Financial review

Financial review continued

This review provides context to the financial performance of the group's banking and insurance operations as detailed in the financial statements. The group's performance over the past seven years is detailed on pages 84 to 89 and the financial ratios generally quoted are defined on page 90.

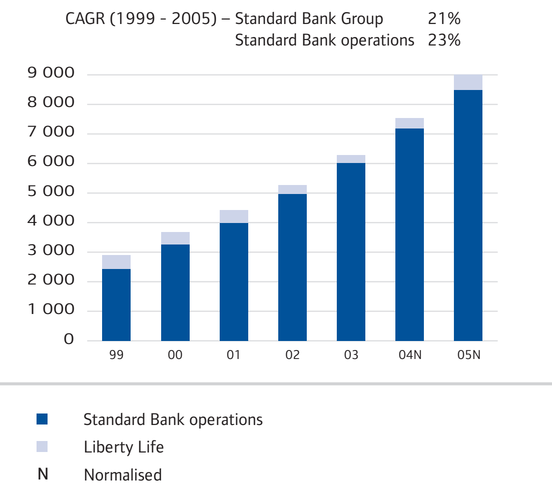
Overview of financial results

Standard Bank Group headline earnings per share for the year to December 2005 increased by 23% to 702,3 cents per share and a return on equity of 27,8% was achieved. These results are based on International Financial Reporting Standards (IFRS). Certain of the accounting conventions under IFRS distort the results from an economic perspective. As discussed under the normalised results section on page 75 of this review, the effect of these distortions has been adjusted for in calculating normalised results. On a normalised basis, headline earnings per share grew 19% and the return on equity was 25,2% (2004: 24,2%).

Broadly, 2005 was positive for emerging market economies as macroeconomic fundamentals and demand for exports from these markets improved. Investment inflows to these markets, aided by global liquidity and increased investor risk appetite, lifted economic activity but reduced profit margins of our corporate and investment banking activities.

South Africa's strong economic growth stemmed substantially from strong local demand. High consumer spending was underpinned by relatively low inflation and interest rates. Net job creation, the positive effect of rising equity and house prices, increased household disposable income and the growing middle class resulted in improved consumer confidence and provided a strong platform for consumer and business banking in South Africa.

Headline earnings (Rm)



Financial highlights

	2005	2004
Return on equity (%)[1]	25,2	24,2
Headline earnings (Rm)[1]	9 013	7 511
Headline earnings growth (%)[1]	20	20
Headline earnings per share (cents)[1]	666,0	558,1
Headline earnings per share growth (%)[1]	19	19
Total dividends declared (cents)	267,0	231,5
Net interest margin (%)	2,93	3,07
Cost-to-income ratio (%)	56,6	58,0
Credit loss ratio (%)	0,41	0,43

[1]*Normalised results.*

Key factors impacting the results

- **Increased consumer activity in South Africa**

  2005 saw continued strong growth in the residential property market and record new vehicle sales. A further 50 basis points reduction in the prime interest rate together with a strengthening economy was conducive to sustained growth in lending and transaction volumes.

- **Rehabilitation of previously impaired loans**

  Corporate & Investment Banking in South Africa and internationally experienced credit recoveries during the year as improved economic conditions in emerging markets led to the recovery of previously distressed counterparties. This helped reduce the group's credit loss ratio to a historic low, despite an increase in the credit loss ratio in Personal & Business Banking SA.

- **Increased funding requirements**

  Customer deposits continue to grow at a slower pace than consumer lending, resulting in an increased reliance on more expensive wholesale funding. In addition, the proportion of term deposits has been increased to lengthen the structure of the funding book in line with internal prudential liquidity guidelines. Consequently, average long-term funding as a percentage of total funding has increased from 15% to 18%. During the year, the group successfully concluded its first asset-backed securitisation transactions: R4,5 billion of mortgage loans and R3,0 billion of vehicle and asset finance receivables.

- **Strong equity markets**

  Investment Management & Life Insurance benefited from a strong run in equity markets. Higher listed property fund prices assisted Corporate & Investment Banking SA to achieve sizeable gains on its property investment portfolio.

- **Intensified competition in emerging markets**

  Emerging markets became increasingly popular with global investors as developing countries' credit ratings continued to improve. In this environment, traditional emerging market players like ourselves are encountering increased competition from the large established global banks in our chosen markets. Consequently, trading margins have contracted. In addition, these more stable environments have reduced trading opportunities for the group's international operations. These trends have led to the international operations' 2005 results being below expectation.

- **Higher compliance costs**

  Increased regulations are becoming a feature in most of the jurisdictions in which the group operates. Staff costs in South Africa were significantly impacted by additional staff requirements to comply with the Financial Intelligence Centre Act (FICA) and other regulations. FICA requirements were also the main driver behind increased communication costs.

- **Adjustments for deemed treasury shares**

  The group's results have been affected by required accounting conventions that do not reflect the underlying economic substance of transactions. Group shares purchased by empowerment partners and group shares held for the benefit of policyholders of Liberty Life are deemed to be treasury shares in terms of IFRS. Consequently the number of shares used for per share calculation purposes is materially lower than the shares enjoying an economic interest in the group, resulting in inflated per share ratios. In addition, fair value adjustments relating to group shares held for the benefit of policyholders and dividends received are eliminated from the group's income statement without a corresponding elimination in policyholders' liabilities, resulting in a mismatch in the income statement.

  The unaudited table below indicates the significant impact that the deemed treasury shares have on the results.

	Normalised	IFRS
Headline earnings (Rm)	9 013	8 464
Headline earnings growth (%)	20	12
Headline earnings per share (cents)	666,0	702,3
Headline earnings per share growth (%)	19	23

  Further details of the accounting treatment and the calculation of normalised results are discussed on page 75.

Business units

The refocusing of operations on key business lines, as described in the chairman and chief executive review, as opposed to geographic segmentation aims to encourage the leveraging of skills, economies of scale and synergies. This basis will be followed as the primary segmentation from 2006 onwards.

On this new basis, Personal & Business Banking comprises 44% of the group's headline earnings, and grew these earnings in 2005 by 22%. Corporate & Investment Banking comprises 45% and grew by 7%, and Investment Management & Life Insurance comprises 7% and grew by 51%.

On a geographical basis, South African banking increased headline earnings by 21% with growth of 23% in Personal & Business Banking SA. The favourable economic conditions benefited the consumer market and underpinned transactional and lending growth. The division maintained a strong focus on service levels and operational efficiencies notwithstanding increased business volumes and compliance requirements. The home loans business concluded another successful year with a 25% growth in new loans registered and low credit losses. Specific focus on the card business resulted in substantial growth in both balances and turnover.

