Absa Group Limited

Interim Risk Management disclosures

30 June 2011

Member of the BARCLAYS Group

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Executive summary: capital and risk management overview

Six months ended 30 June 2011

Highlights

- *Increase in Core Tier I capital indicating improved quality of capital.*
- *Focus on rehabilitating customer arrears and reducing impairments.*
- *Further increase in the amount of surplus liquid assets held, building on the strong growth achieved during 2010.*
- *Interest rate risk management hedging activities positively impacted on the net interest margin, off-setting the negative endowment effects during the period under review.*
- *Advanced Measurement Approach (AMA) approval for operational risk maintained.*
- *Progress made on capital model development in short-term insurance environment.*

Introduction

The risk management environment was challenging during the period under review, as economic conditions remain uncertain. Following its ongoing investment in risk management, the Group continues to be well positioned to take advantage of opportunities.

Capital management

Capital management is a key pillar of the One Absa strategy. The Group continues to monitor market conditions and the effect of global banking conditions, prepare for Basel III and to ensure that the Group has adequate capital available to support future asset growth.

Capital levels remained well above board-approved target ranges for both the Group and the Bank, with Core Tier 1 capital levels improving by 110 basis points (bps). Risk-weighted asset (RWA) optimisation remained a priority with improvements in risk management effected while the impacts of proposed regulatory changes are being analysed and integrated into the business.

The Group's approach to risk management

Risk management is a key pillar of the One Absa strategy. The Group has a structured and disciplined approach to the management of risk. The board-approved Principal Risk Policy (PRP) sets out the scope of the risks, who is responsible for managing them and high level procedures for risk management.

Risk governance

The Group's approach to risk governance aims to balance the demands of dynamic and efficient business decision-making with the requirements of control and transparency. The responsibility for risk governance lies at all levels of the organisation, from directors at board level to individual employees tasked with the responsibility of managing risk. Senior management sets risk management policies to be followed on an organisation-wide basis within the risk appetite set by the board. These policies are clearly communicated throughout the Group and apply to all business units, wholly owned subsidiaries and entities in which the Group has either a majority shareholding or management control.

Oversight of risk management resides with two board committees, namely, the Group Risk and Capital Management Committee (GRCMC) and the Group Audit and Compliance Committee (GACC).

Risk management activities

During the period under review the governance process functioned effectively. The GRCMC obtained sufficient and appropriate information concerning the Group's risk profile. The information included the process employed by executive management for monitoring and managing these risks.

The key highlights and achievements during the period under review are listed below:

Credit risk

Wholesale credit risk marginally improved across certain industries. There was continued emphasis on containing impairments and managing watch lists.

Retail credit conditions were challenging with the total portfolio remaining static during the period under review. Impairments and early delinquencies continued to improve. A reduction of R2,6 billion in the debt counselling book was achieved.

Market risk

Traded market risk remained at low levels and was managed within the risk appetite set. Traded market risk and revenue reflect continued uncertainties and client volumes as well as the current low interest rate environment. These aspects were managed so that a favourable risk-adjusted return was achieved. Internal Models Approach (IMA) approval for trading book general position risk was maintained, with reduced regulatory capital requirements applying from the second half of 2011.

In respect of non-traded market risks, the structural interest rate hedge programme was efficiently managed and equity investment risk exposure in the banking book was selectively exited with a view to create a leaner portfolio, while remaining selective on new investments.

Executive summary: capital and risk management overview

Six months ended 30 June 2011

Liquidity risk

The emphasis on effective liquidity management continued during the period under review.

The Group increased surplus liquid assets while maintaining the loan-to-deposit ratio. The funding term further increased to 26,8% at the reporting date.

Operational risk

The operational risk management team focused on continuing the improvement of controls, risk management systems and processes.

Insurance risk

Substantial work was undertaken to enhance risk management policies and structures, and to achieve a return on capital allocated per product line. Selective disinvestment by Absa Life Limited from equities has resulted in reduced investment risk exposure.

Regulatory risk

A number of laws came into effect in the period under review including, in particular, the Consumer Protection Act and the new Companies Act. The processes and policies impacted by this legislation were integrated into operations.

The Group's risk appetite

The Group's formalised risk appetite framework, which is embedded within key decision-making processes, supports the implementation of the Group's strategy. The Group's risk appetite framework aims to maximise returns without exposing the Group to levels of risk that are outside of its appetite. It is defined as the level of risk that the Group is willing to accept in fulfilling its business objectives. The risk appetite framework impacts the Group's strategy, capital and portfolio management and its day-to-day operations.

The risk appetite framework is developed utilising a formal quantitative method and stress testing techniques based on advanced risk analysis. The framework, set by the board, is used as a basis for setting business unit targets and risk taking limits across the Group. Stress testing and scenario analysis are closely aligned with the risk appetite process and are utilised to evaluate the reasonableness of the appetite levels set on a forward looking basis.

Risk appetite methodology

The Group's risk appetite can be categorised into the following four broad areas:

» earnings volatility in comparison to targets;

» capacity to absorb unexpected losses;

» capital ratio targets; and

» desired dividend payout levels.

The objectives of the risk appetite framework are to:

» assist in protecting the Group's financial performance;

» improve management responsiveness and debate regarding the Group's risk profile;

» assist executive management to improve control and coordination of risk-taking across businesses; and

» enable unused risk capacity to be identified in pursuit of profitable opportunities.

Stress testing

Stress testing is embedded in the risk management of the Group and is a key focus area during the strategic planning processes. Through the use of stress testing and scenario analysis the Group is able to assess the performance of its portfolios under the anticipated economic environment and evaluate the impact on its portfolios during adverse and more favourable economic conditions.

The stress tests simulate the statement of financial position and profit and loss effects of stresses across the Group, analysing the impact on profits and the ability to maintain appropriate capital ratios. Insights gained are fully integrated into the management process that considers forward-looking trends and the Group's financial performance and capital management over a three to five year horizon. Stress testing also forms an integral part of evaluating the Group's risk appetite for reasonableness under specifically designed scenarios. Stress tests are regularly discussed with the regulator.

Risk appetite outcomes are validated by estimating the Group's sensitivity to adverse changes in the business environment, which includes operational risk events that may impact the Group as a whole. Group-wide stress tests allow senior management to gain a better understanding of how portfolios are likely to react to changing economic and geopolitical conditions and how the Group can best react to them.

Besides Group-wide stress testing, a number of stress tests are performed as part of the wider risk management process. Specific stress test analysis is used across all risk types on a more granular level in order to gain a better understanding of the risk profile and the potential effects of changes in external factors. These stress tests are performed at a range of different levels, from analysis covering specific stresses on individual sub-portfolios to portfolio level stresses. In addition, a program of reverse stress testing has been initiated in order to evaluate the impact of events not previously experienced by the Group. It is used to evaluate the impact of low probability, but plausible scenarios.

Six months ended 30 June 2011

Risk disclosures

Risk disclosures contained in this half year report relate to regulatory risk disclosures and are unaudited.

King III

Due to existing practice, risk management will not be significantly impacted by the application of King III in 2011. However, the Group is currently aligning certain policies and procedures within risk management, where necessary. Risk governance structures for information technology were improved and certain oversight measures were revised. The Group does not expect any material issues to arise following the application of King III.

Basel III

The Group has investigated the impacts of Basel III and is prepared for full implementation within the timelines required.

Capital management is not expected to be significantly impacted by the implementation of Basel III although uncertainties remain. Based on an initial assessment, capital requirements and RWAs may increase but overall capital adequacy should remain at levels above the current requirements. RWA optimisation is a key focus area. The Group is participating in ongoing discussions with the regulator concerning the local application and discretionary limits of Basel III.

As a result of the current emphasis on strengthening the liquidity of the Group, no significant impacts are expected following the application of Basel III within the required timelines.

Focus going forward

The Group will continue to monitor the economic situation and ensure it effectively and timeously adapts its risk management policies, procedures, risk appetite and stress tests to deal with the changing demands and challenges of the economic environment. The Group remains committed to developing and enhancing appropriate risk management procedures and practices, and to keeping pace with applicable regulatory requirements and best practice standards in the industry.

Scenario planning, stress testing and risk appetite remain high on the risk governance agenda and will continue to be used to assess the impact of risk management on financial performance, capital and liquidity management and to meet regulatory and business requirements.

In terms of capital and risk management, further strategic areas of focus are as follows:

Capital management

The Group remains focused on preparing for the implementation of Basel II.5 and Basel III. RWA optimisation will be a key focus area during this implementation period. The Group is expected to remain well capitalised and to maintain its current investment grade target rating.

Credit risk

Impairment levels across wholesale and retail credit risk are expected to improve further during the following six months. The Group will remain focused on the value and quality of business in order to achieve balance sheet optimisation.

Mortgage portfolios and, in particular, debt counselling and legal portfolios, remain a strategic focus area.

Market risk

The Group will continue to actively manage its traded RWAs towards more efficient use of capital in anticipation of the increase in traded market risk regulatory capital charges from 2012.

With local interest rates expected to remain low, efficient management of the structural interest rate hedge programme will remain a focus area in the second half of 2011.

In line with the capital, liquidity and balance sheet optimisation programme of the Group, there will be continued focus on reducing equity investment exposures in the banking book, towards creating a leaner portfolio, while remaining selective on new investments.

Liquidity risk

Liquidity risk management will continue to receive focus within the Group for the remainder of 2011 and during 2012. The Group will continue to strengthen its liquidity position ahead of the implementation of Basel III in order to achieve compliance within the required timeframes.

Operational risk

The Group will continue to focus on improvements to its operational risk management processes.

Insurance risk

The management of risk and return on capital will continue to be enhanced in line with developing Solvency Assessment and Management legislation

Regulatory risk

The regulatory environment remains challenging and the Group is constantly reviewing the potential impact of the new regulatory and legislative requirements.

June 2011 highlights

- » *Strong capital position maintained.*
- » *Increase in Core Tier 1 capital indicating an improved quality of capital.*
- » *Board approved capital target ranges incorporating capital buffers above minimum regulatory requirements.*
- » *Focus on RWA optimisation.*

Salient features[1]

Absa Group	30 June 2011	30 June 2010	31 December 2010	Minimum regulatory capital requirements
Capital adequacy (%)				
Core Tier 1	**12,8**	11,9	11,7	5,25
Tier 1	**13,9**	13,1	12,8	7,00
Total	**16,7**	15,8	15,5	9,75
Capital supply and demand for the period/year (Rm)				
Free cash flow generated	**3 762**	1 900	2 017	
Qualifying capital	**68 169**	62 647	65 417	
Total RWAs	**408 397**	395 461	422 713	
Key metrics (%)				
Cost of equity[2]	**14,0**	14,0	14,0	
Return on average RWAs (RoRWA)	**2,23**	2,00	1,99	
Return on average economic capital (RoEC)	**22,4**	19,1	19,7	

Absa Bank	30 June 2011	30 June 2010	31 December 2010	Minimum regulatory capital requirements
Capital adequacy (%)				
Core Tier 1	**11,8**	10,7	10,7	5,25
Tier 1	**13,0**	12,0	11,9	7,00
Total	**16,0**	14,9	14,8	9,75
Capital supply and demand for the period/year (Rm)				
Free cash flow generated	**3 724**	1 183	1 532	
Qualifying capital	**59 954**	54 908	57 801	
Total RWAs	**373 785**	368 313	391 735	
Key metrics (%)				
Cost of equity[2]	**14,0**	14,0	14,0	

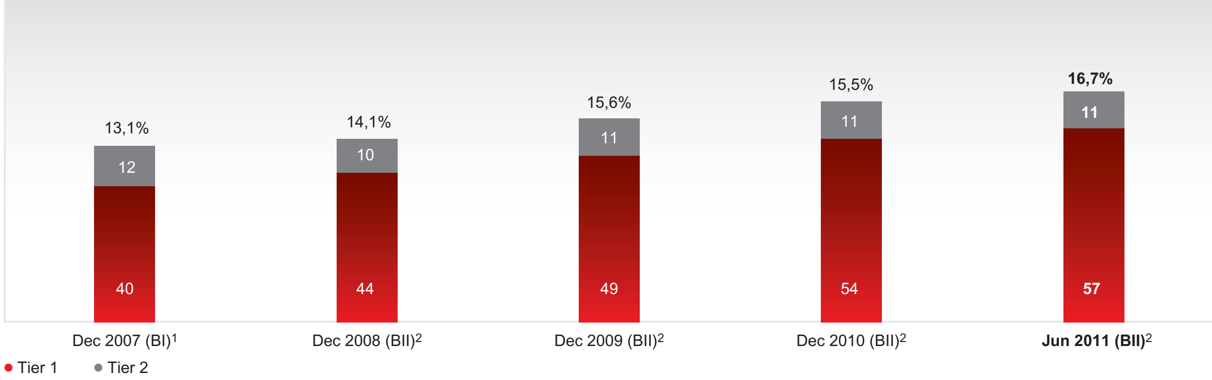
Notes

[1] *Reported ratios include unappropriated profits.*

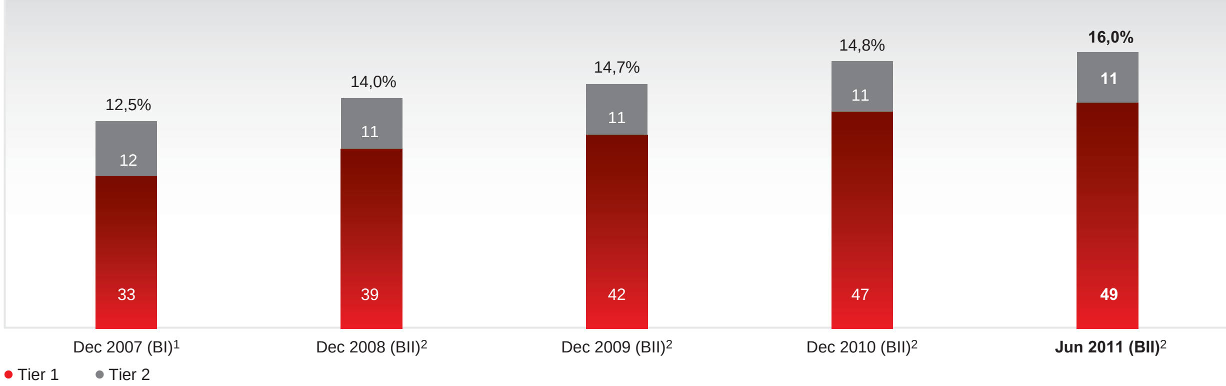
[2] *The average cost of equity is based on the Capital Asset Pricing Model (CAPM).*

Salient features *(continued)*

Absa Group capital adequacy (Rbn and %)



Absa Bank capital adequacy (Rbn and %)



Introduction

Capital management is a key focus area for the Group. The Group's capital management strategy is focused on maximising shareholder value by optimising the level and mix of capital resources. Decisions on allocating capital resources are based on a number of factors including return on economic capital (RoEC) and return on regulatory capital (RoRC), and are part of the internal capital adequacy assessment process (ICAAP).

Strategy

The strategic objectives for capital management are:

» meeting the capital ratios required by regulators and the target ranges set by the board;
» maintaining an adequate level of available capital resources as cover for the economic capital (EC) requirements calculated at a 99,95% confidence level;
» generating sufficient capital to support asset growth;
» maintaining an investment grade credit rating.

Governance

Capital management is a board level priority in the Group. The board assesses and approves the capital management policy, capital target ranges and capital strategy. The Group has a dedicated team that manages and executes these responsibilities. The team presents regular capital reports to the Group Asset and Liability Committee, Group Executive Committee, GRCMC and the board. Risk oversight of the capital management function is provided by the GRCMC, under a specific mandate from the board.

Notes
[1] *BI: Basel I.*
[2] *BII: Basel II.*

Capital management

Six months period in review

The Group has embarked on an initiative to identify and bring about RWA savings. The benefits of this initiative are as follows:

- improved capital adequacy levels – the Group ended the 2010 financial year with a strong capital adequacy position, but there is uncertainty around certain Basel lll rules to be implemented with effect from 2013, and it is expected that these rules will increase the Group's capital requirements;
- freeing up of capital – which lowers the potential need to raise additional capital in the future;
- increase in RoRWAs – optimising RWAs increases RoRWAs. RoRWA is one of the key performance indicators used in conjunction with other metrics to measure the business performance of the Group; and
- improved understanding of risk – many of the RWA optimisation exercises focus on improving data quality and removing excess conservatism, resulting in a more improved measurement of risk. The importance of capital allocation, together with the metrics used to measure business performance, allows the Group to allocate capital on a more accurate risk-vs-return basis.

Approach to capital management

The proper planning and management of capital is essential to the Group to ensure it has sufficient and appropriate capital structures to support its risk appetite, business activities, credit rating and regulatory requirements.

The capital management framework adopted by the Group provides the basis for effective capital planning and structuring, capital issuance, Basel alignment, EC utilisation and economic profit. It provides end-to-end integration of the Group's strategy, risk management and financial processes. The purpose of the framework is to ensure capital consumption in the business divisions has an impact on performance measurement, which in turn translates into management performance assessment, product pricing requirements and the achievement of the Group's desired strategic positioning.

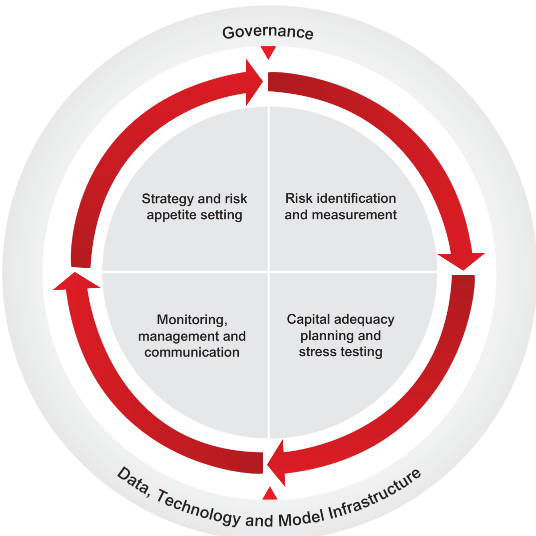
Internal Capital Adequacy Assessment Process (ICAAP)

The Group has adopted a building block approach to achieve a robust and integrated capital management framework. EC forms the foundation of this and is the primary means by which the Group assesses the impact of a changing business environment and strategy on its risk profile and the need for capital.

EC is also a measure of capital required to maintain or achieve a target debt rating. Aside from its application in capital management, EC is a key component of Group level and business unit level applications such as capital management, stakeholder communication, risk-adjusted performance measurement and pricing/structuring.

While the ICAAP is intended to align with regulatory requirements under Pillar 1 and Pillar 2 of Basel ll, the main guiding principle in designing the ICAAP for the Group has been suitability for capital management and other internal applications. The Group considers its ICAAP to be in line with international best practice and is of opinion that it addresses the core banking principles of Pillar 2 of Basel II.

The building blocks of the Group's ICAAP are as follows:



These processes are conducted within an environment with established governance practices and oversight, and are supported by adequate data, technology expertise and model infrastructure.

Stress testing is performed to identify early warning thresholds and risk events that may adversely impact the Group's risk profile. Stress testing is also used to determine adequate capital buffers that are considered sufficient to ensure that both Absa Group and Absa Bank do not breach the minimum regulatory ratios under the stress scenarios and to formulate appropriate management actions. From an ICAAP perspective, stress testing represents the link between capital and risk management. As a result of global events, stress testing has become increasingly important in assessing appropriate levels of capital.

June 2011 disclosures

During the period under review the Group maintained its strong capital adequacy position. The Group continued to focus on RWA demand management (optimisation) and free capital generation.

Regulatory capital

Risk-weighted assets (RWAs)

RWAs are determined by applying the following:

- Advanced Internal Rating Based (AIRB) approach for retail credit;
- Foundation Internal Ratings Based (FIRB) approach for wholesale credit;
- AMA for operational risk;
- In respect of traded market risk, Internal Models Approach (IMA) for general position risk, and Standardised Approach (SA) for issuer specific risk;
- Internal Ratings Based (IRB) market-based simple risk-weighted approach for equity investment risk in the banking book; and
- SA for credit risk in all African entities.

Absa Group RWAs and minimum required capital – Table 1:

	30 June				31 December	
	2011		2010		2010	
	RWAs Rm	Required[1] capital Rm	RWAs Rm	Required[1] capital Rm	RWAs Rm	Required[1] capital Rm
Basel II measurement approach						
Credit risk	**298 851**	**28 391**	286 268	27 195	316 967	30 112
Portfolios subject to the AIRB approach	**146 222**	**13 891**	161 818	15 372	167 618	15 924
Portfolios subject to the FIRB approach	**143 220**	**13 606**	114 733	10 900	140 802	13 376
Portfolios subject to the Standardised Approach	**9 409**	**894**	9 717	923	8 547	812
Equity investment risk						
Market-based (simple risk-weighted approach)	**24 136**	**2 293**	28 814	2 737	25 911	2 462
Market risk	**9 852**	**936**	9 434	896	9 013	856
Standardised Approach	**3 058**	**291**	2 428	230	2 752	261
IMA	**6 794**	**645**	7 006	666	6 261	595
Operational risk[2]						
AMA	**59 037**	**5 609**	53 633	5 095	54 317	5 160
Non-customer assets	**16 521**	**1 569**	17 312	1 645	16 505	1 568
	408 397	**38 798**	395 461	37 568	422 713	40 158

Notes

[1] *The required capital is the regulatory minimum excluding the bank specific (Pillar 2b) add on.*

[2] *AMA for operational risk, except for an immaterial portion of the Group that use the Basic Indicator approach (BIA), or SA.*

June 2011 disclosures *(continued)*

Absa Bank RWAs and minimum required capital – Table 2:

	30 June				31 December	
	2011		2010		2010	
	RWAs Rm	Required[1] capital Rm	RWAs Rm	Required[1] capital Rm	RWAs Rm	Required[1] capital Rm
Basel II measurement approach						
Credit risk	**275 603**	**26 182**	266 564	25 324	294 136	27 943
Portfolios subject to the AIRB approach	**133 186**	**12 652**	158 552	15 063	155 841	14 805
Portfolios subject to the FIRB approach	**142 417**	**13 530**	107 272	10 191	138 285	13 137
Portfolios subject to the Standardised Approach	**—**	**—**	740	70	10	1
Equity investment risk						
Market-based (simple risk-weighted approach)	**26 824**	**2 548**	31 422	2 985	28 670	2 724
Market risk	**9 852**	**936**	9 433	896	9 013	856
Standardised Approach	**3 058**	**291**	2 427	230	2 752	261
IMA	**6 794**	**645**	7 006	666	6 261	595
Operational risk[2]						
AMA	**50 654**	**4 812**	49 382	4 691	48 819	4 638
Non-customer assets	**10 852**	**1 031**	11 512	1 094	11 097	1 054
	373 785	**35 509**	368 313	34 990	391 735	37 215

Capital requirements

The Group manages its capital in accordance with minimum regulatory requirements, EC requirements as well as target ranges approved by the board, as follows:

» from a **regulatory perspective**: net qualifying capital (Tier 1 capital plus Tier 2 capital) must sufficiently exceed Basel II minimum capital requirements to provide a buffer for prudence;

» from an **economic perspective**: available capital resources must be sufficient to meet EC requirements over a 3 year period; and

» in accordance with **board-approved target ranges**: which are derived from stress testing results, and are set above the minimum regulatory requirements.

Capital adequacy

The Group sets target capital ranges/levels for regulated entities to ensure the objectives of capital management are met. Appropriate capital management actions are taken if these target ranges/levels are at risk of being breached.

Capital adequacy and the use of regulatory capital are monitored by employing techniques based on the guidelines developed by the Basel Committee on Banking Supervision (the Basel Committee) and implemented by the South African Reserve Bank (SARB) and other host regulators for supervisory purposes. These techniques include the capital adequacy ratio calculation, which the SARB and other host regulators regard as a key supervisory tool.

Target capital ratios for the Group for the period under review were set by taking the following into account:

» the optimisation of the cost of equity given regulatory constraints on capital composition;

» the preference of rating agencies for permanent capital;

» stressed scenarios;

» proposed Basel amendments; and

» peer analysis.

Target capital ranges/levels were set for the following regulated entities: Absa Group Limited, Absa Bank Limited, Barclays Bank Mozambique S.A. (BBM), National Bank of Commerce (NBC), Absa Life Limited and Absa Insurance Company Limited. Target capital levels for all other entities are equal to minimum regulatory requirements set by the respective regulators.

Notes

[1] *The required capital is the regulatory minimum excluding the bank specific (Pillar 2b) add on.*

[2] *AMA for operational risk, except for an immaterial portion of the Group that use the Basic Indicator approach, or Standardised Approach.*

June 2011 disclosures *(continued)*

Capital adequacy *(continued)*

Absa Group – local, foreign banking and insurance entities – Table 3:

		30 June 2011		30 June 2010		31 December 2010		2011 Total target capital adequacy ratio	
Operations	Regulator	Tier 1 ratio %	Total capital adequacy %	Tier 1 ratio %	Total capital adequacy %	Tier 1 ratio %	Total capital adequacy %	Regulatory minimum %	Board target[1] %
Local entities (South Africa)									
Absa Group[2]	SARB	**13,9**	**16,7**	13,1	15,8	12,8	15,5	**9,75**	**12,00 – 14,00**
Absa Bank[2]	SARB	**13,0**	**16,0**	12,0	14,9	11,9	14,8	**9,75**	**11,50 – 13,50**
Foreign banking entities									
BBM[3]	Banco de Mozambique	**21,9**	**21,9**	14,4	14,4	20,4	20,4	**8,00**	**15,00**
NBC[4]	Bank of Tanzania	**13,0**	**13,0**	14,1	14,1	13,0	13,0	**12,00**	**14,00**
Insurance entities									
Absa Life Limited	FSB[5]	**n/a**	**3,6 x CAR[6]**	n/a	3,1 x CAR[6]	n/a	3,5 x CAR[6]	**1,0 x CAR[6]**	**2,0 x CAR[6]**
Absa Insurance Company Limited	FSB[5]	**n/a**	**54,4% x NWP[7]**	n/a	57,7% x NWP[7]	n/a	53,7% x NWP[7]	**25% x NWP[7]**	**45% x NWP[7,8]**
Absa *idirect* Limited	FSB[5]	**n/a**	**87,9% x NWP[7]**	n/a	54,9% x NWP[7]	n/a	60,1% x NWP[7]	**25% x NWP[7]**	**25% x NWP[7,9]**

Capital supply

The Group increased its total qualifying capital supply by R2,8 billion (2010: R5,4 billion).

Qualifying capital

Regulatory guidelines define 3 tiers of capital:

Primary (Tier 1)

- Primary capital consists of issued ordinary share capital, non-cumulative non-redeemable preference share capital, retained earnings, hybrid debt instruments (in terms of Basel II) and certain accounting reserves.
- Primary capital is reduced by 50% of the amount that expected losses exceed eligible provisions and 50% of first loss credit enhancement provided in respect of securitisation schemes. Further deductions against Tier 1 capital include goodwill and certain investments.
- Primary capital is the highest tier of capital and can be used to meet trading and banking activity requirements.

Secondary (Tier 2)

- Secondary capital includes cumulative preference shares and subordinated debt (prescribed debt instruments).
- Secondary capital is reduced by 50% of the amount that expected losses exceed eligible provisions and 50% of first loss credit enhancement provided in respect of securitisation schemes.
- Secondary capital can also be used to meet trading and banking activity requirements.

Tertiary (Tier 3)

- Tertiary capital comprises prescribed unsecured subordinated debt with minimum original maturity of 2 years.
- The use of Tier 3 is restricted to trading activities only.
- It is not eligible to support counterparty or settlement risk.

Notes

[1] *The board approved the following target ranges for 2011:*

	Total	*Total Tier 1*	*Core Tier 1*
Absa Group	*12,00% – 14,00%*	*10,00% – 12,00%*	*9,00% – 11,00%*
Absa Bank	*11,50% – 13,50%*	*9,50% – 11,50%*	*8,50% – 10,50%*

[2] *Statutory ratios include unappropriated profits.*
[3] *Basel I statutory ratios and regulatory requirements.*
[4] *Basel I regulatory ratios and requirements.*
[5] *FSB: Financial Services Board.*
[6] *Capital adequacy requirement (CAR): actuarial calculation of value at risk on insurance liabilities. 2,0 times (2010: 2,0 times) being the required capital level determined by Absa Life Limited.*
[7] *NWP: Net written premiums.*
[8] *45% (2010: 45%) of NWP, being the required capital level determined by Absa Insurance Company Limited.*
[9] *Quota share reinsurance is used to maintain capital adequacy at a level sufficiently in excess of the regulatory minimum.*

June 2011 disclosures *(continued)*

Qualifying capital *(continued)*

Movements in qualifying capital – Table 4:

	30 June 2011 Absa Group Rm	30 June 2011 Absa Bank Rm
Balance at the beginning of the year	**65 417**	**57 801**
Share capital, premium and reserves	**2 691**	**2 106**
Non-controlling interest – ordinary shares	**86**	**—**
General allowance for credit impairments: SA	**1**	**—**
Regulatory deductions	**(26)**	**47**
Balance at the end of the period	**68 169**	**59 954**

Breakdown of Absa Group's qualifying capital – Table 5:

	30 June 2011 Rm	30 June 2011 %[1]	30 June 2010 Rm	30 June 2010 %[1]	31 December 2010 Rm	31 December 2010 %[1]
Primary capital						
Ordinary share capital	**1 434**	**0,4**	1 433	0,4	1 433	0,3
Ordinary share premium	**4 562**	**1,1**	4 805	1,2	4 590	1,1
Preference share capital and premium	**4 644**	**1,1**	4 644	1,2	4 644	1,1
Reserves[2]	**47 729**	**11,7**	42 552	10,8	45 011	10,7
Non-controlling interest – ordinary shares	**1 301**	**0,3**	1 359	0,3	1 215	0,3
Deductions	**(2 849)**	**(0,7)**	(3 002)	(0,8)	(2 832)	(0,7)
Goodwill	**(572)**	**(0,1)**	(573)	(0,1)	(572)	(0,1)
50% of financial and insurance entities not consolidated	**(62)**	**(0,0)**	(69)	(0,0)	(61)	(0,0)
50% of amount by which expected loss exceeds eligible provisions	**(1 222)**	**(0,3)**	(1 632)	(0,4)	(1 214)	(0,3)
50% of first loss credit enhancement provided in respect of a securitisation scheme	**—**	**—**	(107)	(0,1)	—	—
Other deductions	**(993)**	**(0,3)**	(621)	(0,2)	(985)	(0,3)
	56 821	**13,9**	51 791	13,1	54 061	12,8
Secondary capital						
Subordinated redeemable debt	**12 611**	**3,1**	12 611	3,2	12 611	3,0
General allowance for credit impairment, after deferred tax – SA	**21**	**0,0**	52	0,0	20	0,0
Deductions	**(1 284)**	**(0,3)**	(1 807)	(0,5)	(1 275)	(0,3)
50% of financial and insurance entities not consolidated	**(62)**	**(0,0)**	(68)	(0,0)	(61)	(0,0)
50% of amount by which expected loss exceeds eligible provisions	**(1 222)**	**(0,3)**	(1 632)	(0,4)	(1 214)	(0,3)
50% of first loss credit enhancement provided in respect of a securitisation scheme	**—**	**—**	(107)	(0,1)	—	—
	11 348	**2,8**	10 856	2,7	11 356	2,7
Total qualifying capital	**68 169**	**16,7**	62 647	15,8	65 417	15,5

Notes

[1] *Percentage of capital to RWAs.*

[2] *Reserves include unappropriated banking profits.*

June 2011 disclosures *(continued)*

Qualifying capital *(continued)*

Breakdown of Absa Bank's qualifying capital – Table 6:

	30 June				31 December	
	2011		2010		2010	
	Rm	%[1]	Rm	%[1]	Rm	%[1]
Primary capital						
Ordinary share capital	**303**	**0,1**	303	0,1	303	0,1
Ordinary share premium	**11 465**	**3,1**	10 465	2,8	11 465	2,9
Preference share capital and premium	**4 644**	**1,2**	4 644	1,3	4 644	1,2
Reserves[2]	**34 151**	**9,1**	30 979	8,4	32 045	8,2
Deductions	**(1 864)**	**(0,5)**	(2 244)	(0,6)	(1 877)	(0,5)
Goodwill	**—**	**—**	(1)	(0,0)	—	—
50% of amount by which expected loss exceeds eligible provisions	**(1 356)**	**(0,4)**	(1 798)	(0,5)	(1 389)	(0,4)
50% of first loss credit enhancement provided in respect of a securitisation scheme	**—**	**—**	(53)	(0,0)	—	—
Other deductions	**(508)**	**(0,1)**	(392)	(0,1)	(488)	(0,1)
	48 699	**13,0**	44 147	12,0	46 580	11,9
Secondary capital						
Subordinated redeemable debt	**12 611**	**3,4**	12 611	3,4	12 611	3,3
Deductions	**(1 356)**	**(0,4)**	(1 850)	(0,5)	(1 390)	(0,4)
50% of amount by which expected loss exceeds eligible provisions	**(1 356)**	**(0,4)**	(1 798)	(0,5)	(1 390)	(0,4)
50% of first loss credit enhancement provided in respect of a securitisation scheme	**—**	**—**	(52)	(0,0)	—	—
	11 255	**3,0**	10 761	2,9	11 221	2,9
Total qualifying capital	**59 954**	**16,0**	54 908	14,9	57 801	14,8

Capital transferability

The Group is the primary provider of equity capital to its subsidiaries and capital is held centrally in accordance with the approved annual Group capital plan.

