	72 871	528	
2			52 060		380 009	432 069	29 698		355 486	9 121	
			7 719		242 411	250 130	19 338		226 661	4 099	
			366		59 458	59 824	3 477		50 861	1 426	
2			43 975		78 140	122 115	6 883		77 964	3 596	
163	66 503	88 039	173 862	232 754	724 910	1 131 526	41 774	148 953	646 929	11 888	5 289
452	43 479	13 378	77 878	170 228	117 125	365 231	6 610	133 647	174 088	1 157	
	27	13	29 587	1 622	54 099	85 308	13	1 452	51 355	7	
276	88 540	91 055	34 456	156 683	168 355	359 494	790	53 098	78 302	396	
15			64 005		379 679	443 684	22 976		365 809	7 036	
			9 052		239 032	248 084	15 555		234 527	2 923	
					60 754	60 754	2 789		51 800	1 290	
15			54 953		79 893	134 846	4 632		79 482	2 823	
743	132 046	104 446	205 926	328 533	719 258	1 253 717	30 389	188 197	669 554	8 596	5 422

7.8 Impairments and roll forward

7.8.1 Financial assets carried at amortised cost

At each balance sheet date, the group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired.

First, the group assesses whether there is objective evidence of impairment for financial assets that are individually significant. For those financial assets that are not individually significant, the assessment is done collectively.

Non-performing loans are impaired for doubtful debts identified during periodic evaluations of advances. Retail loans and advances are considered non-performing when amounts are due and unpaid for three months. Corporate loans are analysed on a case-by-case basis taking into account breaches of key loan conditions. The impairment of non-performing loans takes account of past loss experience adjusted for changes in economic conditions and the nature and level of risk exposure since the recording of the historic losses. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

When a loan carried at amortised cost has been identified as impaired, the carrying amount of the loan is reduced to an amount equal to the present value of estimated future cash flows, including the recoverable amount of any collateral, discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised as a credit impairment in the income statement.

If the group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is recognised are not included in a collective assessment for impairment.

Impairment of performing loans can only be accounted for if there is objective evidence that a loss event has occurred after the initial recognition of the financial asset but before the balance sheet date. To provide for latent losses in a portfolio of loans that have not yet been individually identified as impaired, a credit impairment for incurred but not reported losses is recognised based on historic loss patterns and estimated emergence periods. Loans are also impaired when adverse economic conditions develop after initial recognition which may impact future cash flows.

Increases in loan impairments and any subsequent reversals or recoveries of amounts previously impaired are reflected in the income statement. Previously impaired advances are written off once all reasonable attempts at collection have been made and there is no realistic prospect of recovering outstanding amounts. Any subsequent reductions in amounts previously impaired are reversed by adjusting the allowance account and the amount of the reversal is recognised as a reduction in impairment for credit losses in the income statement. Subsequent recoveries of previously written off advances are recognised in the income statement.

Subsequent to impairment, the effects of discounting unwind over time as interest income.

7.8.2 Financial assets classified as available-for-sale

Financial assets classified as available-for-sale are impaired if there is objective evidence of impairment, resulting from one or more loss events that occurred after initial recognition but before the balance sheet date, that have an impact on the future cash flows of the asset. In addition, an available-for-sale equity instrument is generally considered impaired if a significant or prolonged decline in the fair value of the instrument below its cost has occurred. Where an available-for-sale asset, which has been remeasured to fair value directly through equity, is impaired, the impairment loss is recognised in the income statement. If any loss on the financial asset was previously recognised directly in equity as a reduction in fair value, the cumulative net loss that had been recognised in equity is transferred to the income statement and is recognised as part of the impairment loss.

The amount of the loss recognised in the income statement is the difference between the acquisition cost and the current fair value, less any previously recognised impairment loss. If, in a subsequent period, the amount relating to impairment loss decreases and the decreases can be linked objectively to an event occurring after the impairment loss was recognised in the income statement, and where the instrument is a debt instrument, the impairment loss is reversed through the income statement. An impairment loss in respect of an equity instrument classified as available-for-sale is not reversed through the income statement but accounted for directly in equity.

Table 15 overleaf represents the movement in the allowance for impairments relating to loans and advances to customers for the six months ending June 2009.

Table 15: Movement in group loans and advances impairment

	June 2009[1]				December 2008[2]
	Corporate Rm	Retail secured Rm	Retail unsecured Rm	Total Rm	Total Rm
Specific impairments on impaired loans					
Balance at beginning of the period	1 561	4 739	2 296	8 596	3 923
Acquisition of subsidiaries					112
Net impairments raised and released[3]	1 902	3 272	2 219	7 393	9 854
Impaired accounts written off	(101)	(812)	(1 701)	(2 614)	(4 375)
Discount element recognised in interest income	(39)	(735)	(75)	(849)	(986)
Exchange and other movements	(556)	(25)	(57)	(638)	68
Balance at end of the period	2 767	6 439	2 682	11 888	8 596
Portfolio impairments on performing loans					
Balance at beginning of the period	2 707	1 283	1 432	5 422	3 340
Acquisition of subsidiaries					36
Net impairments raised and released	(179)	(137)	322	6	1 996
Impaired accounts written off			(3)	(3)	
Discount element recognised in interest income	(4)			(4)	
Exchange and other movements	(144)	2	10	(132)	50
Balance at end of the period	2 380	1 148	1 761	5 289	5 422
Total	5 147	7 587	4 443	17 177	14 018

[1] *Movements in group loans and impairments for the twelve months ended December 2008.*

[2] *Net provisions raised and released less recoveries of amounts written off in previous years equals the income statement impairment charge.*

[3] *Movements in group loans and impairments for the six months ended June 2009.*

7.9 Analysis by industry

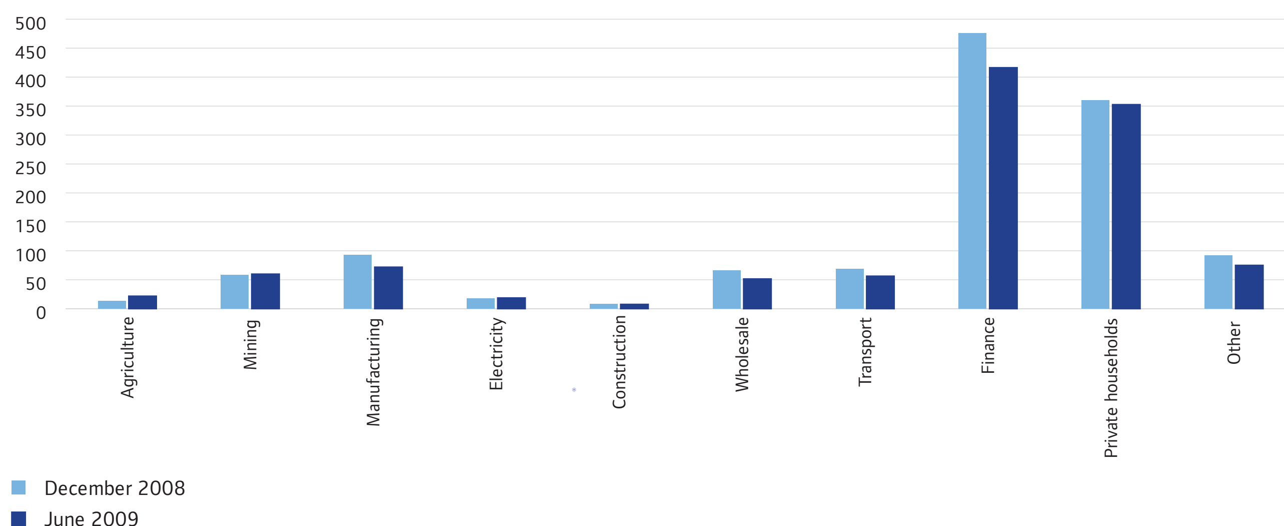
Table 16 overleaf shows the Basel II exposures by type of asset and industry as at 30 June 2009 and 31 December 2008. Graph 3 overleaf represents the total gross exposure by industry for 30 June 2009 and 31 December 2008.