Corporate & Investment Banking SA increased headline earnings by 15%. The benefits of strong loan growth in commercial property lending was partly offset by lower interest margins resulting from more expensive and longer dated funding. Fees and commissions benefited from increased corporate transaction volumes and new electronic banking products. South African trading income increased by 8%, dampened by low volatility in foreign exchange markets. Other income increased following the revaluation and realisation of listed property investments. A net reversal of credit losses occurred for the third consecutive year supported by an exceptionally favourable credit environment. Operating cost growth was contained to 3% largely through lower IT costs, savings on depreciation and premises costs.

Corporate & Investment Banking International's headline earnings were 28% lower following increased competition and tightening spreads against a background of increased global liquidity across most of its markets. Trading income was also adversely impacted by a continued shift from a reliance on proprietary trading, with lower value-at-risk utilisation, to becoming more client focused. A net reversal of credit losses resulted from previously impaired accounts now performing. Strategies to improve performance in this operation are being implemented including an increase in the talent pool, particularly in client facing areas, improved systems and a change in emphasis from product to client focus. In addition, the appointment of Ben Kruger as chief executive of Corporate & Investment Banking across the group should quicken the pace of implementing these strategies.

Following strong earnings growth in Rest of Africa over a number of years, headline earnings growth of 17% was slightly below expectation. Lower lending margins restricted income growth, off a higher cost base. Management's attention in 2005 was mostly inwardly focused on the alignment of products, policies, procedures and systems across all African countries, and integrating these with the South African operations. The focus for 2006 will be to increase transaction flows through the stronger base that has now been established.

Liberty Life had a very good year and increased normalised headline earnings by 47%, notwithstanding a once-off R321 million after tax provision for the Statement of Intent relating to the Pension Funds Adjudicator (PFA) rulings. Significant gains on investments held in the shareholders' portfolio, previously accounted for directly in equity, more than offset this provision. Highlights of Liberty Life's results were improved investment returns and strong growth in new business. The Capital Alliance Holdings Limited (CAHL) integration is on track and benefits are beginning to be extracted.

The group will continue to invest in expanding its activities in emerging markets outside of South Africa. In December 2005, a consortium led by Standard Bank entered into an agreement to buy BankBoston Argentina from Bank of America. This transaction remains subject to fulfilment of provisions of the agreement and obtaining the necessary regulatory approvals in both South Africa and Argentina. The acquisition is only expected to be concluded in the third quarter and is not anticipated to materially affect the 2006 results. Given our interest in Nigeria, we have invested approximately USD185 million in our existing banking operation to meet the new minimum capital requirement set by the Central Bank of Nigeria. This enables us to comprehensively evaluate suitable acquisition opportunities.

Performance against objectives

One of the group's eight values is delivering to its shareholders. The group sets medium-term objectives that are reviewed annually in the context of expected economic conditions to ensure this value is measured and lived. These medium-term objectives, as well as the actual performance against these objectives for the past seven years, are illustrated on page 10. The group achieved three of its four stated objectives in 2005:

- Return on equity (ROE): The group considers ROE as a measure of quantifying its delivery to shareholders. The group's normalised achievement of 25,2%, compares favourably to its normalised objective of 22,5%.
- **Growth in headline earnings per share:** The group's objective is to grow normalised headline earnings per share in excess of domestic inflation (CPIX) plus 10%. The group achieved this objective by increasing headline earnings per share on a normalised basis by 19% compared to the objective of 13,9%, based on average CPIX of 3,9%.
- **Cost-to-income ratio:** Despite restricting cost growth to single digits, this objective was not achieved in 2005. The ratio of 56,6% is above the set objective of 55,5%. The group has improved on its performance of 58,0% in 2004 but lower than expected income growth in its international operations limited this improvement.
- **Credit loss ratio:** In 2004, the group separated its objective for credit losses into a short-term and medium-term objective. The short-term objective was set at a ratio of less than 0,75% of gross loans and advances. The group achieved this challenging objective comfortably with a credit loss ratio of 0,41% (2004: 0,43%). The low credit loss ratio came as a result of the favourable credit climate domestically, sound internal risk processes and recoveries in Corporate & Investment Banking locally and internationally.

Following a review early in 2006, the revised published objectives are:

	2006	Medium-term
Normalised return on equity (%)	24,0	22,5
Normalised headline earnings per share growth	>domestic CPIX +10 %	>domestic CPIX +10 %
Credit loss ratio (%)	<0,75	<1,00
Cost-to-income ratio (%)	≤55,5	Continuous improvement

Banking operations

Income statement analysis

Net interest income (NII)

	2005 %	2004 %
Growth in NII	13	0
Net interest margin – group	2,93	3,07
Net interest margin – Domestic Banking	3,16	3,40

Despite lower margins, strong South African asset growth resulted in increased group net interest income.

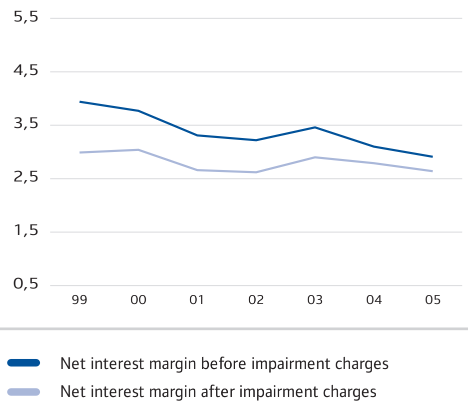
Overall, minimal erosion of lending yields was experienced despite increased amortisation of mortgage origination costs. The group's domestic bank generally avoided market share gains at the expense of low margins.

The lower interest earned on shareholders' funds and transactional deposits such as current accounts continued to squeeze margins as the average prime rate reduced by 66 basis points to 10,65% in 2005 following a further 50 basis points reduction in the domestic prime rate.

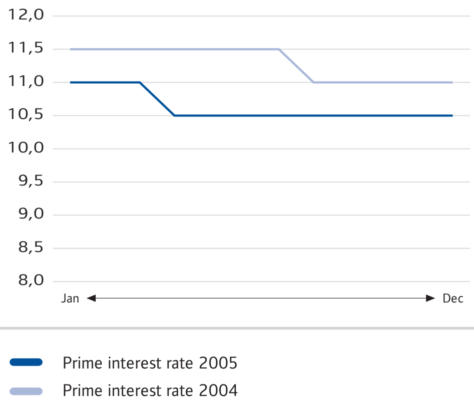
On the funding and liquidity management side, increased utilisation of more expensive wholesale funding to fund asset growth, the lengthening of the average long-term funding ratio from 15% to 18%, and maintaining a prudent liquid assets surplus, impacted margins.