The Group policy stipulates that capital held in Group entities in excess of board-approved target levels/ranges should be repatriated to the Group in the form of dividends and/or capital repatriation, subject to local regulatory requirements, exchange controls and strategic management decisions. Apart from the aforesaid, the Group is not aware of any material impediments to the prompt transfer of capital resources or repayment of intragroup liabilities when due.

Economic capital (EC)

EC capital is defined as the minimum capital needed to maintain an AA Investment rating under an extreme stress scenario. The Group assesses EC requirements by measuring its risk profile using both internally and externally developed models. The Group assigns EC primarily within six risk categories: retail credit risk, wholesale credit risk, traded and non-traded market risk, operational risk, fixed assets risk and equity investment risk in the banking book.

The Group regularly enhances its EC methodology and benchmarks outputs to external reference points. The framework reflects default probabilities during average credit conditions (through-the-cycle (TTC) effect), rather than those prevailing at the reporting date (point-in-time (PIT)), therefore removing cyclicality from the EC calculation.

EC for wholesale credit risk includes counterparty credit risk arising as a result of credit risk on traded market exposures. EC for market risk covers both traded and non-traded market risk. The framework also adjusts EC to reflect time horizon, correlation of risks and risk concentrations.

EC is allocated on a consistent basis across all of the Group's businesses and risk activities. A single cost of equity is applied to calculate the cost of risk. The total average EC required by the Group, as determined by risk assessment models and after considering the Group's estimated portfolio effects, is compared with the supply of EC to evaluate EC utilisation.

Notes

[1] *Percentage of capital to RWAs.*

[2] *Reserves include unappropriated banking profits.*

June 2011 disclosures *(continued)*

Economic capital *(continued)*

Economic capital supply

The supply of EC is calculated as the average available shareholders' equity after adjustment and including preference shares, but excluding other non-controlling interests. The Group's EC calculations form the basis of the Group's submission for Basel II ICAAP.

Funds available for EC are impacted by a number of factors arising from the application of IFRS and are adjusted for in calculating available funds for EC. EC supply includes:

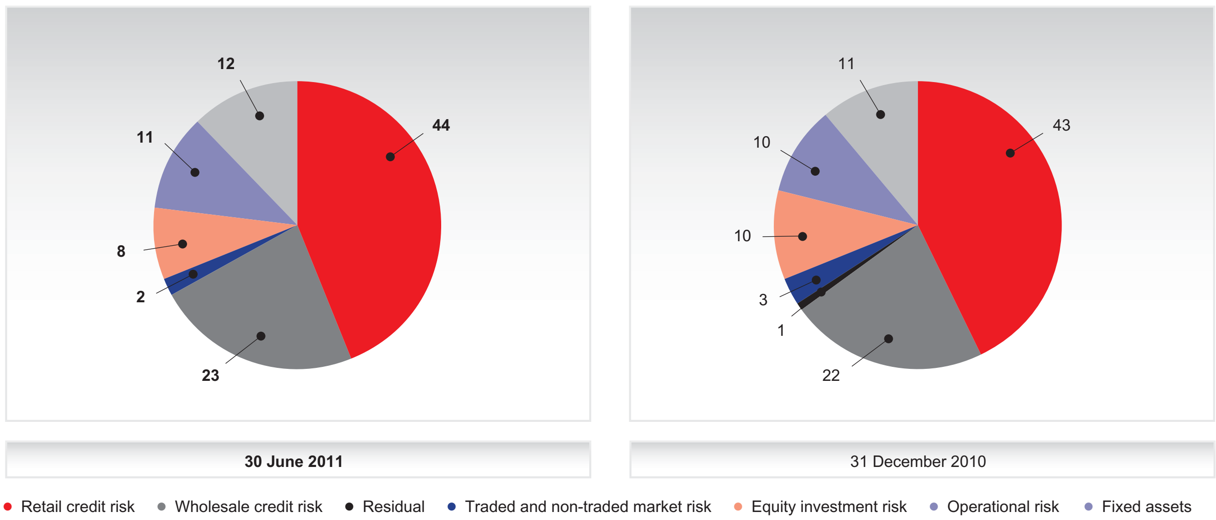
- ordinary shareholders' equity;
- retained earnings, whether appropriated or not; and
- non-redeemable, non-cumulative preference shares.

The following other capital resources are excluded from EC:

- Cash flow hedging reserve – to the extent the Group undertakes the hedging of future cash flows, shareholders' equity will include gains and losses that will be offset against the gain or loss on the hedged item when it is recognised in the statement of comprehensive income at the conclusion of the hedged transaction. Given the future offset of such gains and losses, they are excluded from shareholders' equity when calculating EC.
- Available-for-sale reserve – unrealised gains and losses on such securities are included in shareholders' equity until disposal or impairment. Such gains and losses are excluded from shareholders' equity for the purposes of calculating EC.
- Retirement benefit assets and liabilities – the Group has recorded a surplus with a consequent increase in shareholders' equity. This represents a non-cash increase in shareholders' equity. For the purposes of calculating EC, pension surplus is excluded from shareholders' equity.
- Non-controlling interest.
- Goodwill.
- Other perpetual debt, preference shares and subordinated debt.
- Tertiary capital.

EC allocations reflect varying levels of risk. The EC framework covers not only Basel II Pillar 1 risks but also additional economic risks not covered at all, or inadequately covered in Pillar 1. Further, other risks included in EC are an add-on for concentration risk within the credit portfolio and country transfer risk.

Economic capital[1] (%)



Note

[1] *Excludes insurance due to difference in confidence level in terms of insurance regulation.*

June 2011 disclosures *(continued)*

Credit ratings – Table 7:

	July 2011 Moody's[1] Absa Bank Limited	July 2011 Fitch ratings[2] Absa Bank Limited	Absa Group Limited
National			
Short term	Prime–1.za	F1+ (zaf)	F1+ (zaf)
Long term	Aa1.za	AAA (zaf)	AAA (zaf)
Outlook	Stable	Stable	Stable
Local currency			
Short term	Prime–1	—	—
Long term	A1	A	A
Outlook	Stable	Stable	Stable
Foreign currency			
Short term	Prime–2	F1	F1
Long term	A3	A	A
Outlook	Stable	Stable	Stable
Bank's financial strength	C–	C	C
Baseline Credit Assessment[3]	Baa1	—	—
Viability Rating[4]	—	bbb+	bbb+
Outlook	Stable	Stable	Stable
Support	—	1	1

Basel III

The finalised Basel III framework was released on 16 December 2010. The framework focuses on the following areas:

» stringent new liquidity requirements through the creation of two ratios: liquidity coverage ratio and net stable funding ratio;

» higher and better quality capital, including the creation of conservation and counter-cyclical buffers;

» improved trading risk coverage; and

» leverage ratio caps with a minimum of 3%, also now incorporating off-statement of financial position exposures.

The Group is expected to remain adequately capitalised following the implementation of Basel II.5 and Basel III. However, it is anticipated that the new rules will increase the Group's capital requirements. Certain management actions have been identified to mitigate the impact of this anticipated increase in capital requirements.

There is uncertainty regarding the implementation of certain Basel III rules, particularly the National Discretion items, and the Group is actively engaging with the SARB to obtain more clarity. The Group has deemed it prudent to maintain higher capital levels until clarity is obtained.

The Basel Committee on Banking Supervision (BCBS) is monitoring the potential impact of Basel III by initiating Quantitative Impact studies (QIS) exercises by local regulators worldwide. The Group is participating in the QIS, which covers capital, liquidity and leverage. The QIS will be repeated every six months to refine the expected effects and to investigate the impact of different parameters.

The Group will continue to review its capital position in light of the Basel III rules and will implement appropriate management actions when necessary.

Focus going forward

In the following six months, the Group will focus on:

» maintaining its well capitalised position;

» introducing further RWA optimisation initiatives and preparing for the implementation of Basel II.5 in January 2012 and Basel III with effect from 2013;

» maintaining its investment grade target rating, following its ratings meetings held during the period under review;

» continuing to generate sufficient capital to support asset growth; and

» achieving a return above the cost of equity.

Notes

[1] *Moody's released a rating agency report pertaining to Absa Bank Limited in July 2011. There were no changes in the ratings in the July 2011 report compared to the July 2010 report.*

[2] *Fitch released a rating report pertaining to Absa Bank Limited and Absa Group Limited in July 2011. There were no changes in the July 2011 report compared to the January 2011 report.*

[3] *The baseline credit assessment reflects what the local currency deposit rating of the bank with the given Bank Financial Strength Rating would be without any assumed external support from a government or third party.*

[4] *Fitch introduced a Viability rating on financial institutions around the globe, with effect from July 2011, which represents Fitch's primary assessment of the intrinsic (stand alone) creditworthiness of these institutions.*

Credit risk

Six months ended 30 June 2011

Highlights

- *Focus on rehabilitating customer arrears and reducing impairments.*
- *Improved use of data to optimise management of risk/reward.*
- *Enhanced governance and operational efficiencies.*
- *Submission of the Absa Wholesale AIRB application to the South African Reserve Bank (SARB).*

Key performance indicators

	30 June		31 December
	2011	2010	2010
	%	%	%
Growth in total gross loans and advances to customers	**(1,0)**	(4,0)	(1,0)
Non-performing advances as a percentage of loans and advances	**7,7**	7,6	7,7
Impairment losses ratio	**1,18**	1,50	1,20
Total credit impairments as a percentage of total gross loans and advances to customers	**2,7**	2,8	2,7

Introduction

Credit risk is the risk of loss to the Group arising from the failure of a customer or counterparty to fulfil its payment obligations. Credit risk arises mainly from lending and related banking activities, including underwriting, dealing in traded products such as derivative contracts, as well as securities borrowing and lending products. It may also arise when fair values of the Group's exposure to financial instruments decline.

Strategy

Credit risk is a core component of lending quality and impacts the risk versus reward model. Credit risk has been receiving increased attention as a result of recent economic conditions and subdued growth.

The Group's credit risk strategy involves:

- maintaining an appropriate credit risk environment through continuous investment in skilled and experienced staff;
- operating under a sound credit-granting process using the flexibility of industry leading systems;
- maintaining an appropriate credit administration, measurement and monitoring process;
- ensuring adequate and operationally effective controls over credit risk;
- optimising the use of available credit bureau data to make informed decisions and to build robust models (risk and reward);
- proactively managing credit risk through the economic cycle and ensuring the desired return/economic profit is maintained;
- managing credit risk and the mitigation thereof within the risk appetite boundaries of the Group;
- measuring credit risk inherent in the portfolio using models which are relevant and accurately calibrated; and
- continuing focus on enhancing Absa's collection and recovery process.

Governance

During the period under review, the revised governance frameworks which redefined and articulated the roles and responsibilities of stakeholders' in the credit risk management process, were embedded. The credit risk policy frameworks provide structures within which credit risk is managed and for which credit policies are developed. These policies are approved by the Credit Risk Committee (CRC) and are supported by Business Unit (BU) policies approved at BU level. BU management is responsible for implementing relevant credit policies. Various credit cluster committees exist to perform reviews and provide adequate oversight for the specific risk in a particular business area.

Additional oversight is in place by virtue of the requirement to report to the Governance and Control Committees (GCCs), CRC and ultimately the GRCMC to ensure adequate reviews of controls, risk trends and that credit risk is managed effectively.

Six months period in review

Wholesale credit risk

The domestic economy is gradually moving out of recession, with the recovery more pronounced in some sectors, such as the manufacturing and motor-related industries, while in others, such as commercial property, asset prices remain under pressure. This uneven rebound, combined with systemic uncertainty about the sustainability of the recovery, has resulted in a lack of commitment to infrastructure and working capital investment, with customers instead focusing on de-leveraging their statements of financial position.

The gradual increase in economic activity and concomitant recovery in local equity markets have served to improve the credit quality (in the form of probability of default) across the majority of industries within the wholesale portfolio. Although credit quality has not yet returned to pre-crisis levels, there has been a consistent improvement since the height of the crisis in early 2009, which is expected to continue as the local macro-economic environment stabilises further and major sovereign debt issues are resolved. The improvement is also evident through reduced inflows to the Early Warning List (the Bank's distressed debt list), and reduced specific and portfolio impairment levels.

Retail credit risk

Conditions remained challenging, despite evidence of the expected economic recovery. Growth proved difficult and the total portfolio remained static. The Group reviewed its lending policies on a regular basis to ensure returns were optimised. Impairments remained a key driver with continued improvement apparent.

Early delinquencies continued to improve in all portfolios in line with the economic recovery. The legal books, particularly the secured portfolios, remained under pressure due to the lengthy legal process, exacerbated by the debt counselling process and the subdued mortgage market. Although improved collections processes and strategies for the mortgage legal portfolio and properties in possession started to bear fruit, a protracted recovery period remains expected.

The reduction in the debt counselling book continued, notwithstanding the moratorium on certain mortgage accounts until March 2011. Many accounts entered the legal process and this continued to place the legal portfolios under pressure.

Securitisation

The securitization portfolio reduced in the first half of 2011. Abacas, Absa's securitisation conduit, reduced from R2,5 billion at 31 December 2010 to R2,3 billion at 30 June 2011, and notes held on-statement of financial position reduced from R3,6 billion to R3,1 billion, both due to natural amortisation.

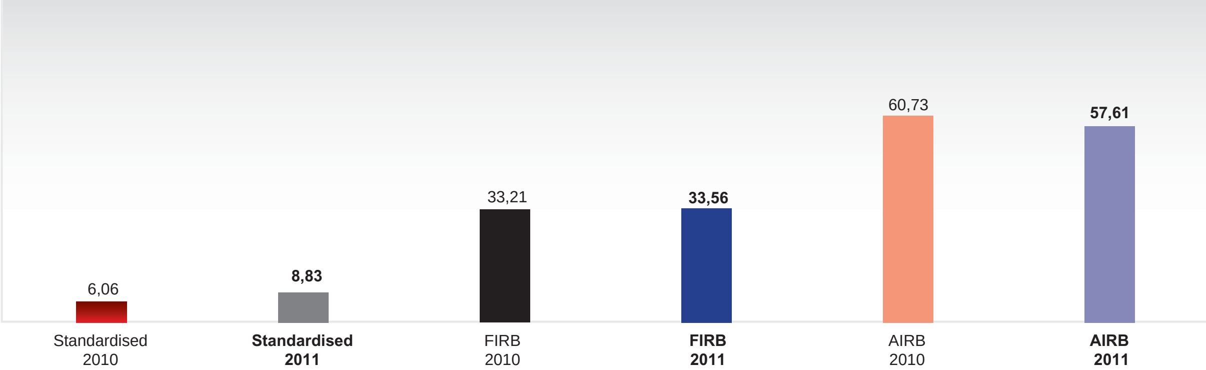
Approach to credit risk

The Group applies both the SA and IRB approaches to various portfolios for the purpose of calculating regulatory capital requirements illustrated in the table below:

Approaches	Standardised	Foundation IRB	AIRB
Reporting of balances	» Statutory reserve and liquid assets » African operations	» Domestic corporate portfolios (including specialised lending portfolios) » Public sector entities » Local government » Municipalities » Sovereign, banks and securities firms	» Domestic retail portfolios (including SMEs)
Assessment applied	» Standard risk weight percentage as prescribed in the regulations relating to banks	» Statistical, structural and expert based models either developed internally or based on service of external vendors	» Automated application and behavioural scoring based on statistical models

Six months ended 30 June 2011

EAD per Basel Approach as at June 2011 (%)



Standardised approach (SA)

The Group's African operations and the statutory liquid asset portfolios are subject to the SA. For capital calculation purposes, these exposures are multiplied by the standard risk weight percentages as set out in the Bank's Act regulations. The Group is investigating the possibility of moving its statutory liquid asset portfolio to the more advanced approach as set out in the aforesaid regulations.

IRB approach

To assess credit risk under this approach, the Group analyses this risk into its common components of probability of default (PD), exposure at default (EAD) and loss given default (LGD), modelled at a customer, facility and portfolio level. These risk components are then used in the calculation of a number of aggregate risk measures such as expected loss (EL), RC and EC.

The assessment of credit risk relies heavily on quantitative models and tools developed internally and supplemented by vendor solutions in a number of areas.

The Group classifies all credit models by materiality, based on a combination of measures aimed at assessing the 'value at stake' (VAS) for the Group. The VAS measure used for a specific model is determined by its relevance for the respective portfolio as well as the risk the model is intended to assess. The pertinent measures for most credit models are EC and the amount of exposure covered by the model.

The levels of materiality at Group level, as prescribed by the MRP, are as follows:

» A high materiality at Group level requiring Executive Model Committee (EMC) approval;

» A significant models requiring Group Exco Committee approval;

» B medium materiality at Group level;

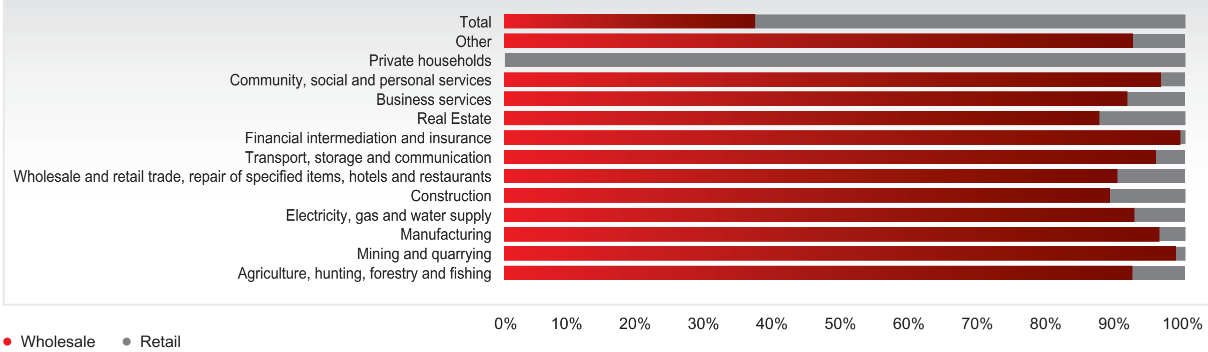
» C low materiality at Group level; and

» D very low materiality at Group level.

All models are monitored on an ongoing basis and validated, at least annually, by an independent validation unit within Group Credit. Monitoring information and validation results are reported to and discussed at the CMMC, the CRTC, the CRC, the EMC and the GRCMC.

The graph below provides a view of the split between the wholesale and retail portfolios per industry.

Total industry EAD – 30 June 2011 (%)



Approach to credit modelling

Absa Retail has in the past two years redeveloped its Basel models based on international best practice. This includes standardisation of methodology and documentation across its Retail portfolios resulting in improved transparency in the capital allocation process, specifically:

- New bespoke scorecards, which incorporated international input, were developed and implemented in August 2010. These replaced the existing generic scorecards that had been in place on implementation of the accord.
- PD methodology was reviewed and subsequently amended based on the variable scaler approach which is used to determine through-the-cycle PD estimates.
- LGD methodologies were reviewed and revised methodologies were adopted, specifically for Absa's retail secured and unsecured portfolios.
- A new downturn LGD methodology was developed in-house and subsequently approved by the regulator. This replaced the generic Federal Reserve formula, commonly used in the industry.

Probability of default (PD)

The PD measures the likelihood of a customer defaulting on its obligations within the next year and is a primary component of the internal risk rating calculated for all customers. The Group uses two types of PDs, namely:

- point-in-time (PIT) PD, which reflects current economic, industry and borrower circumstances; and
- through-the-cycle (TTC) PD, which reflects the Group's assessment of the borrower's long-run average propensity to default in the next year.

Both types of PDs are used extensively in the Group's decision-making processes and several types of rating approaches are employed across the Group. For communication and comparison purposes, the Group maps its PD estimates to a 21 default grade (DG) master scale, aligned to the SARB 26 grade scale used for regulatory reporting purposes (see table 8).

Exposure at default (EAD)

The EAD is the total amount the Group expects to be outstanding from a particular customer at the time of default. The Group calculates these estimates for each facility using models developed using internal and external default data as well as the experience of credit experts.

EAD estimates incorporate both on- and off-statement of financial position exposures resulting in a capital requirement incorporating existing exposures, as well as exposures contingent on a counterparty's use of an available facility. Standard parameters for credit conversion prescribed by the regulator are used for those portfolios on the FIRB approach.

Loss given default (LGD)

The LGD measures the loss expected on a particular facility in the event of default and recognises credit risk mitigants the Group may employ such as collateral or credit risk derivatives. LGD estimates are calculated as a percentage of EAD using models based on internal and external loss data as well as the judgement of credit experts and are primarily driven by the type and value of collateral held. The Group modifies its LGD estimates to distinguish between expected losses over the course of an economic cycle and loss estimates during periods of economic stress (downturn LGD). Standard parameters are used for those portfolios on the FIRB approach, as prescribed by the regulator.

Expected loss (EL) and capital requirements

The PD, EAD and LGD, are building blocks used in a variety of applications that measure credit risk across the entire portfolio. EL is a measurement of loss which enables the application of consistent credit risk measurement across all retail and wholesale credit exposures.

These components are the basis for regulatory and economic capital calculations. EL figures are calculated as the TTC product of PD, EAD and downturn LGD and represent the Group's best estimate of losses for the next year based on long-run estimates that span an entire business cycle.

These estimates are also used in a range of applications, including pricing, customer and portfolio strategy and performance measurement. EL estimates are compared to impairment figures that, while they may be similar, are calculated on a different basis and for different purposes and should therefore not be expected to match one another.

EL is a statistical estimate of the average loss for the loan portfolio for the next 12 months, based on a long-term average loss tendency that incorporates at least one business cycle. This type of measure provides a measure of loss independent of current credit conditions for a particular customer type, and is more stable over time. It is mainly used in the capital measurement processes.

The Group categorises its exposures to a 21-grade internal rating DG scale that corresponds to a statistical probability of customers in that rating class defaulting within a 12 month period. An indicative mapping of the DG buckets to the equivalent international rating agency and regulatory PD bands are set out in the table below:

Approach to credit modelling *(continued)*

Mapping of DG to PD band, alphanumeric agency grades and regulatory bands – Table 8:

		Absa DG to PD mapping			Alphanumeric scale mapping			Regulatory PD band to PD mapping		
Default grade bucket	Note	Min PD (>) %	Max PD (<) %	PD Mid-point %	Standard & Poor's	Moody's	Fitch's	PD band	Lower bound %	Upper bound %
1	1	0,0000	0,0200	0,0100	AAA	Aaa	AAA	1	0,0001	0,0120
2		0,0200	0,0300	0,0250	AA	Aa	AA	2	0,0121	0,0170
3		0,0300	0,0500	0,0400	A+	A1	A+	3	0,0171	0,0240
4		0,0500	0,1000	0,0750	A/A–	A2/A3	A/A–	4	0,0241	0,0340
5		0,1000	0,1500	0,1250	BBB+	Baa1	BBB+	5	0,3410	0,0480
6		0,1500	0,2000	0,1750	BBB+/BBB	Baa1/Baa2	BBB+/BBB	6	0,0481	0,0670
7		0,2000	0,2500	0,2250	BBB	Baa2	BBB	7	0,0671	0,0950
8		0,2500	0,3000	0,2750	BBB/BBB–	Baa2/Baa3	BBB/BBB–	8	0,0951	0,1350
9		0,3000	0,4000	0,3500	BB–	Baa3	BBB–	9	0,1351	0,1900
10	2	0,4000	0,5000	0,4500	BBB-/BB+	Baa3/Ba1	BBB–/BBB+	10	0,1901	0,2690
11		0,5000	0,6000	0,5500	BB+	Ba1	BB+	11	0,0269	0,3810
12		0,6000	1,2000	0,9000	BB	Ba2	BB	12	0,3811	0,5380
13		1,2000	1,5500	1,3750	BB/BB–	Ba2/Ba3	BB/BB–	13	0,5381	0,7610
14		1,5500	1,1500	1,8500	BB/BB–	Ba2/Ba3	BB/BB–	14	0,7611	1,0760
15		2,1500	3,0500	2,6000	BB–	Ba3	BB–	15	1,0761	1,5220
16		3,0500	4,4500	3,7500	B+	B1	B+	16	1,5221	2,1530
17		4,4500	6,3500	5,4000	B+/B	Ba1/B2	B+/B	17	2,1531	3,0440
18		6,3500	8,6500	7,5000	B	B2	B	18	3,0441	4,3050
19		8,6500	11,350	10,0000	B-	B3	B–	19	4,3051	6,0890
20	3	11,350	18,650	15,0000	CCC+	Caa1	CCC–	20	6,0891	8,6110
21		18,650	100,00	30,0000	CCC	Caa2	CCC	21	8,6111	12,177
Default		100,00	100,00	100,00	D	D	D	22	12,177	17,222
								23	17,222	24,355
								24	24,355	34,443
								25	34,443	100,00
								Default	100,00	100,00

The Group DG grading represents a through-the-cycle view of the distribution of the book.

Notes

[1] ***Default grades 1 – 10:*** *assets falling within these DG buckets are regarded as 'investment grade' and, when converted to a rating agency equivalent, these correspond to a BB rating and better.*

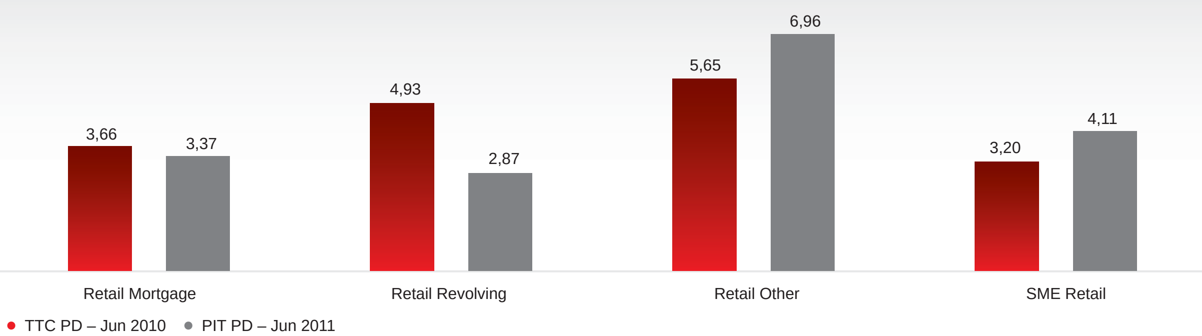
[2] ***Default grades 10 – 19:*** *financial assets in these grades typically require more detailed management attention where clear evidence of financial deterioration or weakness exists. Assets in this category, although currently protected, are potentially weaker credits. These assets contain some credit deficiencies.*

[3] ***Default grades 20 – 21:*** *the probability of default of financial assets in these grades have deteriorated to such an extent that they are included for regular review. Assets so classified must have well defined weaknesses that exacerbate the probability of default. These assets are characterised by the distinct possibility that the borrower will default, and should the collateral pledged be insufficient to cover the asset, the Group will sustain some loss when default occurs.*

Expected versus actual losses

Probability of default[1]

Comparison of PD estimates for the performing book (Retail AIRB) (%)

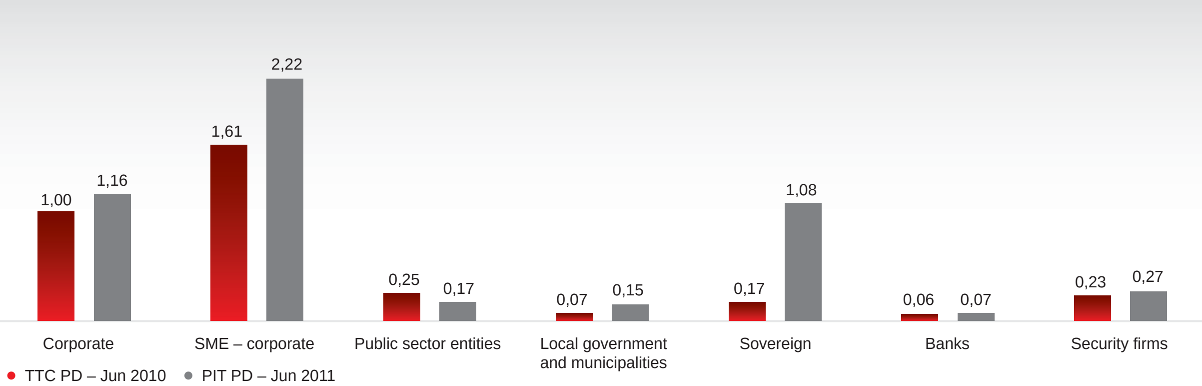


Six months ended 30 June 2011

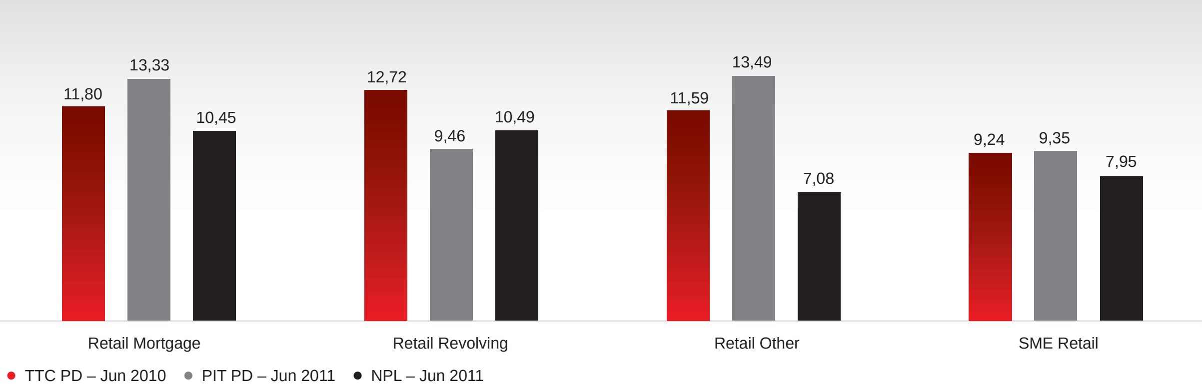
Expected versus actual losses *(continued)*

Probability of default[1] *(continued)*

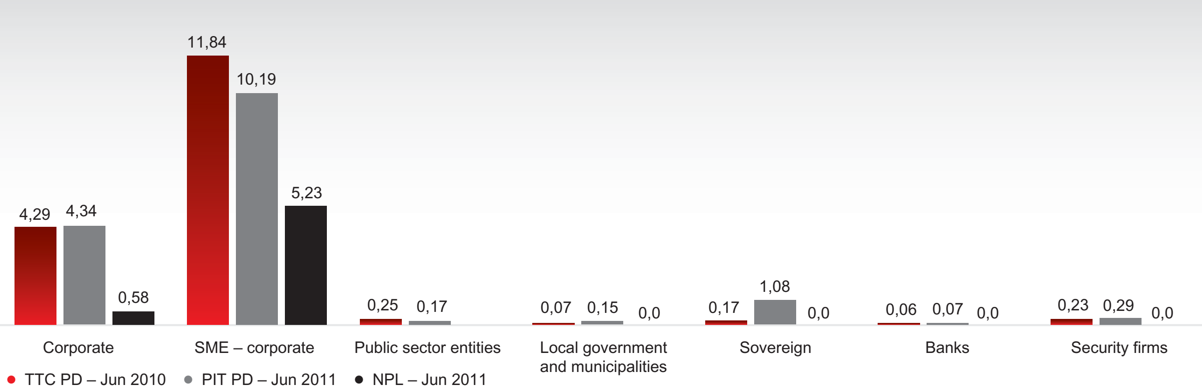
Comparison of PD estimates for performing book (Wholesale FIRB) (%)



Comparison of PD estimates (total book) with non-performing loans (Retail AIRB) (%)



Comparison of PD estimates (total book) with non performing loans (Wholesale FIRB) (%)



The objective of PD back testing is to compare the accuracy of the PD estimates for regulatory purposes with the actual default data.

