Group chief financial officer's report

The group increased headline earnings for the year by 7% to N$353 million (2008: N$330 million). Profit decreased by 10% to N$367 million (2008: N$409 million), mainly as a result of a squeeze on interest margins and equity losses incurred by Swabou Life on the shareholders' investment portfolio. However, direct comparison with the previous year cannot be made because profits in that year were enhanced by non-recurring transactions. The impact of these is summarised below:

N$ million	change	2009	2008
Profit for the year as reported	(10)	**367**	**409**
attributable to preference shareholders		(1)	(1)
attributable to minority interest	(50)	(12)	(24)
attributable to equity holders of the group	(8)	354	384
Headline earnings adjustment			
Loss or profit on revaluation of investment properties			1
Loss or profit on sale of property and equipment			1
Reversal/impairment of associates			(4)
Realised gains on available-for-sale financial assets		(1)	(2)
Profit on sale of shares in subsidiaries			(34)
Gains on initial recognition of VISA shares			(16)
Headline earnings	7	**353**	**330**

Earnings per ordinary share decreased by 6% to 136.1 cents (2008: 145.2 cents). Return on average equity was 23% (2008: 28%). The group's cost income ratio remained at an acceptable level, ending the year at 50% (2008: 46%). The reduced ratios were a direct result of the factors that impacted on profit.

The group comprises three main operating entities: the FNB Namibia Banking Group ("banking group"); Swabou Life Assurance Company Ltd ("Swabou Life"); and OUTsurance Insurance Company of Namibia Limited ("OUTsurance"). All three entities were profitable.

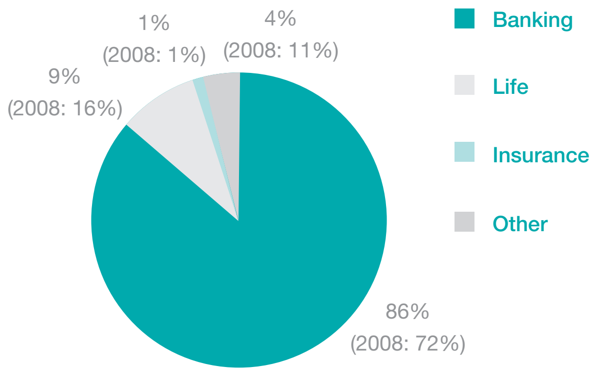
The banking group grew profit by 8% to N$317 million from N$294 million. Normalised earnings grew by 15%.

Swabou Life's profit decreased from N$65 million to N$33 million, mainly as a result of equity losses on the shareholders' portfolio and the N$100 million special dividend paid in October 2008 that reduced the investment income earning base.

OUTsurance's profit decreased to N$2 million (2008: N$5 million), affected by the cost of introducing new personal lines products. This diversification of product lines positions it well for the future.

The chart following illustrates the relative contribution by each segment to after-tax profit. The "other" segment reflects other group companies and group accounting consolidations.

Segment contribution to profit



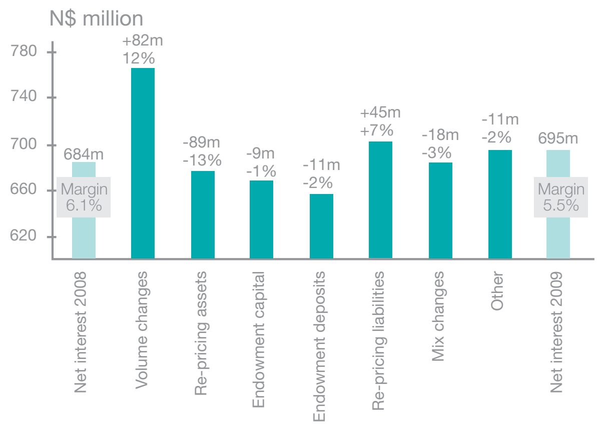
Income statement

Interest income

Net interest income before impairment of advances increased 2% to N$743 million (2008: N$729 million). The growth does not mirror the 15% increase in advances, reflecting the considerable pressure on interest margins. The cost of longer-term funding and the repo rate differential, combined with the negative endowment effect of a decreasing interest rate contributed to margin pressure. Both the timing and the extent of the rate cuts accentuated the margin contraction. The first reduction - 50 basis points - was in December 2008. The remaining 325 basis points came in the last six months of this reporting period. The banking group contributed 94% (2008: 94%) to the group's net interest revenue.