Lending growth was the main contributor to higher net interest income in Rest of Africa and internationally but falling interest rates in key African markets and high levels of global liquidity resulted in tighter margins, partly reducing this benefit.

Group net interest margin (%)



Domestic prime interest rate (%)



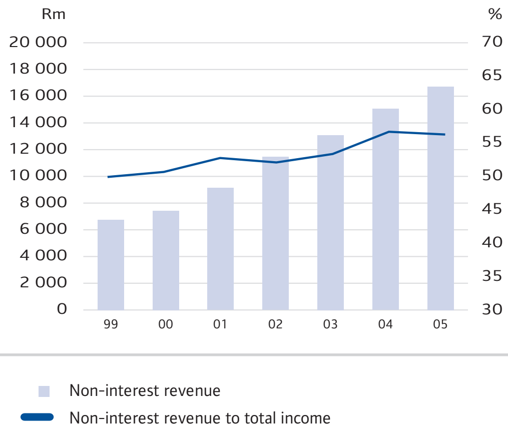
Non-interest revenue (NIR)

	2005 %	2004 %
Growth in NIR	11	15
NIR as a % of total income	56,3	56,7

Growth in non-interest revenue resulted from a 14% increase in fee and commission revenue and growth of 25% in other sources of non-interest revenue. Net trading revenue was marginally lower.

In South Africa, fees and commission benefited from a growing customer base and higher transaction volumes, resulting in growth of 16% despite below inflation price increases. These increased volumes were particularly evident in card-based commissions, point of representation fees and electronic banking where income growth rates of 29%, 13% and 19%, respectively, were achieved. Migration to electronic banking is continuing as the number of Internet transactions increased by 85% and the number of new Internet users increased by 27%. Increased deal flow benefited the corporate finance advisory business and contributed significantly to growth in knowledge-based fees. Rest of Africa recorded fees and commissions growth of 15%, resulting mainly from increased volumes and repricing of electronic banking and point of representation fees. Stanlib benefited from increased assets under management and grew fees by 14%. Internationally, competitive pressures and lower fund management fees led to a reduction of 9% in fee revenue.

Non-interest revenue



Trading revenue grew by 8% in South Africa with improved deal flow in client-based derivative trading. Foreign exchange trading recorded a marginal increase, off a high base, with volumes and market conditions to a large extent the same as in 2004. Buoyant precious metal prices resulted in reduced hedging activity by mines and a consequent reduction in commodity trading revenue. In Rest of Africa, strong growth occurred in foreign exchange trading with favourable spreads and increased volumes from higher volatility being the main drivers.

Corporate & Investment Banking International reported a 9% reduction in trading revenue. Favourable economic conditions in emerging markets resulted in substantially increased competition and tighter spreads, reducing foreign exchange and debt securities trading profits. In commodity markets, revenue was lower, off a high base, as the re-establishment of the energy business team following some key departures is only expected to take effect in 2006.

In South Africa, growth in the other income category resulted mainly from gains in listed property investments and an improved underwriting performance in the short-term insurance operation.

Credit impairment charges

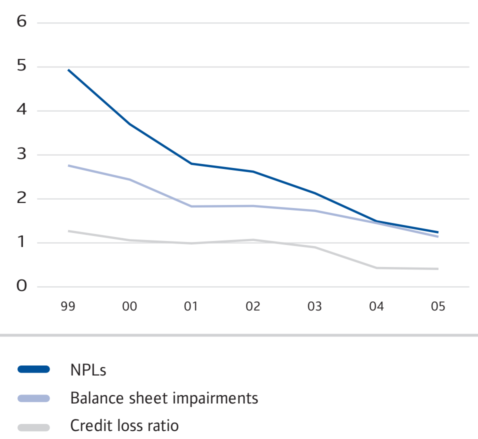
	2005 %	2004 %
Change in the impairment charge	15	(43)
Credit loss ratio	0,41	0,43
Balance sheet impairment as a % of gross loans and advances	1,14	1,45
Gross NPLs (Rm)	4 144	3 910
Gross coverage ratio	47	54

The credit impairment charge increased by 15% off a low base. This growth is made up of a decrease in the charge for non-performing loans and a significant increase in the portfolio charge for performing loans. The benign South African credit conditions of the past two years played a significant role in the low credit losses on non-performing loans.

The charge for non-performing loans was also assisted by the corporate and investment banking businesses in South Africa and internationally ending the year with net recoveries following the rehabilitation of previously non-performing exposures. In Personal & Business Banking SA, strong growth in all categories of consumer lending, especially in card, resulted in a substantially increased charge in rand terms.

This translated into a net credit loss ratio of 0,41% compared to a ratio of 0,43% the prior year. All businesses reflected lower credit loss ratios for the year, except for Personal & Business Banking SA where the ratio increased from 0,59% in 2004 to 0,73% in 2005. This was mainly as a result of a planned increase in risk appetite on credit card lending and the impact of prudent risk quantifications on a relatively young consumer loan book.

Credit loss history (as a percentage of gross loans and advances) (%)



Operating expenses

	2005 %	2004 %
Growth in Domestic Banking	9	17
Growth in the international and rest of Africa operations (rands)	11	5
Growth in total operating expenses	9	10
Cost-to-income ratio	56,6	58,0

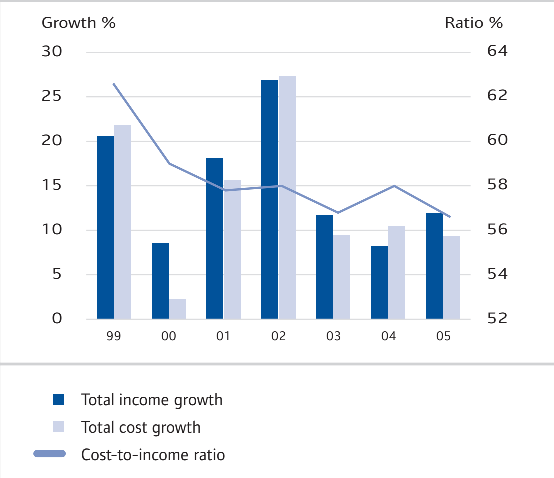
Banking operations contained its overall growth in operating expenses to 9% with staff costs increasing by 12% and other operating expenses growing by 6%.