For each Retail and Wholesale Basel II asset class, the assigned PD for regulatory capital purposes as at 30 June 2010 is compared to the non-performing loans ratio observed in June 2011.

Regulatory PD is adjusted to the cycle through-the-cycle (TTC) while the non-performing loans ratio is observed at a particular point in the cycle (June 2011). To complete the analysis, the observed NPL ratio is also compared to the point-in-time (June 2011) probability of default (PIT PD). A comparison between the TTC PD as at 30 Jun 2010 and PIT PD as at 30 June 2011 for the performing book only (i.e. defaults excluded) is also provided.

Note

[1] *The analysis includes intragroup exposures and excludes Woolworths Financial Services.*

Six months ended 30 June 2011

Expected versus actual losses *(continued)*

Probability of default *(continued)*

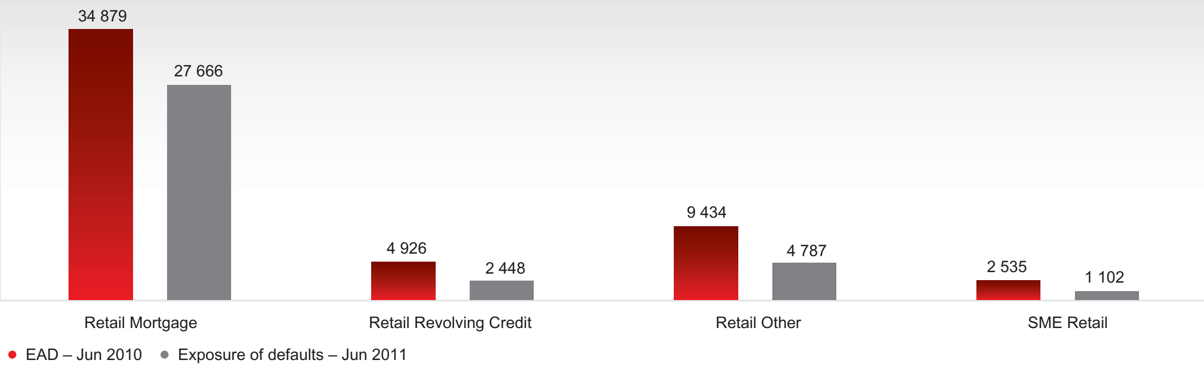
The main conclusions of the analysis are as follows:

- For all asset classes, the regulatory or TTC PD is clearly above the non-performing loans ratio observed in June 2011.
- The PIT PD, i.e. the point-in-time estimates of the model, are above the observed non-performing loans ratio in most cases, except for Retail Revolving.
- When the performing book only is considered (i.e. excluding defaults), the PIT PD as at 30 June 2011 is higher than the TTC PD as at 30 June 2010 for some asset classes.

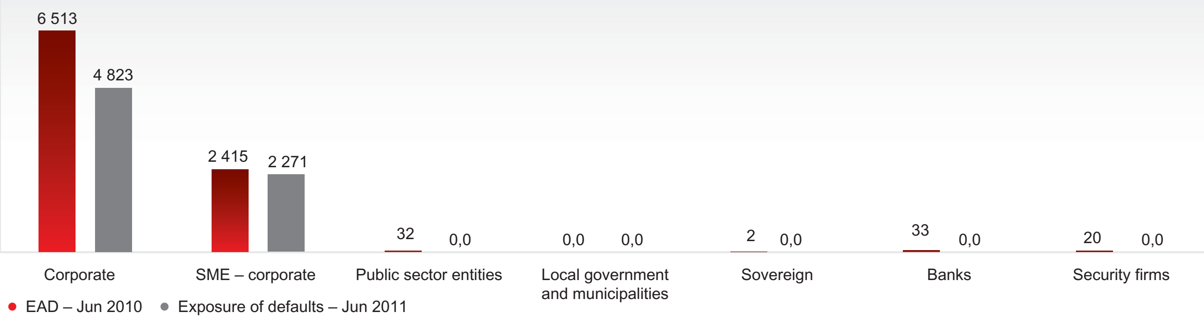
It should also be mentioned that the Retail PIT PD and TTC PD models that were in place during June 2010 were replaced with new models in December 2010. Overall, the new models resulted in a 6% and 23% decrease in the PIT and TTC PD, respectively.

Exposure at default[1]

Comparison of EAD estimates with actual exposure of defaults (Retail AIRB) (Rm)



Comparison of EAD estimates with actual exposure of defaults (Wholesale FIRB) (Rm)



The objective of EAD back testing is to compare the accuracy of EAD estimates for regulatory purposes with the actual exposures of defaults.

For each Retail and Wholesale Basel II asset class, the estimated EAD (Rm) as at 30 June 2010 is compared to the actual exposures in default (Rm) as at the reporting date.

The main conclusions of the analysis are that the actual exposure of defaults as at 30 June 2011 is lower than the estimated EAD as at 30 June 2010 in all cases (30% and 21% lower in total for Retail and Wholesale respectively).

It should also be mentioned that the Retail EAD models that were in place during June 2010 have been replaced with new models in December 2010. Overall, the new models resulted in a 5% decrease in EAD.

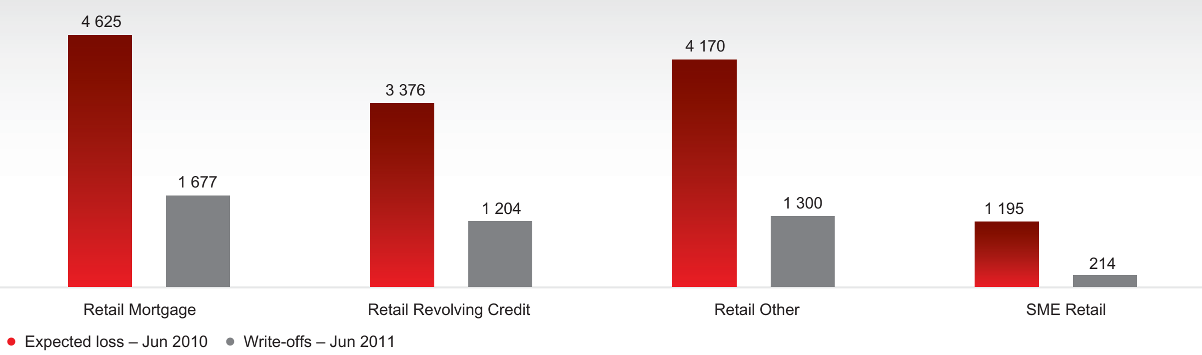
Note

[1] *The analysis includes intragroup exposures and excludes Woolworths Financial Services.*

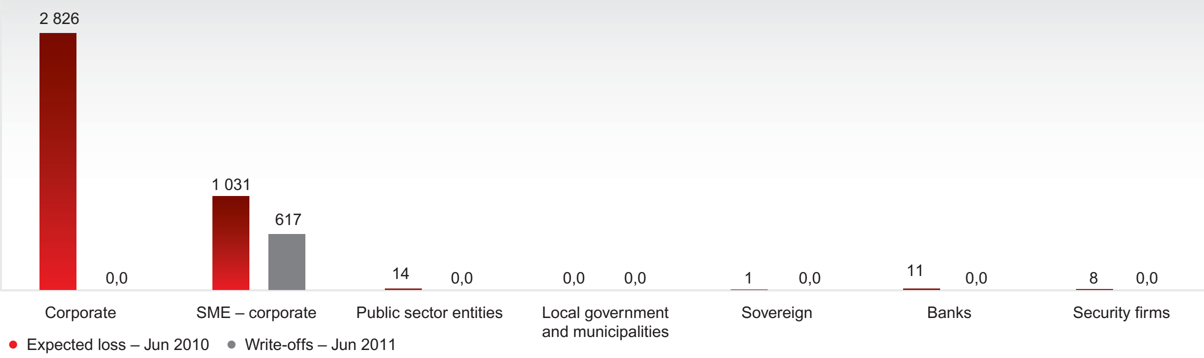
Expected versus actual losses *(continued)*

Expected losses compared to actual write-offs[1]

Comparison of EL estimates with actual write-offs (Retail AIRB) (Rm)



Comparison of EL estimates with actual write-offs (Wholesale FIRB) (Rm)



Note

[1] *The analysis includes intragroup exposures and excludes Woolworths Financial Services.*

The objective of EL back testing is to compare the accuracy of the EL estimates with actual write-off data.

For each Retail and Wholesale Basel II asset class, the estimated EL (Rm) as at 30 June 2010 is compared to the actual amount (Rm) written off for the period under review.

EL is a function of TTC PD, downturn LGD and EAD (EL = TTC PD x downturn LGD x EAD), i.e. it is a through-the-cycle measure adjusted for an economic downturn while the amount written off is observed over a 12 month period (June 2010 to June 2011).

The main conclusions of the analysis are that for all asset classes, the EL estimates are clearly above the actual write-offs observed for the period under review.

It should also be mentioned that the Retail downturn LGD models that were in place during June 2010 were replaced with new models in December 2010. Overall, the new models resulted in a 7% increase in downturn LGD.

Credit risk mitigation, collateral and other credit enhancements

The Group employs a number of techniques to mitigate credit risk:

» strengthening its position as lender in a range of transactions, from retail mortgage lending to large wholesale financing, by structuring a security interest in a physical or financial asset (collateral);

» netting of debtor and creditor balances under regulatory and internal policy, which requires a formal agreement with the customer to net the balances and a legal right to set-off (on- and off-statement of financial position); and

» selective hedging through credit derivatives.

In certain circumstances, depending on the Group's assessment of a customer's financial capacity, financing may be granted on an unsecured basis.

Generally one or more forms of security are sought in the credit approval process. The use and approach to credit risk mitigation (CRM) varies by product type, portfolio, customer and business strategy. Minimum standards, as prescribed in applicable policies and business processes, are applied across the Group and cover:

» general requirements, including acceptable risk mitigation types, and any conditions or restrictions applicable to those mitigants;

Credit risk mitigation, collateral and other credit enhancements *(continued)*

- the maximum LTV ratios, minimum haircuts or other volatility adjustments applicable to each type of mitigant, including, where appropriate, adjustments for currency mismatch, obsolescence and any time sensitivities on asset values;
- the means by which legal certainty is to be established, including required documentation and all necessary steps to establish legal rights;
- acceptable methodologies for the initial and any subsequent valuations of collateral and the frequency with which they are to be revalued;
- actions to be taken in the event of the current value of mitigation falling below required levels;
- management of risk of correlation between changes in credit risk of the customer and the value of CRM, for example, any situation where a customer default materially impacts the value of a mitigant and applying a haircut or recovery value adjustment which reflects the potential correlation risk;
- management of concentration risks, for example, setting thresholds and controls on the acceptability of credit risk mitigants and/or lines of business characterised by a specific collateral type or structure; and
- collateral management to ensure CRM is legally effective and enforceable.

The Group's policies with respect to assessing, acquiring and managing collateral for capital calculation purposes are aligned with regulatory requirements.

Collateral types used by the Group, grouped by type of asset

The following types of collateral are currently held against assets subject to credit risk and are consistent with accepted market practice:

Assets subject to credit risk of financial position	Type of collateral[1]
Cash, cash balances and balances with central banks	» Deposits from customers and cession of ring-fenced bank accounts with cash
Loans and advances to banks	» Bonds and guarantees » Cash » Listed equities » RSA government bonds
Loans and advances to customers	» Assignment of debtors » Bonds over properties (commercial and residential) » Call options to holding companies » Charges on properties » Cession of loan accounts » Debentures » Government guarantees » Guarantees from shareholders and directors » Insurance policies » Life insurance policies » Listed equities » Netting agreements » Parental guarantees » Personal and other company guarantees » Pledged securities » Property and equipment » Put options from holding companies or other companies within the Group » Shares » Suretyships

Note
[1] *This list is not exhaustive. There may be other types of collateral recognised by the Group.*

Credit risk mitigation, collateral and other credit enhancements *(continued)*

Valuation of collateral

Any security taken as part of the credit decision process is valued according to applicable credit policies at the time of credit approval and at regular intervals thereafter. The Group uses a number of approaches for the revaluation of collateral, including physical inspection, statistical indexing and price volatility modelling.

For significant items of security, physical inspections and expert valuations are carried out at regular intervals, and at least annually. Collateral valuations are also updated when an account enters the legal/recovery process to ensure an appropriate impairment allowance can be calculated. In the wholesale portfolios these valuations are reviewed regularly to ensure any impairments raised remain at an appropriate level, including potential gains in the valuation of marketable securities and other market-related instruments that may lead to a partial release of the impairment allowance.

The collateral management process is focused on the efficient handling and processing of a large number of cases in the retail portfolio and the lower end of the corporate sector, therefore relying heavily on the Group's collateral and document management systems. For larger wholesale exposures and capital market transactions, collateral is managed jointly between the credit and legal functions as transactions, and associated legal agreements are often bespoke in nature, in particular, where credit derivatives or customised netting agreements are used as a risk mitigant. All security structures and legal covenants are reviewed at least annually to ensure they remain fit for purpose and consistent with accepted market practice.

Types of guarantor and credit derivative counterparties

In the commercial, corporate and financial sector, the Group often relies on a third party guarantor, which may be a parent company to the borrower, a major shareholder or a bank. Similarly, credit derivative transactions are often used to hedge specific parts of any single name risk in the wholesale portfolio. For these transactions, the most common counterparties or issuers are banks, non-bank financial institutions (NBFIs), large corporates, parastatals and governments. The creditworthiness of the guarantor or derivative counterparty/issuer is assessed as part of the credit approval process and the value of such a guarantee or derivative contract is adjusted accordingly for the purpose of calculating internal LGD estimates.

Use of netting agreements, International Swaps and Derivatives Association (ISDA) master agreements and Collateral Support Annexes (CSAs)

In line with international market practice, the Group endeavours to use netting agreements wherever possible. The Group mainly uses ISDA master agreements as well as CSAs, which provide standardised and commonly accepted processes for managing collateral and margin calls over the lifetime of the transaction. CSAs may place an obligation on the Group unrelated to the underlying instruments in the event of a credit downgrade. Only a small number of the Group's agreements use this tiered structure and an instant downgrade by one rating grade from the current AA-rating (S&P and Fitch) would not trigger such clauses, which would create a requirement for the Group to post additional collateral.

Fair value of collateral for loans past due but not impaired and loans individually impaired

Financial assets past due or individually assessed as impaired (specifically impaired) are for the most part collateralised or subject to other forms of credit enhancements. The effects of such arrangements are taken into account in the calculation of the impairment allowance held against them.

Credit derivatives

The following table provides an overview of the outstanding amount of exposure held in respect of the Group's credit derivative positions, used in the management of its credit portfolio, broken down by product type, indicating whether protection was bought or sold:

Exposure by instrument bought or sold – Table 10:

	30 June								31 December			
	2011				2010				2010			
	Own Credit portfolio				Own Credit portfolio				Own Credit portfolio			
	As protection buyer		As protection seller		As protection buyer		As protection seller		As protection buyer		As protection seller	
	Banking Rm	Trading Rm	Banking Rm	Trading Rm	Banking Rm	Trading Rm	Banking Rm	Trading Rm	Banking Rm	Trading Rm	Banking Rm	Trading Rm
Credit Derivative Product Type												
Credit-default swaps	**—**	**4 509**	**—**	**7 269**	—	1 894	—	6 905	—	2 567	—	7 253
Total return swaps	**—**	**—**	**—**	**—**	—	—	—	—	—	—	—	—
Other	**10 801**	**—**	**577**	**—**	5 762	—	652	—	6 254	—	567	—
Total notional exposure to credit derivative transactions	**10 801**	**4 509**	**577**	**7 269**	5 762	1 894	652	6 905	6 254	2 567	567	7 253

Breakdown of OTC and credit derivative exposure – Table 11:

Derivatives

	June 2011							
	Gross positive fair value Rm	Current netting benefits Rm	Current exposure Rm	Expected positive exposure (CEM) Rm	Expected positive exposure netting (CEM) Rm	Exposure at default Rm	Collateral Value Rm	Notional Value Rm
Commodities	229	151	77	215	52	241	—	3 693
Credit derivatives	106	87	18	1 023	407	634	—	13 191
Equity derivatives	525	315	210	2 015	1 052	1 173	—	32 068
Foreign exchange derivatives	12 703	8 533	4 170	11 724	5 438	10 456	—	572 212
Interest rate derivatives	23 214	18 478	4 737	10 505	5 413	9 829	—	3 644 116
Total	**36 777**	**27 564**	**9 213**	**25 482**	**12 362**	**22 333**	**—**	**4 265 280**

Derivatives

	June 2010							
	Gross positive fair value Rm	Current netting benefits Rm	Current exposure Rm	Expected positive exposure (CEM) Rm	Expected positive exposure netting (CEM) Rm	Exposure at default Rm	Collateral Value Rm	Notional Value Rm
Commodities	3 431	1 351	2 080	1 007	387	2 613	—	18 081
Credit derivatives	1 525	760	765	912	479	1 198	29	11 464
Equity derivatives	1 423	611	812	2 336	842	2 306	3	35 888
Foreign exchange derivatives	8 381	5 429	2 952	10 985	5 713	8 224	494	536 539
Interest rate derivatives	24 286	21 127	3 159	10 711	5 955	7 915	574	3 286 774
Total	39 046	29 278	9 768	25 951	13 376	22 256	1 100	3 888 746

Concentration risk

Due to the composition of the Group's business portfolios, a certain degree of risk concentration in the collateral portfolios is evident. The Group manages these risks through mandate and scale limits that differ across the individual portfolios, for example:

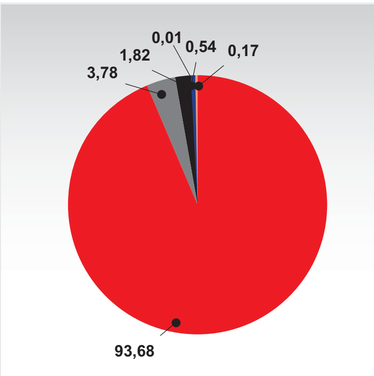
» vehicle and asset finance: limits are placed on the tenure of loans;

» home loans: limits are placed on property values and loan-to-value (LTV) ratios; and

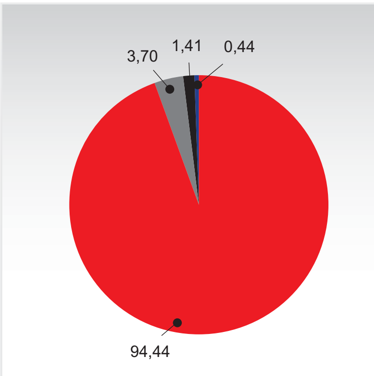
» commercial property finance: limits are placed on the type of asset (e.g. industrial or retail) and geographical area.

Due to the structure of the South African financial markets, a certain level of concentration with respect to derivative counterparties is also to be expected. The Group manages this type of concentration risk through mandate and scale limits, sophisticated, simulation-based exposure models that support a rigorous credit analysis, ongoing monitoring of these counterparties and the Group's mark-to-market (MTM) exposure.

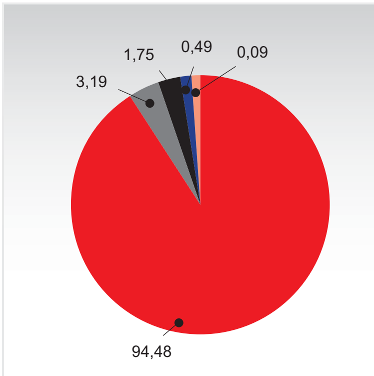
EAD by geography (%)[1]



Six months ended 30 June 2011



Six months ended 30 June 2010



Twelve months ended 31 December 2010

● South Africa ● Europe ● Other African Countries ● North America ● Other ● Asia

Note

[1] *Enhancements to classifications were completed for December 2010 and subsequent disclosures.*

Concentration risk *(continued)*

Wrong way risk

Wrong-way risk is an additional form of concentration risk and arises where a strong correlation exists between the counterparty's PD and the MTM value of the underlying transaction. The Group distinguishes between two types of wrong-way risk, namely:

- specific wrong-way risk, which may arise in transactions with certain structural features, such as the collateralisation of a loan with the borrower's, or related party's shares; and
- general or conjectural wrong-way risk, which may arise where the credit quality of the counterparty is related to the value of the transaction for non-specific reasons (for example, where both the credit quality of the counterparty and the value of the derivative are strongly related to a macro-economic variable).

The Group aims to limit these risk types. However, it recognises the necessity for engaging in certain transactions which could expose it to specific wrong-way risk (such as the funding of broad-based black economic empowerment (BBBEE) transactions).

Counterparty credit risk

Counterparty credit exposure arises from the risk that parties are unable to meet their payment obligations under certain financial contracts, such as derivatives and securities financing transactions (e.g. repurchase agreements). Unlike credit risk, counterparty credit risk implies the bilateral risk of loss.

For allocation of EC to OTC derivative exposures, EAD estimates are treated as MTM loan equivalents, where the amount of capital allocated to a particular transaction is driven by the:

- borrower's netting arrangements;
- borrower's TTC PD;
- trade's residual maturity;
- nature of each trade; and
- net EAD and corresponding LGD.

For RC calculation purposes, the Current Exposure Method (CEM) is applied to OTC derivative exposures. The Group mainly relies on cash, government bonds and negotiable certificates of deposits (NCDs) as collateral for derivative contracts.

The Group intends to apply for permission to use the Internal Model Method (IMM) in the calculation of its RC requirements for these portfolios once the AIRB method for wholesale credit exposures has been embedded. However, during the reporting period, all calculations were based on the CEM. The Group's policies for establishing impairment allowances for traded products' counterparties are based on applicable accounting requirements.

Securitisation

Securitisation transactions, used as part of the Group's credit portfolio, are primarily focused on the effective management of funding requirements. Planned securitisation transactions, market appetite and potential marketing and placement strategies are governed by a delegated mandate from the Board Finance Committee (BFC) and assessed with the assistance of the MRC. There are two main types of securitisation:

- traditional securitisations where an originating bank transfers a pool of assets that it owns to a special purpose entity (SPE) on an arm's length basis; and
- synthetic securitisations where the originating bank transfers only the credit risk associated with an underlying pool of assets, through the use of credit-linked notes or credit derivatives, while retaining legal ownership of the pool of assets.

All securitisation transactions entered into as at the reporting date involved the sale of the underlying assets to the securitisation vehicle. The Group has not originated any synthetic securitisations. Nonetheless, the Group calculates appropriate capital charges in respect of the risk assumed, through the provision of liquidity facilities and retained exposures, as per the Basel II securitisation framework.

As at the reporting date the Group has securitised its own assets relating to the home loan and vehicle finance portfolios. The origination of transactions based on other asset classes, such as CPF are considered on an ongoing basis.

Securitisation activities of the Group

Securitisation transactions have been used as a means of raising long-term funding. The Group applies the IRB approach in assessing its securitisation exposures for RC purposes and uses Fitch, Moody's and S&P as external credit assessment institutions (ECAIs).

Apart from originating and sponsoring securitisations, the Group also acts as an investor and a provider of services, liquidity and credit enhancements to a number of securitisation transactions. Investments in securitisation exposures may be made directly or indirectly through the Group's conduit (Abacas).

Six months ended 30 June 2011

Securitisation *(continued)*

The following table provides a breakdown of the Group's role in each transaction it is involved in:

Roles played by the Group in securitisation schemes – Table 12:

	Originator	Sponsor	Investor (Absa)	Investor (Abacas)	Liquidity provider	Services provider	Credit enhancement/subordinated loan
On the Cards Investment II			√				
Home Obligors Mortgage Enhanced Securities (Proprietary) Limited	√	√	√			√	√
Collateralised Auto Receivables Securitisation Programme Series 1 (Proprietary) Limited	√	√				√	√
Vukile Investment Property Securitisation (Proprietary) Limited			√		√		
Prime Realty Obligors Packaged Securities (Proprietary) Limited					√		
Nqaba Finance (Proprietary) Limited					√		
Grayston Conduit (Proprietary) Limited					√		
Ikhaya RMBS 1 Limited				√	√		
Ikhaya RMBS 2 Limited				√	√		
Asset Backed Arbitage Securities (Proprietary) Limited		√	√		√		√
Private Commercial Mortgages (Proprietary) Limited					√		
Private Commercial Mortgages (Proprietary) Limited					√		
Growthpoint 1 (Proprietary) Limited				√			
Growthpoint 2 (Proprietary) Limited			√				
Blue Granite 1 (Proprietary) Limited			√				
Blue Granite 2 (Proprietary) Limited				√			
Blue Granite 3 (Proprietary) Limited			√				
Thekweni Fund 7 (Proprietary) Limited			√				

The following securitisations schemes have been redeemed in the period under review:

» Private Residential Mortgages 2 (Proprietary) Limited.

» Blue Granite 4 (Proprietary) Limited.

Summary of applicable accounting policies

At the start of a securitisation transaction, assets are sold to the securitisation vehicle at par value and no gains or losses are recognised. The transactions are treated as sales (rather than financing) and for financial reporting purposes, the respective vehicles are consolidated at a Group level.

Any retained interest in the securitisation vehicle is valued on the basis of the respective asset's performance. Where the Group acts as service provider, normal impairment policies are applied and retained tranches are ultimately written off once sufficient capital losses accumulate.

Securitisation exposures

The following table provides a breakdown of the total funding raised through securitisation at the reporting date (excluding Abacas), as well as the ECAIs used in the various asset classes.

Summary of applicable accounting policies *(continued)*

Securitisation assets – Table 13:

	30 June 2011 Amount Securitised Rm	30 June 2011 ECAI	30 June 2010 Amount Securitised Rm	30 June 2010 ECAI	December 2010 Amount Securitised Rm	December 2010 ECAI
Mortgage advances	**5 057**		3 342	Moody's, Fitch and S&P	5 057	Moody's, Fitch and S&P
Instalment debtors	**—**		10 400	Moody's	—	Moody's
Total	**5 057**		13 742		5 057	

Mortgage advances remained consistent during the period under review.

Instalment debtors reflected a nil balance as no securitised assets existed at the reporting date.

Absa originated securitisations performed according to expectations and no triggers were breached.

Outstanding underlying asset securitisation balance including Abacas – Table 14:

	30 June 2011 Retail: mortgages Rm	Retail: instalment sales and leasing Rm	Retail: other[1] Rm	Total Rm
On-balance sheet	**4 682**	**—**	**2 317**	**6 999**
Off-balance sheet	**—**	**—**	**—**	**—**
Total IRB exposures	**4 682**	**—**	**2 317**	**6 999**
Of which Notes issued				
Investment grade	**4 019**	**—**	**2 317**	**6 336**
Sub-investment grade[2]	**1 038**	**—**	**—**	**1 038**

	30 June 2010 Retail: mortgages Rm	Retail: instalment sales and leasing Rm	Retail: other[1] Rm	Total Rm
On-balance sheet	3 103	601	5 080	8 784
Off-balance sheet	—	—	—	—
Total IRB exposures	3 103	601	5 080	8 784
Of which Notes issued				
Investment grade	3 017	570	5 080	8 667
Sub-investment grade[2]	325	31	—	356

	31 December 2010 Retail: mortgages Rm	Retail: instalment sales and leasing Rm	Retail: other[1] Rm	Total Rm
On-balance sheet	4 533	—	2 554	7 087
Off-balance sheet	—	—	—	—
Total IRB exposures	4 533	—	2 554	7 087
Of which Notes Issued				
Investment grade	4 019	—	2 554	6 573
Sub-investment grade[2]	1 038	—	—	1 038

Note

[1] *Retail: Other represents Abacas (the Group is sponsor) being a conduit (asset backed commercial paper programme).*

[2] *Sub-investment grade – BBB and below.*

Six months ended 30 June 2011

Summary of applicable accounting policies *(continued)*

Retained or purchased securitisation exposure by underlying asset type – Table 15:

	30 June						31 December		
	2011			2010			2010		
Exposure Type	**Retained Rm**	**Purchased Rm**	**Total Rm**	Retained Rm	Purchased Rm	Total Rm	Retained Rm	Purchased Rm	Total Rm
Corporate /Sovereign/ Banks	**135**	**—**	**135**	300	—	300	240	—	240
Small- and medium-sized entity	**—**	**226**	**226**	—	420	420	—	936	936
Residential Mortgages	**946**	**824**	**1 770**	605	1 432	2 037	946	993	1 939
Other Retail	**—**	**717**	**717**	4	1 113	1 117	—	351	351
Total	**1 081**	**1 767**	**2 848**	909	2 965	3 874	1 186	2 280	3 466

Retained or purchased securitisation exposure by risk weight band – Table 16:

	30 June				31 December	
	2011		2010		2010	
Risk-weight band	**Retained Rm**	**Purchased Rm**	Retained Rm	Purchased Rm	Retained Rm	Purchased Rm
7 – 10 %	**—**	**—**	—	—	—	—
11 – 19 %	**135**	**638**	300	1 723	240	1 149
20 – 49 %	**—**	**1 074**	350	1 096	—	1 076
50 – 75 %	**—**	**—**	—	—	—	—
76 – 99 %	**—**	**—**	—	—	—	—
100%	**—**	**55**	17	146	—	55
250%	**23**	**—**	135	—	23	—
350%	**—**	**—**	—	—	—	—
425%	**—**	**—**	—	—	—	—
650%	**—**	**—**	—	—	—	—
1 250% or Deducted	**923**	**—**	108	—	923	—
	1 081	**1 767**	910	2 965	1 186	2 280

Six months ended 30 June 2011

Summary of applicable accounting policies *(continued)*

Rated securitised exposures in terms of IRB approach – Table 17:

(Excluding deductions and investors interest in respect of schemes with early amortisation features)

	As at 30 June 2011				
	SME[1] receivables Rm	Retail: mortgages Rm	Retail: Instalment sales and leasing Rm	Retail: Other Rm	Total Rm
Total senior exposure rated BBB or better	**1,0**	**36,9**	**0,9**	**7,9**	**46,7**
Total base risk weight exposures rated BBB or better	**3,4**	**99,3**	**12,1**	**76,2**	**191,0**
Total exposure rated BBB or below	**—**	**7,6**	**5,4**	**—**	**13,0**
	4,4	**143,8**	**18,4**	**84,1**	**250,7**

	As at 30 June 2010				
	SME[1] receivables Rm	Retail: mortgages Rm	Retail: Instalment sales and leasing Rm	Retail: Other Rm	Total Rm
Total senior exposure rated BBB or better	3,7	16,7	1,8	8,1	30,3
Total base risk weight exposures rated BBB or better	6,5	35,4	3,1	140,4	185,4
Total exposure rated BBB or below	5,4	48,4	1,2	—	55,0
	15,6	100,5	6,1	148,5	270,7

	As at 31 December 2010				
	SME[1] receivables Rm	Retail: mortgages Rm	Retail: Instalment sales and leasing Rm	Retail: Other Rm	Total Rm
Total senior exposure rated BBB or better	3,1	33,2	—	7,6	43,9
Total base risk weight exposures rated BBB or better	4,8	103,3	11,1	86,5	205,7
Total exposure rated BBB or below	5,4	19,2	—	—	24,6
	13,3	155,7	11,1	94,1	274,2

Note

[1] *Small- and medium-sized enterprises as defined by the regulations.*

Six months ended 30 June 2011

Summary of applicable accounting policies *(continued)*

RWAs and capital deductions at Group level (IRB) – Table 18:

	30 June 2011 RWAs Rm	Required capital[1] Rm	Primary capital and reserve funds Rm	Secondary capital and reserve funds Rm
Retail: instalment sales and leasing	**188**	**18**	—	—
Retail: mortgages	**1 475**	**140**	—	—
Retail: other	**863**	**82**	—	—
SME receivables	**45**	**4**	—	—
	2 571	**244**	—	—

	30 June 2010 RWAs Rm	Required capital[1] Rm	Primary capital and reserve funds Rm	Secondary capital and reserve funds Rm
Retail: instalment sales and leasing	62	6	2	2
Retail: mortgages	1 162	110	104	104
Retail: other	1, 523	145	—	—
SME receivables	160	15	—	—
	2 907	276	106	106

	31 December 2010 RWAs Rm	Required capital[1] Rm	Primary capital and reserve funds Rm	Secondary capital and reserve funds Rm
Retail: instalment sales and leasing	113	11	—	—
Retail: mortgages	1 597	152	—	—
Retail: other	966	92	—	—
SME receivables	137	13	—	—
	2 813	268	—	—

Note

[1]*Required capital is calculated at 9,5%. This excludes the Group specific (Pillar 2b) add on.*

Six months ended 30 June 2011

Basel II and accounting principles

Impairments

Relevant accounting impairment policy versus expected loss regulatory policy

Impairment methods of assessment and use of allowance accounts

IFRS governs reporting practices of banks and, in part, overlap with the requirements of Pillar 3 and regulation 43 of the Banks Act. IFRS 7 prescribes disclosure requirements pertaining to financial instruments for accounting purposes and, as such, is based on a similar set of data used for Pillar 3 reporting purposes. Regulation 43 requires banks to disclose certain accounting definitions and information, in particular, with respect to impairments, past due loans and advances and charge-offs. The Group regularly reconciles the data used for both financial (IFRS) and regulatory (Pillar 3) disclosures.