Alongside is an analysis of the movement in the components of the banking group's net increase in interest income.

Interest margin analysis



Impairment losses

Despite continued adverse market conditions, the banking group's prudent lending criteria together with the diligent collection of non-performing loans resulted in the impairment charge reducing from the already relatively low charge in the prior year. Total impairments decreased by 47% to N$38 million (2008: N$72 million), which is 0.4% (2008: 0.8%) of total average advances. The impairment charge comprises the following components:

	2009		2008	
	N$ million	% of average advances	N$ million	% of average advances
Specific impairment on non-performing loans	16.1	0.1%	18.2	0.2%
Present value of security of non-performing loans	17.2	0.2%	21.1	0.2%
Total specific impairment	**33.3**	**0.3%**	**39.3**	**0.4%**
Portfolio impairment	5.1	0.1%	33.1	0.4%
Total impairment charge	**38.4**	**0.4%**	**72.4**	**0.8%**

Non interest income

Non interest income increased by 7.5% to N$433 million (2008: N$403 million). The banking group increased non interest income by 31% to N$491 million (2008: N$376 million). For the group as a whole, this was trimmed by a loss of N$94 million (2008: N$36 million loss) when investment portfolios of the insurance operations were revalued to reflect market movements in listed equities.

Fees and commission income increased by 24% to N$405 million (2008: N$326 million), with banking specific fee and commission income contributing the largest part. The migration of the credit card book from First National Bank South Africa to FNB Namibia in November 2008 contributed to the sharp increase. But even without this additional income, year on year growth was 17%, only 5% of which came from price increases. Penalty fees (costs clients could avoid) in the banking group fell by 28%, a pleasing change in consumer behaviour.

Fair value income increased by N$55 million to N$85 million, with N$60 million (2008: N$43 million) attributable to foreign exchange trading income. The significant growth came from a continued focus on sales in a buoyant currency market.

In addition, the prior year included the negative effect of derivative financial instrument revaluations of N$13 million. This became a positive N$24 million in the current year. The corresponding negative fair value adjustment of N$26 million (2008: N$16 million positive) is reflected under *Fair value adjustment to financial liabilities*.

Gains and losses from investment activities include dividends and realised and unrealised investment gains, predominantly from Swabou Life.

Swabou Life's investment portfolio reflects the sharp decline in global equity markets. Fair value losses on revaluation of portfolio investments were N$94 million (2008: N$36 million loss). Of this, the shareholders' portfolio accounted for N$22 million (2008: N$3 million loss). Exposure to equities on the shareholders' portfolio has been reduced subsequently. Losses on policyholders' portfolio were largely countered by a reduction in policyholders' liabilities as liabilities are matched by assets to a significant degree.

In 2008 *Gains and losses from investment activities* included a once-off N$34 million profit resulting from the sale of shares in subsidiaries.

Other non interest income decreased by N$16 million, an amount matching the once-off capital gain that came from the initial recognition of Visa shares in the previous year.

Net insurance premium income grew by 16%.

Swabou Life contributed 76% to net insurance premium income. Swabou Life's premium income increased by 6%, reflecting the net effect of the mature Momentum book and the Swabou Life book that grew at 18%. OUTsurance premiums increased by 58% reflecting increased business resulting from the roll-out of personal lines products.

Net claims and benefits paid increased by 6% to

N$125 million (2008: N$117 million). Swabou Life – once again comprising the bulk of this value – reflected a small decrease, while OUTsurance increased to N$29 million (2008: N$8 million).