Staff cost growth resulted mainly from a 2% increase in headcount necessitated by additional volume and compliance requirements and new IT initiatives. A focus on efficiencies at branch level and productivity at head office resulted in containment of staff numbers despite increased business volumes. In line with the group's remuneration policy, increased profitability resulted in higher incentive payments. Staff costs were further increased by the phase-in of share-based payments relating to the group's equity compensation plans as well as a full year's expense relating to rights to shares acquired by black managers in terms of the Tutuwa initiative, both now required in terms of IFRS.

Growth in other operating expenses resulted mainly from an increase in IT contractor fees as a number of system-based projects in response to operational and regulatory requirements are in progress, including compliance with Basel II. Increased business volumes, higher communication costs and additional client interaction to meet FICA requirements resulted in increased costs in South Africa. Other operating expenses in Rest of Africa grew by 17% due to continued investment in improved IT systems and processes across the continent. Internationally, increasing investment in IT infrastructure and network capabilities coupled with the expansion of regional offices resulted in 6% cost growth.

Across the group, additional compliance related costs amounted to approximately R200 million in 2005.

Cost and income growth



Taxation

	2005 %	2004 %
Effective taxation rate	27,4	28,3
Direct taxation rate	22,6	24,5
Indirect taxation rate	4,8	3,8

The direct taxation rate reduced by 1,9% mainly as a result of a 1% reduction in the South African corporate tax rate, re-evaluation of past liabilities and a release of deferred taxation following the cut in the South African corporate tax rate. This was partly offset by a significantly increased secondary tax on companies cost following the higher dividend payout ratio.

Growth in indirect taxes resulted mainly from an increase in expenses subject to VAT relative to net income before taxation.

Balance sheet analysis

Banking assets

	2005 %	2004 %
Growth in total banking assets	17	14
Growth in total banking assets excluding derivative assets	29	12
Growth in loans and advances	29	17

Strong growth in banking assets excluding derivatives occurred across the group with growth of 28% in Personal & Business Banking SA, 35% in Corporate & Investment Banking SA, 18% in Rest of Africa and 14% in Corporate & Investment Banking International.

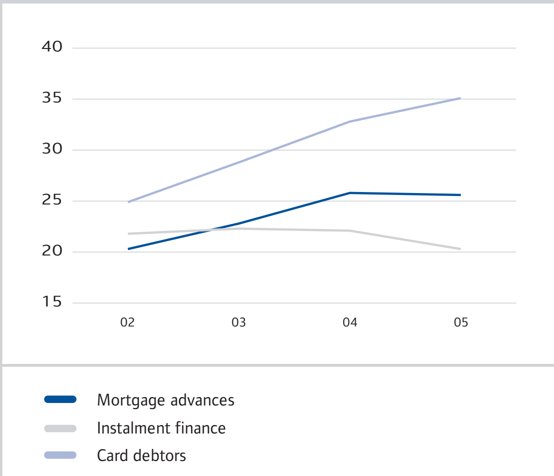
Most consumer lending categories in South Africa benefited from lower interest rates:

- mortgage loans increased by 32% following an increase in the volume and value of new registrations;
- instalment finance was up 15%, mainly as a result of volume growth as average lending values remained largely unchanged. Results reflect an above expectation performance in motor vehicle business for consumers and a disappointing growth rate in the non-motor book; and
- a strong focus was placed on growth in card debtors with a resulting 55% growth in card balances. Growth resulted mainly from new card openings through targeted campaigns and joint ventures, higher levels of revolving credit facilities and increased consumer spending.

The group's market share in South Africa increased in credit card debtors to 35,1% (2004: 32,8%) and decreased in both mortgage lending, down marginally to 25,6% (2004: 25,8%) and in instalment finance down to 20,3% (2004: 22,1%). Both mortgage lending and instalment finance market share statistics were impacted by securitisations, which reduced the ratios by 0,6% and 1,1% respectively.

Corporate & Investment Banking SA recorded growth in external loans and advances of 24%, mainly from increased commercial property lending, new term deals to corporate customers and increased structured trade finance transactions. Internationally, external loan growth of 45% resulted mainly from increased structured and trade finance deals.

Key market shares (%)



Liberty Life

2005 was a good year for Liberty Life. Indexed new business premiums increased by 12%. Net cash inflows from insurance operations amounted to R5,7 billion – the highest level to date. In addition, Stanlib and Liberty Ermitage net cash inflows amounted to R13,3 billion and R0,4 billion respectively. Normalised embedded value per share was 15% higher than last year. During the course of 2005 Liberty Life initiated the disposal of its offshore asset manager, Liberty Ermitage, and the Australian life insurance business, Prefsure, which was included in the acquisition of CAHL.

Liberty Life's published earnings are adjusted to exclude the results relating to Stanlib, this entity's results being consolidated into those of Standard Bank operations.

Equity attributable to ordinary shareholders

	2005 %	2004 %
Growth in ordinary shareholders' funds	13	1
Net asset value per share – normalised (cents)	2 830	2 464

Net asset value as defined by ordinary shareholders' equity grew by 13% to R33 billion. In 2004, the group reported a R4,2 billion elimination against equity attributable to ordinary shareholders for shares acquired in terms of the Tutuwa initiative, deemed to be treasury shares. Following the adoption of IFRS, a further elimination was required for group shares held for the benefit of Liberty policyholders amounting to R1,1 billion, net of minority interest. On a normalised basis (adding these eliminations back) net asset value increased by 15% to R38 billion, representing mainly the retention of earnings and a R0,4 billion net increase in the translation reserve.

Dividends

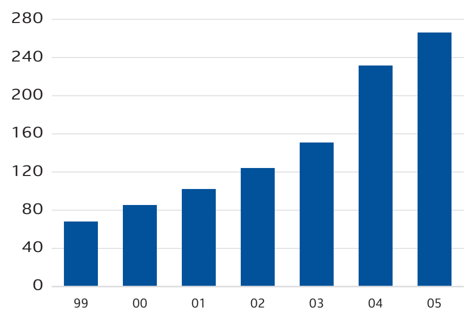
	2005 %	2004 %
Dividend cover (times)	2,5	2,5
Growth in dividends per share	15	53
Dividend yield	3,5	3,5

In March 2005, the group announced a revised dividend policy using a consistent dividend cover ratio for both interim and year-end dividends. This has resulted in a more even spread between interim and final dividends. Due to the much higher number of shares eliminated in terms of IFRS from 2005, dividend cover has now been applied to normalised headline earnings per share for the purpose of arriving at dividend declarations, slightly reducing the reported dividend growth.

