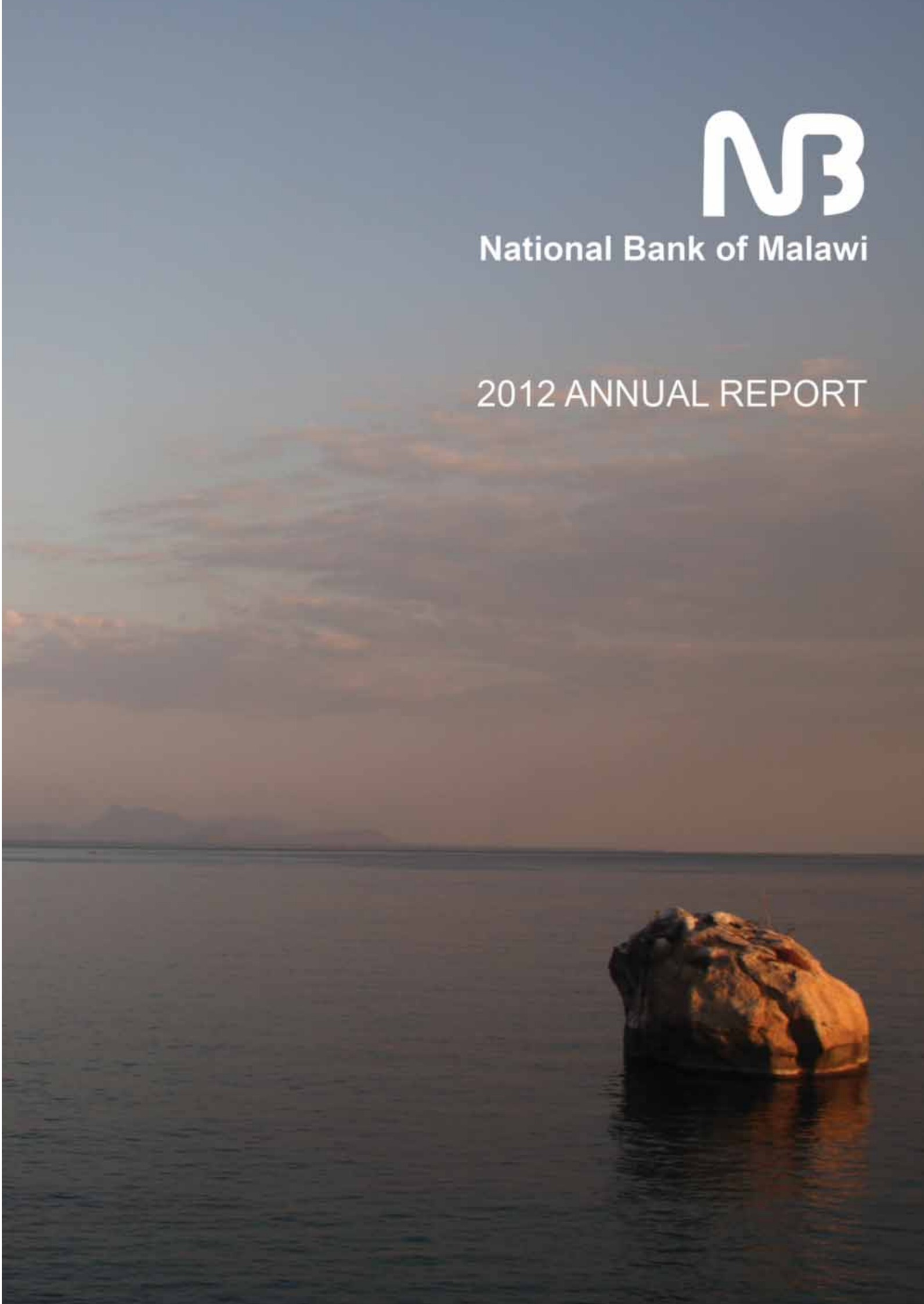




National Bank of Malawi

2012 ANNUAL REPORT



2012
ANNUAL
REPORT



VISION

To be the most successful financial institution in Malawi with a visible presence in the Southern Africa Region.

MISSION STATEMENT

To provide the best financial services in Malawi and the region, distinguished by outstanding service, product innovation and sustained earnings growth.



CORE VALUES

Customer Satisfaction

Always striving to meet our customers' expectations and putting the customer first.

Employee Recruitment and Development

- Employees are the key to the success of National Bank of Malawi
- The Bank will recruit based on merit and competencies required for the job.
- The Bank will ensure that employees are properly trained so that it retains a disciplined and motivated staff.
- The Bank will provide a working environment which is conducive to continuous employee self-development and advancement

Employee Commitment

The Bank will be committed to excellence in its performance and that the employees will have a clear understanding of its objectives and goals.