Table 16: Basel II exposures by type of asset and industry

	On-balance sheet Rm	Off-balance sheet Rm	Repurchase and resale agreements Rm	Derivative instruments Rm	Total gross exposure[1] Rm	Gross defaulted exposures Rm	Impairment of exposures Specific Rm	Impairment of exposures Portfolio Rm
June 2009								
Agriculture	**16 213**	**5 206**	**223**	**116**	**21 758**	**1 082**	**436**	
Mining	**35 356**	**18 123**	**438**	**5 930**	**59 847**	**1 273**	**349**	
Manufacturing	**53 411**	**13 582**	**242**	**4 646**	**71 881**	**1 883**	**585**	
Electricity	**13 817**	**2 291**	**388**	**2 216**	**18 712**	**504**	**26**	
Construction	**4 264**	**2 985**		**361**	**7 610**	**71**	**424**	
Wholesale	**30 007**	**12 639**	**41**	**8 832**	**51 519**	**882**	**425**	
Transport	**44 554**	**9 778**	**26**	**1 965**	**56 323**	**691**	**302**	
Finance	**161 764**	**28 622**	**95 543**	**130 391**	**416 320**	**8 315**	**2 014**	
Private households	**288 575**	**63 977**		**2**	**352 554**	**25 771**	**5 353**	
Other	**64 371**	**10 087**	**298**	**246**	**75 002**	**1 302**	**1 974**	
Total	**712 332**	**167 290**	**97 199**	**154 705**	**1 131 526**	**41 774**	**11 888**	**5 289**
December 2008								
Agriculture	10 231	2 250	465	176	13 122	729	458	
Mining	35 157	11 432	665	10 939	58 193	140	129	
Manufacturing	62 637	21 207	496	8 748	93 088	1 478	388	
Electricity	12 861	2 011	174	2 623	17 669	462	5	
Construction	4 312	2 976		606	7 894	44	195	
Wholesale	34 348	13 100	55	18 979	66 482	741	421	
Transport	58 649	6 979	22	3 268	68 918	382	96	
Finance	157 142	30 060	97 839	191 099	476 140	5 040	557	
Private households	291 799	67 393	424	484	360 100	20 375	5 122	
Other	82 972	8 765	61	313	92 111	998	1 225	
Total	750 108	166 173	100 201	237 235	1 253 717	30 389	8 596	5 422

[1] *Gross – amount before the application of any offset, mitigation or netting.*

Graph 3: Basel II total gross exposure by type of industry (Rbn)



7.10 Analysis by geographic region

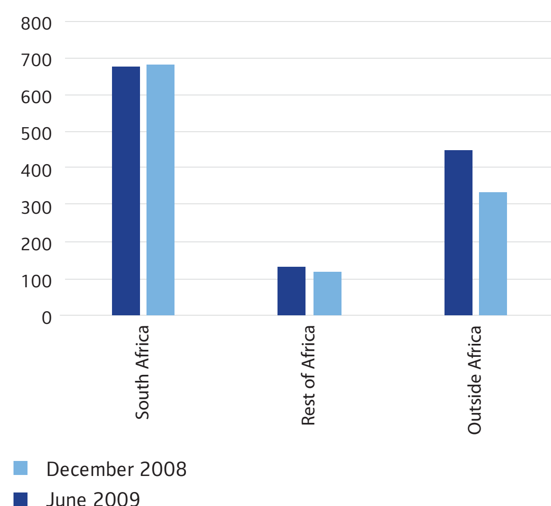
Table 17 shows the group's Basel II exposures by type of asset and geographic region as at 30 June 2009 and 31 December 2008. Graph 4 that follows shows the total gross exposure per geographic region as at 30 June 2009 and 31 December 2008.

Table 17: Basel II exposures by type of asset and geographic region

	On-balance sheet Rm	Off-balance sheet Rm	Repurchase and resale agreements Rm	Derivative instruments Rm	Total gross exposure[1] Rm	Gross defaulted exposures Rm	Impairment of exposures Specific Rm	Impairment of exposures Portfolio Rm
June 2009								
South Africa	469 355	137 639	44 621	28 265	679 880	31 836	8 619	
Other African countries	104 657	10 323	1 760	1 115	117 855	2 499	1 117	
Europe	56 287	6 501	37 114	83 352	183 254	2 083	679	
Asia	38 819	5 658	3 452	5 517	53 446	3 128	634	
North America	9 569	795	1 936	33 026	45 326	420	202	
South America	31 842	6 348	8 308	2 985	49 483	1 623	557	
Other	1 803	26	8	445	2 282	185	80	
Total	**712 332**	**167 290**	**97 199**	**154 705**	**1 131 526**	**41 774**	**11 888**	**5 289**
December 2008								
South Africa	470 536	133 706	39 507	31 612	675 361	23 873	6 474	
Other African countries	114 135	12 819	2 019	1 601	130 574	1 836	1 022	
Europe	71 091	3 202	34 182	149 999	258 474	1 221	249	
Asia	46 082	4 954	9 204	11 434	71 674	1 238	254	
North America	7 223	686	773	36 464	45 146	822	155	
South America	40 482	10 795	14 516	5 028	70 821	1 399	442	
Other	559	11		1 097	1 667			
Total	750 108	166 173	100 201	237 235	1 253 717	30 389	8 596	5 422

[1] *Gross – amount before the application of any offset, mitigation or netting.*

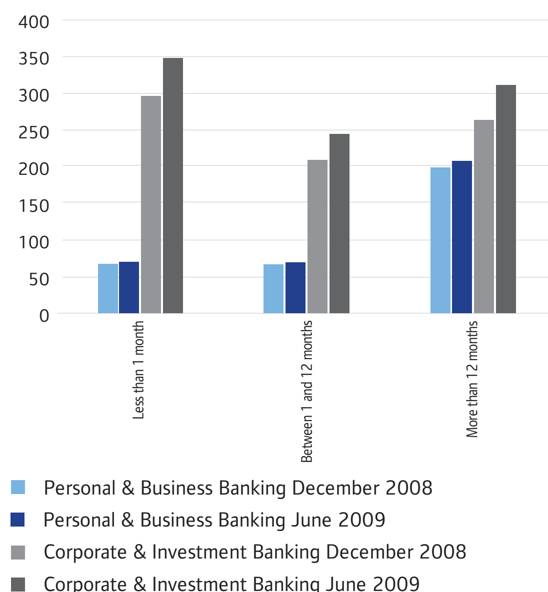
Graph 4: Group Basel II total gross exposure by geographic region (Rbn)



7.11 Residual contractual maturity

Graph 5 below represents the group's Basel II exposures by residual contractual maturity at 30 June 2009.

Graph 5: Group Basel II exposures by residual contractual maturity (Rbn)



7.12 Credit risk mitigation and hedging

Collateral, guarantees, credit derivatives and on- and off-balance sheet netting are widely used by the group to mitigate credit risk. The amount and type of credit risk mitigation depends on the circumstances in each case. Credit risk mitigation policy and procedure ensure that credit risk mitigation techniques are acceptable, used consistently, valued appropriately and regularly, and meet the risk requirements of operational management for legal, practical and timely enforceability. Detailed processes and procedures are in place to guide each type of mitigation used.

The main types of collateral taken are mortgage bonds over residential, commercial and industrial properties, cession of book debts, bonds over plant and equipment and, for leases and instalment sales, the underlying moveable assets financed. All security is valued on an annual basis. Reverse repurchase agreements are underpinned by the assets being financed, which are mostly liquid, tradeable financial instruments.

Guarantees and related legal contracts are often required, particularly in support of credit extension to groups of companies and weaker counterparties. Guarantor counterparties include banks, parent companies, shareholders and associated counterparties. Creditworthiness is established for the guarantor as for other counterparty credit approvals.

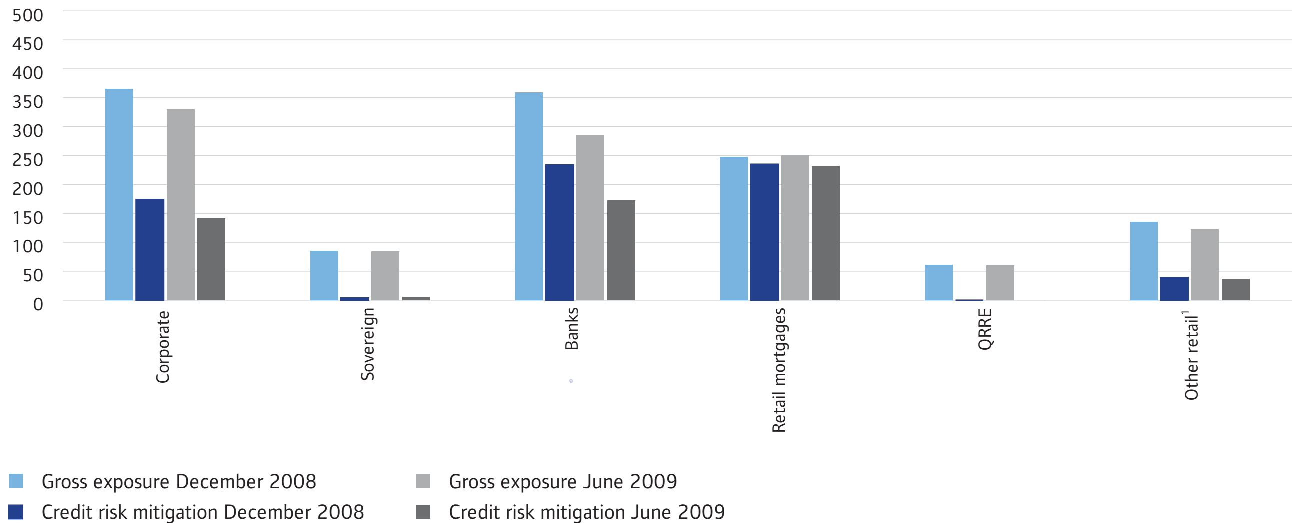
For derivative transactions, the group typically requires the use of internationally recognised and enforceable Institute of Swap Dealers Association (ISDA) agreements with a credit support annex, where necessary. Exposures are generally marked-to-market daily; netting is applied to the full extent contractually agreed by the parties, and cash or near cash collateral posted where contractually provided for. Since the counterparty credit risk of derivatives can vary over time according to market factors, exposures to counterparty credit risk are calculated by adding increases in future potential exposure to the balance of present exposure.