At December 2004 the cover ratio was 2,5 times, down from 3,1 times in 2003. The dividend cover for 2005 has remained unchanged, resulting in total dividends declared of 267,0 cents, 15% higher than the total dividend declared in 2004. The total dividend of 267,0 cents is made up of a final dividend of 145,0 cents (20% lower than 2004) and an interim dividend of 122,0 cents (142% higher than 2004).

The dividend policy is subject to annual review and may be adjusted for business growth, acquisition activity, the impact of Basel II or changes in reported earnings resulting from applying fair value accounting principles.

Dividends per share (cents)



Accounting policies

Basis of preparation

The consolidated financial statements are prepared in accordance with, and comply with IFRS and the South African Companies Act of 1973. The consolidated financial statements are prepared in accordance with the going concern principle under the historical cost basis as modified by the revaluation of financial instruments classified as available-for-sale, financial assets and liabilities held at fair value through profit or loss, investment properties and derivative instruments.

Changes in accounting policies

The accounting policies are consistent with those adopted in the previous year, except for changes made as a result of the adoption of IFRS. The revised IFRS policies have been consistently applied to both years presented with the exception of IAS 32 – Financial Instruments: Disclosure and Presentation, IAS 39 – Financial Instruments: Recognition and Measurement and IFRS 4 – Insurance Contracts, where the group elected to apply IFRS with effect from 1 January 2005 as permitted by IFRS 1 – First time adoption of IFRS.

A detailed report summarising the impact of the IFRS conversion was published during the 2005 interim results announcement and is available on www.standardbank.co.za under financial results. The final impact of conversion to IFRS is provided on page 182 and a summary is provided on the following page. With the exception of reallocations in the income statement and balance sheet line items, mainly in the life insurance operations, since the interim publication, no adjustments have been made impacting profit and equity attributable to ordinary shareholders.

Summary of IFRS adjustments

	Total assets Rm	Equity Rm	Profit attributable to ordinary shareholders Rm
Reported at/for the year ended 31 December 2004[1]	615 596	38 564	7 741
Share-based payment expense	4	(132)	(116)
Deferred taxation adjustment on investment properties and present value of in-force business	47	–	–
Revaluation of residual values	46	46	12
Accounting for leases on a straight-line basis	266	(15)	(5)
Spreading of deferred acquisition costs on instalment finance transactions	–	(3)	3
Consolidation of mutual funds	3 647	(1)	–
Reversal of goodwill amortisation	112	112	98
Goodwill impairment	(48)	(48)	(45)
Reclassification of financial instruments on adoption of IAS 39	10	12	(2)
Accounting for credit losses on an incurred loss basis	(2)	(2)	(2)
Reclassification of reinsurance contracts to liabilities	495	–	–
IFRS values at/for the year ended 31 December 2004	620 173	38 533	7 684
Revaluations resulting from the reclassification of insurance contracts as investment contracts	–	(12)	
Spreading of deferred acquisition costs in Liberty Life	99	41	
Elimination of deemed treasury shares	(3 703)	(3 703)	
Reclassification of financial instruments on adoption of IAS 39	(39)	(39)	
Deferral of profit on initial recognition of unlisted instruments	(21)	(21)	
Accounting for credit losses on an incurred loss basis	115	77	
IFRS values at 1 January 2005	**616 624**	**34 876**	

[1]*Total assets have been adjusted for additional goodwill on acquisition of Standard Bank Mozambique in terms of IFRS 3.*

Normalised results (unaudited)

Headline earnings have been adjusted in calculating normalised headline earnings for required accounting conventions that do not reflect the underlying economic substance of transactions. A common element in these transactions relates to shares in issue deemed by accounting convention to be treasury shares. Consequently the number of shares used for per share calculation purposes are materially lower than the economic substance, resulting in inflated per share ratios. With regard to segmental reporting, normalised adjustments have been made within central funding and Liberty Life with the results of the other business units unaffected.

Black Economic Empowerment Ownership initiative

The group concluded its Black Economic Empowerment Ownership (Tutuwa) initiative in October 2004 when it sold an effective 10% interest in its South African banking operations to a broad-based grouping of black entities.

The group subscribed for 8,5% redeemable cumulative preference shares issued by special purpose vehicles (SPVs) controlled by Standard Bank Group (SBG). The initial repurchase of SBG shares by the SPVs is treated as a reduction in the group's equity. Subsequent to the repurchase of the SBG shares, the SPVs containing these shares were sold to the black participants. The capital and dividends on the preference shares are repayable from future ordinary dividends received on SBG shares. As a result of SBG's right to receive its own dividends back in the form of preference dividends and capital on the preference shares, the subsequent sale of the SPVs and consequent delivery of the SBG shares to the black participants (although legally effected) is not accounted for as a sale. The preference share investment in the SPVs is also not accounted for as an asset. The preference share asset is effectively eliminated against equity as a negative empowerment reserve.

As a consequence of the above, the accounting treatment followed until full redemption, or third party financing is:

- the 8,5% redeemable, cumulative preference shares issued by the SPVs and subscribed for by SBG are not recognised as financial assets, but eliminated against equity;
- the preference dividends received from the SPVs are eliminated against the ordinary dividends paid on the SBG shares held by the SPVs;
- for purposes of the calculation of earnings per share, the weighted average number of shares in issue is reduced by the

number of shares held by those SPVs that have been sold to the black participants. The shares will be restored on full redemption of the preference shares, or to the extent that the preference share capital is financed by a third party; and

- perpetual preference shares issued by the group for the purposes of facilitating the repurchase of SBG shares, are classified as equity. Dividends paid are accounted on declaration and not on an accrual basis.

The "normalised" calculation:

- reverses the elimination of preference shares against equity;
- adjusts headline earnings for preference dividends receivable not recognised in income;
- adds back the number of shares held by the Tutuwa participants to the weighted number of shares in issue, in calculating normalised headline earnings per share; and
- adjusts dividends declared on perpetual preference shares to an accrual basis.

Shares held for the benefit of policyholders

Group companies' shares held by Liberty Life are invested for the risk and reward of its policyholders, not its shareholders, and consequently the group's shareholders are exposed to an insignificant portion of the fair value changes on these shares. In terms of IAS 32, Standard Bank and Liberty Holdings shares held by Liberty Life on behalf of policyholders are deemed to be treasury shares for accounting purposes, with effect from January 2005, and eliminated. The corresponding movement in policyholders' liabilities is however not eliminated resulting in a mismatch in the overall equity and income statement of the group.