Fair value adjustment to financial liabilities

decreased by N$42 million to a loss of N$26 million, reflecting the market movement of listed fixed rate subordinated bonds issued by the banking group as second tier capital in 2007. The bonds are classified as a financial liability carried at fair value through profit and loss. The corresponding N$24 million (2008: N$13 million loss) hedging income is included under *Fair value income*.

Operating expenses

The year on year increase of 12% in operating costs from N$618 million to N$694 million, needs to be viewed in context. It included costs relating to the core banking system currently being localised as required by the Bank of Namibia, as well as FNB Card costs which were not included in the previous year's figure. The adjusted year on year increase in operating costs was 8%, indicating that expenses remained well managed, considering that average inflation dropped to single digit figures only in May 2009 and was at 9% in June 2009.

Tax

Indirect tax decreased by N$6 million to N$12 million, mainly as a result of the relatively lower increase in interest income as against non interest income. This increased the Value Added Tax apportionment ratio of the banking group.

The group's effective tax rate increased from 28% to 33% because of non-taxable capital profits included in the prior year.

Balance sheet

Total assets increased by N$698 million to N$14.1 billion – a year on year growth of 5%.

The large decrease in balances from banks and other financial institutions from N$1 billion to N$479 million reflects the excess liquidity experienced in the previous year. The position has now normalised.

Derivative financial instruments increased by N$92 million to N$130 million. It is in line with the N$54 million increase in the derivative liability to N$116 million, as these are entered on a back to back basis. The difference between the assets and liabilities are mainly the group's own hedges. The growth reflects increased client trading activities in interest rate swaps and forward foreign exchange contracts.

Gross advances increased by a healthy 15%, compared to private sector credit extension of 9.5%. Average advances grew at a slightly more conservative 11%, with a bulge towards the end of the financial year. The growth was mainly driven by overdrafts and managed accounts as well as term loans that grew at 18%. Despite a moderate growth of 9% in property and vehicle finance, the group maintained its position as market leader in both asset classes.

Once again it is pleasing to report that the healthy profile of the advances book was maintained. The impairment charge as a percentage of gross average advances dropped to 0.4% (2008: 0.8%), and average non performing loans as a percentage of gross average advances was at 3.2% (2008: 2.9%). Non performing loans increased by 9%. The difference between a low level income statement charge and a 3.2% non performing loan ratio illustrated the high level of secured lending.

Investment securities reflected the liquid asset requirements of the banking group and Swabou Life investments. The banking group's portfolio was diversified into deposits that also qualified as liquid assets and as a result decreased by 2% to N$920 million. Swabou Life's portfolio decreased by 16% to N$954 million, in line with the general decline in global equity markets.

Deposits increased by 10% - in line with the growth in average advances. Wholesale funding continued to be the dominant source of funding.

Policyholder liabilities decreased in line with the value of insurance assets, following the fall in value of Swabou Life assets.

The post-retirement benefit liability decreased by 42% to N$22 million (2008: N$38 million) after employees were given a choice between receiving early settlement and cancelling premium subsidies or maintaining the benefit. A total of 296 employees accepted the offer and 112 employees remain covered.

Dividend policy

The group has maintained the 2.4 times dividend cover on profit attributable to ordinary shareholders.

Capital management

Banking Group

The optimal level of capital in a banking institution is determined by balancing the requirements of the Regulator, the shareholders, deposit holders and debt holders.

Principles

For a banking institution, capital serves as a foundation for growth and a cushion against unexpected losses. It mitigates economic risk that might otherwise threaten its continuation or lead to loss of faith by stakeholders. It is the policy of the bank to be capitalised at the higher figure of economic capital or regulatory capital inclusive of a buffer.

Economic capital is defined as the capital which the Banking Group must hold, commensurate with its risk profile, under severe stress conditions, to give comfort to third party stakeholders that it will be able to discharge its obligations in accordance with an indicated degree of certainty even under stress conditions, and would continue to operate as a going concern. Tests are performed regularly to assess whether the bank is appropriately capitalised.