Integrity and Trust

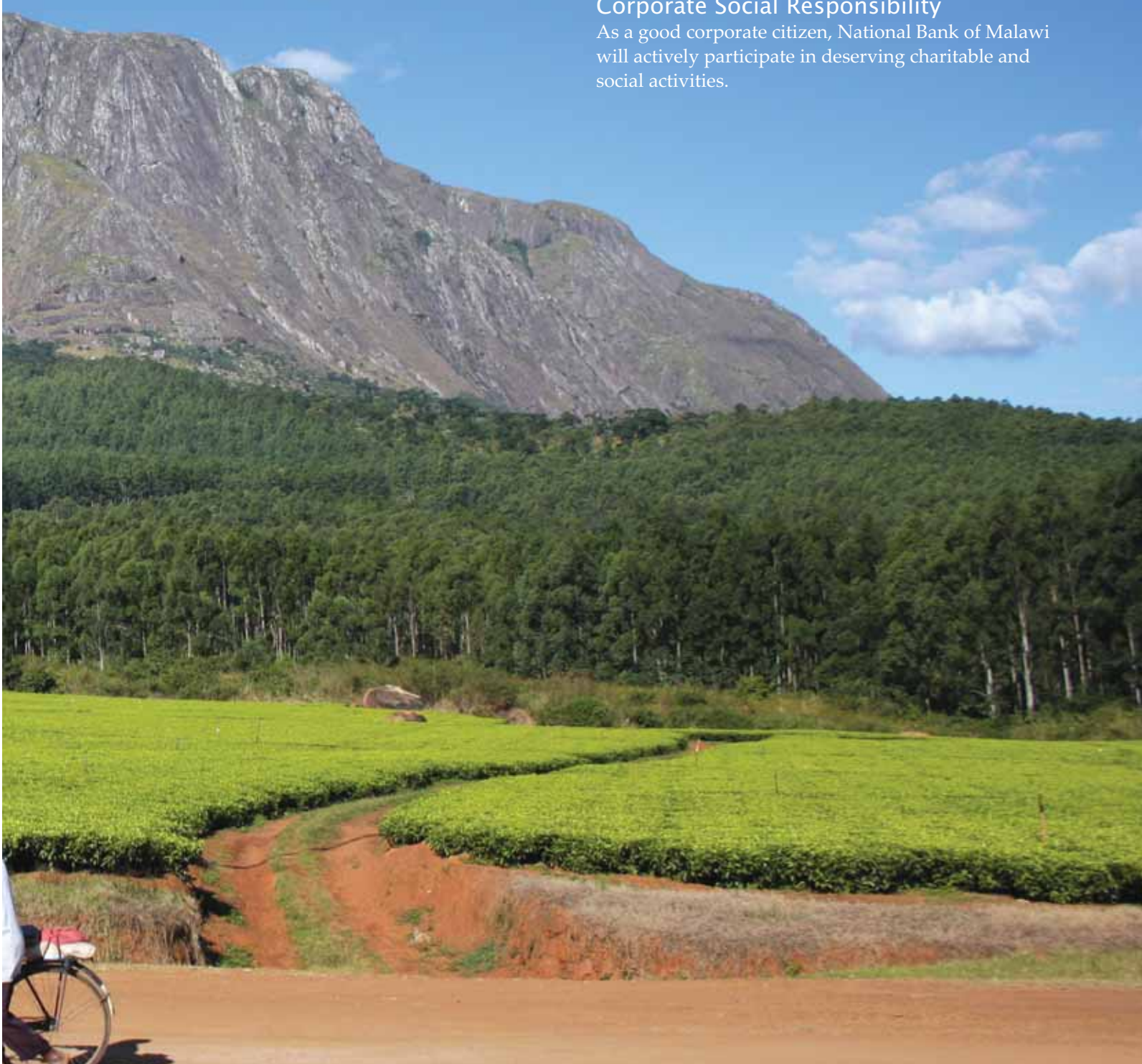
All Bank employees will fully comply with and share the Bank's commitment to high moral, ethical and legal standards.

Team Work

The Bank will build and maintain a culture of mutual respect, recognition and cooperation and promote feedback, effective communication and group work.

Corporate Social Responsibility

As a good corporate citizen, National Bank of Malawi will actively participate in deserving charitable and social activities.