Impairment methods of assessment and use of allowance accounts

The Group establishes, through charges against profit, an impairment allowance for the incurred loss inherent in the lending book. Under IFRS, impairment allowances are recognised where there is objective evidence of impairment as a result of one or more loss events that have occurred after initial recognition of the asset, and where these events had an impact on the estimated future cash flows of the financial asset or portfolio of financial assets. To determine if a loss event has occurred, historical economic information similar to the current economic climate, overall customer risk profile, payment record and the realisable value of any collateral, are taken into consideration.

Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group, which may include the following loss events:

» Significant financial difficulty of the issuer or borrower.

» A breach of contract, such as a default or delinquency in interest or principal payments.

» The Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider, such as in the case of restructuring.

» It becomes probable that the borrower will enter insolvency or other financial reorganisation.

» The disappearance of an active market for that financial asset as a result of financial difficulties.

» Observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets following the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

› adverse changes in the payment status of borrowers in the group; or

› national or local economic conditions that correlate with defaults on the assets in the group.

Impairments in respect of assets which are individually significant or which have been flagged as being in default, are measured individually, and where a portfolio comprises homogeneous assets and appropriate statistical techniques are available, it is measured collectively. The amount of loss is measured as the difference between the asset carrying amount and the present value of estimated future cash flows (excluding future credit losses), discounted at the financial asset's original effective interest rate. Two key aspects in the cash flow calculation are the valuation of all security and the timing of all asset realisations, after allowing for all collection and recovery costs.

For the purposes of a collective evaluation of impairment, financial assets are grouped, based on similar risk characteristics, taking into account asset type, industry, geographical location, collateral type, past due status and other relevant factors. These characteristics are relevant to estimating future cash flows for such groups of assets, indicating the counterparty's ability to pay all amounts due according to the contractual terms of the assets.

Specific impairment is triggered when a contractual payment is missed. The impairment calculation is based on a roll-rate approach, where the percentage of assets moving from the initial delinquency state to default is derived from statistical probabilities, based on experience. The PD is calculated within a certain outcome period. The outcome period is defined as the timeframe within which assets default. Recovery amounts and contractual interest rates are calculated using a weighted average for the relevant portfolio.

Future cash flows for a group of financial assets which are collectively evaluated for impairment purposes are estimated based on the contractual cash flows of the assets within the group and the historical loss experienced for assets with similar credit risk characteristics to those in the group.

Basel II and accounting principles *(continued)*

The impairment allowance also takes into account the expected severity of loss at default, or the LGD, which is the amount outstanding subsequent to write-offs and is therefore not recoverable.

Recovery varies by product and depends, for example, on the level of security held in relation to each loan as well as the Group's position relative to other claimants. The LGD estimates are based on historical default experience. Historical loss experience data is adjusted to incorporate current economic conditions into the data set, which conditions did not exist at the time of the loss experience and/or to remove the effects of conditions in the previous period that do not currently exist.

Unidentified impairment allowances are raised when observable data indicates a measurable decrease in the estimated future cash flows from a group of financial assets since its original recognition, even though the decrease cannot yet be identified for the individual assets in the group. The unidentified impairment calculation is based on the asset's probability of moving from the performing portfolio to the defaulted portfolio as a result of a risk condition which has already occurred, but will only be identifiable at a borrower level at a future date.

An emergence period concept is applied to ensure that only impairments which exist at the reporting date are captured. The emergence period is defined as the time lapse between the occurrence of a trigger event (portfolio impairment) and the impairment being identified at an individual account level (specific impairment). The emergence periods, based on actual experience, vary across businesses and are reviewed annually. The PD for each exposure class is based on historical default experience, scaled for the emergence period relevant to the exposure class. This PD is then applied to the total population on which no specific impairments have been recognised. Where total EL of all credit risk assets exceeds total impairments, the difference is deducted from eligible capital. In the instance that total impairments exceed total EL, the difference is added to eligible capital, subject to a maximum of 0,6% of total RWAs.

Differences in impairment calculations across wholesale and retail operations

Corporate accounts deemed to contain heightened levels of risk are recorded on graded problem loan lists, known as either watch lists or early warning lists (EWL). These EWL's are updated monthly and circulated to the relevant risk control points. Once listing has occurred, exposure is carefully monitored and, where possible, exposure reductions are effected. The lists are graded in line with perceived severity of the risk attached to the lending. Businesses with exposure to corporate customers are escalated through three categories of increasing concern. When an account becomes impaired, it would normally but not necessarily, have passed through all three categories, reflective of the need for increased monitoring and control. Where a borrower's financial health presents grounds for concern, it is immediately placed into the appropriate category. All borrowers are subject to a full review of all facilities, on at least an annual basis. Interim reviews may be performed if necessary.

Within the Retail Banking portfolios, which tend to comprise homogeneous assets, statistical techniques more readily allow impairment to be monitored on a portfolio basis. This is consistent with the Group policy of raising an impairment allowance as soon as objective evidence of impairment is identified following one or more loss events that have occurred, subsequent to initial recognition. Models in use are based on customers' personal and financial performance information over recent periods, which serve as a predictor for future performance. The models' output are regularly reviewed against actual performance and, where necessary, amended to optimise their effectiveness.

Six months ended 30 June 2011

Differences in impairment calculations across wholesale and retail operations

(continued)

Reconciliation of total impairments (identified and unidentified) – Table 19:

	30 June 2011						
Impairment of loans and advances to customers	**Opening balance Rm**	**Net present value unwind on non-performing book Rm**	**Exchange differences Rm**	**Amounts written off Rm**	**Impairment raised identified Rm**	**Impairment raised unidentified Rm**	**Closing balance Rm**
Retail Banking	**10 789**	**(519)**	**—**	**(2 417)**	**2 680**	**(46)**	**10 487**
Absa Business Bank	**2 641**	**(70)**	**6**	**(649)**	**584**	**(4)**	**2 509**
Absa Capital	**471**	**(3)**	**1**	**(3)**	**45**	**(5)**	**506**
Other	**—**	**3**	**—**	**3**	**—**	**—**	**—**
Total	**13 902**	**(589)**	**7**	**(3 073)**	**3 310**	**(54)**	**13 502**

	30 June[1] 2010						
Impairment of loans and advances to customers	Opening[2] balance Rm	Net present value unwind on non-performing book Rm	Exchange differences Rm	Amounts written off Rm	Impairment raised identified Rm	Impairment raised unidentified Rm	Closing balance Rm
Retail Banking	10 130	(333)	—	(1 873)	3 295	(97)	11 123
Absa Business Bank	2 470	(27)	—	(434)	672	19	2 700
Absa Capital	547	(4)	(1)	(118)	76	—	500
Other	11	1	—	(2)	—	—	10
Total	13 158	(363)	(1)	(2 427)	4 043	(78)	14 333

	31 December[1] 2010						
Impairment of loans and advances to customers	Opening[2] balance Rm	Net present value unwind on non-performing book Rm	Exchange differences Rm	Amounts written off Rm	Impairment raised identified Rm	Impairment raised unidentified Rm	Closing balance Rm
Retail Banking	10 130	(671)	—	(3 998)	5 471	(143)	10 789
Absa Business Bank	2 470	(87)	(1)	(1 036)	1 324	(29)	2 641
Absa Capital	547	(8)	(2)	(166)	121	(20)	471
Other	11	2	—	(19)	3	3	—
Total	13 158	(764)	(3)	(5 219)	6 919	(190)	13 902

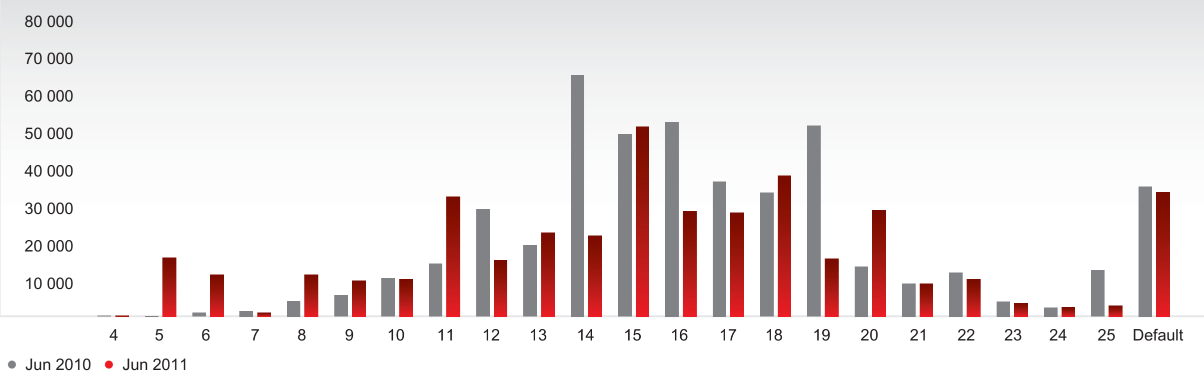
Note

[1]*Prior period numbers were impacted by restatements.*

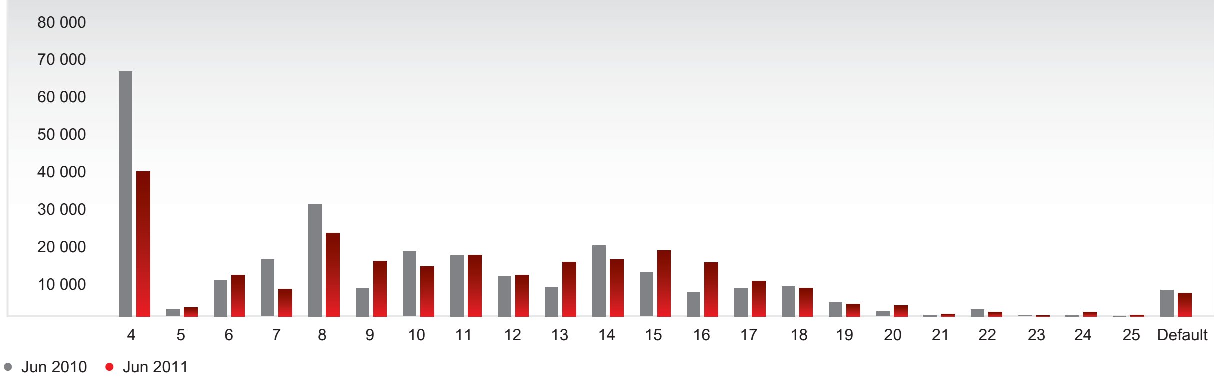
[2]*The opening balance is as at 1 January.*

Differences in impairment calculations across wholesale and retail operations
(continued)

Exposure migration across PD bands – retail operations (Rm)



Exposure migration across PD bands – wholesale operations (Rm)



Credit rating downgrade

The Group enters into derivative contracts with rated and unrated counterparties. To mitigate counterparty credit risk, the Group sets credit protection terms, such as limits on the amount of unsecured credit exposure it will accept, collateralisation in the event of a MTM credit exposure exceeding the current amount and collateralisation and/or termination of a contract when certain credit events occur, including, but not limited to, a downgrade of the counterparty's public credit rating.

Certain counterparties may require the Group to provide similar credit protection terms, to which it may agree from time to time, 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 reciprocal basis.

The impact on the Group of the additional amount of collateral required in the event of a credit downgrade is determined by the negative MTM value on derivative contracts. Where the impact on the Group's liquidity is deemed to be material, the potential exposure is taken into account in model stress testing. However, generally, the extent of legal commitments resulting in additional collateral requirements caused by a rating downgrade is not material and would not have an adverse effect on the Group's financial position.

As at the reporting date, the additional collateral required to be posted for a one-notch downgrade was R8,3 million and for a two-notch downgrade was R42,1 million.

Focus going forward

Wholesale Credit Risk

The Group expects to see further improvement in wholesale impairment levels. It will remain focused on reducing concentrations in perceived higher risk sectors, enhancing the risk control framework and further embedding the AIRB principles in the business.

Six months ended 30 June 2011

Focus going forward *(continued)*

Retail Credit Risk

The Group will continue to focus on value and balance sheet optimisation. The aim is to increase portfolio growth through defining low risk pockets/products and improving decision making processes by continuously assessing market conditions and understanding the impact of economic shifts on the various portfolios. The Group will therefore remain focused on the quality and profitability of new business written.

A key component in the 2011 strategic focus for retail credit risk is the debt counselling and legal portfolios with emphasis on mortgages.

Securitisation

Focus will be placed on reducing the on-statement of financial position securitisation exposures and winding down Abacas through the natural amortisation of the underlying notes.

Regulatory disclosures for credit risk for 2011

Gross exposure per asset class and EAD per approach under Basel II – Table 20:

	30 June 2011						30 June 2010	31 December 2010
Standardised approach	**Utilised (on balance sheet exposure) Rm**	**Off balance sheet exposure Rm**	**Repurchase and resale agreements Rm**	**Derivative instruments Rm**	**Total credit exposure Rm**	**EAD Rm**	EAD Rm	EAD Rm
Corporate exposure	**3 499**	**1 796**	**—**	**—**	**5 295**	**5 295**	5 014	4 895
SME Corporate exposure	3 499	1 796	—	—	5 295	5 295	5 014	4 895
Banks	**1 736**	**—**	**—**	**—**	**1 736**	**1 736**	571	1 514
Public sector entities	**168**	**—**	**—**	**—**	**168**	**168**	508	149
Local government and municipalities	**—**	**—**	**—**	**—**	**—**	**—**	—	—
Retail	**1 255**	**—**	**—**	**—**	**1 255**	**1 255**	1 800	1 362
Sovereign	**52 641**	**—**	**—**	**—**	**52 641**	**52 641**	37 803	49 567
Securities firms	**—**	**—**	**—**	**—**	**—**	**—**	—	—
Total	**59 299**	**1 796**	**—**	**—**	**61 095**	**61 095**	45 696	57 487

Six months ended 30 June 2011

Regulatory disclosures for credit risk for 2011 *(continued)*

Gross exposure per asset class and EAD per approach under Basel II – Table 20:
(continued)

FIRB approach	30 June 2011 Utilised (on balance sheet exposure) Rm	Off balance sheet exposure Rm	Re-purchase and resale agreement Rm	OTC Derivative instruments Rm	Total credit exposure Rm	EAD Rm	30 June 2010 EAD Rm	31 December 2010 EAD Rm
Corporate	148 196	93 515	721	5 150	247 581	179 213	173 605	185 424
Large Corporate	118 216	83 715	721	5 060	207 712	145 553	151 364	159 542
SME Corporate	24 167	7 502	—	—	31 669	27 628	22 241	21 211
Specialised lending – income producing real estate[1]	1 862	801	—	—	2 662	1 869	—	2 500
Specialised lending – project finance[1]	3 951	1 497	—	90	5 538	4 163	—	2 171
Banks	18 144	27 137	12 449	27 912	85 642	35 684	53 916	31 427
Local government and municipalities	5 828	8 480	—	—	14 308	7 851	668	7 325
Public sector entities	1 895	10 886	64	1 650	14 494	7 993	12 736	14 322
Retail	—	—	—	—	—	—	—	14
– SME retail	—	—	—	—	—	—	—	14
Sovereign	1 762	121	450	228	2 561	866	1 094	1 026
Securities firms	57	9 373	1 964	530	11 925	727	8 382	1 903
Total	175 882	149 512	15 648	35 470	376 511	232 334	250 401	241 441

AIRB approach	30 June 2011 Utilised (on balance sheet exposure) Rm	Off balance sheet exposure Rm	Re-purchase and resale agreement Rm	OTC Derivative instruments Rm	Total credit exposure Rm	EAD Rm	30 June 2010 EAD Rm	31 December 2010 EAD Rm
Retail								
– Mortgages	250 626	50 959	—	—	301 585	263 837	292 113	272 267
– SME retail	16 282	10 822	—	—	27 104	21 219	28 216	22 600
– Revolving credit	24 796	26 032	—	—	50 827	45 375	48 741	43 646
– Other	68 914	3 404	—	—	72 317	68 364	88 855	72 378
Total	360 617	91 217	—	—	451 833	398 795	457 925	410 891

Note

[1] *Enhancements to December 2010 disclosures. Comparatives for June 2010 are not available.*

Six months ended 30 June 2011

Regulatory disclosures for credit risk for 2011 *(continued)*

EAD exposure by geography – Table 21[1]:

As at 30 June 2011

	South Africa Rm	Europe Rm	Other African Countries Rm	North America Rm	Other Rm	Asia Rm	Total Rm
Standardised approach	**50 999**	**—**	**10 096**	**—**	**—**	**—**	**61 095**
Internal Ratings Based	**597 494**	**26 179**	**2 474**	**3 757**	**1 156**	**69**	**631 129**
– FIRB	**198 699**	**26 179**	**2 474**	**3 757**	**1 156**	**69**	**232 334**
– AIRB	**398 795**	**—**	**—**	**—**	**—**	**—**	**398 795**
Total	**648 493**	**26 179**	**12 570**	**3 757**	**1 156**	**69**	**692 224**

As at 30 June 2010

	South Africa Rm	Europe Rm	Other African Countries Rm	Other Rm	Total Rm
Standardised approach	35 847		9 849	—	45 696
Internal Ratings Based	705 302	457	2 443	576	708 778
Total	741 149	457	12 292	576	754 474

As at 31 December 2010

	South Africa Rm	Europe Rm	Other African Countries Rm	North America Rm	Other Rm	Asia Rm	Total Rm
Standardised approach	48 215	—	9 272	—	—		57 487
Internal Ratings Based	622 451	22 640	3 146	3 455	615	25	652 332
– FIRB	410 891	—	—	—	—	—	410 891
– AIRB	211 560	22 640	3 146	3 455	615	25	241 441
Total	670 666	22 640	12 418	3 455	615	25	709 819

Note

[1]Enhancements to classifications were completed for December 2010 and subsequent disclosures.

Six months ended 30 June 2011

Regulatory disclosures for credit risk for 2011 *(continued)*

PDs, EADs and LGDs by risk grade under the FIRB approach as at 30 June – Table 22:

	30 June 2010	30 June 2011										
		Corporate					SME Corporate				Specialised lending –	
Risk Grade	Average PD %	Average PD %	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %
Non-default	0,76	6,31	43,06	110,21	790	141 337	6,29	88,23	276	25 588	25,37	51,86
1	—	—	—	—	—	—	—	—	—	—	—	—
2	—	—	—	—	—	—	—	—	—	—	—	—
3	—	—	—	—	—	—	—	—	—	—	—	—
4	0,03	0,03	44,71	14,40	1	8 691	0,03	12,50	—	—	0,00	0,00
5	0,04	0,04	45,00	100,87	—	2 020	0,04	13,69	—	1	0,00	0,00
6	0,06	0,05	39,70	18,52	2	8 746	0,06	14,84	—	81	36,48	17,13
7	0,08	0,08	44,25	25,77	2	6 339	0,09	19,33	—	2	36,74	17,30
8	0,11	0,11	41,99	30,45	5	9 157	0,13	23,20	—	67	35,36	23,27
9	0,16	0,16	41,30	36,53	8	11 188	0,18	33,27	—	102	36,42	29,50
10	0,22	0,22	43,99	45,30	9	8 965	0,23	39,82	2	1 765	38,67	38,77
11	0,32	0,32	42,92	53,08	18	13 370	0,32	46,00	3	2 395	36,20	43,63
12	0,45	0,45	43,53	64,73	16	7 796	0,45	51,45	5	2 746	38,58	52,50
13	0,62	0,63	44,12	75,98	31	10 813	0,63	62,33	6	2 038	36,89	231,35
14	0,92	0,91	42,37	84,07	44	11 274	0,91	69,92	10	2 578	37,05	66,95
15	1,26	1,26	43,04	95,58	75	13 734	1,23	75,48	17	3 316	38,63	81,86
16	1,90	1,82	43,87	109,06	92	11 416	1,84	89,39	18	2 147	39,88	83,55
17	2,57	2,53	43,78	118,88	78	6 910	2,55	96,17	28	2 529	35,00	92,54
18	3,54	3,64	44,01	132,12	74	4 706	3,69	103,16	37	2 363	37,15	94,40
19	5,00	5,23	44,00	148,77	49	2 111	5,12	132,57	26	1 157	0,00	0,00
20	7,01	7,00	43,62	164,78	52	1 730	7,09	126,70	34	1 142	36,67	109,62
21	10,01	9,98	43,62	185,55	17	397	10,23	155,48	11	249	0,00	0,00
22	13,86	14,03	40,97	216,19	29	492	13,89	160,54	33	569	38,40	158,60
23	20,62	20,62	42,10	246,70	6	74	20,66	197,52	13	141	0,00	0,00
24	29,53	29,82	39,49	218,29	135	1 143	29,23	209,99	8	62	0,00	0,00
25	37,17	39,88	44,89	239,00	48	266	39,79	207,80	25	138	0,00	0,00
Default	100,00	100,00	27,62	172,41	1 112	4 215	100,00	69,39	508	2 040	0,00	0,00
Total	3,36	3,82	42,60	72,62	1 903	145 553	9,70	79,76	784	27 628	38,06	78,69

Credit risk

Six months ended 30 June 2011

30 June
2011

income producing real estate		Specialised lending – project finance				Public sector entities				Local governments	
Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %
13	1 869	16,59	26,51	19	4 163	25,50	40,75	6	7 993	36,82	70,92
—	—	—	—	—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—	—	—	—	—
—	—	50,00	16,81	—	—	45,00	14,44	—	334	45,00	15,39
—	—	0,00	0,00	—	—	0,00	0,00	—	—	45,00	15,46
0	17	0,00	0,00	—	—	0,00	0,00	—	—	45,00	19,65
0	4	0,00	0,00	—	—	45,00	27,23	—	825	45,00	24,03
0	17	0,00	0,00	—	—	39,60	26,86	2	3,855	45,00	32,48
0	21	45,00	39,04	1	710	26,33	21,56	1	2,421	45,00	37,76
0	200	0,00	0,00	—	—	45,00	47,20	—	49	44,98	48,16
0	31	45,00	52,49	—	104	45,00	61,06	—	13	45,00	53,03
1	389	45,00	65,55	—	6	45,00	65,26	—	20	45,00	66,58
0	79	45,00	75,15	4	1 511	45,00	76,43	—	15	45,00	74,33
1	277	45,00	87,86	4	995	45,00	86,28	—	42	45,00	84,29
3	568	0,00	0,00	—	—	45,00	103,84	—	34	45,00	99,60
0	10	45,00	109,33	3	400	45,00	106,45	3	381	45,00	110,44
0	—	0,00	0,00	—	—	45,00	122,71	—	—	45,00	121,91
1	95	45,00	137,02	7	437	45,00	137,17	—	4	45,00	133,32
—	—	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00
1	51	0,00	0,00	—	—	0,00	0,00	—	—	45,00	163,72
—	—	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00
6	110	0,00	0,00	—	—	0,00	0,00	—	—	45,00	219,82
—	—	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00
—	—	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00
—	—	0,00	0,00	—	—	0,00	0,00	—	—	45,00	240,32
—	—	0,00	0,00	—	—	0,00	0,00	—	—	45,00	0,00
13	1 869	45,00	81,23	19	4 163	36,74	29,63	6	7 993	45,00	31,16

Six months ended 30 June 2011

and municipalities		Sovereign				Banks				Securities firms				Total				30 June 2010
Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	Average LGD %	Average risk weight %	Expected loss Rm	EAD Rm	Average LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	E AD Rm
5	7 851	12,40	25,41	4	866	36,34	66,58	8	35 684	20,51	30,22	—	727	42,85	56,90	1 125	226 079	243 228
—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
—	25	2,76	0,89	—	510	40,24	12,91	4	29 084	45,00	14,42	—	108	40,81	13,10	5	38 752	65 497
—	5	0,00	0,00	—	—	45,00	15,89	—	410	0,00	0,00	—	—	45,00	13,01	—	2 436	1989
—	2 164	0,00	0,00	—	—	45,00	21,44	—	4	0,00	0,00	—	—	40,71	10,15	3	11 012	9 620
—	151	45,00	27,73	—	4	45,00	27,70	—	1	45,00	24,44	—	1	44,35	23,85	3	7 327	15 205
3	4 780	45,00	30,63	—	327	39,37	26,41	2	3 906	40,58	30,56	—	174	41,78	21,54	11	22 284	29 970
—	42	0,00	0,00	—	—	45,00	39,87	—	287	45,00	38,26	—	2	39,12	22,89	10	14 773	7 658
—	435	45,00	0,00	—	—	44,92	45,26	2	1 872	45,00	45,34	—	18	44,05	28,26	13	13 304	17 366
—	67	0,00	0,00	—	—	45,00	55,13	—	75	5,56	6,85	—	338	42,41	22,94	22	16 393	16 306
—	30	0,00	0,00	—	—	45,00	67,62	—	2	45,00	65,48	—	32	43,14	35,14	22	11 021	10 765
—	98	0,00	0,00	—	—	45,00	72,18	—	—	0,00	0,00	—	—	44,21	39,29	41	14 554	7 983
—	7	0,00	0,00	—	—	45,00	90,96	—	8	45,00	91,32	—	44	42,58	47,91	59	15 225	18 990
—	3	0,00	0,00	—	—	45,00	99,90	—	2	45,00	85,47	—	—	42,63	45,25	94	17 657	11 731
—	4	0,00	0,00	—	—	45,00	112,34	—	—	45,00	116,68	—	9	43,99	60,15	115	14 367	6 476
—	26	45,00	122,35	—	—	45,00	122,96	—	8	0,00	0,00	—	—	43,82	63,12	106	9 473	7 534
—	3	45,00	136,90	—	—	45,00	135,74	—	17	0,00	0,00	—	—	43,64	75,47	121	7 625	8 039
—	—	0,00	0,00	—	—	45,00	150,95	—	4	0,00	0,00	—	—	44,03	71,27	75	3 272	3 811
—	—	0,00	0,00	—	—	45,00	173,28	—	—	45,00	146,13	—	1	42,98	72,81	88	2 924	1 314
—	—	0,00	0,00	—	—	45,00	194,20	—	4	0,00	0,00	—	—	44,13	84,70	29	650	480
—	2	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00	—	—	40,78	113,50	67	1 173	1 897
—	—	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00	—	—	43,79	112,30	19	215	246
—	—	0,00	0,00	—	—	0,00	0,00	—	—	0,00	0,00	—	—	39,77	154,30	143	1 205	328
2	9	45,00	240,60	4	24	0,00	0,00	—	—	0,00	0,00	—	—	44,93	120,72	78	437	23
—	—	0,00	0,00	—	—	0,00	0,00	—	—	45,00	562,50	—	—	27,64	46,85	1 620	6 255	7 173
5	7 851	20,12	18,94	4	866	40,50	16,57	8	35 684	25,61	24,13	—	727	41,97	45,45	2 744	232 334	250 401

Six months ended 30 June 2011

Regulatory disclosures for credit risk for 2011 *(continued)*

PDs, EADs and LGDs by risk grade under the AIRB approach as at 30 June – Table 23:

	30 June 2010	30 June 2011				
		Mortgages				
Risk Grade	Average PD %	Average PD %	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm
Non-default	4,16	6,33	12,44	31,24	955	238 498
1	—	—	—	—	—	—
2	—	—	—	—	—	—
3	—	—	—	—	—	—
4	0,03	0,03	0,00	0,00	—	—
5	0,05	0,04	11,01	1,19	—	11 492
6	0,06	0,05	11,40	1,63	1	10 934
7	0,08	0,08	0,00	0,00	—	—
8	0,11	0,11	11,78	3,08	—	1 108
9	0,16	0,16	13,07	4,60	1	5 488
10	0,23	0,23	13,76	6,22	3	9 476
11	0,32	0,32	12,81	7,21	12	29 640
12	0,45	0,45	12,59	9,05	5	9 040
13	0,65	0,66	13,73	13,03	18	19 902
14	0,99	0,90	13,78	16,03	16	12 703
15	1,27	1,24	13,91	20,12	66	37 861
16	1,82	1,80	13,48	24,73	41	16 943
17	2,62	2,55	14,15	32,54	48	13 161
18	3,62	3,80	14,01	38,35	65	13 081
19	5,18	5,21	14,14	47,12	91	12 578
20	7,13	7,45	14,55	57,90	236	21 918
21	10,70	9,49	14,98	66,20	81	5 788
22	13,84	14,90	14,66	76,24	49	2 284
23	20,32	21,03	15,70	89,03	77	2 295
24	29,02	28,99	14,54	84,73	55	1 302
25	42,07	39,78	15,63	88,25	90	1 505
Default	100,00	100,00	17,31	0,00	4 790	25 338
Total	11,44	11,27	14,55	22,19	5 747	263 837

Credit risk

Six months ended 30 June 2011

30 June 2011							
SME Retail				Retail revolving credit			
LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm
53,88	52,55	464	20 261	76,07	69,33	879	42 957
—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—
29,58	3,04	0	2	0,00	0,00	—	—
87,64	2,19	0	710	88,67	2,15	1	2 962
35,81	5,12	0	199	88,71	3,79	—	10
57,51	5,20	0	1	88,64	4,02	—	293
80,17	7,77	0	15	69,10	4,51	7	8 628
45,30	13,61	0	16	67,40	5,83	4	3 954
43,85	18,80	0	129	88,64	9,42	1	371
64,48	19,80	1	559	83,54	14,17	2	825
41,51	24,41	4	2 056	83,15	16,98	—	91
60,29	31,92	3	815	88,61	23,25	2	331
42,18	38,15	6	1 576	74,77	25,88	26	3 938
56,74	42,72	27	3 849	80,84	37,44	14	1 376
55,82	52,12	14	1 359	75,90	48,24	20	1 529
53,87	59,93	24	1 691	77,75	59,94	30	1 659
49,35	62,68	37	2 022	72,73	77,35	360	12 109
57,56	79,59	25	834	75,71	92,15	65	1 723
51,97	82,92	42	1 072	76,63	117,69	72	1 308
61,77	103,29	31	522	78,54	147,78	50	624
47,84	93,85	130	1 946	78,15	175,38	67	598
56,75	134,85	17	147	78,58	206,47	48	305
73,11	187,37	18	92	79,05	229,92	27	126
32,31	86,84	85	649	78,42	222,77	83	197
39,28	211,67	242	958	74,54	44,08	1 565	2 418
51,93	61,46	706	21 219	74,45	46,49	2 444	45 375

