



Group Managing Director's Report

When I took up the position I did so with considerable enthusiasm and a very positive view of the opportunities available to Mercantile. Clearly I was anticipating challenges but, quite frankly, the scale of the issues we have faced was beyond anything I remotely anticipated and the financial consequences have led to us re-evaluating the businesses we were involved in. We have got out of some businesses, sold others and refocused others. The focus for the next year will be on consolidation and gradual rebuilding as we are able to free up or generate capital. This obviously has to be done in a responsible manner and will of necessity be a slow process.

THE RESULT FOR THE YEAR

We have generated a loss for the year at an attributable level of R646.8 million. The magnitude of the loss masks to a large extent many of the achievements of the year. To my mind, the most important of these were:

- Clarity about the shareholding structure and the assumption of control by CGD
- The disposal of the Registrars businesses
- The disposal of other non-core businesses
- Improvement in risk management

Some R507 million of the loss is in respect of provisions against advances. The majority of these advances were made before 1999 and there is little doubt in my mind that in a number of instances they were granted with a poor understanding of the risks and with inappropriate risk management systems in place to monitor and control them. As part of ongoing efforts to improve risk management and the quality of management information, management commenced a comprehensive review of the advances book, in January 2002, with a view to ensuring that the book was appropriately risk graded. This exercise involved the risk grading of each individual advance as well as an evaluation of the securities held against such advances. As a result of this exercise, I am confident to report that non-performing advances have been properly identified. Adequate provisions in this regard have been created and foundations have been laid, through the installation of appropriate preventative and detective controls, to ensure a more pro-active management of credit risk.

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CAPITAL ISSUES

Unfortunately, the consequence of the losses is that capital adequacy levels have dropped below those required by the South African Reserve Bank ("SARB"). We have therefore had to raise regulatory capital and this has been done in two tranches. The first was announced in November 2001 and took the form of an issue of shares for cash to CGD of R120 million which was concluded in March 2002. The second took the form of a guarantee as explained further in note 10 of the directors' report.

CGD'S COMMITMENT TO MERCANTILE

The issue of shares for cash mentioned above took CGD's shareholding in Mercantile from 28% to 64.1% and established CGD as Mercantile's controlling shareholder. This began a new era for Mercantile.

During July 2002 CGD undertook to guarantee a portion of the Group's non-performing book thereby restoring the Group's capital to a level that exceeds the SARB's requirements.

Mercantile depositors and other customers are assured of the continued support of the controlling shareholder CGD who confirm that it is willing to safeguard the financial soundness and stability of Mercantile, including the maintenance of capital adequacy.

The commitment from CGD goes of course way beyond capital and the support they have already given in this regard. Their support translates very tangibly to our customer base and employees and is fundamental in the rebuilding process that will take place over the next year.

THE WAY FORWARD FOR NEXT YEAR

As mentioned before, next year will be a period of consolidation and rebuilding. We will remain in the businesses we are currently in. All require work but all will benefit from the stability provided by the major shareholder. The Retail Bank in particular has been

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frustrated by a lack of clarity and uncertainty. To a large extent, this has been removed. CGD is a substantial player in this industry world-wide and we look forward to learning from the broader group. We are cautiously optimistic about the Alliance Banking business that once again will benefit from an increased involvement from CGD.

We have already identified a number of areas where we can reduce costs and increase efficiencies and management is vigorously exploring these. There are also opportunities to grow income and these will be similarly explored.

On a personal note I would like to express my appreciation to the board, my fellow executives and to all the staff for their extraordinary efforts in difficult times this year. A particular vote of thanks should go to our chairman, Mr Barry Wood for his sound guidance. I look forward to working with the new chairman and board and would especially like to welcome Dr Rui Ribas to the executive.



R J SYMMONDS

Group Managing Director

9 July 2002



Steering a tighter ship towards a greater horizon