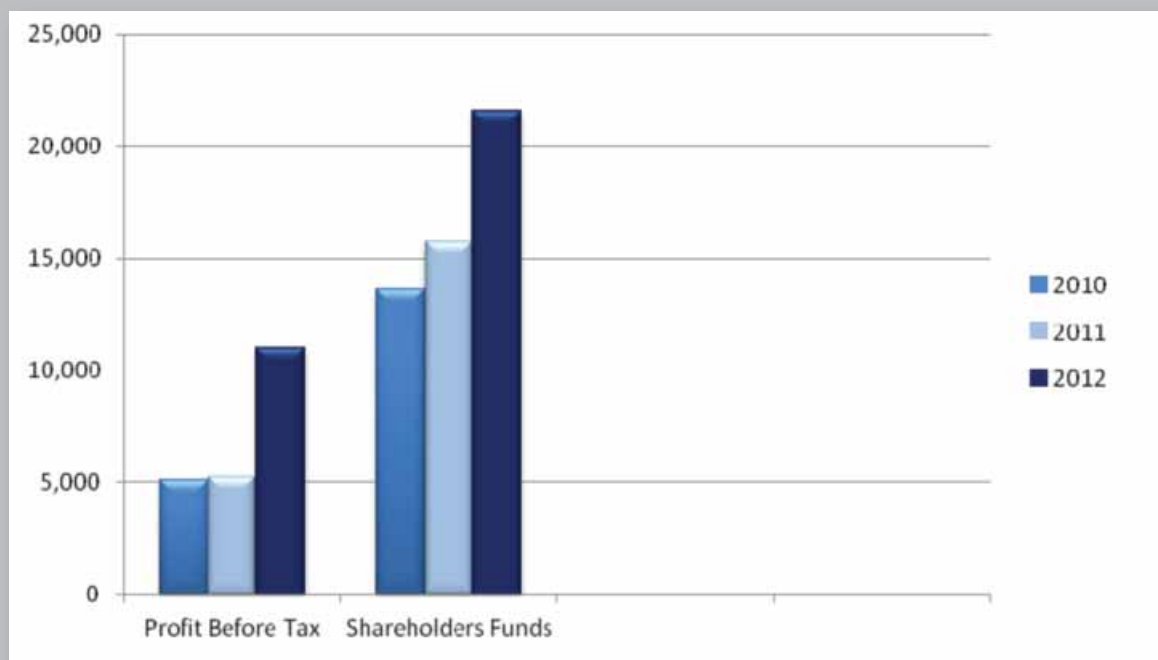
CONTENTS

Group Financial Highlights	6
Current Directors	8 - 9
Report of the Directors	10 - 11
Chairman's Report	12 - 13
Senior Management	16 - 17
Chief Executive Officer's Statement	18 - 22
Corporate Activities	24 - 29
Selected Key Clients' Activities	32 - 35
Economic Review and Prospects for 2012	36
Corporate Governance Statement	38 - 39
Statement of Directors' Responsibilities	40
Independent Auditor's Report	41
Statements of Financial Position	42
Statements of Comprehensive Income	43
Statements of Changes in Equity	44 - 45
Statements of Cashflows	46
Notes to the Financial Statements	47 - 105
Correspondent Banks	106
Head Office and Service Centres	107
Map of Malawi - NBM Service Centres	108

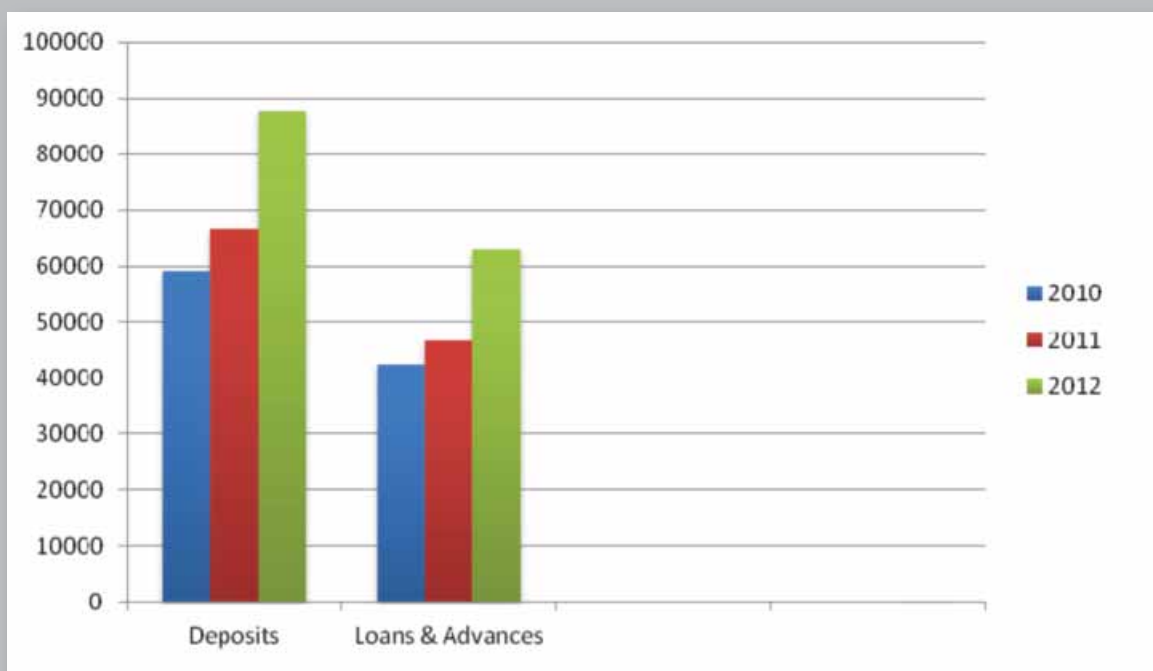
GROUP FINANCIAL HIGHLIGHTS

	K'm 2010	K'm 2011	K'm 2012	% Change 12 vs 11
Profit before tax	5,078	5,236	11,005	110%
Shareholders Funds	13,584	15,703	21,567	37%
Deposits	59,023	66,751	87,480	31%
Loans and Advances	42,529	46,573	63,001	35%

K'M



K'M



CURRENT DIRECTORS



CURRENT DIRECTORS



Front Row (From Left)

Zunzo E. Mitole (Mrs) (39)
LLB (Hons)(Mw)
Ag. Company Secretary

Dr. Matthews A P Chikaonda (58)
BA (Hons), MBA, Ph.D.
Chairman

Elias J Kambalame (66)
BA (Econ.)
Director

Back Row (From Left)

George B Partridge (49)
B.Soc.Sc, (Econ), Msc
(Finance), FCCA,
CPA (Mw)
Director

Macfussy M Kawawa (48)
B.Acc (Hons), FCCA, CPA
(Mw), MBA
Director

Pius P Mulipa (59)
Dip. (Mgt), BA, MSc
(Mgt)
Director

Chris A Kapanga (53)
ACII, MBA, Chartered
Insurer
Director

Elizabeth Mafeni (Mrs) (44)
MBL, FCCA, B.Com.
Director





The directors have pleasure in presenting the Consolidated and Separate Financial Statements of National Bank of Malawi for the year ended 31 December 2012.