Demand for capital

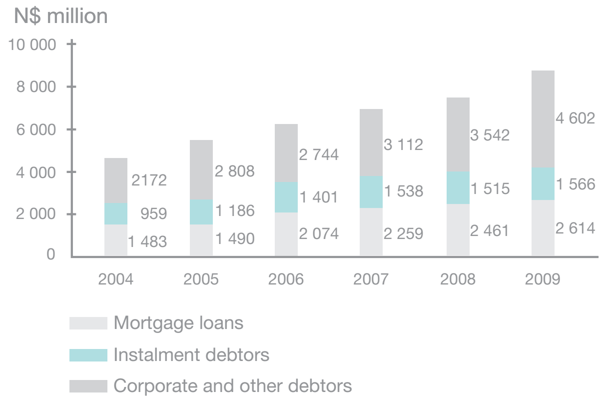
The Bank of Namibia requires banking institutions to hold a minimum amount of capital equal to, or more than, 10% of the calculated risk weighted assets. Furthermore, as a subsidiary of FirstRand Bank Holdings Limited, regulated by the South African Reserve Bank ("SARB"), the Group needs to abide by regulations currently requiring a minimum of 9.5% by the SARB method of calculating risk weighted assets.

Current capital requirements in the Banking Institutions Act 1998 (No. 2 of 1998) are based on the International Capital Accord of the Basel Committee established in 1988. This capital accord has been revised and Basel II, as adapted by the Bank of Namibia, will be effective from 1 January 2010.

The main changes lie in the calculation of risk weighted assets and the closer alignment of capital levels to true underlying economic risks. As a subsidiary of a South African Banking Group, where the principles of Basel II were adopted on 1 January 2008, First National Bank of Namibia Limited has complied with the standardised approach to calculate capital for credit, market and operational risks.

Indications are that compliance with Basel II will not require a material increase in our current economic capital estimates or minimum regulatory levels. The following graph depicts the growth in the major classes of risk weighted assets since the merger with Swabou in 2003/2004:

Growth in the major classes of risk weighted assets



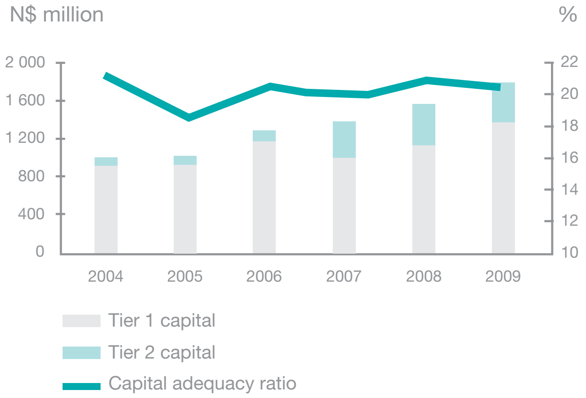
Supply of capital

As the bank generates earnings that are adequate to meet new capital requirements, the focus of management is on arriving at the most cost-effective capital structure. The relatively higher cost of capital, as against debt, means capital levels have to be managed to the minimum required, thus increasing the true economic value added to shareholders.

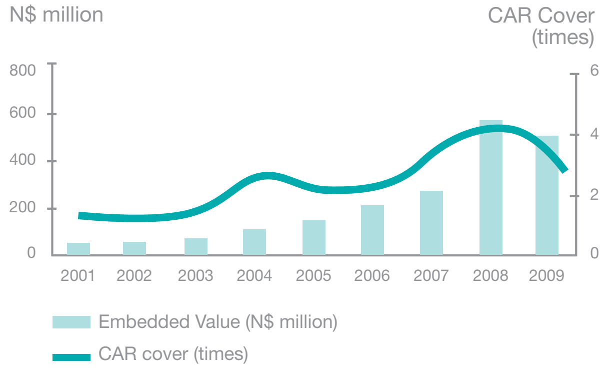
The Bank of Namibia allows the appropriation of current year profits to capital only on audited results. Maximum exposures to single borrowers are linked to the capital base. This results in the determination of maximum exposure being reviewed only at year-end and could impede balance sheet growth during the year. Upon implementation of Basel II based regulations, current year profit will form part of qualifying capital once appropriated by the board.