The accounting consequences in the consolidated financial statements are:

- the investment in group shares is set off against equity in the group financial statements;
- within equity, the cost price of the group shares is eliminated against ordinary shareholders' funds and minority interests;
- the fair value movements are eliminated from the income statement, reserves and minority interests;
- dividends received on group shares are eliminated against dividends paid; and
- no adjustment is, however, made for policyholder liabilities. Increases in the fair value of group shares and dividends declared on these shares increases the liability to policyholders. The increase in the liability to policyholders is accounted for in the income statement. The increase in assets held to match the liability position is however eliminated against equity. This results in a mismatch in the income statement.

The equity and profit impact is attributable to Standard Bank ordinary shareholders to the extent of the effective holding in Liberty Life (30%).

The weighted average number of shares in issue for earnings per share is calculated by deducting the full number of group shares held (100%) and not the effective 30% owned by the group, as the accounting standard IAS 33 – Earnings per share does not contemplate minority portions of treasury shares. This further exaggerates the reduction in the number of shares for purposes of calculating per share ratios.

For purposes of calculating the normalised results, the adjustments described above are reversed and the group shares held on behalf of policyholders are treated as issued to parties external to the group.

Adjustments to normalised number of shares

	2005		2004	
	Issued number of shares Million	Weighted average number of shares Million	Issued number of shares Million	Weighted average number of shares Million
IFRS	1 207	1 205	1 253	1 322
Add back: SBG shares held by Tutuwa SPVs	99	99	99	24
Add back: SBG shares held in policyholder funds	46	49		
Normalised	1 352	1 353	1 352	1 346

Adjustments to normalised results

	Headline earnings			Ordinary shareholders' equity
	Standard Bank operations Rm	Liberty Life Rm	Group Rm	Group Rm
IFRS values – 2004	7 187	351	7 538	29 064
Preference dividend accrual	(114)		(114)	(114)
8,5% cumulative redeemable preference dividend and shares recognised	83	4	87	4 360
Normalised values – 2004	7 156	355	7 511	33 310
IFRS values – 2005	8 145	319	8 464	32 931
Preference dividend accrual	3		3	(111)
8,5% cumulative redeemable preference dividend and shares recognised	342	25	367	4 378
Fair value movements and dividends received on deemed treasury shares		179	179	1 072
Normalised values – 2005	8 490	523	9 013	38 270

Capital adequacy and allocation

The group manages its capital base to achieve a balance between maintaining prudent capital ratios to support business growth and depositor confidence, and the objective to provide competitive returns to shareholders.

Regulatory capital

The group is subject to regulation and supervision by a number of South African and international regulators.

The 25 banks in the group are required to meet minimum capital requirements of regulators in those countries in which they operate. Banking regulations are generally based on the guidelines developed by the Basel Committee under the auspices of the Bank for International Settlements. In addition to the requirements of host country regulators, all banking operations are also expected to comply with the capital adequacy requirements in terms of South African banking regulations. As a consequence, the group's individual banking operations are capitalised at the higher capital adequacy levels in terms of either host country or South African requirements.

The capital adequacy ratio, which reflects the capital strength of an entity compared to the minimum regulatory requirement, is calculated by dividing capital by risk-weighted assets.

Capital is split into three tiers. Tier I (primary capital) represents the permanent forms of capital such as share capital, share premium and retained earnings. Perpetual, non-cumulative preference shares also qualify as tier I capital. Tier II (secondary capital) includes medium- to long-term subordinated debt, revaluation reserves and general debt provisions. Tier III (tertiary capital) represents short-dated subordinated debt instruments to support a bank's trading activities.

Risk-weighted assets are determined by applying prescribed risk weightings to on- and off-balance sheet exposures according to the relative credit risk of the counterparty. Included in overall risk-weighted assets is a notional risk weighting for market risks, counterparty risks and large exposure risks relating to trading activity.

The use of non-equity forms of regulatory capital plays an important part in the group's capital management process:

- Domestically, Standard Bank of South Africa (SBSA) redeemed R2,7 billion of tier II capital bonds that were eligible for redemption during June and December 2005. As part of a refinancing programme and also to strengthen the bank's capital base in view of strong risk-weighted assets growth, SBSA issued R3 billion 10 year tier II bonds at a spread of 10 basis points over the R157 bond in May 2005 following an earlier issue of R2 billion tier II capital during November 2004.
- International operations raised USD250 million of tier II bonds in October 2005 at a spread of 115 basis points over LIBOR. This issue was part of a strategy to improve the gearing of the regulatory capital base of the group's London based operations and to refinance the redemption of USD100 million of tier II bonds that were eligible for redemption in November 2005. The proceeds of the above issue were also used to repay, to the pool of strategic capital, USD53 million of capital invested by the group in its international operations.
- Within Rest of Africa, Standard Bank Swaziland issued E35 million tier II bonds, the first bank tier II issue in Swaziland. The optimisation of capitalisation levels and

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structuring in the African operations will receive greater focus during 2006.

The group's life insurance operations based in South Africa are regulated by the Financial Services Board. The capital requirements are calculated by a statutory actuary in terms of the guidance notes issued by the Actuarial Society of South Africa. Consistent with the group focus on optimising capital utilisation and shareholder value, Liberty Life similarly has an ongoing process to review its capital structure, which led to a R2 billion tier II bond issue during July 2005.

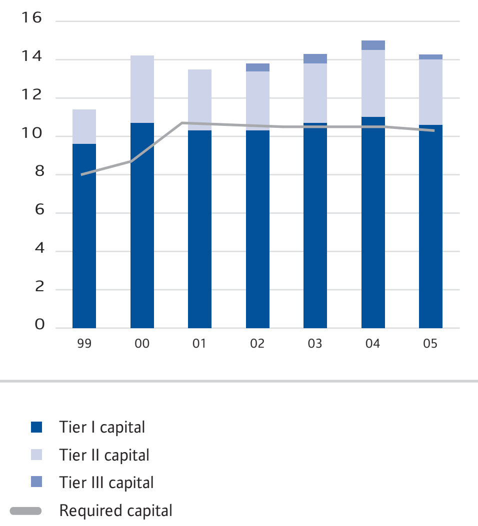
Capital adequacy ratios

The group's capital adequacy ratio reduced to 14,2% from 15,0% at December 2004, still well above the weighted average regulatory requirement of 10,3% for the 25 banks across the group. Tier I capital adequacy reduced from 11,0% to 10,5% due to strong growth in risk-weighted assets marginally exceeding retention of capital following the reduction in dividend cover. In addition, the group utilised R677 million to buy back 10,2 million shares thus counteracting the impact on earnings per share of shares issued in relation to the group's equity compensation plans.