CAPITAL

The authorised share capital of the Bank is K500m (2011: K500m) divided into 500,000,000 Ordinary Shares of K1 each. The issued capital is K467m (2011: K467m) divided into 466,931,738 (2011: 466,931,738) fully paid Ordinary Shares of K1 each.

The shareholders and their respective shareholdings are:

	2012 %	2011 %
Press Corporation Limited	51.5	51.5
Old Mutual Group	24.5	24.5
Members of the public	22.2	22.2
Employees (ESOP)	1.8	1.8
	100.0	100.0

PROFIT AND DIVIDENDS

The directors report a consolidated profit before tax of K11,005m (2011: K5,236m) for the year. A final dividend of

K1,500m (2011: K1,261m) is proposed for the year. Two interim dividends of K1,134m and K1,200m (2011: one interim dividend of K840m) were paid to shareholders on 31 August 2012 and 28 December 2012, respectively.

DIRECTORS

The following directors, appointed in terms of Article 52 of the Articles of Association, served in office during the year:

Chikaonda, Dr. M A P	All year
Mulipa, P P	All year
Kambalame, E	All year
Partridge, G B	All year
Kawawa, M M	All year
Kapanga C	All year
Mafeni E Mrs.	All year
Pote G	Up to May, 2012
Mawindo, D	Up to May, 2012

The directors report a consolidated profit before tax of K11,005m (2011: K5,236m) for the year. A final dividend of K1,500m (2011: K1,261m) is proposed for the year.

DIRECTORS' INTERESTS

The following directors held shares in the Bank as at 31 December 2012:

Mulipa, P P	20,367 (2011: 20,367) Ordinary Shares
Partridge, G B	639,634 (2011: 605,634) Ordinary Shares
Kawawa, M M	113,255 (2011: 104,456) Ordinary Shares

From 2006 to 2010, the Bank made offers of options under the ESOP scheme to G B Partridge and M M Kawawa amounting to 30,800 and 21,500 Ordinary Shares, respectively. There were no other contracts between the Bank and its directors nor were there any arrangements to enable the directors of the Bank to acquire shares in the Bank.

DONATIONS

During the year, the Bank made charitable donations of K32m (2011: K10m).

ACTIVITIES

The Group is engaged in the business of commercial banking and stockbroking.

Subsidiaries of National Bank of Malawi	Percentage of control	Nature of operations
NBM Capital Markets Limited	100% (2011: 100%)	Investments and Fund Management
NBM Securities Limited	100% (2011: 100%)	Dormant
National Bank of Malawi Nominees Limited	100% (2011: 100%)	Holding of investments as nominee
Stockbrokers Malawi Limited	75% (2011: 75%)	Registered Stockbroker
NBM Bureau de Change Limited	100%	Bureau de Change

AREAS OF OPERATION

The Bank has 29 (2011: 28) service centres throughout the country. The Bank and its subsidiaries' registered offices and principal places of business are in Blantyre.


AUDITORS

The auditors, Deloitte, have signified their willingness to continue in office and a resolution is to be proposed at the forthcoming Annual General Meeting in relation to their appointment as auditors in respect of the year ending 31 December 2013.

BY ORDER OF THE BOARD



Zunzo E. Mitole (Mrs)
Ag. Company Secretary



Although there was a generally unfavourable business climate in the first half of the year, the bank recorded significant growth in all its business lines during the second half...

THE OPERATING ENVIRONMENT

The operating environment in the first half of 2012 was generally poor due to excessive government controls on several aspects of the economy including the revival of a strict exchange controls regime and the artificial fixing of the exchange rate. This resulted in low business confidence levels which considerably slowed down economic activity, recording a GDP growth rate of only 1.9%.

The new administration which took over government in April (in line with the provisions of the Republican Constitution) embraced a more liberal and market oriented approach to economic management and sent positive signals of business recovery prospects. The IMF which had previously suspended its program revived its relationship with government culminating into an agreement of a new program. Donor support programs previously suspended due to poor economic management and governance concerns were also restored. Consequently confidence started to return in the second half of the year and business operating capacity improved.

PERFORMANCE

I am pleased to announce a group pre-tax profit of MK11b,

compared with MK5.2b earned in 2011, representing a 110% increase.

Although there was a generally unfavourable business climate in the first half of the year, the bank recorded significant growth in all its business lines during the second half due to the monetary reforms, the first phase of a comprehensive government Economic Recovery Program (ERP).

The NBM Towers Business Centre and Office Complex and other properties were revalued as at 31st December 2012, resulting in the bank writing back to income a total of MK838m out of previously recognised fair value adjustment losses.

STRATEGY AND PROSPECTS

As will be read in the Economic Review section of this Annual Report, at the projected GDP growth rate of 5% in 2013, the business outlook is positive and there are signs of improved economic performance than in the previous year. However, the bank still expects continued macroeconomic instability during the adjustment process that the country is going through. We envisage that inflation and the high interest rates will peak during the first half of the year before the possible commencement of a downward trend in the later part of the year, perhaps with



Dr Matthews A.P. Chikaonda, Chairman

some measure of stability in the exchange rate.