To manage actual or potential portfolio risk concentrations in areas of higher credit risk and credit portfolio growth, the group implements hedging and other strategies from time to time. This is typically done at individual counterparty, sub-portfolio and portfolio levels.

Syndication, distribution and sale of assets, asset and portfolio limit management, credit derivatives and credit protection are used. Implementation and performance are measured regularly and reporting tools are in place to ensure effective monitoring.

The group's Basel II exposure and total credit risk mitigation for portfolios under the IRB and standardised approaches per primary asset class as at 30 June 2009 and 31 December 2008 are analysed in Graph 6 overleaf.

Graph 6: Group Basel II exposure and mitigation by asset class (Rbn)



[1] *Other retail consists of SME retail and retail other.*

7.13 Policy for securing collateral

Each credit division has specialised legal practitioners who are responsible for ensuring that legally valid, binding and enforceable loan agreements and amendments to standard security documents are in place where required. Security is provided to the group by counterparties accepting lending facilities. In certain instances, further counsel is sought from external attorneys in respect of unusual forms of security or where security is provided by foreign companies.

7.14 Wrong way risk exposures

Wrong way risk arises where there is a positive correlation between counterparty default and transaction exposure. Transactions where this may arise are, for example, reverse repurchase and collateralised forward sale transactions. This risk is addressed by taking into consideration the higher than normal correlation between the default event and exposure to a counterparty when calculating the potential exposure on these transactions.

7.15 Collateral required in the event of a credit rating downgrade

The group enters into derivative contracts with rated and unrated counterparties. To mitigate counterparty credit risk, the group stipulates credit protection terms such as limitations on the amount of unsecured credit exposure it will accept, collateralisation if mark-to-market credit exposure exceeds those amounts and collateralisation and/or termination of the contract if certain credit events occur, including but not limited to a downgrade of the counterparty's public credit rating.

Certain counterparties require that the group provide similar credit protection terms. From time to time, the group may agree to provide those terms on a restrictive basis. Rating downgrades as a collateralisation or termination event are generally only conceded to highly rated counterparties and, whenever possible, on a bilateral reciprocal basis. In exceptional cases, the group may concede such rating downgrades to unrated counterparties when their size, credit strength and business potential are deemed acceptable.

The impact on the group of the amount of collateral it would have to provide given a credit downgrade is determined by the negative mark-to-market on derivative contracts where such a collateralisation trigger has been conceded.

Where the impact on the group’s liquidity of a collateral call linked to downgrading is deemed to be material, the potential exposure is taken into account in model stress testing. Generally, however, the extent of legal commitments that could result in collateral calls triggered by a rating downgrade is not material and would not have an adverse effect on the group's financial position.

A detailed analysis of credit risk mitigation used by the group is provided per asset class for the IRB and standardised approaches as at 30 June 2009 and 31 December 2008 in Tables 18 and 19 overleaf.

Table 18: Basel II credit risk mitigation for portfolios under the IRB approach

	Eligible financial collateral Rm	Other eligible IRB collateral Rm	Guarantees and credit derivatives Rm	Effects of netting agreements Rm	Total credit risk mitigation Rm
June 2009					
Asset class					
Corporate	66 322	33 177	23 866	16 372	139 737
Sovereign	2 568	132	2 968		5 668
Banks	65 050	329	4 511	100 986	170 876
Retail exposure		268 792			268 792
Retail mortgages		231 831			231 831
QRRE		242			242
Other retail		36 719			36 719
Total	133 940	302 430	31 345	117 358	585 073
December 2008					
Asset class					
Corporate	81 611	35 744	28 054	26 203	171 612
Sovereign	2 719	203		9	2 931
Banks	71 103	354	5 914	155 064	232 435
Retail exposure		273 628			273 628
Retail mortgages		234 730			234 730
QRRE		238			238
Other retail		38 660			38 660
Total	155 433	309 929	33 968	181 276	680 606

Table 19: Basel II credit risk mitigation for portfolios under the standardised approach

	Eligible financial collateral Rm	Guarantees and credit derivatives Rm	Total credit risk mitigation Rm
June 2009			
Asset class			
Corporate	989	22	1 011
Sovereign	625		625
Banks	310	726	1 036
Retail exposure	139	1	140
Total	2 063	749	2 812
December 2008			
Asset class			
Corporate	1 923	26	1 949
Sovereign	643		643
Banks	882	241	1 123
Retail exposure	146		146
Total	3 594	267	3 861

7.16 Analysis of over-the-counter derivatives

Tables 20 to 22 below present the group's exposure in terms of over-the-counter derivatives across various markets such as equities, foreign exchange and gold for all relevant Basel II asset classes and collateral held as at 30 June 2009 and 31 December 2008.

Table 20: Basel II over-the-counter derivatives exposure

	June 2009 Rm	December 2008 Rm
Notional principal amount of over-the-counter derivatives		
Interest rate products	**6 466 670**	7 597 343
Forex and gold	**969 842**	1 119 701
Equities	**53 658**	166 087
Precious metals	**99 946**	60 557
Other commodities	**196 869**	188 584
Credit derivatives	**129 485**	154 432
Protection bought	**60 927**	72 467
Protection sold	**68 558**	81 965
Total	**7 916 470**	9 286 704

Table 21: Basel II over-the-counter derivatives exposure

	June 2009 Rm	December 2008 Rm
Gross positive fair value of over-the-counter derivatives	**154 707**	236 987
Interest rate products	**66 772**	83 285
Forex and gold	**49 999**	71 321
Equities	**1 920**	2 392
Precious metals	**3 504**	6 725
Other commodities	**26 085**	60 112
Credit derivatives	**6 427**	13 152
Protection bought	**5 586**	12 626
Protection sold	**841**	526
Netting benefits	**(117 357)**	(181 276)
Net current credit exposure (i.e. net fair value)	**37 350**	55 711
Exposure at default	**66 248**	79 049

Table 22: Basel II over-the-counter derivatives exposure

	June 2009 Rm	December 2008 Rm
Collateral		
Cash	**10 287**	19 395

7.17 Analysis of securities financing transactions

Tables 23 and 24 show the group's exposure in terms of securities financing transactions such as repurchase agreements, resale agreements, securities lending and securities borrowing agreements for all relevant Basel II asset classes and collateral held as at 30 June 2009 and 31 December 2008.

Table 23: Basel II securities financing transactions exposure

	June 2009 Rm	December 2008 Rm
With master netting agreement	**33 108**	35 785
Without master netting agreement	**63 793**	64 355
Total	**96 901**	100 140

Table 24: Basel II securities financing transactions collateral

	June 2009 Rm	December 2008 Rm
Cash	**33 315**	29 161
Commodities	**545**	1 459
Debt securities	**62 397**	67 753
Equities	**2 124**	4 834
Total	**98 381**	103 207
Exposure at default	**6 782**	8 190

7.18 Securitisation

The group has used securitisation primarily as part of its funding strategy for its South African operations to provide added flexibility in mitigating structural liquidity risk and diversifying the funding base. Credit risk transfer and capital relief are factored in when deciding the economic merits of each new securitisation issue.

The group has entered into securitisation transactions in the normal course of business in which it transferred recognised financial assets directly to third parties or special purpose entities. Total assets originated by the group and subsequently securitised amounted to R18 billion at 30 June 2009 (December 2008: R18 billion).

The following external credit assessment institutions have rated the group's securitisations:

Securitisation category	Rating agency
Corporate	Fitch
Retail mortgages	Moody's Investor Services and Fitch
Retail instalment sale and leasing	Moody's Investor Services and Fitch
Retail other	Fitch

The group fulfils a number of roles in the process of securitising assets including sponsor, administrator, hedge counterparty, commercial paper dealer, liquidity facility provider of asset backed commercial paper conduits (special purpose legal entities), originator, seller, dealer, settlement agent, subordinated lender, shareholder, calculating agent and account bank.

The credit granting, monitoring and debt management processes followed for securitised assets are the same as for similar assets in the group. Performing loans, non-performing loans and related provisions are included in the group results.

To calculate the regulatory capital on securitised assets that are retained by the group, both the AIRB and standardised approaches are used and the group has adopted the ratings based approach under AIRB.