Credit risk

Six months ended 30 June 2011

Retail – other				Total				30 June 2010
LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	LGD %	Exposure weighted average risk weight %	Expected loss Rm	EAD Rm	EAD Rm
51,56	58,36	1 607	63 831	32,13	52,66	3 910	365 548	423 128
—	—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—	—
0,00	0,00	—	—	29,58	11,78	0	2	226
62,73	7,80	—	590	31,00	12,27	2	15 754	157
0,00	0,00	—	—	11,90	6,75	1	11 143	1 013
58,60	12,11	—	775	66,83	17,80	1	1 069	1 505
50,37	14,11	1	1 400	61,07	13,67	8	11 151	4 181
74,06	26,61	—	127	36,34	21,22	6	9 585	5 716
73,78	38,13	—	6	16,97	24,32	4	9 982	10 222
68,45	36,98	2	984	17,24	19,82	18	32 008	14 106
40,51	28,63	7	3 888	24,16	29,36	17	15 075	28 673
66,41	52,43	5	1 298	19,60	34,99	28	22 346	19 060
47,43	46,05	15	3 445	32,29	40,44	62	21 662	64 531
59,32	65,72	57	7 703	25,85	38,66	163	50 789	48 709
44,74	56,54	69	8 361	28,18	54,95	143	28 192	51 991
42,76	57,97	121	11 177	31,94	60,92	224	27 688	36 093
61,28	87,66	244	10 392	47,88	72,37	706	37 604	33 069
64,30	78,50	29	296	26,42	67,84	211	15 431	50 967
51,95	81,21	159	4 128	24,25	70,51	511	28 426	13 402
50,90	84,62	87	1 803	29,73	83,62	249	8 737	8 858
57,37	114,27	452	5 114	46,94	107,32	698	9 942	11 790
49,13	111,70	89	863	30,68	111,01	230	3 610	4 018
61,54	155,78	173	969	38,27	125,75	274	2 489	2 457
48,61	127,16	97	512	29,62	133,10	354	2 863	12 385
68,41	148,48	2 345	4 533	34,44	38,21	8 942	33 247	34 796
53,79	73,93	3 952	68 364	30,08	41,06	12 852	398 795	457 924

Regulatory disclosures for credit risk for 2011 *(continued)*

Residual contractual maturity of exposures – Table 24:

	30 June 2011 Exposure at default				
Residual contractual maturity of exposures	**Current to 6 months**	**6 Months to 1 year**	**1 year to 5 years**	**More than 5 years**	**Total**
Banks	17 575	2 862	7 257	7 990	35 684
Corporate Exposure	75 795	12 966	24 262	66 190	179 212
Corporate	66 033	12 000	22 942	44 578	145 553
SME Corporate	9 755	805	—	17 068	27 628
Specialised lending – income producing real estate	—	95	—	1 773	1 869
Specialised lending – project finance	6	65	1 320	2 771	4 163
Local governments and municipalities	2 278	1 075	1 204	3 293	7 851
Public sector entities	3 753	991	48	3 201	7 993
Retail	14 153	420	—	384 223	398 795
Mortgages	—	—	—	263 837	263 837
Retail – other	280	—	—	68 084	68 364
Retail revolving credit	9 266	—	—	36 109	45 375
SME Retail	4 607	420	—	16 193	21 219
Securities firms	150	43	458	77	727
Sovereign	184	113	20	549	866
	113 887	18 469	33 249	465 523	631 129
Standardised exposures					61 095
					692 224

	31 December 2010 Exposure at default				
Residual contractual maturity of exposures	Current to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years	Total
Banks	13 868	917	9 744	6 898	31 427
Corporate Exposure	63 083	11 661	43 483	67 197	185 424
Corporate	53 129	11 018	42 546	52 849	159 542
SME Corporate	9 520	510	1	11 180	21 211
Specialised lending – income producing real estate	188	127	291	1 894	2 500
Specialised lending – project finance	246	6	645	1 274	2 171
Local governments and municipalities	2 621	1 108	424	3 172	7 325
Public sector entities	1 331	2 041	6 336	4 614	14 322
Retail	47 768	542	—	362 595	410 905
Mortgages	128	—	—	272 139	272 267
Retail – other	6 036	—	—	66 342	72 378
Retail revolving credit	36 487	—	—	7 159	43 646
SME Retail	5 117	542	—	16 955	22 614
Securities firms	349	—	1 554	—	1 903
Sovereign	283	—	133	610	1 026
	129 303	16 269	61 674	445 086	652 332
Standardised exposures					57 487
					709 819

Regulatory disclosures for credit risk for 2011 *(continued)*

RWAs and required capital – Table 25:

FIRB and AIRB[1]	As at 30 June 2011 RWAs[2]	As at 30 June 2011 Required capital[3]	As at 31 December 2010 RWAs[2]	As at 31 December 2010 Required capital[3]
Banks	**5 913**	**562**	5 569	529
Corporate Exposure	**132 584**	**12 595**	125 786	11 950
Corporate	**105 696**	**10 041**	106 812	10 147
SME Corporate	**22 036**	**2 093**	15 413	1 464
Specialised lending – income producing real estate	**1 471**	**140**	1 513	144
Specialised lending – project finance	**3 381**	**321**	2 048	195
Local governments and municipalities	**2 447**	**232**	3 094	294
Public sector entities	**2 368**	**225**	6 019	572
Retail	**145 791**	**13 850**	167 492	15 912
Mortgages	**60 017**	**5 701**	81 900	7 781
SME Retail	**13 087**	**1 243**	52 356	4 974
Retail revolving credit	**21 281**	**2 022**	21 128	2 007
Retail – other	**51 406**	**4 884**	12 108	1 150
Securities firms	**175**	**17**	287	27
Sovereign	**164**	**16**	173	16
	289 442	**27 497**	308 420	29 300
Standardised approach	**9 409**	**894**	8 547	812
	298 851	**28 391**	316 967	30 112

Notes

[1]*Comparatives for June 2010 are not available.*

[2]*RWAs and required capital include securitisation balances. Refer to table 18 for a more detailed analysis of securitisation information.*

[3]*Required capital is calculated at 9,5% of RWAs.*

Credit risk mitigation (CRM) – Table 26:

IRB approach	June 2011 Original credit and counter-party exposure Rm	June 2011 Effects of netting agree-ments Rm	June 2011 Ex-posure after netting and credit risk Rm	June 2011 Eligible financial colla-teral Rm	June 2011 Other eligible IRB colla teral Rm	June 2011 Mitiga-tion af-fecting LGD esti-mates Rm	30 June 2010 Miti-gation affecting LGD esti-mates Rm	31 December 2010 Miti-gation affecting LGD esti-mates Rm
Asset class								
Banks	**85 642**	**21 275**	**64 367**	**3 898**	**1**	**3 899**	25 818	886
Corporate Exposure	**247 581**	**2 861**	**244 721**	**2 057**	**85 027**	**87 083**	98 935	103 222
Corporate	**207 712**	**2 860**	**204 852**	**2 057**	**63 803**	**65 859**	80 104	81 187
SME Corporate	**31 669**	**—**	**31 669**	**—**	**18 685**	**18 685**	18 831	18 096
Specialised lending – income producing real estate	**2 662**	**—**	**2 662**	**—**	**2 539**	**2 539**	—	3 939
Specialised lending – project finance	**5 538**	**1**	**5 538**	**—**	**—**	**—**	—	—
Local governments and municipalities	**14 308**	**—**	**14 308**	**—**	**101**	**101**	—	4
Public sector entities	**14 494**	**94**	**14 400**	**1 464**	**215**	**1 680**	590	1 003
Retail	**451 833**	**—**	**451 833**	**53 942**	**559 748**	**613 690**	604 604	627 530
Mortgages	**301 585**	**—**	**301 585**	**—**	**543 840**	**543 840**	546 368	555 650
SME Retail	**27 104**	**—**	**27 104**	**—**	**15 908**	**15 908**	—	49 168
Retail revolving credit	**50 827**	**—**	**50 827**	**—**	**—**	**—**	—	—
Retail – other	**72 317**	**—**	**72 317**	**53 942**	**—**	**53 942**	58 236	22 712
Securities firms	**11 925**	**187**	**11 738**	**334**	**—**	**334**	993	—
Sovereign	**2 561**	**30**	**2 531**	**479**	**9**	**487**	1 004	492
Total	**828 344**	**24 447**	**803 898**	**62 174**	**645 101**	**707 274**	731 944	733 137

Market risk

Six months ended 30 June 2011

Highlights

- » *Traded market risk remained low. Risk and revenue reflect continued challenging markets and client volumes and the current low interest rate environment, but were managed to deliver favourable risk-adjusted returns.*
- » *Interest rate risk in the banking book managed to low levels, while efficiently maintaining the structural hedging programme.*
- » *Interest rate risk management hedging activities positively impacted on the net interest margin, off-setting the negative endowment effects during the period under review.*
- » *Selected assets in the equity investment portfolio were exited towards creating a leaner portfolio, while remaining selective on new investments.*

Key performance indicators

	30 June		31 December
	2011	2010	2010
Average traded market risk DVaR (Rm)	**25,80**	27,03	27,85
Traded market risk RC (at 8% of RWAs) (Rm)	**788**	755	721
Banking book AEaR for 2% interest rate shock (% of Group NII)	**<5%**	<5%	<5%
Equity investments in the banking book RWAs (Rm)	**24 136**	28 814	25 911

Introduction

Market risk is the risk that the Group's earnings or capital, or its ability to meet business objectives, will be adversely affected by changes in the level or volatility of market rates or prices such as interest rates, foreign exchange rates, equity prices, commodity prices and credit spreads. Market risk mainly arises from trading activities and equity investments. The Group is also exposed to market risk through non-traded interest rate risk in its banking book.

Strategy

The Group's market risk management objectives are:

- » understanding and controlling market risk through robust measurement, controls and oversight;
- » facilitating business growth within a controlled and transparent risk management framework;
- » ensuring traded market risk resides mainly in Absa Capital; and
- » ensuring a higher degree of interest rate mismatch margin stability and lower interest rate risk over an interest rate cycle in the banking book.

Governance

Market risk is managed under the Group's market risk policy framework, as approved by the GRCMC, and in accordance with PRP requirements. The board approves the market risk appetite for trading and non-trading activities, as recommended by the GRCMC. A market risk limits framework is set within the context of the approved market risk appetite. The Group Chief Risk Officer appoints a Principal Risk Owner (PRO) responsible for implementing and managing the market risk policy framework.

The head of each BU, assisted by an independent business risk management team, is accountable for all market risks associated with the activities of each BU. Each BU is responsible for the identification, measurement, management, control and reporting of market risks as outlined in the market risk policy framework. Market risk oversight and challenge is provided as set out in the governance structure below:

Market risk governance structure

	Committees			Teams
Board level	GRCMC			
Group level	Market Risk Committee (MRC)	Group Alco	Group Investment Committee (GIC)	» Chief Risk Officer (CRO) » Principal Risk Owner (PRO) » Group market risk team
Business unit level	Trading Risk Committee (TRC)	Business and cluster Alcos	Business Investment Committees	Independent business risk management teams
	Traded Position Risk Review forum (TPRR)			
	Absa Capital Valuation Governance forum			

All market risks are reported to the GRCMC on a quarterly basis, along with a monthly highlights dashboard. The MRC meets monthly to review, approve and make recommendations concerning the market risk profile including risk appetite, policies, limits and utilisation. The Group Alco meets monthly to review market risk capital requirements and performance against balance sheet management objectives.

Absa Capital's market risk is managed by the Absa Capital market risk team and reviewed monthly by the TRC, with a weekly traded positions risk review. The Absa Capital product control team's responsibilities include valuation control, independent price testing and bid-offer testing, the results of which are reviewed monthly by the Absa Capital Valuation Governance Forum. Absa Capital's asset and liability risks are monitored monthly by the Absa Capital Alco.

The Group Treasury and the African subsidiaries' treasuries manage non-traded asset and liability market risks. Each of the African subsidiaries has its own Alco which monitors asset and liability market risks, and reports into the Africa Alco and Group Alco. The Group and Absa Capital market risk teams maintain regular contact with the African subsidiaries' treasuries and risk teams and conduct on-site supervision visits to oversee a comprehensive risk management and reporting framework.

Equity investments are managed under the new ventures and asset policy framework, which requires a specific sign-off procedure to be followed prior to the approval of an investment, and requires regular post-implementation performance reviews. The GIC considers, approves and monitors all investments or divestments of the Group in accordance with its terms of reference, the new ventures and asset policy framework, the directives of the GCE and the board. Where appropriate, the GIC grants sub-mandates to management to facilitate smaller transactions.

At the BU level, the GIC is supported by the Absa Capital Investment Committee and the Absa Business Bank Investment Committee. The market risk team independently monitors equity investment risk at a consolidated level.

Six months period in review

Traded market risk

The trading environment for the period under review continued to be characterised by slow economic growth and unclear market direction, resulting in continued low customer activity. The high South African market interest rate volatility observations at the end of 2008 and in early 2009 rolled out of the two year DVaR historical data set, and were replaced by less volatile observations. Traded market risk and revenue therefore continued to reflect uncertainties and client volumes and lower volatility. These aspects were effectively managed and a favourable risk-adjusted return was delivered. IMA approval for trading book general position risk was maintained together with a reduction in the regulatory capital requirement from the second half of 2011. Upgraded traded market risk measurement systems architecture were put in place, delivering enhanced performance and scalability to support trading expansion plans. New Basel II.5 trading book capital charges, notably the stressed VaR and incremental risk charges, will translate into an increase in the Group's trading risk regulatory capital charge from 2012. Readiness preparations began in 2010, with final embedment during 2011, along with enhanced specific risk measurement developments. Stressed VaR and incremental risk is now reported daily and monthly respectively for internal purposes. In anticipation of these future regulatory capital charges, the Group further continues to actively manage its traded RWAs towards more efficient use of capital. To strengthen controls, the trader limits attestation process was fully automated, with the intranet-based training and attestation process completed by all relevant front office staff during the period under review.

Interest rate risk in the banking book

Interest rate risk in the banking book was managed to low risk appetite levels. A hedge programme for structural products and equity remains in place, contributing towards a higher degree of stability of the mismatch margin component of the net interest margin over a full interest rate cycle. With South African interest rates having reached exceptionally low levels, efficient management of the structural hedge programme was a key focus. Interest rate risk management hedging activities positively impacted on the net interest margin during the period under review, off-setting the negative endowment effects over the same period. The Group remains exposed to interest rate reset risk, arising from the timing difference between mainly prime linked assets funded with liabilities with a three month repricing profile after hedging, with an adverse impact in a decreasing interest rate environment and vice versa. During the period under review, the impact from reset risk was marginally positive. Prepayment and recruitment risk from fixed rate loan offerings to customers continues to be managed on customer behaviour risk principles.

Equity investment risk in the banking book

Equity investment exposure was managed down during the period under review, creating a leaner portfolio while being selective in terms of new investments. Notably, the remaining Visa Incorporated shares were disposed of during the period under review, while Absa Capital has successfully realised more than R1 billion of its equity investment assets since the beginning of 2010.

Approach to market risk

Traded market risk

Objectives and policies

Traded market risk is primarily the result of facilitating customers in wholesale markets, which includes market making, offering hedge solutions, pre-hedging and assisting customers with executing large trades. Not all customer trades are hedged instantaneously or completely, giving rise to traded market risk. The Group's policy is to concentrate its traded market risk exposure within Absa Capital.

In Absa Capital, market risk occurs in both the trading book and the banking book, as defined for regulatory purposes. Interest rate risk in Absa Capital's banking book is subjected to the same rigorous measurement and control standards as described below for its trading book, but the associated sensitivities are reported as part of the interest rate risk in the banking book sensitivity analyses further on pages 55 to 58.

Measurement and control

A suite of complementary techniques is used to measure and control traded market risk on a daily basis, which includes DVaR, tail risk and stress testing.

Daily value at risk (DVaR)

DVaR is an estimate of the potential loss that might arise from unfavourable market movements if current positions were to be held unchanged for one business day, measured to a confidence level of 95%. Daily losses exceeding the DVaR figure are likely to occur, on average, five times in every 100 business days.

Absa Capital uses an internal DVaR model based on the historical simulation method. Two years of unweighted historical price and rate data are applied and updated daily. This internal model is also used for measuring value at risk over both a one-day and 10-day holding period at a 99% confidence level for regulatory back testing and regulatory capital calculation purposes respectively. This internal model has been approved by the SARB to calculate regulatory capital for the trading book. The model approval covers general position risk across all approved interest rate, foreign exchange, commodity, equity and traded credit products. Issuer specific risk is currently reported in accordance with the regulatory SA.

DVaR is an important market risk measurement and control tool and consequently the performance of the model is regularly assessed for continued suitability. The main technique employed is back testing, which counts the number of days when daily trading losses exceed the corresponding DVaR estimate. The regulatory standard for backtesting is to measure daily losses against DVaR assuming a one-day holding period and a 99% level of confidence. The regulatory green zone of four or less exceptions over a 12-month period is consistent with a good working DVaR model. Back testing reports are monitored daily. For Absa Capital's trading book, green model status was maintained throughout 2010 and up to the reporting date.

DVaR estimates do have a number of limitations. These are:

- historical simulation assumes that the past is a good representation of the future. This may not always be the case;
- the assumed time horizon will not fully capture the market risk of positions that cannot be closed out or hedged within this time horizon;
- DVaR does not indicate the potential loss beyond the selected percentile;
- DVaR is based on positions as at close of business and consequently intra-day risk, the risk from a position bought and sold on the same day, is not captured; and
- prudent valuation practices are used in the DVaR calculation when there is difficulty obtaining rate/price information.

To complement DVaR, tail risk metrics, stress testing and other sensitivity measures are used.

Tail risk metrics

Tail risk metrics highlight the risk beyond the percentile selected for DVaR. The two tail risk metrics chosen for daily monitoring, using the current portfolio and two years of price and rate history, are:

- the average of the worst three hypothetical losses from the historical simulation; and
- expected shortfall (also referred to as expected tail loss), which is the average of all hypothetical losses from the historical simulation beyond the 95th DVaR percentile.

Approach to market risk *(continued)*

Stress testing

Stress testing provides an indication of the potential size of losses that could arise in extreme conditions, which assists in identifying risk concentrations across business lines and assists senior management in capital planning decisions. Absa Capital performs two main types of stress/scenario testing. Firstly, risk factor stress testing is carried out, where extended historical stress moves are applied to each of the main risk categories including interest rate, equity, foreign exchange, commodity and credit spread risk. Secondly, the trading book is subjected to multi-factor scenarios that simulate past periods of significant market disturbance and hypothetical extreme yet plausible events. Scenarios are reviewed at least annually.

Stress results are monitored daily in accordance with a stress limits and triggers framework. If a potential stress loss exceeds the corresponding trigger, the positions captured by the stress test are reviewed, discussed and minuted by the Absa Capital market risk team and the respective Absa Capital business heads, including the merits of the position and the appropriate course of action.

Risk limits

Risk limits are set and reviewed at least annually to control Absa Capital's trading activities in line with the defined risk appetite of the Group. Criteria for setting risk limits include relevant market analysis, market liquidity and business strategy. Trading risk limits are set at aggregate, risk category and lower levels and are expressed in terms of DVaR. This is further supported by a comprehensive set of non-DVaR limits, including foreign exchange position limits, interest rate delta limits, option based limits, tail risk and stress triggers and limits. Performance triggers are also used as part of the risk management process.

Interest rate risk in the banking book

Objectives and policies

Interest rate risk is the risk that the Group's financial position may be adversely affected by changes in interest rate levels, yield curves and spreads. Non-traded interest rate risk arises in the banking book from the provision of retail and wholesale (non-traded) banking products and services, as well as from certain structural exposures within the statement of financial position, mainly due to repricing timing differences between assets, liabilities and equity. These risks impact both the earnings and the economic value of the Group.

The Group's objective for managing interest rate risk in the banking book is to ensure a higher degree of interest rate mismatch margin stability and lower interest rate risk over an interest rate cycle. This is achieved by hedging material exposures with the external market. A limits framework is in place to ensure that retained risk remains within approved risk appetite.

Risk management strategies considered include:

» strategies regarding changes in the volume, composition, pricing and interest rate risk characteristics of assets and liabilities; and

» the execution of applicable derivative contracts to maintain the Group's interest rate risk exposure within limits.

Where possible, hedge accounting is applied to derivatives that are used to hedge interest rate risk in the banking book. In cases where hedge relationships do not qualify for hedge accounting, mismatches may arise due to different bases used in fair valuing the hedges and the underlying banking book exposure. Applicable accounting rules as stipulated in the Group's accounting policies are followed.

As part of Group Treasury's balance sheet management role, interest rate exposures arising from the repricing mismatches of assets and liabilities in the domestic banking book are transferred from the BUs to Group Treasury through matched funds transfer pricing. These positions are aggregated and the net exposure is hedged with the market via Absa Capital. As a result of mainly timing considerations, interest rate risk may arise when some of the net position remains with Group Treasury.

Structural interest rate risk arises from the variability of income from non-interest bearing products, managed variable rate products and the Group's equity, and is managed by Group Treasury. Structural balances are typically hedged using a portfolio of swaps where the maturity is based on the assumed stability of the underlying balance.

Interest rate risk also arises in each of the African subsidiaries' treasuries in the course of managing the balance sheet and facilitating customer activity. The risk is managed by local treasury functions, subject to modest risk limits and other controls.

Measurement and control

The techniques used to measure and control interest rate risk in the banking book include repricing profiles, annual earnings at risk, DVaR and tail metrics, economic value of equity sensitivity and stress testing.

Approach to market risk *(continued)*

Measurement and control *(continued)*

Repricing profiles

Instruments are allocated to time periods with reference to the earlier of the next contractual interest rate repricing date and the maturity date. Instruments which have no explicit contractual repricing or maturity dates are placed in time buckets according to management's judgement and analysis, based on the most likely repricing behaviour. For example, retail deposits are repayable on demand or at short notice, but form a stable base for the Group's operations and liquidity needs due to the broad customer base (numerically and by depositor type). Currently, the contractual profiles of assets are not adjusted for customer prepayment features. Repricing profiles are monitored monthly.

Annual earnings at risk (AEaR)

AEaR measures the sensitivity of net interest income over the next 12 months to a specified shock in interest rates. AEaR is assessed across a range of interest rate scenarios, including parallel and key rate shocks, yield curve twists and inversions, as appropriate for each business. The AEaR calculation takes the assumed behavioural profile of relevant structural product balances into account. Currently, the contractual profiles of assets are not adjusted for customer prepayment features. AEaR is monitored monthly against approved internal limits, which limits are calibrated for a standardised 200 bps adverse shock.

Daily value at risk (DVaR)

Apart from Absa Capital, the Group uses a simplified approach to calculate interest rate risk in the banking book DVaR at a 95% confidence level, which is monitored against approved internal limits. It is used as a complementary tool to AEaR. DVaR is also supplemented by tail metrics. DVaR is monitored daily in respect of Group Treasury, and at least monthly, in respect of African subsidiaries' treasuries.

Economic value of equity (EVE) sensitivity

EVE sensitivity measures the sensitivity of the present value of the banking book, at a specific point in time to a specified shock to the yield curve. Like DVaR, EVE is a present value sensitivity, and complementary to income sensitivity measures such as AEaR. EVE sensitivity is monitored monthly.

Stress testing

Stress testing is carried out by Group Treasury and the risk functions in African subsidiaries to supplement DVaR and AEaR metrics. The stress testing is tailored to each banking book and consists of a combination of stress scenarios and historical stress movements applied to the respective banking books. Stress results are monitored at least monthly.

Prepayment and recruitment risk

Embedded customer optionality risk may also give rise to interest rate risk in the banking book. This risk arises from a customer's right to buy, sell or in some manner alter the cash flow of a financial contract. Embedded customer optionality is distinct from direct optionality, which arises through the underlying product structure (e.g. capped rate loan products). The Group's policy requires such direct option risk to be hedged explicitly.

Prepayment risk arises in relation to transactions where a customer option is embedded in the product. This risk most commonly arises in relation to fixed rate loans offered to retail customers, where the customer has an option to repay the loan prior to contractual maturity and where the Group is unable to collect full market related compensation. The risk is controlled through book and term limits, funding (hedging) new loans according to the expected repayment profile and tracking deviations of actual customer behaviour from the expected profile. The risk is monitored monthly.

Recruitment risk arises when the Group commits to providing a product at a predetermined price for a period into the future. Customers have the option to take up this offer. Controls include campaign rules, pre-funding of anticipated take-up and management of the resultant residual risk.

Embedded customer optionality risk was not material during 2010 and up to the reporting date.

Foreign exchange risk

The Group is exposed to two sources of foreign exchange risk, namely, transactional and translational risk.

Transactional foreign exchange risk

Transactional foreign exchange risk arise as a result of banking assets and liabilities which are not denominated in the functional currency of the transacting entity. The Group's policy is for transactional foreign exchange risk to be concentrated and managed within the Absa Capital trading book.

Some transactional foreign exchange risk arises within the African subsidiaries' treasuries in the course of foreign currency balance sheet management and facilitation of customer activity. This risk is minimised in accordance with modest transactional open position and DVaR limits, as approved by the MRC. Foreign exchange risk is monitored daily against these limits. Average foreign exchange DVaR for the period under review amounted to R0,3 million for 2011 (30 June 2010: R0,3 million; 31 December 2010: R0,3 million) on an undiversified basis across these treasuries.

In accordance with the Group's policy there were no significant net open currency positions outside the Absa Capital trading book at either 30 June 2011 or 2010 that would give rise to material foreign exchange gains and losses being recognised in the statement of comprehensive income or in equity as a result of a foreign exchange rate shock.

Approach to market risk *(continued)*

Foreign exchange risk *(continued)*

Translational foreign exchange risk

Translational foreign exchange risk arises from capital resources (including investments in subsidiaries and branches, intangible assets, non-controlling interest, deductions from capital and debt capital instruments) and RWAs being denominated in foreign currencies. Changes in foreign exchange rates result in changes in the South African rand (ZAR) equivalent value of foreign currency denominated capital resources and RWAs.

Translational foreign currency risk can be mitigated through derivatives or borrowings in the same currency as the functional currency involved, designated as net investment hedges, or through economic hedges.

The impact of a change in the exchange rate between ZAR and any relevant currencies, would be:

» a higher or lower ZAR equivalent value of non-ZAR denominated capital resources and RWAs. This includes a higher or lower currency translation reserve within equity, representing the translation of non-ZAR subsidiaries, branches and associated undertakings net of the impact of foreign exchange rate changes on derivatives and borrowings designated as hedges of net investments;

» a higher or lower profit after tax, arising from changes in the exchange rates used to translate items in the statement of comprehensive income; and

» a higher or lower value of available-for-sale investments denominated in foreign currencies, impacting the available-for-sale reserve.

The Group's translational foreign exchange risk arises primarily from its investments in foreign subsidiaries and branches.

Translational hedging considerations include exchange control regulations, the strategic nature of the investment, materiality of the risk, prevailing foreign exchange rates, market liquidity, cost of hedging and the impact on capital ratios. Based on these considerations, no foreign currency net investment hedges were in place during 2011.

Translational foreign exchange risk may give rise to sensitivity of the Group's capital ratios, from the ratio of foreign currency capital resources to foreign currency RWAs. To minimise volatility of capital ratios caused by foreign exchange rate movements, the Group aims to maintain an appropriate foreign currency capital structure by maintaining the ratio of foreign currency Core Tier 1, Tier 1 and total capital resources to foreign currency RWAs in line with the Group's capital ratios. This is primarily achieved by subsidiaries issuing capital or holding retained earnings in local currencies, but could also be achieved through Group issuance of debt capital in non-ZAR currencies.

Translational foreign exchange risk is monitored regularly to consider the need for mitigating actions towards minimising material fluctuations. A sensitivity analysis is provided in table 33.

Asset management structural market risk

Asset management structural market risk arises where the fee and commission income earned by asset management products and businesses is affected by a change in market levels, primarily through the link between income and the value of assets under management. The risk is measured in terms of AEaR, to reflect the sensitivity of annual earnings to shocks in market rates, notably interest rates and equity. It is Group policy that BUs monitor and report this risk and regularly assess potential hedging strategies. This exposure currently arises mainly within Absa Financial Services. Asset management structural market risk was not material during the period under review.

Equity risk in the banking book

Objectives and policies

Equity investment risk refers to the risk of adverse changes in the value of listed and unlisted equity investments. These investments are longer term investments held in the banking book for non-trading purposes. Investments are entered into for one or more of the following reasons:

» enhancing long-term sustainable income;

» positioning the Group strategically for future markets/benefits;

» achieving BU growth objectives;

» improving internal efficiencies in a cost effective way; and/or

» improving the Group's asset or customer base.

The Group's governance of equity investments is based on the following key principles:

» a formal approved governance process;

» a segregation of governance committees based on the nature of the investment and discretion limits;

» key functional specialists reviewing investment proposals;

» adequate monitoring and control after the investment decision has been implemented; and

» ongoing implementation of best practice based on current market trends, hurdle rates and benchmarks.

Equity investments are managed under the new ventures and asset policy framework, in accordance with the purpose and strategic benefits of such investments, rather than on MTM considerations only. Consideration is given to the merits of investment proposals, the impact of the proposal on the investment portfolio, the effectiveness of the exit strategy and the likelihood of achieving the targeted return in terms of that particular investment. Criteria considered for new investments and investment reviews cover a comprehensive set of financial, commercial, legal (and technical, where required) matters. The performance of these investments is monitored relative to the objectives of the portfolio.

Approach to market risk *(continued)*

Equity risk in the banking book *(continued)*

Objectives and policies *(continued)*

The majority of the Group's equity investments are held in Absa Capital and ABB. Absa Capital's investments range across different industries and are monitored in terms of risk and return by the Private Equity and Capital Management departments within Absa Capital. ABB is mainly focused on commercial property investments across a range of property sectors, which are monitored in terms of risk and return by the ABB Specialist Equity department. Equity and other investments held by insurance entities of the Group are addressed in the insurance risk management section of this report.

Relevant accounting policies

IAS 39 requires all equity investments to be fair valued, except for unquoted equity investments, the fair value of which cannot be reliably measured and is then measured at cost. Accounting policies regarding subsidiaries and investments in associates and joint ventures are discussed separately in note 1.3 of the December 2010 Group financial statements.

The fair value of equity investments is determined using appropriate valuation methodologies which, depending on the nature of the investment, include discounted cash flow analysis, enterprise value comparisons with similar companies and price-earnings comparisons. For each investment, the relevant methodology is applied consistently over time.

Listed and unlisted investments are either designated at fair value through profit or loss or as available-for-sale. Investments in entities that form part of the venture capital and similar activities of the Group have been designated at fair value through profit or loss. The designation has been made in accordance with IAS 39, based on the scope exclusion provided in IAS 28. The relevant accounting policies for equity investments are discussed in note 1.7 of the December 2010 Group financial statements.

Measurement and control

Equity investment risk is monitored monthly in terms of regulatory and economic capital requirements, complemented by a range of additional risk metrics and stress testing. The equity investment risk profile is further tracked across a range of dimensions such as geography, industry and currency. The risk monitoring is done in accordance with a risk appetite, mandate and scale limits framework.

The Group has adopted the market-based simple risk weight approach to calculate RWAs and regulatory capital for equity risk in the banking book. According to this approach, RWAs are calculated using weighting of 300% and 400% for listed and unlisted equity investments respectively. RC requirements in respect of investments in associates and joint ventures, defined as financial companies as specified by the regulations relating to banks, are calculated with reference to either the pro rata consolidation methodology or the deduction approach.

Economic capital for equity risk in the banking book is based on investment type and portfolio risk modelling, subject to a floor of 50% of statement of financial position value.