The above developments will be complemented by a better harvest season than in 2012 and the continued goodwill of the donors. This should be good for business generally, and commercial banking in particular, albeit that for a greater part of the year the economy will still be affected by challenges of adjustment.

The bank is well equipped with the necessary resources, and an ambitious 5-year strategic plan to stay on a sustainable growth path. The strategy embraces the use of technology and entrenchment of appropriate attitudes in staff to address improvements in customer service, delivery platforms and widening the product range, while at the same time repositioning the spread and depth of its investments as well as strategic partnerships. I am confident that 2013 will be another year of strong performance for the bank.

BOARD OF DIRECTORS

Mr. G. Pote and Mr. D. Mawindo resigned from the Board during the year and the process of identifying replacements is at an advanced stage. On behalf of the shareholders, and on my own behalf, I would like to take this opportunity to thank the two

directors who have left the Board for their valuable contributions and support during their tenure and wish them well in their new responsibilities. I also wish to thank fellow directors for their support, dedication and co-operation and look forward to working with them in 2013 and beyond.

MANAGEMENT AND STAFF

I am deeply grateful to our workforce for showing professionalism and rising up to the challenges that emerged during the year which enabled the bank to achieve such commendable results. On behalf of my fellow directors and the shareholders I wish to convey my sincere gratitude and congratulations to them. I am confident that as the bank faces new challenges, we can count on their commitment, loyalty, hard work and professionalism.

Matthews A.P. Chikaonda, Ph.D
CHAIRMAN

Make Malawi Cash Free



SENIOR MANAGEMENT



SENIOR MANAGEMENT



Seated (From Left)

Charles Dulira (44)
BA (Public Administration)
Head, Human Resources

Zunzo E. Mitole (Mrs) (39)
LLB (Hons)(Mw)
Ag. Company Secretary

George B Partridge (49)
B.Soc.Sc, (Econ), MSc (Finance),
FCCA, CPA (Mw)
Chief Executive

Eluphy Salamba (45)
B.Comm (Business Admin),
MSc (LCM)
Head, Credit Management

Harry Mukaka (45)
BA (Public Admin.), MBA
Head, Treasury and Financial Institutions

John Mitchell (48)
BSc. (Technical Education),
MSc (Computing)
Head, Information Technology

Isaac J Kanje (51)
B.Acc (Hons), FCCA, CPA (Mw),
CISA, FIBSA, MBA
Head, Risk

Harold Jiya (41)
B.com., ACIB, MBA
Head, Corporate Banking



Standing (From Left)

Tayemu H Masikini (55)
 Post Graduate Diploma in
 Computing, BSc.
Head, Administration

Oswin Kasunda (46)
 B.Com, Msc (St.Mgt)
**Head, Personal and
 Business Banking**

Austin N D Musyani [54]
 BA[Public Admin.], MPA, MBA.
**Head, Customer Service
 and Transactional Banking**

Daniel Jere (39)
 B.Acc, ACMA, CGMA,
 CPA(Mw)
Head, Internal Audit

William Kaunda(43)
 BSc, MSc (Bus Mgt)
**Head, Cards
 and e-Banking**

Brian Boby (48)
 B.Soc.Sc., MBA
Head, Operations

Wilkins G. Mijiga (41)
 B.Soc.Sc. (Econ)
Chief Marketing Officer

Macfussy M Kawawa (48)
 B.Acc (Hons), FCCA,
 CPA (Mw), MBA
**General Manager &
 Chief Financial Officer**

Deposits and loans and advances grew by 31% and 35 % respectively. Total earning assets grew by 44% while total income increased by 61%.

PERFORMANCE OVERVIEW

The operating business environment in the first half of 2012 was poor. It was characterized by low business confidence levels arising out of poor political governance and economic policies generally, and an overvalued exchange rate in particular. The exchange rate had been artificially fixed for the previous 3 years and as a result, there were acute foreign exchange shortages which resulted in the inability of the country to pay its external bills.

A significant amount of external arrears had built up and the perception of country risk got worse. This led to the scaling down and closures of some client operations as businesses could not import raw materials. Distribution logistics were severely affected due to persistent shortages of fuel. These negative developments on bank customers had adversely impacted on the bank business through the underutilization of some of our products.

Businesses started to recover in the second half of the year following the change of government. The new government

implemented market oriented monetary reforms which had an immediate positive impact on our customers and consequently, the bank. The bank therefore recorded significant growth in the second half of the year. Deposits and loans and advances grew by 31% and 35% respectively. Total earning assets grew by 44% while total income increased by 61%.

CORPORATE BANKING

The slow-down in business activity in the first half of the year resulted in the underutilisation of loan and overdraft facilities and a reduction in international trade business. The relaxation of exchange controls on the current account and introduction of other market oriented economic policies by the new administration culminated into increased activities and improved utilisation of bank products and services during the second half of the year.

Among other initiatives, the bank introduced a specific US dollar line of credit that enabled us extend medium to long-term loans at favourable rates to exporters to boost their productive capacity to take advantage of the favourable exporters' environment that



George B Partridge, CEO

had just been created by the liberalization of the exchange rate and the relaxation of exchange controls. These facilities, which are also in support of the government's efforts to broaden the country's export base, have been well received by the market.