The contraction in the local and international securitisation markets experienced in 2008 continued during the first half of 2009. As a result the group did not use new securitisations as an alternative source of funding in this period.

In the first six months of 2009, Blue Granite Investments No.1, Blue Granite Investments No. 2, Blue Granite Investments No. 3 and Blue Granite Investments No. 4 exceeded a number of arrears related triggers during the period, however, all existing mortgage advance securitisations were maintained within covenant levels. The breach of certain arrears related triggers resulted from the deterioration in the underlying asset performance. Accordingly, these SPVs are required to trap cash in arrears reserves and have started repayment to note holders earlier than expected. As at 30 June 2009, R276 million had been repaid to note holders.

With regards to the instalment sale securitisation vehicles, Accelerator Fund 1 exercised its clean up call option during April 2009 in accordance with its transaction documents and the Securitisation Regulations promulgated under the Banks Act, 1990. All note holders and the subordinated lender were repaid in full. The Accelerator Fund 2 principal deficiency experienced during the second half of 2008 was reversed in the first half of 2009.

7.18.1 Analysis of securitisation activity for the period

Table 25 below shows the group's securitisation activity for 30 June 2009 and 31 December 2008, which was mainly in the secondary role of investor. The group's risk of first loss through subordinated loans to securitisation SPEs was R263 million as at 30 June 2009, and this exposure was assessed for impairment as part of the normal credit provisioning process.

Table 25: Basel II securitisation activity for the year

	June 2009				December 2008
	Corporate Rm	**Retail mortgages Rm**	**Retail loans Rm**	**Total Rm**	Total Rm
Primary role					
As originator	**44**			**44**	521
Secondary role					
As investor		**205**		**205**	5 070
Total activity for the year	**44**	**205**		**249**	5 591

7.18.2 Analysis of retained securitised on-balance sheet exposures

Table 26 overleaf presents an analysis of the group's retained securitised on-balance sheet exposures under the IRB and standardised approaches as at 30 June 2009 and 31 December 2008 by creditworthiness, defined in terms of the group master rating scale.

Table 26: Basel II securitised on-balance sheet exposures under the IRB and standardised approaches by asset class

	June 2009				December 2008
	Corporate Rm	Retail mortgages Rm	Retail loans Rm	Total Rm	Total Rm
IRB					
Personal & Business Banking		753	18	771	834
Investment grade		619	18	637	700
Sub-investment grade		134		134	134
Corporate & Investment Banking	1 682	5 953	1 649	9 284	3 561
Investment grade	1 682	5 953	1 649	9 284	3 561
Total IRB exposures	1 682	6 706	1 667	10 055	4 395
Standardised					
Personal & Business Banking		318		318	320
Investment grade		318		318	320
Total Standardised exposures		318		318	320

7.18.3 Analysis of securitised off-balance sheet exposures

Table 27 below presents an analysis of the group's securitised off-balance sheet exposures under the IRB approach as at 30 June 2009 and 31 December 2008, and by creditworthiness defined in terms of the group master rating scale. There were no off-balance sheet securitised exposures under the standardised approach. Disclosed numbers in Table 27 are related to the liquidity support provided.

Due to rating agency requirements relating to commercial paper issued by Blue Titanium, an asset-backed commercial paper conduit sponsored and managed by SBSA, the terms of the credit support provided by SBSA to Blue Titanium were amended in May 2009. In order to calculate and report the exposures in terms of the Basel II capital adequacy requirements, the underlying exposures (assets held by Blue Titanium) have now been included in Table 26 as on-balance sheet exposures. This exposure was previously reported in Table 27 as a part of the off-balance sheet exposure.

Table 27: Basel II securitised off-balance sheet exposures under the IRB approach by asset class

	June 2009				December 2008
	Corporate Rm	Retail mortgages Rm	Retail loans Rm	Total Rm	Total Rm
Investment grade		2 694		2 694	10 384
Total IRB exposures		2 694		2 694	10 384

7.18.4 Analysis of capital deductions with respect to securitised investments retained by the group

Table 28 below represents the capital deductions required with respect to the securitised investments under the IRB and standardised approaches as at 30 June 2009 and 31 December 2008.

Table 28: Basel II securitisation capital deductions by approach

	Risk weighted assets Rm	Primary capital and reserve funds Rm	Secondary capital and reserve funds Rm
June 2009			
IRB	**2 085**	**67**	**67**
Standardised	**193**	**1**	**1**
Total	**2 278**	**68**	**68**
December 2008			
IRB	1 539	67	67
Standardised	194	1	1
Total	1 733	68	68

8. Country and cross-border risk

8.1 Framework and governance

The management of cross-border country limits is delegated to the group country risk management committee (GCRC). For all countries with limits, there is a formal review process which concentrates on countries rated 7 and higher, on a 1 to 25 rating scale, referred to as medium- and high-risk countries. The GCRC, a sub-committee of GROC, sets the maximum cross-border risk appetite for each country and ensures the effective approval, measurement, monitoring and control of cross-border risk.

An internal rating model is used to determine the ranking of each country. In determining ratings, extensive use is made of the group's network of operations, country visits and external sources of information. The model inputs are continuously updated to reflect economic and political changes in individual countries. Ratings are also benchmarked against those determined by rating agencies and other parties.

Countries designated as higher-risk are subject to increased central monitoring.

9. Liquidity risk

9.1 Definition

Liquidity risk arises when the group is unable to meet its payment obligations when they fall due. This may be caused by the group's inability to liquidate assets or to obtain funding to meet its liquidity needs.

9.2 Framework and governance

The nature of banking and trading results in continuous exposure to liquidity risk. The group's liquidity management framework, which is unchanged from the previous reporting period, is designed to measure and manage liquidity positions such that increasing funding requirements and payment obligations can be met at all times, under both normal and considerably stressed conditions. Under the delegated authority of the board, the group asset and liability committee (ALCO) sets liquidity risk standards in accordance with regulatory requirements and international best practice. This ensures that a comprehensive and consistent governance framework for liquidity risk management is followed across the group. Each banking entity in the group has an ALCO responsible for ensuring compliance with liquidity risk policies. Both the Africa ALCO and International Capital committee report into the group ALCO chaired by a deputy group chief executive.

9.3 Liquidity and funding management

The group is substantially aligned to the Basel committee's principles for sound liquidity management issued in September 2008.

Each banking entity within the group is required to incorporate the following elements as part of a cohesive liquidity management process:

- maintaining a sufficiently large liquidity buffer;
- ensuring a structurally sound balance sheet;
- short- and long-term cash flow management;
- foreign currency liquidity management;
- preserving a diversified funding base;
- undertaking regular liquidity stress testing and scenario analysis; and
- maintaining adequate contingency funding plans.

The cumulative impact of these elements is monitored by group ALCO and the process is underpinned by a system of extensive controls. These include the application of purpose built technology, documented processes and procedures, independent oversight and regular independent reviews and evaluations of system effectiveness.

In periods of stable market conditions, the group's consolidated liquidity risk position is monitored on at least a monthly basis by the relevant ALCOs. In periods of increased volatility, the frequency of meetings is increased significantly to facilitate appropriate management action.

9.4 Liquidity buffer

Portfolios of highly marketable securities over and above prudential requirements are maintained as protection against unexpected disruptions in cash flows. These portfolios are managed within limits. As at 30 June 2009, the value of the group's unencumbered surplus liquidity, over and above prudential requirements, totalled R136,2 billion compared to R96,8 billion as at 31 December 2008.

9.5 Structural requirements

The maturity analysis provides the basis for effective management of exposure to structural liquidity risk.

Behavioural profiling is applied to assets, liabilities and off-balance sheet commitments with an indeterminable maturity or drawdown period, as well as to certain liquid assets. Behavioural profiling assigns probable maturities based on actual customer behaviour. This is used to identify significant additional sources of structural liquidity in the form of liquid assets and core deposits, such as current and savings accounts that exhibit stable behaviour although they are repayable on demand or at short notice.

By way of illustration, Table 29 below shows the group's cumulative maturity mismatch between assets and liabilities for the 0 to 1 month bucket up to the 3 to 6 months bucket, after applying behavioural profiling, denote net liabilities in brackets.

Table 29: Group behaviourally adjusted liquidity mismatch

	0-1 month Rm	2-3 months Rm	3-6 months Rm
June 2009			
Net liquidity mismatch	**59 363**	**(63 085)**	**(41 681)**
Cumulative mismatch	**59 363**	**(3 722)**	**(45 403)**
December 2008			
Net liquidity mismatch	35 348	(68 913)	(30 995)
Cumulative mismatch	35 348	(33 565)	(64 560)

Limits are set internally to restrict the cumulative liquidity mismatch between expected inflows and outflows of funds in different time buckets. One of the mechanisms employed to ensure adherence to these limits is the active management of the long-term funding ratio. The ratio is defined as those funding related liabilities with a remaining maturity of greater than six months as a percentage of total funding related liabilities.