The group's target level of capitalisation (excluding strategic pools of surplus capital that might be held from time to time) approximates 9% for tier I and 13% for total capital adequacy. A broad mix is targeted of 60% ordinary shareholders' funds, 10% other forms of tier I capital such as preference shares and 30% tier II and tier III capital instruments. Capital management activities take place against the backdrop of these guidelines and the demands on capital arising from the group's operating requirements.

Liberty Group is well capitalised with a capital adequacy cover of 2,0 times (2004: 2,5 times) the minimum regulatory capital requirement (CAR). Liberty Life's long-term CAR ratio target is 1,7 times.

Capital adequacy (%)



Regulatory capital and risk-weighted assets

	2005 Rm	2004 Rm
Regulatory capital		
Ordinary shareholders' equity	32 931	29 064
Minority interest	281	318
Perpetual preference shares	2 983	2 983
Elimination of insurance operations[1]	(2 122)	(2 872)
Impairments and other	(520)	(382)
Tier I capital	33 553	29 111
Preference share capital	8	8
Tier II bonds	9 467	8 042
Credit impairments for performing loans	1 236	1 036
Revaluation reserve	210	243
Tier II capital	10 921	9 329
Tier III capital	854	1 282
Total capital	45 328	39 722
Risk-weighted assets (closing balances)		
On-balance sheet	257 424	212 218
Off-balance sheet	20 834	15 742
Trading activity notional assets	40 021	37 188
Standard Bank operations	318 279	265 148

[1]*In accordance with Basel II principles relating to the treatment of insurance entities, insurance operations are excluded from the capital base of the banking group and its related risk-weighted assets. Capital in insurance operations in excess of statutory minimum requirements is accordingly not recognised in group capital. Comparatives have been restated accordingly.*

Capital adequacy ratios and targets

	Effective group constraint (including buffers) %	SARB regulatory constraint %	Target %	2005 %	2004 %
Standard Bank Group					
Total capital adequacy ratio	13,4	10,0	13,0	14,2	15,0
Tier I capital adequacy ratio	9,4	6,0	9,0	10,5	11,0
Preference shares as % of Tier I		20,0		8,9	10,2
Tier II and Tier III as % of Tier I		100,0		35,1	36,5
Lower Tier II as % of Tier I		50,0		28,2	27,6
Ordinary equity as % of capital			60,0	67,4	65,8
Preference shares as % of capital			10,0	6,6	7,5
Tier II and Tier III as % of capital			30,0	26,0	26,7

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Capital adequacy of banking subsidiaries

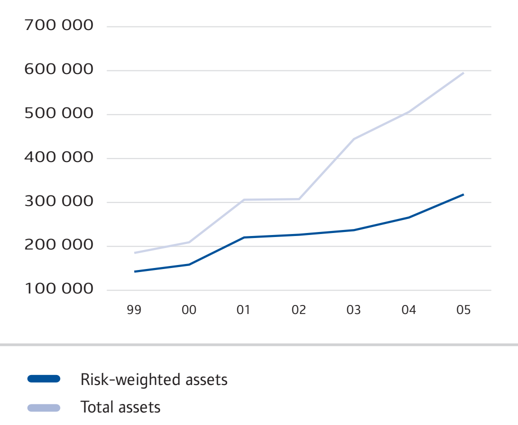
	2005				2004				2005
	Tier I capital %	Tier II capital %	Tier III capital %	Total capital %	Tier I capital %	Tier II capital %	Tier III capital %	Total capital %	Host regulatory requirement %
Standard Bank Group	10,5	3,4	0,3	14,2	11,0	3,5	0,5	15,0	–
The Standard Bank of South Africa	8,6	3,6	0,3	12,5	9,1	3,8	0,5	13,4	10
Rest of Africa									
Stanbic Bank Botswana	12,1	3,7	–	15,8	11,9	4,1	–	16,0	15
Stanbic Bank Congo	11,0	–	–	11,0	10,8	–	–	10,8	10
Stanbic Bank Ghana	18,0	0,3	–	18,3	16,8	–	–	16,8	10
Stanbic Bank Kenya	14,7	0,7	–	15,4	19,8	–	–	19,8	12
Stanbic Bank Malawi	15,0	4,2	–	19,2	14,8	4,9	–	19,7	10
Standard Bank Mauritius	24,0	0,7	–	24,7	17,6	0,6	–	18,2	10
Standard Bank Mozambique	13,5	–	–	13,5	18,4	–	–	18,4	10
Stanbic Bank Nigeria[1]	307,0	–	–	307,0	26,8	0,3	–	27,1	10
Stanbic Bank Tanzania	9,2	0,9	–	10,1	8,8	0,8	–	9,6	10
Stanbic Bank Uganda	14,6	1,1	–	15,7	17,3	0,5	–	17,8	12
Stanbic Bank Zambia	21,5	0,1	–	21,6	18,6	0,1	–	18,7	10
Stanbic Bank Zimbabwe	22,4	3,8	–	26,2	15,3	3,7	–	19,0	10
Standard Bank Lesotho	17,2	0,4	–	17,6	10,0	0,5	–	10,5	8
Lesotho Bank (1999)	16,1	0,7	–	16,8	21,9	0,7	–	22,6	8
Standard Bank Namibia	9,7	3,5	–	13,2	9,0	3,8	–	12,8	10
Standard Bank Swaziland	6,1	3,2	–	9,3	7,7	0,8	–	8,5	8
SIH, incorporating	8,1	5,7	0,5	14,3	8,2	6,1	0,8	15,1	10-12
– Standard Bank London									
– Standard Bank Asia Limited									
– Standard Merchant Bank Asia									
– Banco Standard de Investimentos Anonima									
– ZAO Standard Bank									
Standard Bank Jersey	9,1	2,3	–	11,4	9,5	2,5	–	12,0	10
Standard Bank Isle of Man	5,9	5,2	–	11,1	7,1	4,4	–	11,5	10
Aggregate regulatory capital requirement				10,3				10,5	
Liberty Life (calculated in terms of the Long-term Insurance Act) – CAR – times covered				2,0				2,5	