Defined benefit pension risk

The Group maintains different pension plans with defined benefit and defined contribution structures for former and current employees. In respect of defined benefit plans, the ability to meet the projected pension payments is maintained through investments and regular contributions. Market risk arises because the estimated market value of the pension plan assets might decline, or their investment returns might reduce, or because the estimated value of the pension liabilities might increase, resulting in a funding deficit. In these circumstances, the Group could be required or might choose to make additional contributions to the defined benefit plan. Financial details of the pension plans are provided in note 44 of the December 2010 Group financial statements.

2011 market risk disclosures

Traded market risk

Analysis of traded market risk exposure

The following table reflects the 95% DVaR for Absa Capital's trading book activities as measured by the Group's internal models approach for general trading position risk.

Absa Capital traded market risk exposure, as measured by average total DVaR, decreased to R25,80 million for the period under review, which is down 5% to the six months ended 30 June 2010 (R27,03 million) and down 7% compared to the full 2010 financial year (R27,85 million). This was mainly due to a decrease in average equity DVaR. Average DVaR over the period has been generally low due to low client activity across most asset classes and lower market volatility. The Markets business, however, continued to perform solidly, delivering a favourable risk-adjusted return for the period under review.

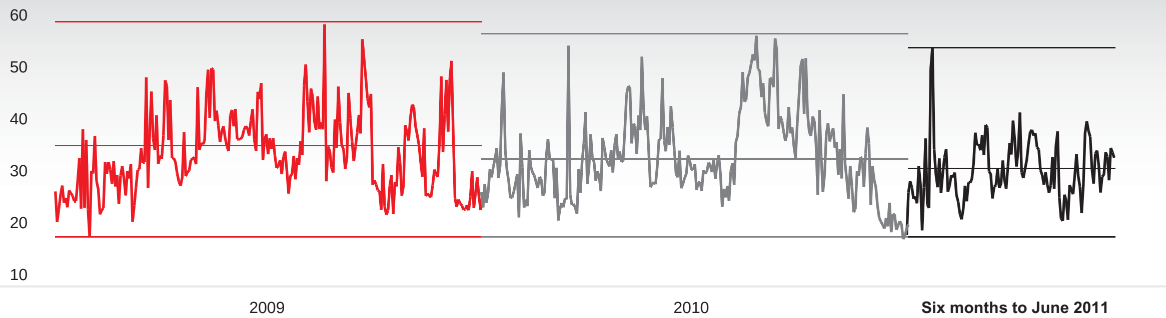
2011 market risk disclosures *(continued)*

Absa Capital trading book DVAR summary – Table 27:

	Six months ended 30 June 2011				Six months ended 30 June 2010				12 months ended 31 December 2010			
	Average Rm	High[1] Rm	Low[1] Rm	Rm	Average Rm	High[1] Rm	Low[1] Rm	Rm	Average Rm	High[1] Rm	Low[1] Rm	Rm
Interest rate risk[2]	**21,10**	**36,69**	**15,31**	**23,18**	21,08	36,64	10,16	20,28	22,15	36,64	10,16	17,36
Foreign exchange risk	**8,94**	**25,68**	**1,89**	**6,67**	8,26	38,09	1,57	3,17	7,47	38,09	1,57	3,56
Equity risk	**4,17**	**7,73**	**2,38**	**2,94**	9,98	26,13	4,67	14,04	9,17	26,95	2,54	5,02
Commodity risk	**1,96**	**4,12**	**0,72**	**2,79**	1,17	2,87	0,30	1,63	1,41	4,78	0,30	0,71
Diversification effect	**(10,37)**	**n/a**	**n/a**	**(7,87)**	(13,46)	n/a	n/a	(11,83)	(12,35)	n/a	n/a	(9,24)
Total DVaR[3]	**25,80**	**44,77**	**15,75**	**27,71**	27,03	45,01	18,00	27,29	27,85	46,55	15,13	17,41

The graph below shows the history of Absa Capital's total trading book DVaR on a daily basis for 2009 and 2010 and the six months to June 2011. Throughout this period, Absa Capital's total trading book DVaR remained within the approved DVaR limit and within the approved risk appetite. Absa Capital does, on some occasions in the conduct of client transactions, take on significantly larger-than-usual market risk. However, this is always undertaken within the Group's market risk governance framework.

Absa Capital trading book DVaR (daily values, period average high and low) (Rm)

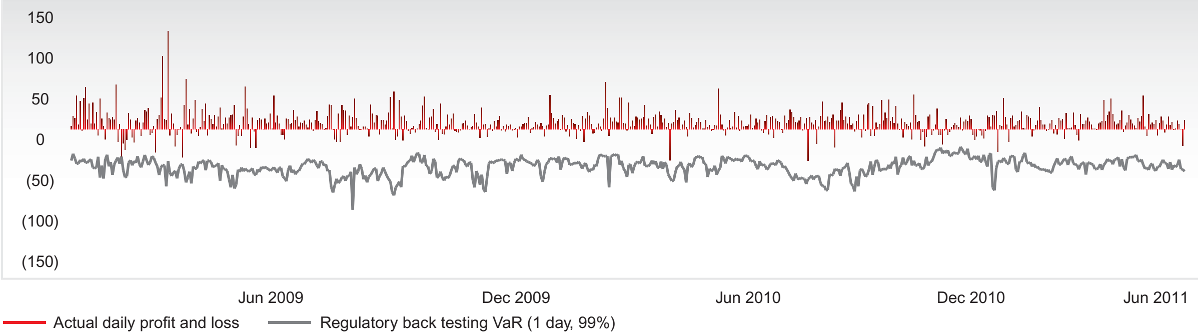


Comparison of value at risk estimates with trading revenues

The graph that follows compares the total value at risk estimates over a one-day holding period at a 99% confidence level with the daily revenues generated by the trading units from 2009 to 2010 and the six months to 30 June 2011. Revenue as reported here includes net trading book income, excluding net fees and commissions.

Over the 12 months to 30 June 2011 there were no instances where an actual daily trading loss exceeded the corresponding value at risk estimate.

Absa Capital daily trading book revenue back tested against regulatory value at risk (Rm)



Notes

[1] *The high (and low) DVaR figures reported for each category did not necessarily occur on the same day as the high (and low) total DVaR. Consequently, a diversification effect number for the high (and low) DVaR figures would not be meaningful and is therefore omitted from the above table.*

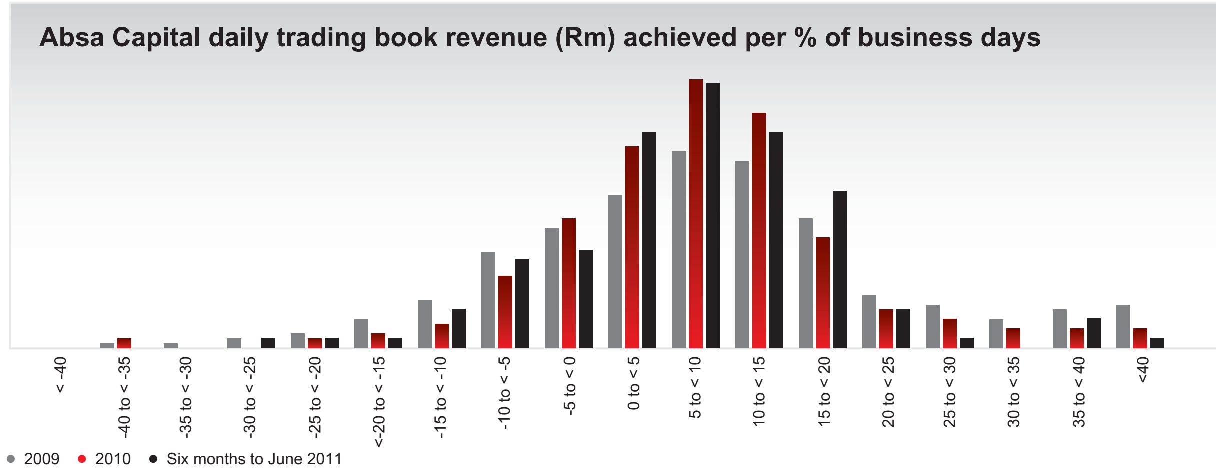
[2] *Credit spread risk is reported together with interest rate risk.*

[3] *The total value at risk over a 10-day holding period at a 99% confidence level as at 30 June 2011 was R163,51 million (30 June 2010: R113,92 million; 31 December 2010: R97,67 million).*

2011 market risk disclosures *(continued)*

Analysis of trading revenue

The histograms below show the distribution of daily trading revenue for the Absa Capital trading book for the 12 months of 2009 and 2010, and the six months to 30 June 2011. Revenue includes net trading book income, excluding net fees and commissions. The distributions are skewed to the profit side. The average daily trading revenue for the reporting period decreased compared to the six months ended 30 June 2010 and the full 2010 financial year. The percentage of positive revenue days were 79% over the period under review (30 June 2010: 83%; 31 December 2010: 78%). Revenue for the reporting period was however generated utilising lower average DVaR and achieving a reduction in revenue volatility, which continued to solidify performance delivery.



2011 market risk disclosures *(continued)*

Minimum regulatory capital requirement for traded market risk

The Group's traded market risk minimum regulatory capital requirement comprises two elements:

- Trading book positions where the market risk is measured under a SARB approved internal VaR model. The capital requirement is calculated based on the internal model with a 10-day holding period at a 99% confidence level, and other regulatory 60-day averaging and capital multiplier specifications. This approach currently applies to close to 100% of the Group's general position risk across interest rate, foreign exchange, commodity, equity and traded credit products. A description of the Group's internal model and controls may be found on page 48.
- Trading book positions which have not yet met SARB or the Group's internal conditions for inclusion within the approved internal model. The capital requirement is calculated using standardised regulatory rules. This approach currently applies to the Group's issuer specific risk exposures.

The total traded market risk minimum capital requirement increased by 4% or R33 million to R788 million year on year to the reporting date (30 June 2010: R755 million) driven mainly by an increase in specific risk measured under the standardised approach and partially offset by a decrease in general position risk measured under the internal models approach. A reduced regulatory capital requirement will apply from the second half of 2011 in line with the recent internal model approval review for general position risk.

Minimum regulatory capital requirement (at 8% of RWAs) for traded market risk – Table 28:

	Minimum capital requirement		
	As at 30 June		As at 31 December
	2011 Rm	2010 Rm	2010 Rm
Internal models approach (DVaR model based)	**543**	561	501
Standardised approach	**245**	194	220
Interest rate risk	**132**	89	134
Equity risk	**59**	81	36
Foreign exchange risk, including gold	**—**	—	—
Commodity risk	**—**	—	—
Options	**54**	24	50
Total traded market risk capital requirement	**788**	755	721

Interest rate risk in the banking book

Three separate interest rate sensitivity analyses for the Group's banking book are set out below, namely, the repricing profile of the book, the potential effect of changes in market interest rates on annual earnings and equity reserves.

Interest rate sensitivity analysis – repricing profile

The repricing profile of the Group's domestic, Africa subsidiary and consolidated banking books shows that the consolidated banking book remains asset sensitive, or positively gapped, as interest-earning assets reprice sooner than interest-paying liabilities before and after derivative hedging activities. Accordingly, future net interest income remains vulnerable to a decrease in market interest rates.

Asset sensitivity, as represented by the cumulative 12 month interest rate gap, increased from 2010 to 2011. The main reason for the increased sensitivity as reported for the African subsidiary banking books is due to the further refinement and implementation of product structural assumptions with the aim to closely represent the reality of the markets and to facilitate better risk management.

2011 market risk disclosures *(continued)*

Expected repricing profile – Table 29:

	As at 30 June 2011			
	On demand – 3 months Rm	**4 – 6 months Rm**	**7 – 12 months Rm**	**Over 12 months Rm**
Domestic bank book[1]				
Interest rate sensitivity gap	**130 760**	**(27 463)**	**(35 299)**	**(34 048)**
Derivatives[2]	**(100 965)**	**17 334**	**23 422**	**60 209**
Net interest rate sensitivity gap	**29 795**	**(10 129)**	**(11 877)**	**26 161**
Cumulative interest rate gap	**29 795**	**19 666**	**7 789**	**33 950**
Cumulative gap as a percentage of Absa Bank Limited's total assets (%)	**4,4**	**2,9**	**1,1**	**5,0**
Foreign subsidiaries bank books[3]				
Interest rate sensitivity gap	**1 729**	**(70)**	**1 477**	**472**
Derivatives[2]	**115**	**(0)**	**(12)**	**(114)**
Net interest rate sensitivity gap	**1 844**	**(70)**	**1 465**	**358**
Cumulative interest rate gap	**1 844**	**1 774**	**3 239**	**3 597**
Cumulative gap as a percentage of foreign subsidiaries' total assets (%)	**19,2**	**18,5**	**33,8**	**37,5**
Total				
Cumulative interest rate gap	**31 639**	**21 440**	**11 028**	**37 547**
Cumulative gap as a percentage of the Group's total assets (%)	**4,4**	**3,0**	**1,5**	**5,2**

	30 June 2010			
	On demand – 3 months Rm	4 – 6 months Rm	7 – 12 months Rm	Over 12 months Rm
Domestic bank book[1]				
Interest rate sensitivity gap	131 505	(27 990)	(40 666)	(31 624)
Derivatives[2]	(105 907)	4 589	38 367	62 952
Net interest rate sensitivity gap	25 598	(23 401)	(2 299)	31 327
Cumulative interest rate gap	25 598	2 197	(102)	31 225
Cumulative gap as a percentage of Absa Bank Limited's total assets (%)	3,8	0,3	(0,0)	4,6
Foreign subsidiaries bank books[3]				
Interest rate sensitivity gap	406	(243)	(788)	240
Derivatives[2]	94	0	0	(82)
Net interest rate sensitivity gap	500	(243)	(788)	158
Cumulative interest rate gap	500	257	(531)	(373)
Cumulative gap as a percentage of foreign subsidiaries' total assets (%)	5,4	2,8	(5,7)	(4,0)
Total				
Cumulative interest rate gap	26 098	2 454	(633)	30 852
Cumulative gap as a percentage of the Group's total assets (%)	3,6	0,3	(0,1)	4,3

Notes
[1] *Includes exposures held in the Absa Capital banking book.*
[2] *Derivatives for interest rate risk management purposes (net nominal value).*
[3] *Includes NBC and BBM.*

2011 market risk disclosures *(continued)*

Expected repricing profile – Table 30: *(continued)*

	31 December 2010			
	On demand – 3 months Rm	4 – 6 months Rm	7 – 12 months Rm	Over 12 months Rm
Domestic bank book[1]				
Interest rate sensitivity gap	128 494	(33 570)	(26 521)	(33 699)
Derivatives[2]	(120 901)	32 111	24 474	64 316
Net interest rate sensitivity gap	7 593	(1 459)	(2 047)	30 617
Cumulative interest rate gap	7 593	6 134	4 087	34 704
Cumulative gap as a percentage of Absa Bank Limited's total assets (%)	1,1	0,9	0,6	5,1
Foreign subsidiaries bank books[3]				
Interest rate sensitivity gap	435	(394)	(591)	410
Derivatives[2]	122	0	0	(121)
Net interest rate sensitivity gap	557	(394)	(591)	289
Cumulative interest rate gap	557	163	(428)	(139)
Cumulative gap as a percentage of foreign subsidiaries' total assets (%)	6,0	1,8	(4,6)	(1,5)
Total				
Cumulative interest rate gap	8 150	6 297	3 659	34 565
Cumulative gap as a percentage of the Group's total assets (%)	1,1	0,9	0,5	4,8

Interest rate sensitivity analysis – impact on earnings

The following tables show the AEaR resulting from impacts to net interest income for 100 and 200 bps up and down movements in market interest rates on the Group's banking books. Assuming no management action is taken in response to market interest rate movements, a hypothetical immediate and sustained parallel decrease of 200 bps in all market interest rates would, as at the reporting date, result in a pre-tax reduction in projected 12-month net interest income of R565 million (30 June 2010: R503 million; 31 December 2010: R389 million). A similar increase would result in an increase in projected 12-month net interest income of R597 million (30 June 2010: R504 million; 31 December 2010: R341 million). AEaR therefore remains low, at well below 5% of the Group's net interest income, for a 200 bps rate shock.

A sensitivity analysis by major currency market interest rates indicates that earnings sensitivity to ZAR market interest rates constitutes 93% of the total earnings at risk at the reporting date (30 June 2010: 96%; 31 December 2010: 96%), therefore indicating that the Group remains primarily exposed to South African market interest rates.

Annual earnings at risk for a 100 and 200 bps change in market interest rates – Table 31:

	Change in market interest rates			
	200 bps decrease	**100 bps decrease**	**100 bps increase**	**200 bps increase**
As at 30 June 2011				
Domestic bank book[1] (Rm)	**(526)**	**(258)**	**271**	**558**
Foreign subsidiaries' bank books[2] (Rm)	**(39)**	**(19)**	**19**	**39**
Total (Rm)	**(565)**	**(277)**	**290**	**597**
Percentage of the Group's net interest income (%)	**(2,4)**	**(1,2)**	**1,2**	**2,5**
Percentage of the Group's equity (%)	**(0,9)**	**(0,4)**	**0,5**	**0,9**
As at 30 June 2010				
Domestic bank book[1] (Rm)	(483)	(253)	233	484
Foreign subsidiaries' bank books[2] (Rm)	(20)	(10)	10	20
Total (Rm)	(503)	(263)	243	504
Percentage of the Group's net interest income (%)	(2,2)	(1,2)	1,1	2,3
Percentage of the Group's equity (%)	(0,8)	(0,4)	0,4	0,8
As at 31 December 2010				
Domestic bank book[1] (Rm)	(376)	(176)	157	328
Foreign subsidiaries' bank books[2] (Rm)	(13)	(7)	7	13
Total (Rm)	(389)	(183)	164	341
Percentage of the Group's net interest income (%)	(1,7)	(0,8)	0,7	1,5
Percentage of the Group's equity (%)	(0,6)	(0,3)	0,3	0,5

Notes

[1] *Includes Absa Bank Limited's domestic banking book, which includes exposures held in the Absa Capital banking book.*

[2] *Includes NBC and BBM. African subsidiaries' interest rate sensitivities are shown on a 100% (rather than actual) shareholding basis.*

Six months ended 30 June 2011

2011 market risk disclosures *(continued)*

Interest rate sensitivity analysis – impact on equity reserves

Market interest rate changes may affect equity (capital) in the following three ways:

- higher or lower profit after tax resulting from higher or lower net interest income;
- higher or lower available-for-sale reserves reflecting higher or lower fair values of available-for-sale financial instruments; and
- higher or lower values of derivatives held in the cash flow hedging reserve.

The pre-tax effect from net interest income sensitivity is reported in the preceding sensitivity analysis. The effect of taxation can be estimated using the 2011 tax rate.

The equity reserve sensitivities that follow are illustrative, based on simplified scenarios, and consider the impact on the cash flow hedges and available-for-sale portfolios which are MTM through reserves. The impact on equity is calculated by revaluing fixed rate available-for-sale financial assets, including the effect of any associated hedges, and derivatives designated as cash flow hedges, for an assumed change in market interest rates.

The increased sensitivity of cash flow hedging reserves from June 2010 to June 2011 is due to an increase in interest rate swaps executed to hedge the fixed rate exposure associated with structural balances and fixed rate retail and commercial deposits. The increase sensitivity of available-for-sale reserves from June 2010 to June 2011 is due to additional statutory liquid assets purchased during the year, classified as available-for-sale. During the period under review the sensitivity for both the cash flow hedge and available-for-sale reserves remained stable.

Sensitivity of reserves to market interest rate movements – Table 32:

	30 June 2011 Impact on equity Rm	30 June 2011 Maximum impact[1] Rm	30 June 2011 Minimum impact[1] Rm
+ 100 bps parallel move in all yield curves			
Available-for-sale reserve	**(831)**	**(831)**	**(793)**
Cash flow hedging reserve	**(1 723)**	**(1 748)**	**(1 671)**
Total	**(2 555)**	**(2 563)**	**(2 464)**
As a percentage of Group equity (%)	**(4,7)**	**(4,7)**	**(4,6)**
– 100 bps parallel move in all yield curves			
Available-for-sale reserve	**831**	**831**	**793**
Cash flow hedging reserve	**1 723**	**1 748**	**1 671**
Total	**2 555**	**2 563**	**2 464**
As a percentage of Group equity (%)	**4,7**	**4,7**	**4,6**

	As at 30 June 2010 Impact on equity Rm	As at 30 June 2010 Maximum impact[1] Rm	As at 30 June 2010 Minimum impact[1] Rm
+ 100 bps parallel move in all yield curves			
Available-for-sale reserve	(675)	(738)	(675)
Cash flow hedging reserve	(1 694)	(1 694)	(1 506)
Total	(2 368)	(2 368)	(2 238)
As a percentage of Group equity (%)	(4,0)	(4,0)	(3,8)
– 100 bps parallel move in all yield curves			
Available-for-sale reserve	675	738	675
Cash flow hedging reserve	1 694	1 694	1 506
Total	2 368	2 368	2 238
As a percentage of Group equity (%)	4,0	4,0	3,8

	As at 31 December 2010 Impact on equity Rm	As at 31 December 2010 Maximum impact[1] Rm	As at 31 December 2010 Minimum impact[1] Rm
+ 100 bps parallel move in all yield curves			
Available-for-sale reserve	(841)	(875)	(675)
Cash flow hedging reserve	(1 731)	(1 794)	(1 506)
Total	(2 572)	(2 655)	(2 238)
As a percentage of Group equity (%)	(4,1)	(4,3)	(3,6)
– 100 bps parallel move in all yield curves			
Available-for-sale reserve	841	875	675
Cash flow hedging reserve	1 731	1 794	1 506
Total	2 572	2 655	2 238
As a percentage of Group equity (%)	4,1	4,3	3,6

Note

[1] *The maximum and minimum impacts reported for each reserve category did not necessarily occur for the same month as the maximum and minimum impact reported for the total.*

2011 market risk disclosures *(continued)*

Foreign currency translation risk in the banking book

The Group's translational foreign exchange exposure arises primarily from its net investments in foreign subsidiaries and branches. The following table shows the carrying value of foreign currency net investments and the pre-tax impact on equity of a 5% change in the exchange rate between ZAR and the relevant functional foreign currencies.

The Group's total foreign currency net investment exposure and sensitivity remains low. The increase in Mozambican metical exposure since 30 June 2010 is mainly as a result of the recapitalisation of BBM. The 7% increase in total exposure since 31 December 2010 is mainly as a result of GBP/ZAR exchange rate movements.

Foreign currency translation sensitivity analysis – Table 33:

Functional foreign currency	Sterling Rm	Tanzanian shilling Rm	Mozambican metical Rm	Total Rm
As at 30 June 2011				
Foreign currency net investments	**1 619**	**310**	**452**	**2 381**
Impact on equity from a 5% currency translation shock	**81**	**15**	**23**	**119**
As at 30 June 2010				
Foreign currency net investments	1 545	427	227	2 199
Impact on equity from a 5% currency translation shock	77	21	11	109
As at 31 December 2010				
Foreign currency net investments	1 481	276	477	2 234
Impact on equity from a 5% currency translation shock	74	14	24	112

From a capital adequacy perspective, as at the reporting date the Group has 3,70% (30 June 2010: 3,50%; 31 December 2010: 3,86%) of its qualifying capital in foreign currency banking entities, against 2,84% (30 June 2010: 3,08%; 31 December 2010: 2,96%) of its RWAs. A 5% adverse change in the exchange rate between the ZAR and each of the functional currencies would impact the Group's total capital adequacy ratio (including unappropriated profits) minimally between one and two bps.

Equity investment risk

Equity investment risk in the banking book (regulatory definition)

The equity portfolio subject to regulatory and economic capitalisation under equity risk in the banking book rules of the Banks Act, excludes third-party equity investments under management for which the Group does not bear the risk, selected associates treated under the pro rata consolidation methodology, and equity investments held by insurance entities (as these entities are regulated separately, and addressed in the insurance risk management section of this report).

The size, composition, RWAs and economic capital requirement of the Group's equity investments in the banking book are reflected in the following table after the recognition of guarantees. As at the reporting date, the statement of financial position value of such investments amounted to R6 277 million (30 June 2010: R7 568 million; 31 December 2010: R6 757 million). Of the R6 277 million investment exposure as at the reporting date, R5 924 million is held for capital gains purposes and the remainder is for strategic and other purposes.

Equity investment exposure was managed down further during the reporting period towards creating a leaner portfolio, causing a decrease in the statement of financial position values. Notably the remaining Visa Incorporated shares were disposed of during the reporting period. Absa Capital has successfully realised close to R1 billion of its equity investment assets since the beginning of 2010. Absa Capital Private Equity earnings continued to improve, given positive realisations, stable valuations and lower funding costs.

2011 market risk disclosures *(continued)*

Equity investments in the banking book – Table 34:

	As at 30 June 2011 Rm	As at 30 June 2010 Rm	As at 31 December 2010 Rm
Statement of financial position	**6 277**	7 568	6 757
Exchange traded investments, associates and joint ventures[1]	**882**	1 329	1 025
Privately held traded investments, associates and joint ventures[2]	**5 395**	6 239	5 732
Fair value of exchange traded investments, associates and joint ventures[3]	**882**	1 329	1 039
RWAs	**24 136**	28 814	25 911
Exchange traded investments, associates and joint ventures	**2 647**	3 954	3 074
Privately held traded investments, associates and joint ventures	**21 489**	24 860	22 837
Economic capital	**3 305**	4 562	4 036
Exchange traded investments, associates and joint ventures[1]	**610**	1 033	399
Privately held traded investments, associates and joint ventures[2]	**2 695**	3 529	3 637

Realised and unrealised gains/(losses) for equity investments in the banking book as per specific SARB Pillar 3 disclosure requirements are reflected in the following table:

Realised and unrealised gains/(losses) on equity investments – Table 35:

	Year to date 30 June 2011 Rm	Year to date 30 June 2010 Rm	Year to date 31 December 2010 Rm
Cumulative realised gains/(losses) arising from sales and liquidations	**29**	60	117
Total unrealised gains/(losses) recognised directly in the statement of financial position	**5**	4	(19)

To address the specific SARB Pillar 3 disclosure requirements for equity risk in the banking book relating to unrealised gains/(losses), it should be noted that:

- » the Group does not have any latent revaluation gains/(losses), i.e. unrealised gains/(losses) which are not recognised in the statement of financial position or statement of comprehensive income; and
- » the Group does not have unrealised gains/(losses) that are recognised in primary or secondary capital and reserve funds without being recognised in the statement of comprehensive income. This is due to an IFRS principle adopted by the Group, i.e. all unrealised gains/(losses) that are not recognised in the statement of comprehensive income cannot be recognised in primary or secondary capital and reserve funds.

Focus going forward

Traded market risk

The Group will benefit from a reduced regulatory trading risk capital requirement from the second half of 2011 in line with the recent internal model approval review. However, in anticipation of the increase in traded market risk regulatory capital charges from 2012, the Group will remain focused on facilitating customer business and actively managing its traded RWAs towards achieving more efficient use of capital. With developments in place and internal parallel runs already underway in respect of the new Basel II.5 trading book stressed VaR and incremental risk capital charges, the focus will be on associated regulatory model waiver applications and parallel runs for regulatory reporting purposes commencing in the following six months.

Interest rate risk in the banking book

Efficient management of the structural interest rate hedge programme will remain a focus area in the following six months.

Equity investment risk in the banking book

In line with the capital, liquidity and balance sheet optimisation programme of the Group, there will be continued focus on reducing equity investment exposures towards creating a leaner portfolio, while remaining selective on new investments.

Notes

[1] *Includes significant minority financial investments deducted from net qualifying regulatory capital, amounting to Rnil as at 30 June 2011 (30 June 2010: R11 million; 31 December 2010: Rnil).*

[2] *Includes significant minority financial investments deducted from net qualifying regulatory capital, amounting to R23 million as at 30 June 2011 (30 June 2010: R24 million; 31 December 2010: R23 million).*

[3] *To address specific SARB Pillar 3 requirements for equity risk in the banking book relating to the value of investments, it should be noted that the difference between the statement of financial position value and fair value of associates and joint ventures amounts to Rnil as at 30 June 2011 (30 June 2010: Rnil; 31 December 2010: R14 million). The difference in previous periods relates to conservative impairments applied on the listed associates, which followed a prudent and considered assessment by the board, therefore resulting in the fair value of the said investments being higher than the statement of financial position values. Additionally, there are no differences between the fair value and market value of exchange traded investments, associates and joint ventures.*

Liquidity risk

Six months ended 30 June 2011

Highlights

- *Liquidity risk management process remained robust and comprehensive.*
- *Further increase in amount of surplus liquid assets held, building on the strong growth achieved during 2010.*
- *Further improvement in wholesale funding term, thereby further strengthening the position attained at 31 December 2010. The key contributors were a strong demand for senior unsecured debt in local capital markets and demand for longer dated money markets funding.*
- *Cost of liquidity remained broadly stable and well controlled. Funding taken on during 2010, when liquidity premiums were higher, continued to impact profitability.*

Key performance indicators

	30 June		31 December
	2011	2010	2010
	%	%	%
Long-term funding ratio	**26,8**	24,6	25,6
Loan-to-deposit ratio	**90,5**	95,5	91,9

Introduction

Liquidity risk is the risk that the Group is unable to meet its payment obligations when they fall due and to replace funds when they are withdrawn, the consequences of which may be the failure to meet obligations to repay depositors and to fulfil commitments to lend. Liquidity risk, more generally, is the risk that an entity will be unable to continue operating as a going concern due to a lack of funding.

Liquidity risk is inherent in all banking operations and confidence can be affected by a range of institution specific and market-wide events including, but not limited to, market rumours, credit events, payment system disruptions, systemic shocks, terrorist attacks and even natural disasters.

The appropriate and efficient management of liquidity risk by banks is of utmost importance in ensuring confidence in the financial markets and in ensuring that banks pursue sustainable business models, thereby fulfilling their key economic role of maturity transformation (i.e. the process by which banks transform deposits from customers, which tend to be of a shorter-term nature, into loans, which tend to be of a longer-term nature).

The efficient management of liquidity risk is essential to the Group to ensure:

- normal banking operations continue uninterrupted;
- the interests of all stakeholders in the Group are protected;
- financial market confidence is maintained at all times; and
- liquidity risk is managed in line with regulatory liquidity requirements at all times.

Strategy

The liquidity funding strategy of the Group is based on the following objectives:

- growing and diversifying the funding base to support asset growth and other strategic initiatives;
- further lengthening the Group's funding profile in order to continue improving key liquidity metrics and reducing the Group's liquidity risk exposure;
- continuing to build surplus liquid asset holdings in view of the Basel liquidity requirements; and
- focusing on lowering the weighted average cost of funding, within agreed parameters for liquidity risk.

Governance

Group Treasury is responsible for managing liquidity risk on behalf of the Group. As part of the overall liquidity risk management control process, independent oversight and regular independent reviews are conducted to assess the effectiveness of the function.

Group Treasury reports monthly to the MRC thereby ensuring a constant review of the liquidity position of the Group. The GRCMC, under delegated authority from the board, reviews and approves the control framework and policy for liquidity risk management.

Six months period in review

The close attention given to liquidity risk continued into 2011. The Group carefully monitored liquidity risk to ensure the management of the risk remained appropriate.

Wholesale funding tenor has shown an increasing trend during the period under review, with the long-term funding ratio reaching a level of 26,8% by the reporting date.

The loan-to-deposit ratio has reduced further due to solid core deposit growth combined with the Group's focussed loan strategy.

Liquidity risk

Six months ended 30 June 2011

Approach to liquidity risk

A dedicated team in Group Treasury implements the liquidity risk framework and policy and ensures liquidity risk is adequately managed across all BUs. Group Treasury also monitors and manages the Group's liquidity position to ensure full regulatory compliance in respect of liquidity risk management and reporting. Group Treasury takes cognisance of the contractual and business-as-usual liquidity positions, as well as of the liquidity position under stress.