9.6 Cash flow management

Active liquidity and funding management is an integrated effort across a number of functional areas. Short-term cash flow projections are used to plan for and meet the day-to-day requirements of the business, including adherence to prudential and internal requirements. Long-term funding needs are derived from projected balance sheet structures and positions are regularly updated. An active presence is maintained in professional markets, supported by relationship management efforts among corporate and institutional clients.

9.7 Foreign currency liquidity management

A number of parameters are observed to monitor changes in either market liquidity or exchange rates. Key to this is the restriction of foreign currency loans and advances in relation to foreign currency deposits.

9.8 Diversified funding base

The group employs a diversified funding strategy, sourcing liquidity in domestic and offshore markets.

Concentration risk limits are used within the group to ensure that funding diversification is maintained across products, sectors, geographic regions and counterparties. In terms of the latter, limits are internally set to restrict single and top ten depositor exposures within the sight to three-month tenors to below 10% and 20% of total funding related liabilities respectively.

Primary sources of funding are in the form of deposits across a spectrum of retail and wholesale clients, as well as long-term capital market funding. The group remains committed to increasing its core deposits and accessing domestic and foreign capital markets when favourable to meet its evolving funding requirements.

9.9 Liquidity stress testing and scenario analysis

Stress testing and scenario analysis forms an important part of the group's liquidity management process. Anticipated on- and off-balance sheet cash flows are subjected to a variety of bank specific and systemic stresses and scenarios to evaluate the impact of unlikely but plausible events on liquidity positions. Stresses and scenarios are based on hypothetical events as well as historical events.

This analysis is fully integrated into the group's existing liquidity risk management framework. It provides assurance as to the group's ability to generate sufficient liquidity under adverse conditions and provides meaningful input in defining target liquidity risk positions.

9.10 Contingency funding plans

Contingency funding plans are designed to, as far as possible, protect stakeholder interests and maintain market confidence to ensure a positive outcome in the event of a liquidity crisis. The plans incorporate an extensive early warning indicator methodology supported by clear and decisive crisis response strategies.

Early warning indicators cover bank specific and systemic crises and are monitored according to assigned frequencies and tolerance levels. Crisis response strategies are formulated for the relevant crisis management structures and address internal and external communications, liquidity generation and operations, as well as heightened and supplementary information requirements.

10. Market risk

10.1 Definition

The identification, management, control, measurement and reporting of market risk, which is consistent with the previous financial reporting period, has been categorised as follows:

Trading book market risk

These risks arise in trading activities where the group acts as a principal for clients in the market. The group's policy is that all trading activities are contained in the group's trading operations.

Equity investments

These risks arise from equity price changes in listed and unlisted investments, which are approved by the appropriate equity governance committees across the group.

Banking book interest rate risk

These risks arise from the structural interest rate risk caused by the differing repricing characteristics of banking assets and liabilities.

10.2 Framework and governance

The board grants general authority to take on market risk exposure to GROC, which delegates this authority to the group ALCO. Group ALCO sets market risk standards to ensure that the measurement, reporting, monitoring and management of market risk across the group adheres to a common governance framework. Each bank in the group has an ALCO to monitor compliance with these market risk standards. The Africa ALCO and International ALCO report into the group ALCO, which is chaired by a deputy group chief executive.

Market risk management units, independent of trading operations and accountable to business unit ALCOs, monitor market risk exposures in trading and banking activities. Exposures and excesses are monitored daily, and reported monthly to business unit ALCOs and quarterly to the group ALCO, GROC and GRCMC.

10.3 Market risk measurement

The techniques used to measure and control market risk include:

- value-at-risk (VaR);
- stress tests;
- other market risk measures;
- annual net interest income at risk;
- economic value of equity; and
- economic capital.

10.3.1 Daily value-at-risk

The group generally uses the historical VaR approach to derive quantitative measures, specifically for market risk under normal conditions. Normal VaR is based on a holding period of one day and a confidence interval of 95%. Daily losses exceeding the VaR are likely to occur, on average, 13 times in every 250 days.

The use of historic VaR has limitations as it is based on historical correlations and volatilities in market prices and assumes that future prices will follow the observed historical distribution.

The group back-tests its VaR models to verify the predictive ability of the VaR calculations and ensures the appropriateness of the models. Back-testing compares the daily hypothetical profit and losses under the one-day buy and hold assumption to the prior day's VaR.

Where the bank has received internal model approval, a VaR using a confidence level of 99% is used to determine market risk regulatory capital.

10.3.2 Stress tests

Stress testing provides an indication of the potential losses that could occur in extreme market conditions. The stress tests carried out by the group include individual market risk factor testing and combinations of market factors per trading desk and combinations of trading desks. Stress tests include a combination of historical, hypothetical and Monte Carlo type simulations.

10.3.3 Other market risk measures

Other market risk measures specific to individual business units include permissible instruments, concentration of exposures, gap limits, maximum tenor and stop loss triggers. In addition, most approved products that can be independently priced and properly processed are permitted to be traded. All VaR limits require prior approval from their respective ALCOs.

The market risk departments independently validate and document new pricing models and perform an annual review of existing models to ensure they are still relevant and behaving according to expectations.

10.3.4 Annual net interest income at risk

A dynamic forward-looking annual net interest income forecast is used to quantify the group's anticipated interest rate exposure. This approach involves forecasting of changing balance sheet structures and interest rate scenarios, to determine the effect that these changes may have on future earnings. The analysis is completed under normal and stressed market conditions.

10.3.5 Economic value of equity

By capturing all expected future cash flows, economic value of equity is the preferred measure for determining long-term sensitivity to interest rate changes. However, the cash flows of certain asset and liability classes, in particular those associated with ambiguous maturity behaviour, are highly dependent on the underlying assumptions. To reduce the margin for error, the sensitivity of equity is calculated as the expected change in net interest income over a five-year horizon, given a considered rate shock and is stated in present value terms.

10.3.6 Economic capital

Economic capital methodologies are used to calculate all categories of market risk sensitive capital allocations and are used to determine each business's capital charge.

10.4 Trading book market risk positions

10.4.1 Analysis of trading book market risk exposures

The VaR is principally used for client flows where there is limited trading for the bank's own account. This demonstrates the strategy and structure of the group. Table 30 shows the aggregated historical VaR for the group's trading positions. The maximum and minimum VaR amounts show the bands in which the values at risk fluctuated during the periods specified.

VaR models have been approved by the regulators for all South African trading units except exotics and specific risk on interest rates. Standard Bank Plc (subsidiary based in United Kingdom) has regulatory model approval for resource and local markets businesses and applications for their remaining businesses are in process.

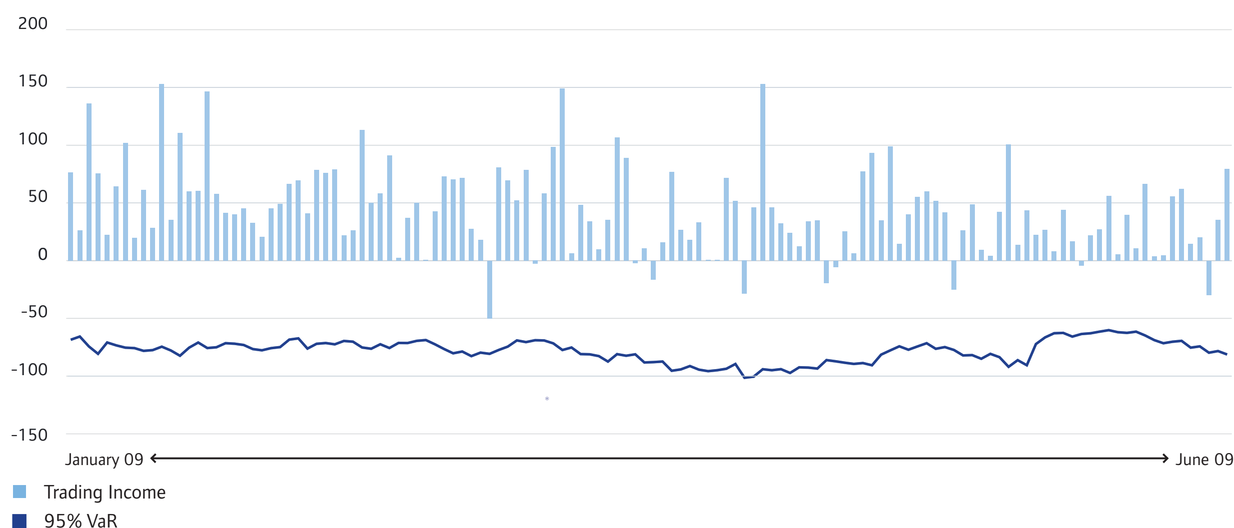
Table 30: Trading book VaR analysis by market variable