With the improving general business environment and the consolidation of our project finance desk, we had concluded several groundbreaking deals and are positive of some good years ahead arising from such transactions.

PERSONAL AND BUSINESS BANKING

Personal, Retail Banking and SME business recorded remarkable growth in 2012, the challenging business environment notwithstanding. Personal and leasing business grew by over 50% while the SME sector business grew by just over 20%. The opening of new service centres, most notably the ultra modern Henderson Street Service Centre also resulted in significant increase in the recruitment of a new customer base.

The bank continues to focus on Personal and SME Banking as one area of growth, the emphasis being on provision of customer

centric solutions. Going forward the strategic focus is on further segmentation of the personal and SME banking portfolio, so as to allow adequate latitude for introduction of tailor made solutions to suit each identified segment.

SERVICE DELIVERY CHANNELS

Rebranding and Restructuring

In order to strategically focus its resources towards being proactively customer centric, the bank split its Customer Service and Transactional Banking Division into two separate divisions, Customer Service and Cards and e-Banking.

Through the newly formed Customer Service Division, the bank made significant progress towards enhancement of its frontline customer flow management. By the end of the year, the electronic queuing management system had been successfully implemented at seven of our major outlets. Through this innovation, which has brought with it a more efficient and transparent management of queues in the banking halls, in line with our values on fairness, the customer experience has improved tremendously. Roll out to the remaining service centres is expected to be completed by the end of the first half of 2013.



Chitipa Service Centre



Chitipa Service Centre was officially opened in the first quarter of 2012 bringing the number of our Service Centres to 29. In response to business and customer needs we plan to continue with establishment of additional Service Centres using a combination of agency as well as brick and mortar presence.

CARDS AND e-BANKING SERVICES

Cards and e-Banking division was created in the course of the year and is tasked with the responsibility of repositioning the bank in its growing payments business. We aim to continue consolidating our leading edge in card and e-banking business in Malawi. The division is responsible for the popularization and the growth of alternative banking channels which includes expansion and proliferation of ATM products, Merchant Services (POS), Electronic Funds Transfer, e-commerce, Internet and Mobile Phone Banking.

Going forward the Bank intends to venture into new areas of payments business, and forge strategic partnerships with key players such as MasterCard and PayPal in addition to the current Visa International. Locally the Bank is actively involved in the development of the National Switch in order to garner the benefits of interoperability among local banks' systems.

BASEL II COMPLIANCE AND INFORMATION TECHNOLOGY SYSTEM

Malawi banks are supposed to comply with Basel II by 1st January 2014. In this connection, and as part of the continuing efforts to enhance the performance of the Bank's IT systems, various infrastructure components of the T24 and other related systems were upgraded. This included memory and bandwidth upgrades to improve processing performance and provide more facilities, flexibility, interfaces and stability.

We commenced the procurement of a number of additional functional modules to be added to the T24 system, all aimed at enhancing the system's capability to enable the bank serve its customers better and fully comply with the new Basel Accords. In this regard Misys Almonde was procured as the bank's Basel II platform on market risk. The system is expected to be fully operational by June 2013, ahead of the regulatory deadline.

TREASURY

Revenue from treasury operations was one of the major sources of income for the bank in the year. Earnings from foreign exchange significantly exceeded budget despite the subdued performance in the first half of the year which was largely due to foreign exchange availability challenges the country continued to experience following the poor tobacco season and the suspension of a program with the IMF, which left many bilateral donors withhold aid. As the country's economy is slowly recovering, and with a new IMF program now on track, we expect a much more improved trading environment in 2013.

Money market income also exceeded budget largely due to better yields experienced for a better part of the year, a situation likely to continue for the greater part of 2013.

The equities desk performed well above expectation as a result of the continued recovery of the Malawi Stock Exchange market. We expect a flat performance in 2013 as a few counters appear to be struggling, a situation likely to persist for those counters.

HUMAN RESOURCES AND CONTINUOUS DEVELOPMENT

The major focus in 2012 continued to be on Cultural Transformation related activities. Having conducted the hugely successful cultural transformation workshops in 2011 for managers and Change Agents, attention in 2012 shifted to the remaining staff members in all units of the Bank to make them also appreciate the need for Cultural change.

Staff continued to excel in their personal development with a number of them completing their masters' degree studies and some attaining the professional qualifications of chartered banker and certified chartered accountant. In the course of the year, we offered scholarships to two managers to pursue studies for masters' degrees in Risk Management and Business Management respectively.

The bank also continued to offer short-term in house courses to its employees at its purpose built Learning and Growth Centre, covering customer care and general banking operations.

SUBSIDIARY AND ASSOCIATE COMPANIES

Stockbrokers Malawi Limited (SML)

In the year under review, the company recorded strong performance. It turned around from a loss making position in spite of a very challenging operating environment, registering 54% increase in revenue and a growth in the money market book of 71%. A pre tax profit of MK49.95m was recorded (2011: MK3.71m loss).

With the current positive developments in the operating environment, and the strategies in place, it is expected that the company will continue to register significant progress in both business growth and profitability.