Business-as-usual liquidity management

Business-as-usual liquidity risk management refers to managing the cash flows experienced by a bank in the course of conducting business. The business-as-usual environment tends to display fairly high probability, low severity liquidity events and requires balancing of the Group's day-to-day cash needs. Group Treasury focuses on a number of key areas, including:

» continuous management of net anticipated cash flows (between assets and liabilities) within approved cash outflow limits;

» active daily management of the funding and liquidity profile taking cognisance of the board-approved liquidity risk metrics designed to achieve the Group's business-as-usual liquidity risk tolerance and to position the bank to deal with stress liquidity events;

» maintaining a portfolio of highly liquid assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;

» active participation in local money and capital markets to support day-to-day funding needed to refinance maturities, meet customer withdrawals and support growth in advances;

» monitoring and managing liquidity costs; and

» constantly assessing and evaluating various funding sources to grow and diversify the Group's funding base in order to achieve an optimal funding profile and sound liquidity risk management.

Key risk metrics used in business-as-usual liquidity management

Risk metric	Purpose of metric
Short-, medium- and long-term funding ratios	Provides a measure of the contractual term of the funding used. For example, the long-term funding ratio shows the proportion of total funding that has a remaining contractual term in excess of six months.
Interbank funding ratio	Provides an indication of the extent to which reliance is placed on funding from other banks.
Short-term maturity cash flow mismatches (at a contractual and behavioural level)	Provides a measure of the extent to which cash flow mismatches occur in the short term (i.e. less than one month.
Cash outflow limits	Measures expected cash outflows against predetermined limits.
Concentration of deposits	Provides a measure of the extent to which reliance is placed on funding from certain customers or market sectors.

Stress liquidity risk management

Stress liquidity risk management refers to managing liquidity risk during times of unexpected outflows arising from Group specific or systemic stress events. Group Treasury regularly performs liquidity scenario analysis and stress testing to assess the adequacy of the Group's stress funding sources, liquidity buffers and contingency funding strategies to deal with such events. Scenario analysis and stress testing encompasses a range of realistic adverse events, that, while remote, could have a material impact on the liquidity of the Group's operations.

Through scenario analysis and stress testing, the Group aims to manage and mitigate liquidity risk by:

» determining, evaluating and testing the impact of adverse liquidity scenarios;

» identifying opportunities for rapid and effective responses to a crisis;

» setting liquidity limits, sources of stress funding and liquidity buffers as well as formulating a funding strategy designed to minimise liquidity risk. Group Treasury's overall objective is to ensure that, under a moderate to high liquidity stress event, the Group's stress funding sources and liquidity buffers exceed the estimated stress funding requirements for a period of at least 30 days. Stress testing and scenario analysis are used to evaluate the efficiency of identified sources of stress funding along a continuum of risk scenarios and to formulate and test contingency plans.

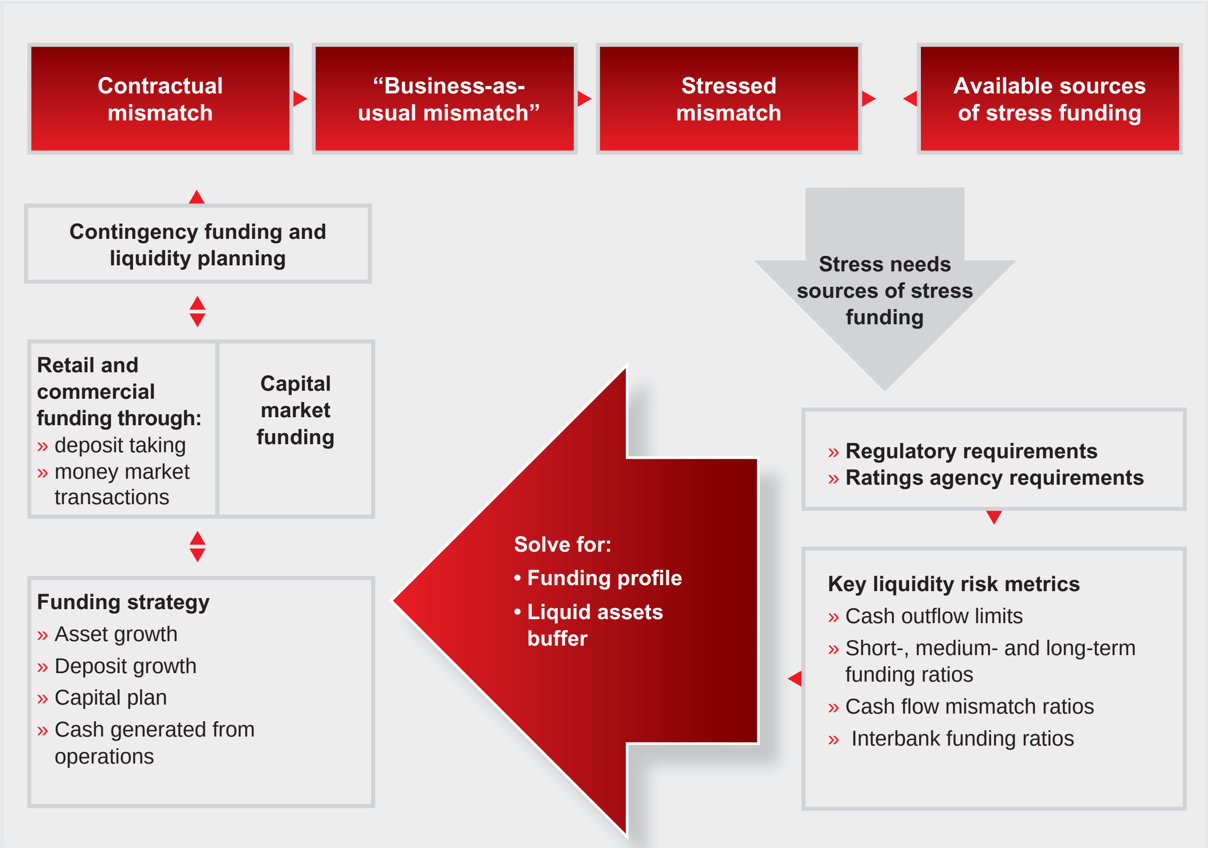
Key risk metric used in stress liquidity risk management

Risk metric	Purpose of metric
Survival horizon	Provides a measure of the adequacy of the bank's liquidity resources during times of stress, measured as the number of days that the bank is expected to survive a defined liquidity scenario.

A detailed Contingent Funding and Liquidity Plan (CFLP) has been designed to protect depositors, creditors and shareholders facing adverse liquidity conditions. The CFLP considers early warning indicators and sets out the crisis response strategy addressing sources of stress funding, strategies for crisis avoidance/minimisation and the internal and external communication strategy with key stakeholders. Liquidity simulation exercises are performed regularly to test the robustness of the CFLP and to ensure key stakeholders remain up to date on liquidity matters.

First half of 2011 in review *(continued)*

The liquidity risk management approach of Absa is summarised in the diagram below:



2011 liquidity risk disclosures

Regulatory changes in 2011

The focus given by management to the potential implications of the proposed Basel liquidity framework during 2010 continued unabated into 2011. The Group is participating in further Quantitative Impact Studies which have been released by the Basel Committee of Banking Supervision to fine-tune the calibration of the proposed liquidity ratios. The proposed Basel liquidity rules afford a large amount of discretion to national supervisors (i.e. the SARB). National Treasury has acknowledged that South African banks face a challenge in relation to the Basel liquidity framework as a result of the structural features of the South African economy in the document entitled "A safer financial sector to serve South Africa better". A task force was created by National Treasury and is currently working on ways in which parts of the financial system could be addressed in the light of the issues faced. Absa is an active participant in this (and other) initiatives regarding the potential impact of the Basel liquidity rules on the South African banking sector.

Banks are expected to start reporting information under the Basel liquidity framework from 2012, but compliance with the two key liquidity Basel ratios is only expected at a later stage as indicated in the table below:

Key metrics under Basel liquidity risk framework and timeframes or compliance

Risk metric	Purpose of metric	Compliance required by:
Liquidity coverage ratio (LCR)	To promote short-term resilience of a bank's liquidity risk profile by ensuring it has sufficient high-quality liquid assets to survive a significant stress scenario lasting for one month.	2015
Net stable funding ratio (NSFR)	To promote resilience over a longer time horizon (one year) by creating additional incentives for banks to fund their activities with more stable sources of funding on an ongoing basis.	2018

Six months ended 30 June 2011

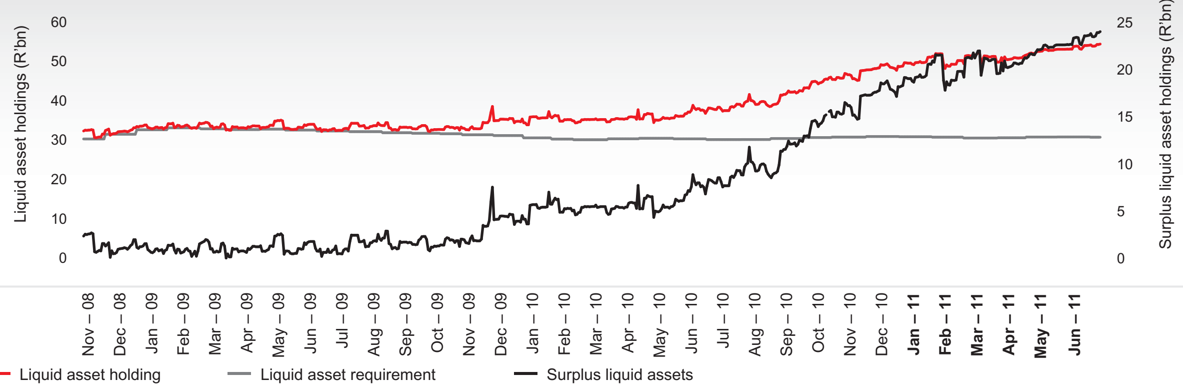
2011 Liquidity risk disclosures *(continued)*

The Group has further increased the amount of surplus liquid assets held and the funding term of its wholesale funding book during 2011 ahead of the timeframes for compliance with the Basel rules outlined in the table above.
More information on the progress made to date during 2011 and on the plans for the remainder of 2011 can be found in the sections that follow.

Surplus liquid assets held

The amount of surplus liquid assets held by Absa Bank Limited (defined as unencumbered liquid assets held in excess of the amount required to be held by law) have further increased during the period under review. As at the reporting date, R22 billion of surplus liquid assets was held in respect of Absa Bank Limited, an increase of R5 billion on the amount held at 31 December 2010. The further strengthening of the liquid assets position of the Bank is summarised in the graph below:

Summary of liquid asset holdings held by Absa Bank Limited over period 1 November 2008 to 30 June 2011

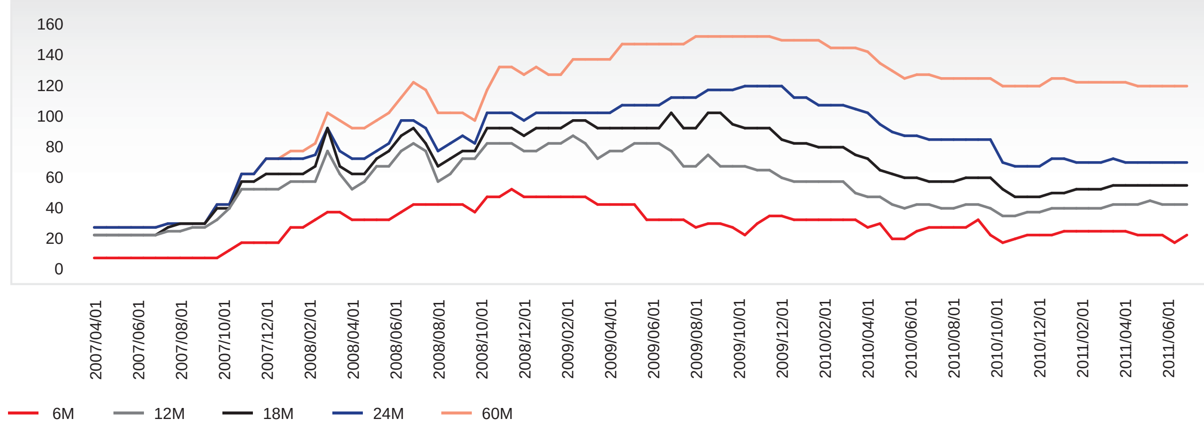


The cost of maintaining the liquidity pool of Absa Bank Limited (consisting of liquid assets held to comply with regulatory requirements, plus surplus liquid assets held over and above the minimum regulatory requirements) is a function of the cost of funding used to purchase the liquid assets compared with the return earned on the liquid assets purchased.

Cost of liquidity

The beginning of 2010 saw liquidity premiums (i.e. the excess return or 'premium' demanded by the market to invest funds with banks for longer periods of time than overnight) at historically high levels. As an example, the liquidity premium for 12-month funding was as high as 80 bps at the beginning of 2010. The graph below indicates that liquidity premiums remained high for most of 2010, meaning that South African banks had to secure funding for a large part of the year at cost levels far exceeding pre-crisis levels. The cost started reducing towards the end of 2010. During 2011 the cost of liquidity remained broadly stable. However, funding taken on during 2010, when liquidity premiums were higher, is still having an impact on profitability. The cost of liquidity is currently still higher than pre-crisis levels, especially for longer term funding.

Liquidity premiums (bps)

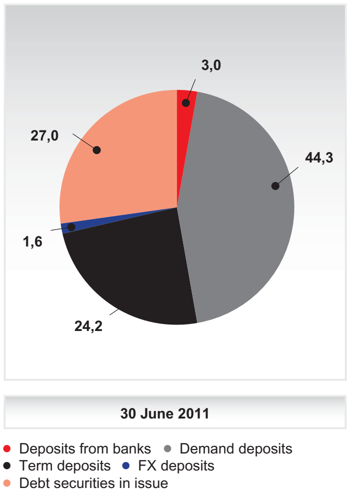


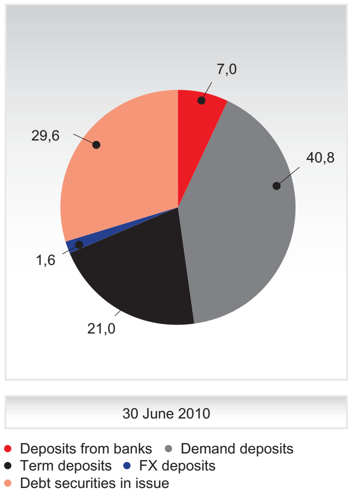
2011 Liquidity risk disclosures *(continued)*

Funding structure

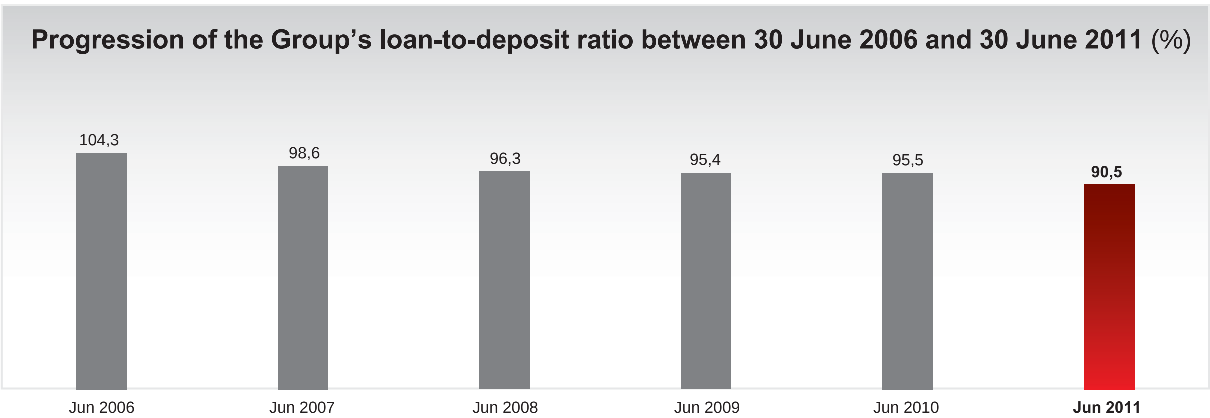
At the reporting date, Retail Banking remains partly funded by retail deposits, whereas ABB remains in a self-funded position. The Group places reliance on wholesale funding markets for the balance of funding required, and Absa Capital acts as the Group's 'face to the market' for obtaining the required wholesale funding. The reliance on wholesale funding has reduced over the past 12 months as can be seen from the analysis below:

Summary of funding composition (%)





The progression of the loan-to-deposit ratio of the Group is summarised in the graph below. The ratio has improved by 5,0% during 2011, as a result of solid core deposit growth combined with the Group's focused loan strategy.



Six months ended 30 June 2011

2011 Liquidity risk disclosures *(continued)*

A more detailed breakdown of the loan-to-deposit ratio for the Group is provided in the table below:

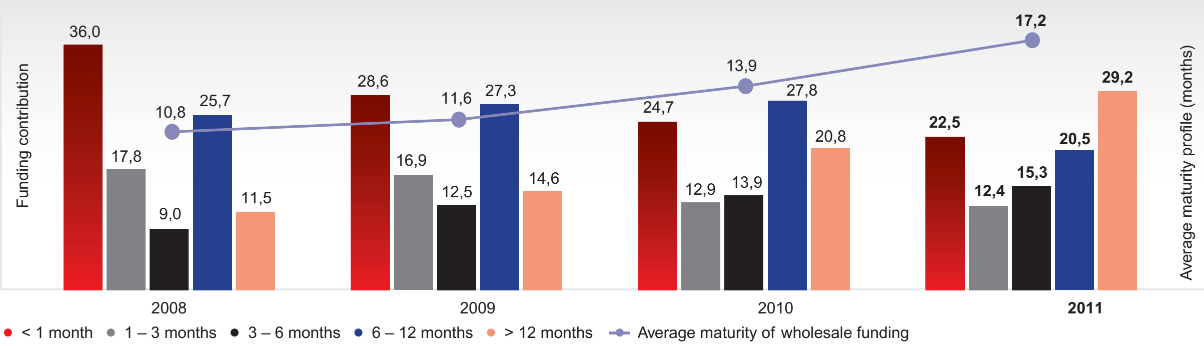
Loan-to-deposit ratio breakdown of assets and deposits

	30 June 2011 Rm	2010 Rm
Advances		
Loans and advances to customers	**495,5**	500,0
Deposits		
Deposits due to customers	**398,3**	359,9
Debt securities in issue	**148,5**	163,7
	546,8	523,6
Ratio	**90,5**	95,5

Lengthening the funding profile of the Group's funding base is a key strategic aim. Despite structural constraints in the South African economy which limit the extent to which South African banks are able to lengthen their funding profiles, the Group continued to take steps during 2011 to further lengthen the funding profile within these constraints.

The graph below summarises the extent to which Absa Bank Limited has been able to extend its wholesale funding profile since 30 June 2008. The weighted average remaining term of wholesale funding has continued to increase and reached a level of 17 months as at the reporting date. The proportion of wholesale funding that has a term in excess of 12 months has also seen a marked increase over the past 12 months, from 20,8% at 30 June 2010 to 29,2% at 30 June 2011.

Progression in wholesale funding composition of Absa Bank Limited as at 30 June (% and months)

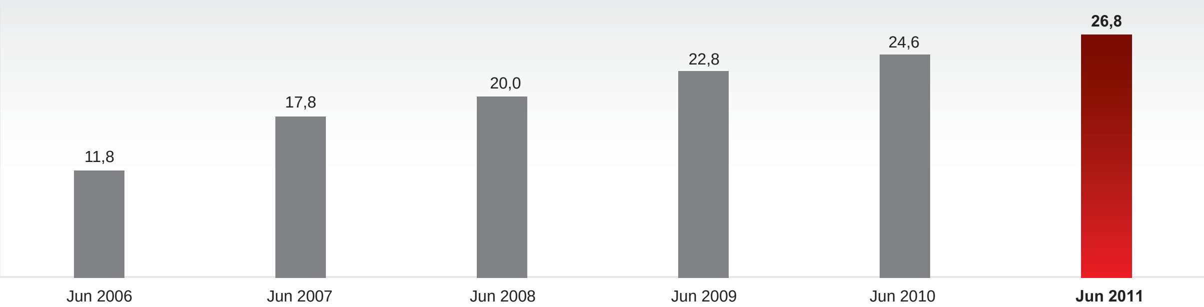


A key metric used to track the funding structure of Absa Bank Limited is the long-term funding ratio, which reflects the proportion of total funding which has an outstanding term in excess of six months. The progression in Absa Bank Limited's long-term funding ratio is shown below. From this analysis a marked improvement in funding structure is evident, with an increase in the average long-term funding ratio of 2,2% over the 12 months ending 30 June 2011.

Six months ended 30 June 2011

2011 Liquidity risk disclosures *(continued)*

Average long-term funding ratio for Absa Bank Limited as at 30 June (%)

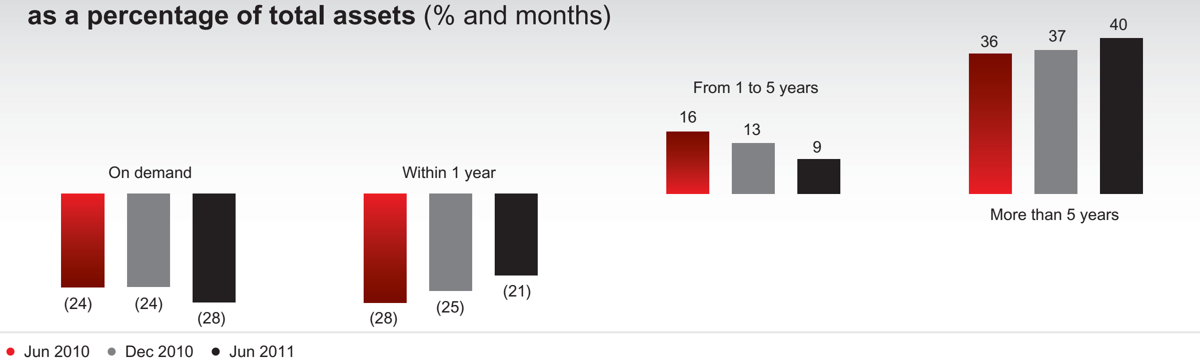


Capital markets funding is used as a further tool for the extension of the funding term of the Group. The Group has successfully issued R5,9 billion of senior unsecured debt in the capital markets during the 6 months ending 30 June 2011.

Contractual and behavioural liquidity mismatch positions

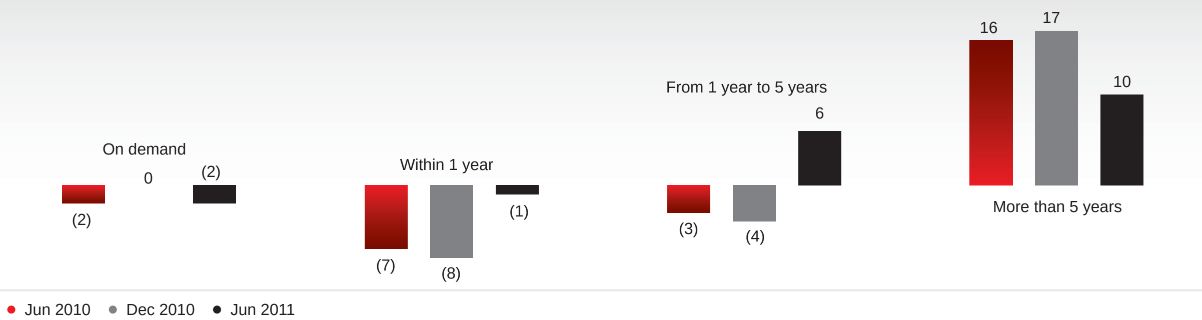
The graph below summarises the contractual mismatch position in respect of Absa Bank Limited. The contractual mismatch position over one year has improved during 2011 due to prudent liquidity management practices and a further extension in funding term.

Contractual mismatch position of Absa Bank Limited as at the reporting date, expressed as a percentage of total assets (% and months)



Behavioural (business-as-usual) mismatches are managed within board-approved limits. The behavioural mismatch position has shown significant improvements in 2011, despite the challenging economic environment.

Behavioural mismatch position of Absa Bank Limited as at 30 June, expressed as a percentage of total liabilities to the public (%)

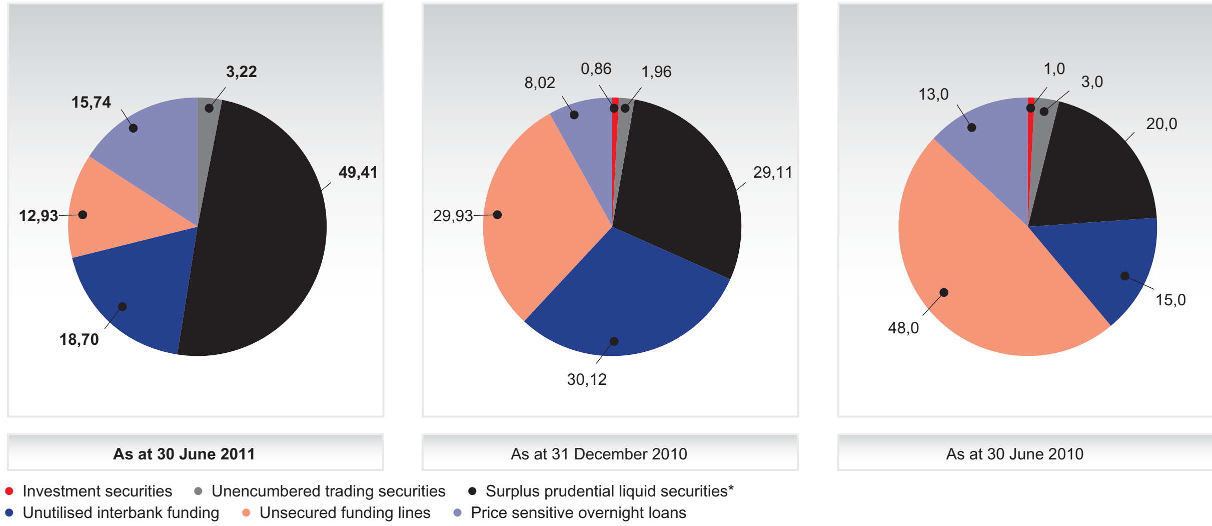


Liquidity risk disclosures *(continued)*

Stress and scenario testing

As at the reporting date, Absa's survival horizon was well in excess of internal limits, with sources of stress funding exceeding funding required. The steps taken during 2010 to reduce reliance on unsecured funding sources and to increase surplus liquid assets held, was continued into 2011. The graphs below show Absa's sources of stress funding as at 30 June 2010 and 30 June 2011. Note that the graph only shows the composition of liquidity resources over and above statutory liquidity requirements.

Summary of sources of stress funding in respect of Absa Bank Limited (%)



Focus going forward

Liquidity risk measurement and management continued to receive attention globally during the period under review. This attention is expected to continue for the second half of 2011 as well as into 2012. Although the final Basel rules afford banks a period of time before full compliance is required, the Group will maintain its focus on liquidity risk and further strengthen its liquidity risk position ahead of Basel III, to ensure full compliance within the required timeframes.

Operational risk

Six months ended 30 June 2011

Highlights

- *The Group maintained the AMA approval.*
- *Focus on control enhancements continued with emphasis on financial and violent crime, anti-money laundering measures, technology controls and effective business continuity.*

Introduction

Operational risk is the risk of direct or indirect losses resulting from inadequate or failed internal processes or systems, human error or external events. Operational risk exists in the natural course of business activity.

Strategy

Operational risk is managed under the operational risk management framework adopted by the Group, which is an ancillary framework of the Group's overall risk management framework. The AMA to operational risk is applied throughout the Group, with the exception of Absa's African operations and certain small entities.

The objective of the operational risk management framework is to ensure the Group manages operational risks in an optimal and consistent manner making certain these risks are measured accurately and the Group is adequately capitalised.

Governance

Operational risk is governed by means of a clear hierarchy of governance committees. These committees include BU, segment and Group level operational risk committees, segment and Group level GCC's as well as the GRCMC at board level. Operational risk processes also form an inherent part of the internal audit process.

Approach to operational risk

The Group manages operational risk through the PRP, which consists of clearly defined individual frameworks.

The aim in managing operational risk is to increase the efficiency and effectiveness of the Group's resources, and to make use of growth opportunities while minimising operational risks.

Six months period in review

The recent focus on the control environment in the Group was evident, in that losses remained fairly stable (with a slight downward trend). Large losses remained well under control with a clear improvement seen during 2011.

The Group implemented major control improvements during the period under review as part of the continued focus on control enhancements. Some of these improvements were as follows:

- technology related controls were reviewed and enhanced;
- the fraud oversight process was further embedded, which process combines ongoing investigation with the lessons learnt;
- focus on the control environment of the Africa businesses', specifically on crime and technology; and
- all critical processes and systems have been appropriately catered for and secured to protect against any disaster or other forced break in normal operations.

Financial crime remained one of the primary risks of the Group, while the risk of failures in the execution of processes remained secondary risks. An integrated approach to these risks adopted in 2010 continued through the period under review. People risk, a main focus area during the previous financial year, remained a priority. The tough economic climate, combined with other pressures such as increased complexity in the work environment, lack of skills and increasing regulation meant the Group faced higher risks than usual in this environment.

Six months ended 30 June 2011

2011 Operational risk disclosures

Basel II measurement elected

The Group has elected to measure operational risk by using the AMA. The AMA approach is applied to the majority of the BUs in the Group. A few small entities are still measured using the SA and Basic Indicator Approach (BIA).

Capital modelling

The model used to determine the Group's operational risk capital was rigorously reviewed, validated and approved in accordance with the Group's model risk governance processes. Operational risk capital is allocated on a risk-sensitive basis to segments and BUs in the form of EC charges, thereby improving controls and the management of these risks within appetite levels.

The AMA capital model methodology has been used consistently since 2008. The AMA model follows a key risk scenario-based approach that uses internal and external loss data.

Key risk scenarios (KRSs) are the main drivers of the model. The Group believes this is currently the most effective way to measure unexpected losses. KRSs also provide a forward-looking view of operational risk.

Coverage of the AMA model

The AMA model is used Group-wide to calculate EC and RC. The exceptions to this approach include:

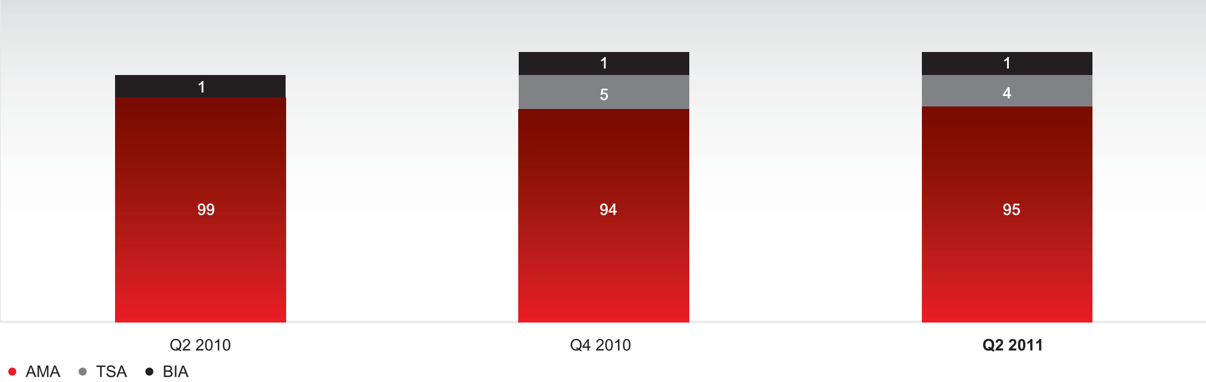
» joint ventures and non-controlling interests where the Group is unable to dictate the operational risk framework or capital methodology;

» any cross-border legal entities where local regulatory policy/requirements either do not permit the use, or do not support the practical implementation of the AMA model; and

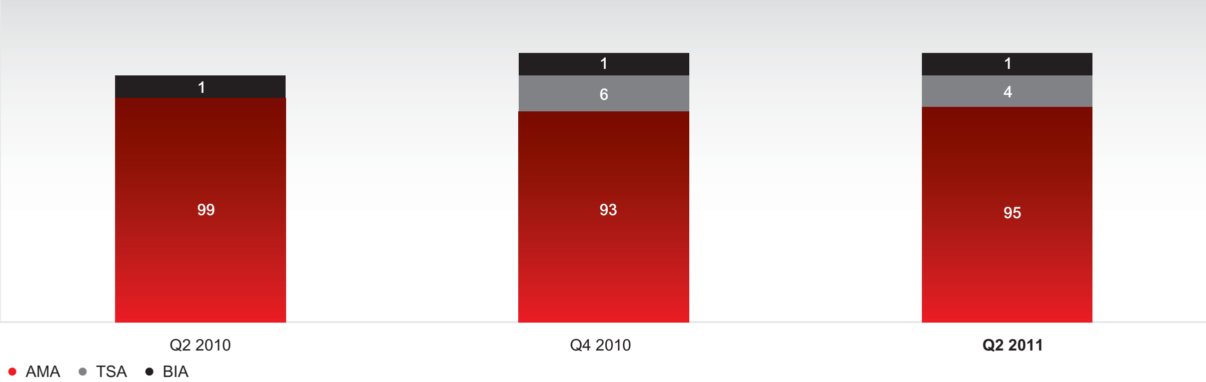
» certain subsidiaries where partial AMA (SA/BIA) is applied.