	Normal VaR			
	Maximum[1] Rm	Minimum[1] Rm	Average Rm	Closing Rm
June 2009				
Commodities	**36,4**	**15,9**	**22,6**	**32,1**
Forex	**17,4**	**5,1**	**8,3**	**8,9**
Equities	**14,5**	**2,3**	**7,7**	**9,4**
Debt securities	**72,8**	**48,7**	**58,8**	**69,0**
Diversification benefit[2]			**(28,5)**	**(38,2)**
Aggregate	**81,3**	**59,6**	**68,9**	**81,3**
December 2008				
Commodities	28,7	13,3	20,0	17,6
Forex	9,2	1,2	3,5	4,4
Equities	43,6	14,4	24,3	15,6
Debt securities	106,8	30,1	49,5	68,8
Diversification benefit[2]			(31,9)	(33,3)
Aggregate	126,2	44,8	65,4	73,1

[1] *The maximum and minimum VaR figures reported for each market variable do not necessarily occur on the same days. As a result, the aggregate VaR will not equal the sum of the individual market VaR values, and it is inappropriate to ascribe a diversification effect to VaR when these values may occur on different dates.*

[2] *Diversification benefit is the benefit of measuring the VaR of the trading portfolio as a whole, i.e. the difference between the sum of the individual VaRs and the VaR of the whole trading portfolio.*

Graph 7: Income of trading units and value-at-risk (Rm)

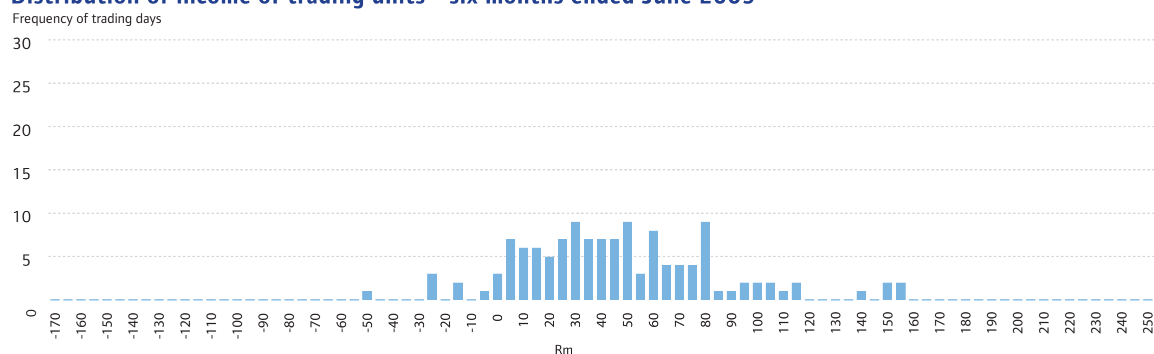


10.4.2 Analysis of trading revenue

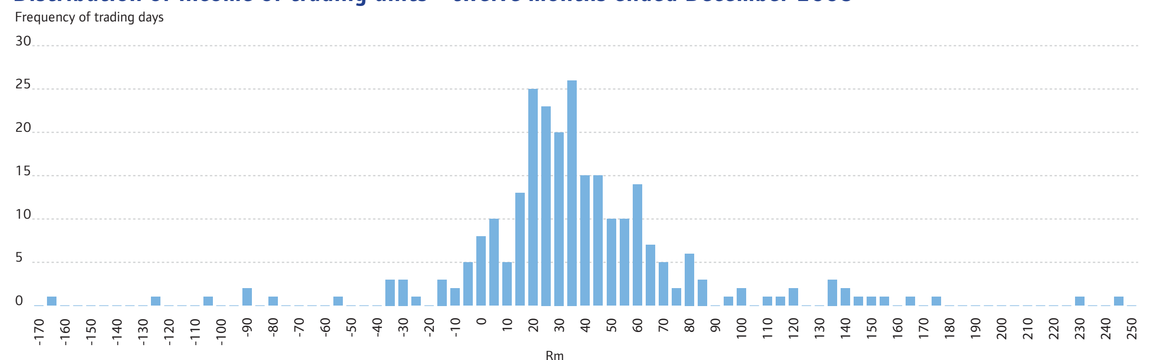
Graph 8 below shows the distribution of daily income and losses for the six months ended 30 June 2009 and 30 June 2008 as well as the twelve months ended 31 December 2008. It captures trading volatility and shows the number of days in which the group's trading related revenues fell within particular ranges.

The distribution is skewed to the profit side. In the six months ended 30 June 2008, the trading profit and loss was positive for 116 out of 127 days, whereas in the six months ended 30 June 2009, the trading profit and loss was positive for 121 days out of 128. In the 12 months ended 31 December 2008, the trading profit and loss was positive for 227 out of 260 days.

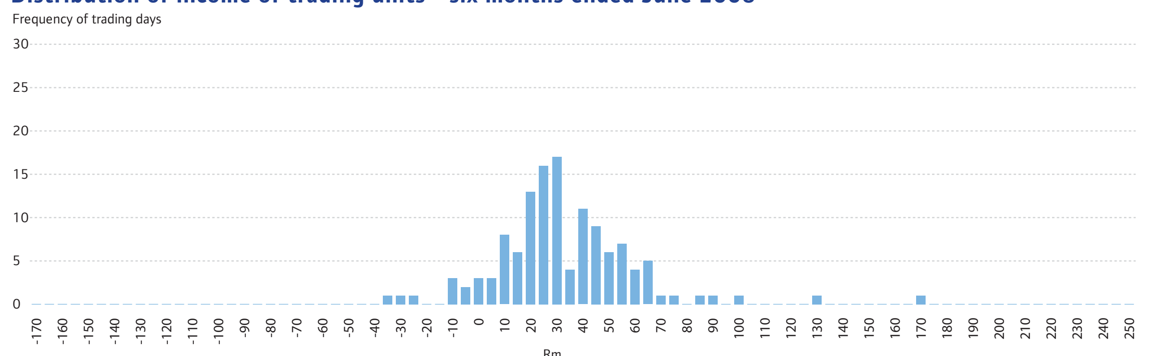
Graph 8:
Distribution of income of trading units - six months ended June 2009



Distribution of income of trading units - twelve months ended December 2008



Distribution of income of trading units - six months ended June 2008



10.5 Analysis of banking book equity positions

As with trading book equity investments, listed and unlisted investments are approved by the appropriate equity governance committees in accordance with delegated authority limits. Market risk on investments is managed in accordance with the purpose and strategic benefits of such investments, rather than purely on mark-to-market considerations. Reviews and re-assessments on the performance of the investments are undertaken periodically.

10.5.1 Accounting techniques and valuation methodologies

Financial instruments include all financial assets and liabilities held for liquidity, investment, trading or hedging purposes. Financial instruments are accounted for and valued in terms of accounting policy 5 – *Financial Instruments* disclosed in the 2008 annual report available on the group website.

Table 31: Equity positions in the banking book

	June 2009 Rm	December 2008 Rm
Fair value[1]		
Total[2]	**4 107**	4 014
Listed	**1 198**	1 292
Unlisted	**2 909**	2 722

[1] As the differences between fair value and carrying value are immaterial, only fair value is disclosed.

[2] Banking book equity exposures are equity investments which comprise listed and unlisted private equity and strategic investments, and do not form part of the trading book.

Table 32: Realised gains from the sale or liquidation of equity positions in the banking book

	June 2009 Total Rm	December 2008 Total Rm
Investments classified as available-for-sale	**39**	194

Table 33: Unrealised gains recognised on the balance sheet on equity positions in the banking book

	June 2009 Total Rm	December 2008 Total Rm
Available-for-sale movements recognised directly in equity	**187**	(48)

10.6 Interest rate risk in the banking book

10.6.1 Analysis of banking book interest rate risk exposure

Banking-related market risk exposure principally involves managing the potentially adverse effect of interest rate movements on net interest income and the economic value of equity.

10.6.2 Framework and governance

The group's approach to managing interest rate risk is governed by applicable laws and regulations, and is guided by best international practice and the competitive environment in which the group operates. Interest rate risk on the banking book is transferred to and managed by the group's treasury operations under supervision of the local ALCO. Each bank in the group manages this risk on a stand-alone basis. All entities within the group also calculate economic capital to support the interest rate risk of the banking book.

10.6.3 Interest rate risk measurement

The analytical techniques used to quantify banking book interest rate risk include both earnings and valuation based measures. Cognisance is taken of embedded optionality, such as loan prepayments and other accounts where the behaviour differs from the contractual position. The results obtained from forward-looking dynamic scenario analyses, as well as Monte Carlo simulations, assist in evaluating the optimal hedging strategies on a risk-return basis. Desired changes to a particular interest rate risk profile are achieved through the restructuring of the balance sheet and, where appropriate, the use of derivative instruments.