United General Insurance Company (UGI)

The Company registered significant growth in Profit after tax from MK46m in 2011 to MK92 million in 2012, mainly on account of investment income. Gross premium written grew by 34% from MK1.94 billion in 2011 to MK2.6 billion and similarly Net premium written grew by 26% from MK1.5 billion to MK1.9 billion. The company managed to contain expenses, which were 17% (2011: 19%) of gross premium written. However, claims continued to be an industry challenge resulting into an overall loss ratio of 67%.

The company's debtors' situation remarkably improved in 2012 due to the introduction of the Premium Payment Directive by the registrar which has significantly assisted in the management of the solvency ratio. In spite of this improvement, the solvency ratio fell below the minimum threshold and was subject of corrective action by shareholders at the time of reporting.

NBM Capital Markets Limited

NBM Capital Markets, a wholly owned subsidiary of the bank became fully operational in 2012.

The company works in parallel with the Financial Management Services (FMS) Department of National Bank which has over

the years been offering both investment management and fund administration services to our investors. As a Fund Manager and Investment Advisor, NBM Capital has now taken over the investment function from the FMS department, which continues to offer fund administration services to various clients in the market.

After 9 months of operation NBM Capital reported satisfactory performance and turned in a small profit after tax.

Having successfully gone through the settling in phase, the company which has assets under management standing at over MK15 billion looks well prepared to deliver even better results in 2013.

NBM Bureau de Change

The performance of NBM Bureau de Change, a wholly owned subsidiary of the Bank has been mixed; being poor in the initial stages due to numerous foreign exchange controls placed on the business in addition to start up teething challenges and only improved when a number of those restrictions were removed in the course of 2012 following a number of policy shifts by the present government.

Prospects for profitable business appear good, with the continued efforts by government to liberalise the economy further, although new entrants may also bring in more competition.

CSR ACTIVITIES

The Bank has continued to take issues of Corporate Social Responsibility(CSR) seriously. During the year under review, we committed ourselves to uplifting the lives of the under privileged by empowering them to become self-reliant.

The Bank made a contribution of MK10.0 million to the rural community of T/A Kwataine in Ntcheu District to assist the local people with a Maternity Health Clinic. The donation is aimed at reducing maternal deaths and improving women's health and survival of newly born babies.

The Bank also responded to an appeal from World Vision International to assist the rural people of Chikwina Mpamba Area Development Program in Nkhata Bay District with clean and safe water by donating MK3.5 million to a water project.

The activities of the MK50million pledged towards the establishment of a Masters' Degree Programme in Commercial Law at the University of Malawi continued this year by making a donation of MK8.2 million towards the procurement of books and computers. The bank has so far disbursed about MK29m towards this venture.

The Bank also continued its 4 year refurbishment programme of a TB ward at the country's biggest referral hospital, Queen Elizabeth Central, with a MK5.0 million donation.

Other notable donations during the year included: MK2.4 million to Malawi Against Physical Disabilities, for wheel

chairs and MK1.8 million worth of beds, mattresses and blankets at Chitipa District Hospital, among others.

OUTLOOK

Pressure on prices is expected to be sustained well into the second quarter due to expected high government borrowing coupled with the exchange rate pass through effects as the Kwacha continues to depreciate against major currencies.

This pressure is expected to abate towards the end of the second quarter as export proceeds become available on the market from tobacco exports. A good maize harvest should in due course help reduce food inflation.

Looking into 2013, the forecast is for the monetary authorities to continue maintaining a tight monetary policy stance until inflation which is on the rise is brought under control. Government borrowing is also expected to be significant to cover up for the extra budgetary expenditure and arrears that have built up over the years with suppliers. Given these developments, interest rates are expected to remain high until the third quarter of 2013. Demand for banking products is therefore expected to be rather dampened in real terms as a consequence of the high cost of borrowing.

We therefore foresee continued challenges in 2013, though of a different kind. The bank is however ready to overcome these challenges and we envisage a strong performance through our ability to leverage on our core strengths and exploiting opportunities in the market that focus on maximizing value delivery platforms through staff multiskilling, maintenance of effective IT platforms and product innovation among other initiatives, guided by our new 2013-2017 five year strategic plan.

CONCLUSION

In conclusion, I would like to thank the Chairman and the Board of directors for their guidance, support and direction during the year. I also convey my sincere gratitude to my senior management colleagues for their creativity, commitment and outstanding contributions in a year full of challenges. My profound gratitude and appreciation goes to all members of staff for their dedication and hard work and call upon them to redouble their efforts in 2013 and beyond as we face the challenge of implementing our new 5-year strategic plan.

Finally I take the opportunity to sincerely thank our customers and our correspondent banks worldwide for their custom and trust in our bank, especially in the past few years that saw deteriorating country risk. I look forward to their support and confidence that they have continued to show to this bank despite past country risk challenges.

George B Partridge
CHIEF EXECUTIVE OFFICER

CORPORATE ACTIVITIES



NBM Towers official opening

Her Excellency, the State President of the Republic of Malawi, Dr Joyce Banda graciously officially opened NBM Towers on 24 July 2012.



Unveiling the plaque

Tour of NBM Towers



MK10 million donation to Safe Motherhood



NBM Towers (Front view) hosting:

- NBM Head Office
- Henderson Street Service Centre
- Stockbrokers Malawi Limited
- NBM Capital Markets

Vice President of the Republic of Malawi The Right Hon. Khumbo Kachali (L), NBM Board Chairman Dr Matthews Chikaonda (C) and NBM's CEO Mr George Partridge.