The board of directors approved a 5.5% buffer above the 10% minimum level determined by the Bank of Namibia. This is

Qualifying capital and capital adequacy ratio



Embedded value versus CAR cover of Swabou Life



mainly to allow for growth until the next financial year's profits are appropriated to capital. The buffer is also influenced by economic capital requirements. The above graph depicts the growth in qualifying capital as well as the capital adequacy ratio.

Dividend payment

The banking group declared an interim dividend of N$74 million in February 2009 and a final dividend will be declared taking into consideration the group's dividend payment requirements as well as the group's policy of a 2.4 times dividend cover.

Insurance operations

OUTsurance's capital adequacy is measured by the solvency margin that is the free reserve ratio of shareholders' funds expressed as a percentage of net premium income. The solvency margin at 30 June 2009 was 42% (2008: 59%), a sound and healthy position.

Swabou Life's policy is to invest capital required for the capital adequacy requirement (CAR) in cash or near cash instruments. The objective is to ensure a sufficient excess of assets over liabilities to guard against severely negative conditions in future. When the Momentum transaction was approved, the court determined that Swabou Life must maintain a CAR cover of 2 times. In terms of the capital management framework of Swabou Life, the company will maintain a buffer of 0.5 times above that minimum.

The CAR of Swabou Life is N$94.8 million (30 June 2008: N$68.3 million). Free reserves cover the capital adequacy requirement 3.0 times (30 June 2008: 5.1 times).

The embedded value decreased to N$526 million (2008: N$589 million restated). The embedded value decreased as result of the payment of the total dividend payment of N$100 million. The value of in-force increased by 10% to N$301 million (30 June 2008: N$274 million) and the value of new business was N$59 million (30 June 2008: N$69 million).

Conclusion

The group is cautiously optimistic about performance in the 2009/2010 year. It recognises the more benign local economic outlook - with lower interest rates and inflation – but acknowledges the negative impact of global recession.

It does not expect consumer spending to recover fully until the second half of 2010, specifically in the financing of property and vehicles. Therefore it continues to position itself strategically in carefully selected markets to achieve sustainable growth.

Focus will remain on improving efficiencies and cost management to counter continued pressure on both interest and non interest income, as well as increased computer costs expected to arise from localising the core banking system.

Erwin Tjipuka
Group Chief Financial Officer

Capital adequacy of the banking group

N$ million	Balance 2009	Balance 2008	Risk weight %	Risk adjusted balance 2009	Risk adjusted balance 2008
Risk-adjusted assets and off-balance sheet exposures					
Cash, including foreign currency, claims on government and Bank of Namibia	1 198	1 171			
Public sector body advances	536	290	10	54	29
Other bank advances and letters of credit	634	1 210	20	127	242
Mortgage advances (excluding commercial)	5 229	4 922	50	2 614	2 461
Other assets and advances	5 987	4 786	100	5 987	4 786
Total	13 584	12 379		8 782	7 518

N$ million	2009	2008
Regulatory capital		
Tier 1		
Share capital and share premium	1 143	1 143
Retained profits	491	282
Capital impairment: Intangible assets	(261)	(283)
Total tier 1	1 373	1 142
Tier 2		
Eligible subordinated term debt (limited to 50% of total Tier 1 capital)	260	260
General risk reserve, including portfolio impairment	152	147
Revaluation reserves		10
Total tier 2	412	417
Total tier 1 and tier 2 capital	1 785	1 559
Risk-weighted capital ratios		
Tier 1	15.6%	15.2%
Tier 2	4.7%	5.5%
Total	20.3%	20.7%