10.6.4 Interest rate risk limits

Interest rate risk limits are set in terms of changes in forecasted net interest income and the economic value of equity. Economic value of equity sensitivity is calculated as the net present value of aggregate asset cash flows less the net present value of aggregate liability cash flows.

Table 34: Interest rate sensitivity analysis

		Rand	US Dollar	Sterling	Euro	Other	Total
June 2009							
Decrease in basis points		**200**	**100**	**100**	**100**	**100**	
Sensitivity of annual net interest income	Rm	**(1 683)**	**(32)**			**(65)**	**(1 780)**
Sensitivity of equity[1]	Rm	**(283)**	**59**			**81**	**(143)**
December 2008							
Decrease in basis points		200	100	100	100	100	
Sensitivity of annual net interest income	Rm	(1 814)	30	6	12	(147)	(1 913)
Sensitivity of equity[1]	Rm	(141)	88			150	97

[1] *Actual change in equity resulting from the changes in reserves caused by the change in derivatives mark-to-market held as cash flow hedges or available-for-sale positions.*

10.6.5 Economic capital

The sensitivity of the economic value of equity forms the basis for calculating the required economic capital to mitigate interest rate risk in the banking book. This calculation is performed using a universe of stochastic scenarios, rather than a single yield curve shock.

10.6.6 Hedging of the endowment risk

The endowment risk emanating from the anticipated turn in the economic cycle is hedged as and when it is considered opportune using derivative instruments such as swaps and interest rate swaptions.

10.6.7 Group risk diversification

The group risk diversification benefit, which takes into account the fact that interest rate changes across currencies are unlikely to be perfectly correlated, is calculated quarterly.

This consolidated view is used to obtain a strategic view of the enterprise. However, positions and balance sheets are managed at the local entity level, not taking into account marginal contribution to the group due to diversification.

10.6.8 Analysis of banking book interest rate sensitivity

Table 34 indicates the sensitivity in rand equivalents of the group's net interest income and equity in response to a parallel yield curve rate shock after taking all risk mitigating instruments into account, with all other variables held constant.

Assuming no management intervention, a downward 100 basis points parallel rate shock in all yield curves would decrease the forecast net interest income for the six months ended 30 June 2009 by R0,9 billion (December 2008: R1,0 billion).

10.7 Foreign currency risk

The group's primary exposures to foreign currency risk arises as a result of the translation effect on the group's net assets in foreign operations, intra-group foreign denominated debt and foreign denominated cash exposures.

The group capital management committee delegates the management of this risk to the net asset value currency risk management committee. This committee manages the risk according to existing legislation, South African exchange control regulations and accounting parameters. It takes into account naturally offsetting risk positions and manages the group's residual risk by means of forward exchange contracts, currency swaps and option contracts. Hedging is undertaken in such a way that does not interfere with or constrain the normal operational activities of business units. The net asset value currency risk management committee meets regularly to reassess the hedging or diversification strategy in the event of changes in currency views.

Due to South African exchange control limitation, hedging activities are restricted to ensuring a diversified mix of foreign currency exposures in the group's net foreign investment subsidiaries. Hedging of rand/foreign currency exposure is limited and only permitted for planned and specific, future investment related cash flows.

The repositioning of the currency profile, which is co-ordinated at group level, is a controlled process based on underlying economic views of the relative strength of currencies. In terms of the foreign currency risk governance process outlined above, the group does not ordinarily hold open exposures of any significance in respect of the banking book. Gains or losses on derivatives that have been designated in terms of either net investment or cash flow hedging relationships are reported directly in equity, with all other gains and losses on derivatives being reported in profit and loss.

11. Operational risk

11.1 Definition

Operational risk is the risk of loss suffered as a result of inadequacy of or a failure in internal processes, people and systems or from external events. This includes information risk and legal risk, but excludes reputational risk and strategic risk.

11.2 Framework and governance

The group's operational risk management (ORM) framework is set out in the group ORM governance standard, which defines a common framework for managing all operational risks. The group's ORM framework is designed to be fit-for-purpose. In developing the framework, the group has embraced principles that meet and often exceed regulatory requirements. The framework, together with policies and methodologies, ensures a consistent approach to the identification, assessment, management and monitoring of operational risk across the group.

While the group operational risk committee (GORC) provides the primary oversight role, GROC ensures that the ORM framework provides optimal benefit for the group while ensuring regulatory compliance. The GRCMC, as the board delegated risk oversight body, reviews the ORM framework annually. In addition, the board considers operational risk at every meeting, either as a specific agenda item or through the review of the minutes of other risk committees.

An independent review of the group's ORM framework is also performed by group internal audit to ensure that operational risk practices are embedded in each business.

11.3 The management and measurement of operational risk

Independent ORM functions have been established at group and business unit levels with separate yet interactive roles. These risk functions oversee the ORM on behalf of GORC and business unit executive committees, but risk ownership remains with business unit management.

Risk assessments are an integral part of the overall risk management process and cover the key components of identification, assessment and management of risk. The group uses the risk and control self-assessment (RCSA) process to analyse its business activities and identify operational risks that could affect the achievement of its business objectives. The implementation of a comprehensive RCSA process is an integral element of ORM and is therefore compulsory throughout the group. An effective RCSA process is a key component of developing a risk profile and understanding the residual risk.

Risk assessments are supplemented with loss data experience. The group ensures the systematic tracking of operational risk losses and near miss events by business line through a centralised database. The detailed loss data collection process occurs at a decentralised level within each functional area. The information is then consolidated by ORM who are responsible for defining the parameters, database fields and maintaining the integrity of the data.

Line management in each functional area is responsible for the loss data collection process supported by an independent operational risk function.

The group uses key risk indicators to monitor exposures to key risks identified in the RCSA process. The key risk indicators process is an important component in the management of operational risk and contributes to the development of the group's operational risk profile.

The group maintains adequate insurance to cover key operational and other risks. Insurance is not considered as an alternative to effective preventative and detective controls but as a compensatory control, providing protection from the consequences of control failure.

Operational risk appetite is determined by setting tolerance thresholds for financial and non-financial impacts. These are used to guide escalation and mitigation strategies. Tolerances are set through specific risk indicators and these are generally reliant on senior management's assessment of acceptable risk.

Business units have developed materiality thresholds, both financial and non-financial, for the immediate escalation of material incidents to the various business and risk management structures within the group. These materiality thresholds also determine which exposures need to be reported to the various management and board risk committees.

Operational risk reports are produced on a monthly and quarterly basis by the ORM functions across the group. These reports set out potential and actual exposures, material incidents and applicable action plans.

The group has adopted the standardised approach (TSA) for operational risk and is in the process of developing and implementing an AMA (advanced measurement approach) compliant operational risk framework.

11.4 Business continuity management

Business continuity management in the group has improved the ability of all critical operations to manage any unexpected business disruptions and/or crises. The group continually enhances the process of assessing needs, identifying gaps and single points of failure, improving recovery strategies and keeping plans current by running regular exercises. The group has improved its resilience strategy by increasing the number of critical business operations using the dual site strategy. The group also embarked on an awareness campaign to raise awareness of business continuity and to ensure that employees know their roles in the event of a crisis.

The status of the organisation's business continuity management capability is continually monitored through various reporting structures with relevant information flowing through to the respective governance committees and the board.

11.5 Information risk management

Information risk is defined as the risk of accidental or intentional unauthorised use, modification, disclosure or destruction of information resources, which compromise their confidentiality, integrity or availability.

Information has become indispensable to doing business. The growing dependence on information and information systems, coupled with the risks, benefits and opportunities these resources present, have made information risk an increasingly critical facet of overall risk management for the group.

Information risk management deals with all aspects of information whether spoken, written, printed, electronic or relegated to any other medium regardless of whether it is being created, viewed, transported, stored or destroyed.

To reduce adverse impacts to an acceptable level, group information risk management has:

- established a framework, aligned with best practice methodologies to guide the development and management of a comprehensive information risk management (IRM) programme that supports business objectives;
- implemented an effective IRM structure having no conflicts of interest, with sufficient authorities and adequate resources;
- made use of metrics and monitoring processes to ensure compliance and provide feedback on the effectiveness of IRM programmes;
- raised security awareness for all users; and
- established security policies that are complete and consistent with group strategy.

11.6 Fraud risk management

The group takes a "zero tolerance" approach to fraud and corruption. In the case of staff, disciplinary, civil or criminal action is taken. Employees found guilty of dishonesty through the group's disciplinary processes are listed on relevant industry databases of dismissed staff.

Fraudulent activities in the South African banking industry are continuously monitored through the group's participation in industry bodies such as the South African Bank Risk Intelligence Centre and the South African Fraud Prevention Services.

To effectively manage fraud risk, the group requires each business unit to identify all inherent fraud risks and implement controls to mitigate them according to the risk/reward approach.

The group focuses on combating intelligence-driven operations with significant emphasis placed on neutralising syndicates that commit fraud against the bank. Emphasis is also placed on risk factors that contribute to fraud.