The AMA model implies excellence in the management of operational risk and, as and when appropriate, the Group aims to achieve maximum coverage using the AMA model.

Economic capital (%) by approach for operational risk



Required capital (%) by approach for operational risk



2011 Operational risk disclosures *(continued)*

Insurance mitigation

Insurance is used as a mechanism to mitigate operational risks. The Group's Short-Term Insurance Committee (STIC) is responsible for insurance design and for managing the principal insurance programmes that mitigate key aspects of the Group's operational risk. The STIC ensures these policies are current and remain applicable to the Group's operating environment. The STIC also oversees more specific insurance cover purchased at Group or segment level to discharge statutory and regulatory duties, or to meet counterparty commitments and stakeholder expectations.

The primary insurance policies purchased by the Group are:

» comprehensive crime and electronic crime;

» directors' and officers' liability;

» professional indemnity; and

» various asset policies.

Reporting of Pillar 3 and IFRS requirements in relation to operational risk (I2)

The Group recognises the significance of operational risk and is committed to enhancing the measurement and management of operational risk. Within the Group's operational risk framework, qualitative and quantitative methodologies and tools are applied Group-wide to identify and assess operational risks and to provide management with information for determining appropriate mitigating measures.

Focus going forward

Operational risk remains a key priority for the Group and for the rest of the year, the following are key areas of focus:

» minimising financial crime through enhancements in automation of key controls to minimise and reduce loss producing activities;

» increasing automation to enhance business and to ensure the Group keeps pace with ever-changing technologies, such that customers ultimately benefit from these changes;

» procuring compliance with changes in the regulatory landscape as well as ensuring the changing legislative landscape is fully utilised to reap rewards intended for all stakeholders; and

» enhancing talent retention and recruitment practices through the launch of various innovative retention and training strategies.

The board and senior management will continue to put the necessary emphasis on the management of operational risk through consistent implementation and monitoring of policies, processes and systems in all material products, services and activities, in line with an approved risk appetite and tolerance levels.

Regulatory risk

Six months ended 30 June 2011

Highlights

- *Successful integration of new processes and procedures into operations to comply with recent laws and regulations.*
- *Focus on control enhancements in respect of regulatory risk.*
- *Continued focus on enhancing controls relating to anti-money laundering, anti-terrorist financing and anti-bribery and corruption.*

Introduction

Regulatory Risk arises from a failure or inability to comply with applicable laws, regulations and/or supervisory requirements. Non-compliance could lead to penalties, censure, criminal prosecution or loss of licence to operate.

Strategy

Regulatory risk is managed under the Group Compliance Policy and the Regulatory Risk Control Framework.

The objective of the Compliance Risk Management Framework is to provide a framework within which management and the Absa Compliance Function can operate in order to reinforce a compliance culture throughout the Group and to ensure the Group manages its regulatory risk on an ongoing basis.

Governance

Regulatory risk forms an inherent part of the Group's governance processes. Oversight and monitoring is provided by cluster level governance and control committees, the GCCs, the GACC and the board of directors.

Six months period in review

The following were the main areas of focus for the period under review:

- in line with the Group's ongoing focus on controls, the Group Compliance function continued to assist management with enhancing controls relating to regulatory risk;
- anti-money laundering, anti-terrorist financing, anti-bribery measures and corruption and sanctions remained an important focus area for the Group; and
- steps were successfully taken to integrate new regulatory requirements, including the Companies Act and the Consumer Protection Act.

Focus going forward

Following the financial crisis, there has been greater regulatory scrutiny and an increase in regulatory requirements worldwide. This trend is expected to continue well into the future. The Group is well placed to manage the new requirements and will continue to enhance its control environment in respect of regulatory risk.

Six months ended 30 June 2011

Highlights

» *Progress has been made on capital model development in the short-term insurance environment and use of results on Own Risk and Solvency Assessment discussions with business.*

» *Revised asset allocations have been implemented in the Absa Life investment portfolios following an asset-liability modelling exercise conducted in 2010.*

» *Insurance risk taken on in Absa Life Botswana with effect from 1 March 2011.*

» *Selective disinvestment by Absa Life Limited from equities resulted in reduced investment risk exposure.*

Key performance indicators

	30 June		31 December
	2011	2010	2010
	%	%	%
Short-term loss ratio	**68,2**	67,1	69,9
Value of Absa Life new business margins	**8,5**	7,2	6,6
Return on shareholders' assets versus benchmark	**2,3 vs 2,6**	2,8 vs 0,2	13,8 vs 10,7

Introduction

Insurance risk, from management's perspective, is the risk that future claims and expenses will exceed the allowance for expected claims and expenses in the estimation of policyholder liabilities and in product pricing.

Within the Group, life insurance underwriting activities are undertaken by Absa Life Limited, Absa Life Botswana Limited and Woolworths Financial Services (Proprietary) Limited through an Absa Life cell captive. Short-term insurance underwriting activities are undertaken by Absa Insurance Company Limited, Absa Insurance Risk Management Services, Absa *idirect* Limited and Absa Manx Insurance Company Limited (Absa Manx). The nature of the operations of these entities gives rise to four types of insurance risk:

» short-term insurance underwriting risk;

» life insurance underwriting risk;

» life insurance mismatch risk; and

» life and short-term insurance investment risk (including interest rate, foreign exchange and equity investment risk).

Strategy

The insurance entities listed above actively pursue profitable growth opportunities that provide diversification of underlying risks. By diversifying the nature of the insurable interest, the insurance entities reduce their exposure to certain insurance risks and also reduce the risk of many claims arising from the same event.

In particular:

» there is a focus on seeking sources of business that complement the traditional bancassurance products by providing diversification benefits;

» agricultural insurance provides a diversification benefit in relation to property insurance as it is impacted differently by weather patterns; and

» risk exposures in the rest of Africa may have a low or potentially negative correlation versus corresponding South African risks.

There is a high level of focus on enhanced risk management to ensure the insurance entities understand and manage existing risks, and that appropriate consideration is given to the risks related to potential new business lines. The continued internal focus on enhanced risk management will ensure the insurance entities are prepared for the developing Solvency Assessment and Management legislative environment.

Governance

The boards of directors, together with management, of the insurance entities, take primary responsibility for the management of short-term insurance underwriting risk, life insurance underwriting risk, life insurance mismatch risk and investment risk.

In terms of the principal risk control framework, management identify, assess, control, manage and report on all risks related to insurance underwriting, mismatch and investments. Within the bancassurance cluster, the Absa Financial Services Governance and Control Committee and the Capital and Investment Risk Committee, as well as the Actuarial Review Committees and Capital and Investment Committees, are responsible for monitoring risk management, control effectiveness and principal risk reporting across all insurance entities.

Insurance risk *(continued)*

Approach to insurance risk

Underwriting risk, life insurance mismatch risk and investment risk are core to the business of the insurance entities.

The successful management of these risks is fundamental to the success of the insurance entities. Short-term insurance underwriting risk is managed through underwriting authority mandates and by referral to an Underwriting Review Committee, when required. Risk governance is monitored through the entity and Absa Financial Services Governance and Control Committees, the Actuarial Review Committee and Principal Risk reporting.

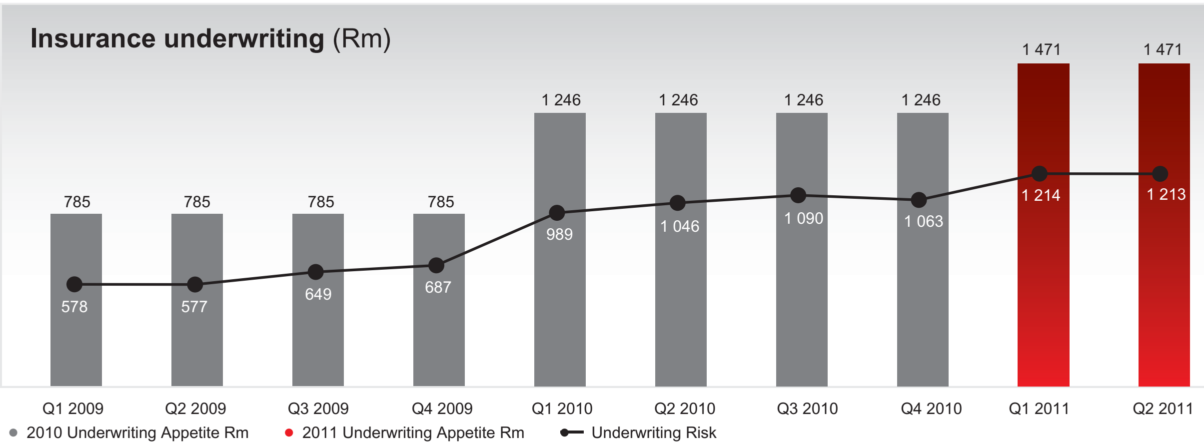
An Underwriting Risk Forum monitors life insurance underwriting performance and quality on a monthly basis to ensure risk taken is in line with risk priced and reserved for. Risk governance is monitored through the entity and Absa Financial Services Governance and Control Committees, the Actuarial Review Committee and Principal Risk reporting.

A monthly Investment Risk Committee meeting monitors life insurance mismatch risk. A quarterly review is undertaken, conducted by the Absa Financial Services Capital and Investment Risk Committee and the Actuarial Review Committee. Monthly entity Investment Risk Committee meetings monitor investment risk across the insurance entities. A quarterly review is undertaken by the Absa Financial Services Capital and Investment Risk Committee and the Actuarial Review Committees.

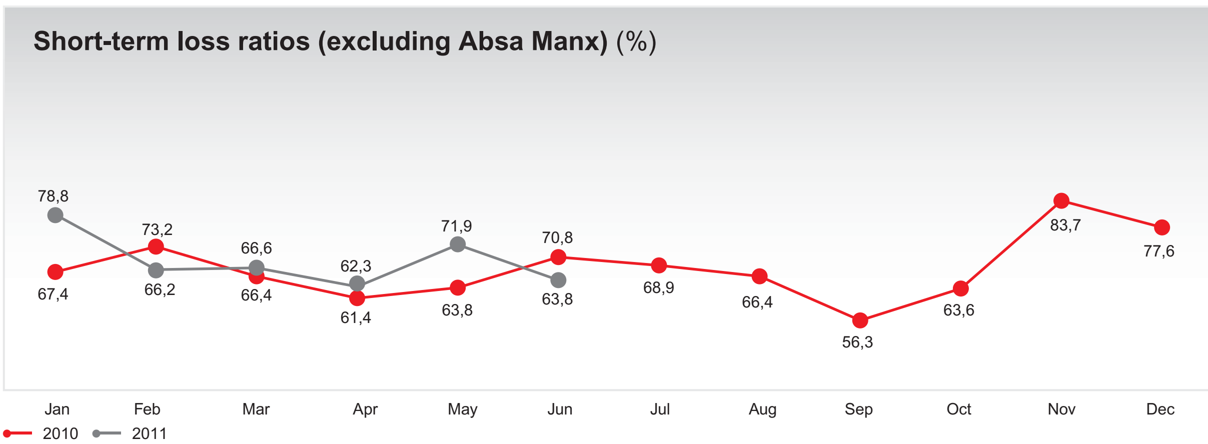
Six months period in review

All risk types have remained well within appetite limits. Re-alignment of Absa Life portfolios to revised asset allocations has proceeded in line with plan. Disinvestment from Absa Life equities has resulted in a decrease in investment risk. Progress has been made on capital model development in the short-term insurance environment and use of results in Own Risk and Solvency Assessment discussions with business.

Short-term and life insurance underwriting risk utilisation was monitored quarterly against the appetite set for the year. Utilisation varied as expected in line with underlying business growth, and remained within appetite throughout the period under review.



Short term insurance loss ratios decreased from January to February, but increased in May due to adverse experiences in agricultural insurance.

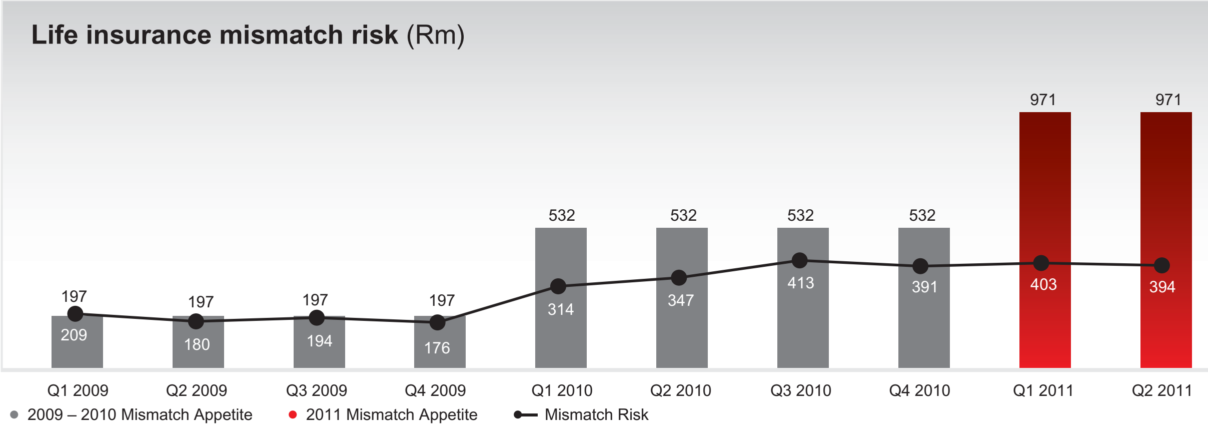


Six months ended 30 June 2011

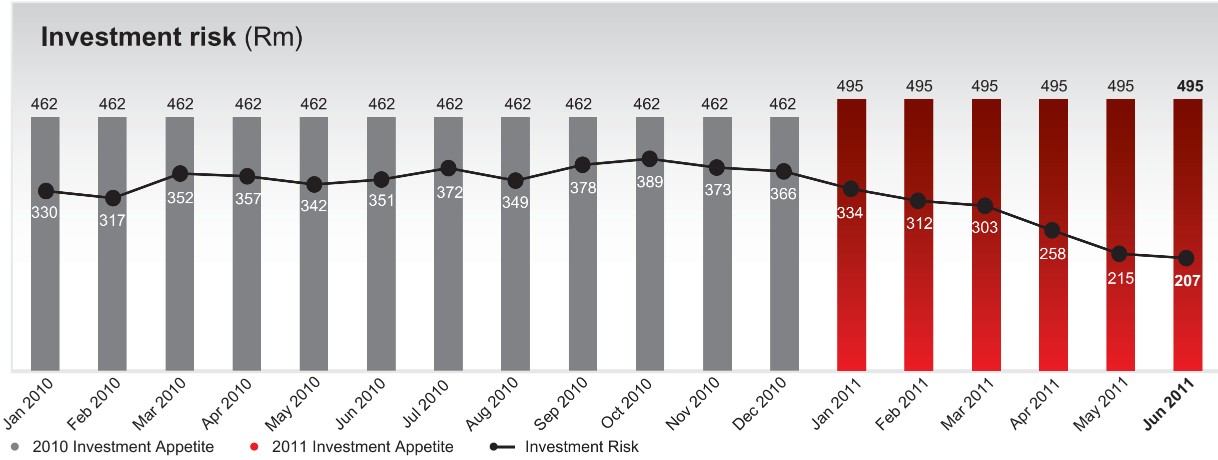
Six months period in review *(continued)*

Life Insurance Mismatch Risk

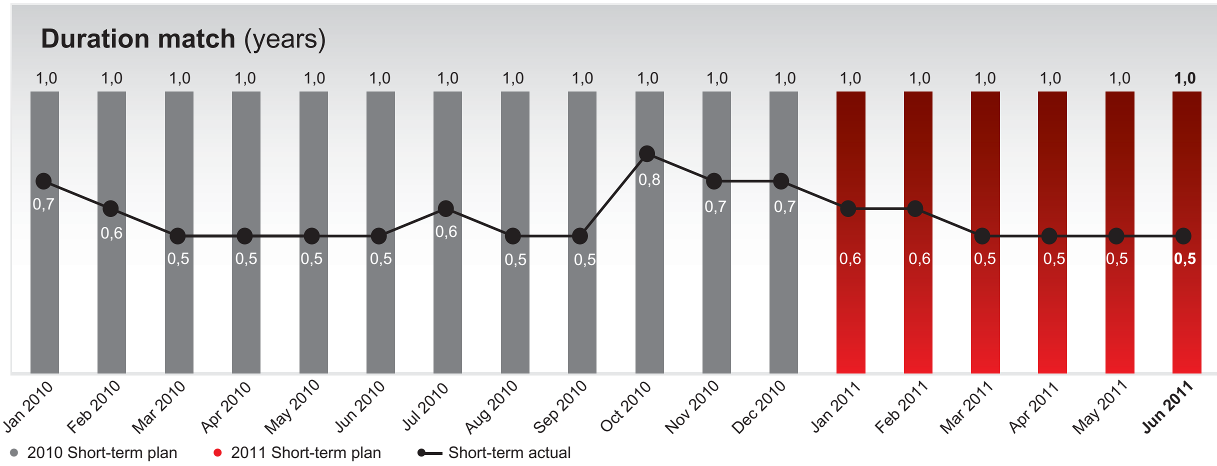
Life insurance mismatch risk was well within appetite for both quarters due to benign investment conditions.



Investment risk decreased significantly over the period under review, in particular due to disinvestment from equities held by Absa Life. Only one equity hedge now remains, which will expire in September 2011.



The duration of the interest bearing investments backing policyholder liabilities remained within limit for short-term insurance assets.



2011 Insurance risk disclosures

Underwriting risk is influenced by the type and nature of insurance activities undertaken and is impacted by:

» the risk appetite of the insurance entities;
» the nature of underwriting exposures underlying the products and services;
» portfolio characteristics; and
» the nature and extent of reinsurance cover.

2011 Insurance risk disclosures *(continued)*

Underwriting risk is monitored separately for the short-term insurance and life insurance entities.

Short-term insurance underwriting risk describes the risk associated with the underwriting of fixed and/or moveable assets, accidents, guarantees and liabilities.

Monthly monitoring of loss ratios identifies portions of the business where claims are increasing versus underlying rates. This may result in a review of required rate changes or changes to policy conditions. Volumes of business are monitored for increases in volumes out of line with management expectations indicating that rates may be low versus the market. Extensive claims control measures are in place including assessment of claims, checks of total potential claim versus sum insured (averaging), and bulk procurement.

Risk management per product line	**Homeowners comprehensive insurance**	Multiple, similar claims make claim rates more predictable in normal circumstances. Assessment and adjustment of potential claims is undertaken. Cover is included in the catastrophe reinsurance purchase.
	Personal lines, accident and travel insurance	Scientific pricing using multiple risk factors is used in risk selection and to charge premiums matched to underlying risk. Assessment and adjustment of potential claims is undertaken. Cover is included in the catastrophe reinsurance purchase.
	Commercial insurance for small, medium and large companies	In underwriting these risks, significant focus is placed on the quality of fire protection and other risk measures. Assessment and adjustment of potential claims is undertaken. Catastrophe reinsurance is purchased to protect against natural catastrophes, in particular earthquakes and against large individual losses.
	Agricultural insurance	Diversification is sought across crops, seasons and geographical regions. Stop loss reinsurance is in place to protect against excessive claims. Risks are individually underwritten before being taken on. Constant assessment of crop development and then adjustment of potential claims is undertaken.
	Specialist lines	Risks underwritten by Underwriting Management Agencies are only undertaken with specialists in their respective areas with track records of underwriting and claims control. Reinsurance for relevant risks is included in the main or specific reinsurance treaties.
Reinsurance	The impact of large individual claims is limited through low retention levels per risk with the balance being protected through reinsurance. The accumulation of net exposures due to multiple claims is limited through the purchase of catastrophe reinsurance. Catastrophe reinsurance, particularly related to earthquake risk, is purchased to cover losses of up to R2,8 billion.	
Reinsurer credit risk	Credit risk in respect of reinsurance partners is managed by transacting with a wide range of reinsurers, and only reinsurers with good credit ratings. The creditworthiness of reinsurers is considered on an annual and ongoing basis. Reinsurers must be assigned a minimum ‘A’ rating by Standard and Poor’s (or equivalent rating by Moody’s or A.M. Best). Management must approve any exceptions to this rating with notification to the boards of directors of the respective insurance entities.	
Concentration risk	The main concentration risk arises from exposure to personal and commercial business in Pretoria, Johannesburg and the East Rand. These exposures are reduced significantly through reinsurance protection. The maximum expected loss for a one in 250 year event is a loss of R2,8 billion.	

2011 Insurance risk disclosures *(continued)*

Life insurance underwriting risk describes the risk associated with insuring the life and/or health of individuals or groups of individuals.

The number of risks falling outside of set underwriting mandates is reviewed to determine whether underwriting rules need to be tightened or risk parameters reviewed. Annual experience studies and analysis of surplus enable the actual experience to be investigated. The non-economic pricing and reserving bases (i.e. mortality, morbidity, persistency and expense assumptions) are revised for any changes in trends that are considered to be sustainable in future.

Risk management per product line	**Mortgage protection and complex underwritten life business**	The main risks are mortality and morbidity. This is the only life insurance business that is individually underwritten. Premium rates differentiate by gender, age, smoker status, socio-economic class and occupation. Sub-standard risks generally receive additional premium loadings or are declined. Correct pricing and effective underwriting control the mortality and morbidity risks. Exposure in excess of a retention limit for each policy is reinsured to reduce the variability of the claims experience and the exposure to a single life. Most policies have premium guarantee terms that vary from one year *(for yearly renewable business)* to 25 years (*for products that have an investment component attached*). For products with an investment component the overall premium rate is guaranteed but the investment portion is not guaranteed and could be reduced at the discretion of Absa Life. However, it is a company policy when products are priced to have no intention to increase premium rates over the policy term. Experience is monitored to confirm that actual experience is in line with pricing assumptions.
	Funeral business	The main risk is mortality, increased by high Aids rates experienced in the target market. The risk is exacerbated by premium rates that are the same irrespective of the age of policyholders since significant changes in the age profile of customers could impact on experience. Limitation of cover for certain pre-existing conditions for defined time periods (*generally two years*), applies. Strict experience monitoring limits the risk, combined with the contractual right to increase premiums with a three month notice period. The intention is not to exercise this right, but the Group does have the option to do so. Reinsurance is not used as sums assured per individual life are minimal.
	Credit life business	The main risks are retrenchment and mortality. Treaty reinsurance arrangements are in place whereby risk is shared with external business partners. The right to change premiums with a 30 day notice period is retained. Premiums generally do not differentiate by gender, age or smoker status and demographic shifts could introduce additional insurance risk.
	Group life business	The main risk is mortality risk. Treaty reinsurance arrangements are in place whereby risk is shared with external business partners. Contracts and premium rates are reviewable annually. Additional catastrophe reinsurance cover will be considered for accumulation of losses that may occur due to the geographical concentration of a group.
Reinsurance	A formal reinsurance policy has been approved by the board of directors of Absa Life. Reinsurance is used for large individual risks, for risks where Absa Life needs to build knowledge and experience, and to obtain technical assistance. Catastrophe reinsurance is used for protection against a large number of dependent losses.	

2011 Insurance risk disclosures *(continued)*

Reinsurer credit risk	Reinsurer credit risk is managed by transacting solely with reinsurers that have good credit ratings, and by holding additional capital in line with regulatory requirements. Although a parental guarantee is not in place for all companies, they are all 100% subsidiaries of their international parent companies and operate under the same name, effectively ensuring a parental guarantee. Reinsurers' ratings, notified disputes and collection experience are used to determine if any reinsurance assets should be impaired. As at the reporting date the reinsurance assets were unimpaired as none of the reinsurance amounts receivable were past due.
Concentration risk	Little concentration of insurance risk exists in respect of individual lives, and liability exposure is well spread geographically. Concentration in terms of size of individual policies is low and retention limits are in place with excess reinsurance to cover large individual exposures. In the case of group life business, geographical concentration of risk potentially exists. In addition to comprehensive quota share reinsurance, catastrophe reinsurance is used to provide protection against accumulation of losses on retained risks.

Life insurance mismatch risk describes the risk that the profile of assets held to back Absa Life policyholder liabilities is inappropriate to match the profile of those liabilities.

Mismatch risk is quantified by determining the extent to which assets fall when compared to the liabilities when market conditions change.

Mismatch risk	The mismatch risk arising in respect of Guaranteed Maturity Value (GMV) reserves is managed in terms of the requirements prescribed by the Actuarial Society of South Africa (ASSA) in PGN110.
Interest rate risk	Interest rate risk is managed by setting and monitoring asset durations versus targeted levels for the interest bearing investments backing the rand reserves and GMV reserves. Monthly meetings are held with the asset manager to monitor duration versus targets.

Life and short-term investment risk describes the risk associated with changes in asset values and includes interest rate, foreign exchange and equity investment exposures.

Investment risk is monitored by performing regular asset liability matching exercises, monitoring market volatility, comparing actual performance with benchmark performance, and monitoring mandated asset allocation, tracking errors and durations of fixed interest assets. Investment risk is further monitored by measuring and comparing the actual risk exposure in terms of economic capital to an approved limit, based on a value-at-risk calculation.

Investment risk is mitigated through diversified asset allocations appropriate to underlying liability profiles, investment mandates and the hedging of equity risks.

Short-term insurance investment risk	A single investment strategy is maintained for short-term insurance shareholder assets and for assets backing short-term insurance policyholder liabilities. Assets are invested in short dated interest bearing assets and preference shares. The duration of interest bearing assets is monitored against a maximum effective duration.
Life insurance investment risk	The Absa Life insurance shareholders' funds are invested in a balanced portfolio. Revised asset allocations are being implemented in 2011 following a comprehensive asset liability matching exercise conducted in the last quarter of 2010. Domestic assets have a limit on active equity exposures. Hedging strategies are followed in respect of domestic equities.
Counterparty credit risk	Counterparty credit risk in respect of investments is managed by investing with a spread of issuers with good credit ratings. Counterparty credit risk in respect of equity hedging instruments is managed by transacting only with counterparties with good credit ratings.
Liquidity risk	The short-term insurance businesses invest mainly in short dated interest bearing assets, with limits on investments in less liquid assets such as preference shares and corporate bonds. The life insurance businesses are less exposed to liquidity risks due to low risk of large cumulative claims. Liquidity risk is managed through close management of potential cash outflows in discussion with the asset manager.

Focus going forward

The insurance entities will continue to focus on the enhancement of short-term insurance underwriting discipline, the monitoring of concentration risk and on business growth opportunities that support diversification of underlying risks.

The development of risk utilisation methodologies will continue, with an aim of enhanced monitoring of risk appetite and capital requirements across the insurance businesses for both earnings impacts and solvency requirement reporting.

Representatives of the insurance entities will keep abreast of developments through representation on the three pillars of the Solvency Assessment and Management project. Deadlines will be met as required in respect of potential application for partial approval of the short-term insurance internal model, and submission of Quantitative Impact Study results.

Investment strategies that enhance management of life insurance mismatch risk will continue to be reviewed.

Glossary

Abbreviations and acronyms used in the Absa Group Pillar 3 risk disclosures for the six months ended 30 June 2011.

A

Abacas	Asset Backed Collaterised Securities (Proprietary) Limited
ABB	Absa Business Bank
AbCap	Absa Capital
AEaR	annual earnings at risk
AIC	Absa Insurance Company LImited
Aids	acquired immune deficiency syndrome
AIRB	Advanced Internal Ratings Based
Alco	Group Alco and Balance Sheet Management Committee
AMA	Advanced Measurement Approach
ASSA	Actuarial Society of South Africa

B

Basel II	Basel II Capital Accord
BBBEE	broad-based black economic empowerment
BBM	Barclays Bank Mozambique S.A.
BFC	Board Finance Committee
BIA	Basic Indicator Approach
bps	basis points
BU	business unit

C

CA	Companies Act 71 of 2008
CAGR	compound annual growth rate
CAPM	capital asset pricing model
CAR	capital adequacy requirement
CFLP	contingency funding and liquidity plan
CMMC	Credit Model Monitoring Committee
COC	cost of required capital
CoE	cost of equity
CoRC	Concentration Risk Committee
CPA	Consumer Protection Act 68 of 2008
CPF	Commercial Property Finance
CRC	Credit Risk Committee
CRM	credit risk mitigation
CRO	Chief Risk Officer
CRTC	Credit Risk Technical Committee

D

DG	default grade
DVaR	daily value at risk

E

EAD	exposure at default
EC	economic capital
ECAI	external credit assessment institution
EL	expected loss
EMC	Executive Model Committee
EWL	early warning lists
Exco	Executive Committee

F

FASSA	Fellow of the Actuarial Society of South Africa
FICA	Financial Intelligence Centre Act, No 38 of 2001
FIRB	Foundation Internal Ratings Based
FSB	Financial Services Board

Reference tools

Six months ended 30 June 2011

G	
GACC	Group Audit and Compliance Committee
GCE	Group Chief Executive
GGCC	Group Governance and Control Committee
GIC	Group Investment Committee
GHV	Guaranteed maturing value
GRCMC	Group Risk and Capital Management Committee

H	
HIV	human immunodeficiency virus

I	
ICAAP	internal capital adequacy assessment process
IFRS	International Financial Reporting Standards
IMA	Internal Models Approach
Insurance	Short-term Insurance
IRB	Internal Ratings Based

J	

K	
King II	King Report on Corporate Governance for South Africa, 2002
King III	Code of Governance Principles for South Africa, 2009
KPI	key performance indicators
KRSs	key risk scenarios

L	
LGD	loss given default
Life	life insurance
LTV	loan-to-value

M	
MRC	Market Risk Committee
MRP	market risk policy
MTM	mark-to-market

N	
NAV	net asset value
NBC	National Bank of Commerce Limited
NCA	National Credit Act, No 34 of 2005
NPL	non-performing loan
NWP	net written premium

O	
ORC	Operational Risk Committee
OTC	over-the-counter

P	
PD	probability of default
PRO	Principal Risk Owner
PRP	principal risks policy

R	
R	rand
RC	regulatory capital
R&CC	Risk and Control Committee
RoA	return on average assets
RoE	return on average equity
RoEC	return on average economic capital
RoRC	return on regulatory capital
RSA	Republic of South Africa
RWAs	risk-weighted assets

Six months ended 30 June 2011

S

SA	Standardised Approach
SARB	South African Reserve Bank
SME	small and medium enterprises
SPE	special purpose entity
STIC	Short-Term Insurance Committee

T

TDC	Technical Disclosure Committee
TPRR	Trading Position Risk Review Forum
TRC	Trading Risk Committee
TTC	through-the-cycle

U

UL	unexpected loss

V

VAF	Vehicle and Asset Finance
VAS	value at stake

W

WFS	Woolworths Financial Services (Proprietary) Limited

Z

ZAR	South African rand