[1]*High levels of capital in Nigeria relative to risk-weighted assets were due to a further capitalisation of the bank to meet new local minimum capital requirements.*

Analysis of risk-weighted assets

	2005 Unweighted assets Rm	2005 Risk-weighted assets Rm	2004 Unweighted assets Rm	2004 Risk-weighted assets Rm
On-balance sheet assets				
Domestic Banking	452 038	215 219	391 668	179 845
Rest of Africa	30 043	17 075	25 348	14 641
Corporate & Investment Banking International	122 660	23 861	107 128	15 207
Stanlib and central funding (including group eliminations)	(11 013)	1 269	(18 124)	2 525
	593 728	257 424	506 020	212 218
Off-balance sheet assets				
Domestic Banking		16 861		12 462
Rest of Africa		1 685		1 831
Corporate & Investment Banking International		2 288		1 449
		20 834		15 742
Trading notional assets				
Domestic Banking		11 623		14 264
Corporate & Investment Banking International		28 398		22 924
		40 021		37 188
Standard Bank operations	593 728	318 279	506 020	265 148

Standard Bank operations' risk-weighted assets trend (closing balances) (Rm)



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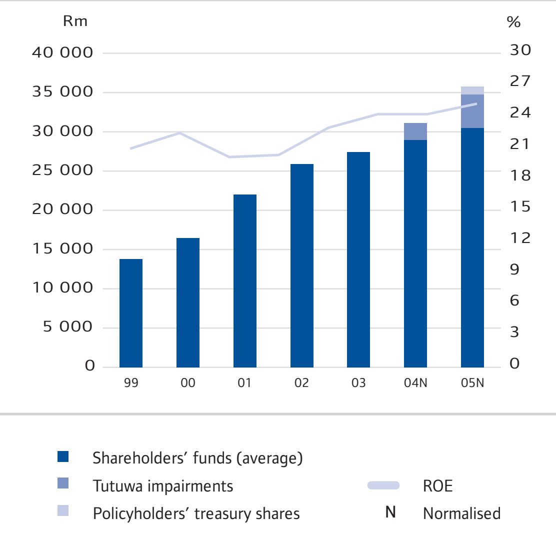
Economic capital

The group's approach to the measurement and management of economic risk capital is being aligned to be consistent with Basel II requirements in relation to the internal capital adequacy assessment process (ICAAP).

The allocation of economic capital to business units considers both risk capital as well as regulatory capital requirements in order to ensure that the business units focus on generating adequate returns for actual capital that needs to be held. Economic capital is therefore set at the higher of risk or regulatory capital requirements.

Return on equity based on economic capital allocations forms part of a balanced set of business unit financial performance indicators, which are monitored regularly. Cost of equity and weighted average cost of capital estimates are calculated for each market in which the group operates to serve as objective performance benchmarks and investment criteria.

Return on ordinary equity



Currency profile of group capital

A significant proportion of the group's activities are based outside South Africa. The group's plans for acquisitions also lie predominantly outside South Africa. As a consequence, 39% (2004: 35%) of the group's shareholders' funds are foreign currency denominated; 12% (2004: 8%) is deployed in African operations and 27% (2004: 27%) supports international operations or is held as surplus capital for future expansion. The increase in capital deployed in African operations results from the further capitalisation of the group's Nigerian subsidiary to be in compliance with new minimum capital levels of Naira 25 billion (approximately R1,2 billion).

Appropriate hedging strategies are implemented to create a more balanced currency profile given an overweight position of the US dollar in the group's foreign capital base in favour of a more balanced spread of exposures to US dollar, sterling and euro. Before accounting for currency hedging initiatives, 16% (2004: 16%) of the group's shareholder funds was exposed to US dollar, 3% (2004: 5%) to sterling and 7% (2004: 6%) to euro. After hedging, the main non-rand currency exposures of shareholder funds are 11% (2004: 8%) US dollar, 10% (2004: 13%) sterling and 5% (2004: 6%) euro.

The group remains averse to an overconcentration of its net asset value in US dollars and has hedges in place to support this strategy. The strengthening of the USD relative to GBP and euro has accordingly given rise to losses on currency hedges on USD invested in Corporate & Investment Banking International.

Given the group's presence in many countries, its shareholder funds will always be exposed to currency movements. Current South African Reserve Bank exchange controls do not allow for hedging of foreign currency risks on external capital into rand. Accordingly, the group's currency hedging is limited to movements within the basket of external currencies.

Economic returns generated by Standard Bank Group

	Change %	2005 Rm	2004 Rm
Average ordinary equity (normalised)	15	35 743	31 073
Headline earnings (normalised)	20	9 013	7 511
Cost of equity charge	3	(4 289)	(4 164)
Economic profits on normalised headline earnings	41	4 724	3 347
Other changes in net asset value		514	(1 237)
Translation gains/(reversals)		397	(1 272)
Other reserve movements		117	35
Total economic return	>100	5 238	2 110

Closing shareholders' funds exposure to currencies

	Total	Rand	Dollar	Sterling	Euro	Other	
						ZAR linked	Various
	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Closing currency exposure							
December 2005 underlying exposures	32 931	20 188	5 162	1 194	2 317	854	3 216
Currency profile changes due to hedging strategies			(1 601)	2 191	(526)		(64)
December 2005 actual exposures	32 931	20 188	3 561	3 385	1 791	854	3 152
December 2004 exposures excluding hedging activities	29 064	18 889	4 738	1 414	1 819	768	1 436
Currency profile changes due to hedging strategies			(2 402)	2 402			
December 2004 actual exposures	29 064	18 889	2 336	3 816	1 819	768	1 436

	%	%	%	%	%	%	%
Closing currency profile of shareholders' funds							
2005 before hedging	100	61	16	3	7	3	10
2005 after hedging	100	61	11	10	5	3	10
2004 before hedging	100	65	16	5	6	3	5
2004 after hedging	100	65	8	13	6	3	5

Group finance focus for 2006

The group's finance function strives to constantly enhance decision making by providing information relevant to management, regulators, investors and other parties. This is done through a disciplined and comprehensive approach to financial reporting.

As internal operational needs and external regulatory and investor requirements are constantly evolving, the following matters will receive increased focus in 2006:

- further alignment of reporting segments, previously largely geographically based, into business segments based on main product groupings;
- embedding principles required for compliance with Basel II in 2008;
- coordination of a group-wide economic capital allocation process to ensure optimum allocation of capital in line with quantified risk appetite; and
- further alignment of financial disclosure and timing of reporting with international best practice.