11.7 Environmental risk

Environmental risk is governed by the safety, health and environmental risk oversight committees which comprise executive representation from various divisions across the group. The mandate of the group committee is to set the

strategic direction and review and assess the integrity of the management systems, as well as to ensure consistency, effective communication and compliance. Environmental management and risk mitigation will in future form part of a sustainability management programme currently being implemented.

11.8 Legal risk

Legal risk arises where:

- the group's businesses may not be conducted in accordance with applicable laws in the countries in which it operates;
- incorrect application of regulatory requirements takes place;
- the group may be liable for damages to third parties; and
- contractual obligations may be enforced against the group in an adverse way, resulting in legal proceedings being instituted against it.

Although the group has processes and controls in place to manage legal risk, any failure to do so could result in legal proceedings that have a financial and reputational impact on the group.

11.9 Compliance risk

11.9.1 Approach to compliance risk management

The group's approach to managing compliance risk is proactive and premised on internationally accepted principles of risk management. It is also aligned with the methodologies used by the group's other risk assurance functions. Group Compliance provides leadership on complying with money laundering and terrorist financing control and emerging legislative developments, through specialist support units. In line with international best practice, responsibility for compliance remains with executive management. To support the group's approach to compliance risk management, ongoing monitoring takes place to ensure adherence to the group compliance policy and standards.

11.9.2 Framework and governance

Compliance risk management is an independent core risk management activity overseen by the group chief compliance officer whose position is mandated and approved by the Bank Supervision Department (BSD) of the South African Reserve Bank (SARB). The group chief compliance officer has unrestricted access to the chief executives of the Standard Bank Group and SBSA and to the chairman of GAC, and also engages with the BSD on a regular basis. He reports independently to GAC.

The group's compliance framework is based on the principles of effective compliance risk management stated in the Banks Act, 1990, as amended. The group operates a decentralised compliance risk management structure whereby each primary business unit has a compliance function headed by a designated compliance officer, who reports to the group chief compliance officer.

Executives who are responsible for all aspects of compliance risk management are subject to the appropriate corporate governance reporting structures. All business units are responsible for compliance with relevant legislation and are responsible for reporting on compliance matters to the group risk compliance committee (GRCC), which is chaired by the group chief compliance officer.

11.9.3 Regulation and supervision

The group operates in a highly regulated industry and across multiple jurisdictions. Supervision is undertaken by various regulatory bodies in South Africa, although the group's primary regulator is the BSD of the SARB. Host country regulators supervise the group's operations in all other jurisdictions. BSD supervises the group on a consolidated basis and the relationship is one of mutual trust built through regular meetings and open communication.

The FSB regulates the non-banking aspects of the financial services industry in South Africa, including financial advisory and intermediary services, insurance, retirement funds and collective investment schemes.

The Financial Intelligence Centre (FIC) aims to provide, within the appropriate policy framework, financial intelligence for use in the fight against crime, money laundering and terrorist financing in South Africa. Regular communication takes place with the FIC on a formal and informal basis. In keeping with global expectations, the BSD has taken pre-emptive steps to supervise banks' compliance with the Financial Intelligence Centre Act, No 38 of 2001 in co-operation with the FIC.

As a member of the Financial Action Task Force (FATF), South Africa underwent a mutual evaluation in 2008 to assess the effectiveness of its framework. The FATF

final report was issued in April 2009 and while there was general approval of the legal enforcement framework a number of opportunities for improvement were noted. Key issues included the application of relevant Know Your Customer requirements for certain client categories as being too liberal, and that aspects of customer due diligence and transparency of ownership requires focus. The FIC has reported that some provisions of the Financial Intelligence Centre Act, 2001 will need to be revisited.

The group interacts with various other industry and regulatory bodies in South Africa and in the other jurisdictions in which it operates. A list of regulators is available in the sustainability report which can be accessed on the Standard Bank website.

Regulatory developments which impacted compliance risk management in 2008 continued to affect business planning during 2009, with heightened focus on consumer protection, fair lending and environmental legislation. Open and positive engagement with regulators has greatly facilitated the implementation of current, amended and new legislation and regulations. The implementation of the revisions to the Banks Act, 1990 to accommodate primarily Basel II requirements in 2008, has been embedded in bank operations, but the unfolding banking and economic meltdown has required the BSD to consider proposed amendments to the legal framework for the regulators and supervisors of banks during 2009/10.

Developments relating to consumer protection and the fair treatment of customers continues to be a key priority with the effective implementation date of the Consumer Protection Act in the second quarter of 2010.

Legislation relating to the prevention of money laundering and terrorist financing is also being enhanced to afford supervisors greater powers of inspection. The proposed introduction of the Consumer Protection Bill and enhancements to the Code of Banking Practice will provide additional protection to consumers.

11.9.4 Money laundering control

Legislation pertaining to money laundering and terrorist financing control imposes significant requirements in terms of customer identification, record keeping and training requirements, as well as obligations to detect, prevent and report money laundering and terrorist financing. The group is committed to continually improving its control measures as the regulatory environment evolves. The group's minimum standards are regularly reviewed to align them with international best practice, and the effectiveness of money laundering surveillance systems across the group are continually improved.

11.9.5 Occupational health and safety

The health and safety of employees, customers and other stakeholders is a priority and the group aims to identify and reduce the potential for accidents or injuries in all its operations. Training of health and safety officers and staff awareness is an ongoing endeavour. Standards that support uniform health and safety requirements across all group operations are being developed. Comprehensive information on the group's initiatives in this regard is available in the sustainability report available on the group's website.

11.9.6 Compliance risk management training

As part of its commitment to training and development, the group promotes ongoing training to ensure that it has the appropriate skills to achieve its business objectives.

12. Business risk

Business risk relates to the potential revenue shortfall compared to the cost base due to strategic and/or reputational reasons. From an economic capital perspective, business risk capital requirements are calculated as the potential loss arising over a one year time frame within a certain level of confidence as implied by the group's chosen target rating. The group's ability to generate revenue is impacted by, amongst other things, the external macro-economic environment, its chosen strategy and reputation in the markets in which it operates.

The approach followed by the group in quantifying business risk is to estimate a net revenue/(loss) distribution for each business unit using historical management accounting data. This is based on a Monte-Carlo simulation with the objective of deriving a net revenue/(loss) distribution from which economic capital may be determined at the 99,925% confidence level. Business units have a clear understanding of their value drivers that impact on their profitability. These are modelled as part of the planning and forecasting processes to assess sensitivity of changes in these value drivers on their business performance.

Business risk is governed by group executive committee which is ultimately responsible for managing the costs and revenues of the group. In addition, mitigation of business risk is undertaken in a number of ways including:

- comprehensive due diligence during the investment appraisal process (in particular new acquisitions);
- stakeholder engagement to ensure positive outcomes from external factors beyond the group's control;
- consistently monitoring the profitability of product lines and customer segments;
- maintaining tight control over the cost base of the group, including the management of its cost-to-income ratio. This allows for early intervention and management action to reduce costs where necessary; and
- being alert and responsive to changes in market forces.

13. Reputational risk

Reputational risk results from damage to the group's image which may impair its ability to retain and generate business. Such damage may result from a breakdown of trust, confidence or business relationships. Safeguarding the group's reputation is of paramount importance to its continued success and is the responsibility of every member of staff.

14. Conclusion

Our continued commitment to strong risk management during the global financial crisis has proved to be effective and is reflected in our strong capital and liquidity position. We recognise that maintaining and continually enhancing our risk management capabilities will be critical in the months ahead to ensure that earnings are achieved within approved levels of risk appetite.

Acronyms and abbreviations

AIRB	Advanced internal ratings based approach
AFR	Available financial resources
ALCO	Asset and Liability Committee
AMA	Advanced Measurement Approach
Basel	Basel Capital Accord
BSD	Bank Supervision Department
EAD	Exposure at default
FATF	Financial Action Task Force
FIRB	Foundation internal ratings based approach
FSB	Financial Services Board
GAC	Group audit committee
GCC	Group credit committee
GORC	Group operational risk committee
GRCMC	Group risk and capital management committee
GRCC	Group risk compliance committee
GROC	Group risk oversight committee
Group	Standard Bank Group and its banking operations
ICAAP	Internal capital adequacy assessment process
IFRS	International Financial Reporting Standards
IRM	Information Risk Management
IRB	Internal ratings-based approach
IRRBB	Interest rate risk of the banking book
LGD	Loss given default
ORM	Operational risk management
PD	Probability of default
QRRE	Qualifying revolving retail exposure
RCSA	Risk and control self-assessment
SARB	South African Reserve Bank
SBSA	The Standard Bank of South Africa
SME	Small and medium enterprise
SPE	Special purpose entity
Tier I	Primary capital
Tier II	Secondary capital
Tier III	Tertiary capital
TSA	The standardised approach
VaR	Value-at-risk