A great day it was! The two top officers Mr George Partridge (CEO) and Mr Macfussy Kawawa (General Manager) celebrating.

The invited guests



NBM staff in a special NBM Towers cloth.



NBM Towers (Back view)



The launch of Cultural Transformation Programme termed "Project Evolution"



Staff parades in streets of major cities in celebration of Project Evolution.



CSR activities



MK8.2 million for the establishment of a Master's Degree program.



CSR activities



Celebrating Christmas with pensioners



Participating in a nationwide tree planting exercise



Excellence Awards at the University of Malawi

CSR activities



Catholic University MK1 million donation for a water project.



Sponsorship of Sports



Construction of a MK10 million Maternal Clinic underway in Ntcheu

CSR activities



Kids from Nkhudzi Bay Primary School received lanterns and notebooks.



Kettie Kondowe (L) of Legal Department cheering orphans during Festive Season.

SELECTED KEY CLIENTS



SELECTED KEY CLIENTS

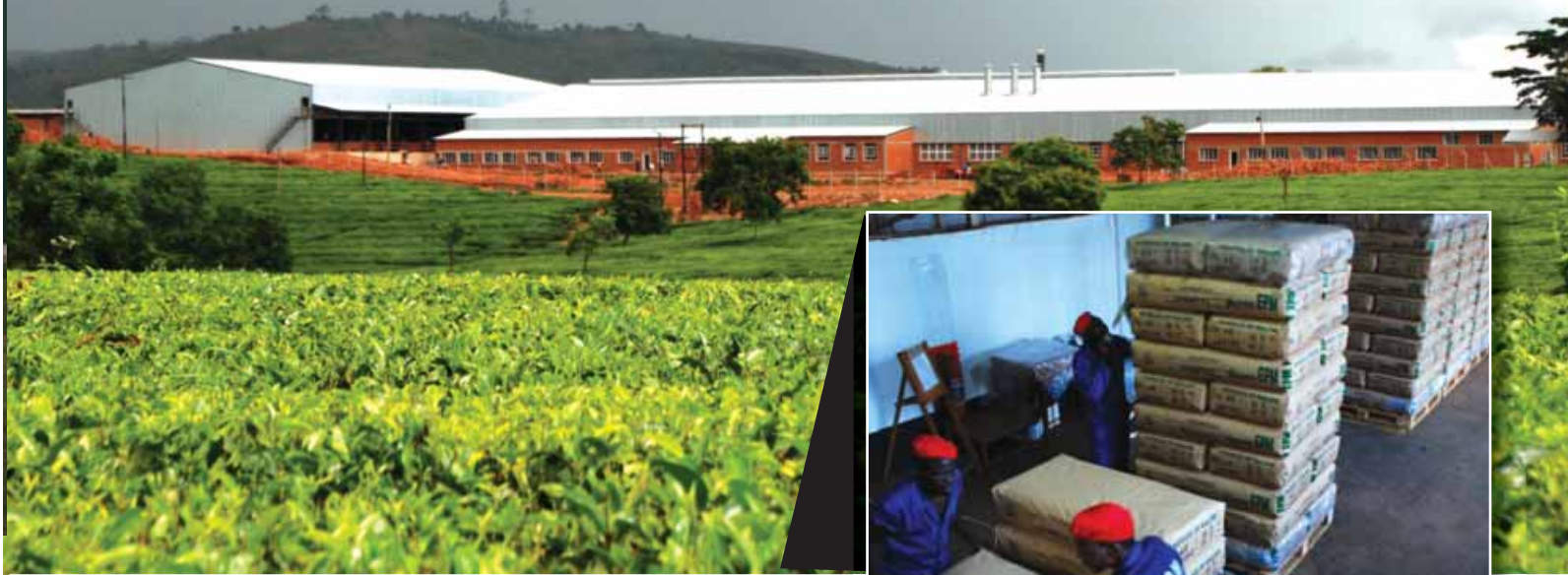


BBGL, Lilongwe new plant



Ulemu Mchuma Puma Filling Station – Blantyre





Eastern Produce – New tea factory in Makwasa



Laudadel Tea Factory in Mulanje



MPICO office complex City Centre, Lilongwe.



SELECTED KEY CLIENTS



Farmers World Limited, Malawi's growing power



Annie's Lodge, Exceeding your expectations



finger lick



DEVELOPMENTS IN 2012

The Malawi economy registered modest GDP growth of 1.9% in 2012, (2011: 4.3%) due to contraction in the agricultural and manufacturing sectors. In particular, tobacco saw record low production levels at only 79.8 million Kgs (2011 : 237 million Kgs) raking in USD177.8 million (2011 : USD293.7 million). In addition to poor economic management, lower than average rainfall in some areas had also negatively impacted on the output of many crops.

An overvalued local currency as a result of over 3 years of fixing the exchange rate and a return to a closed and controlled economy during this period led to the reluctance of foreign exchange earners to bring their export proceeds back into the country. These policies also motivated the smuggling of crops such as maize, legumes and tobacco to the neighboring countries of Mozambique, Zambia and Tanzania. These events fueled the scarcity of foreign exchange hence reducing the capacity of the manufacturing industry to import necessary raw materials and fuel.

The second quarter of 2012 saw the introduction of key market-oriented reforms following the death of President Bingu wa Mutharika and the coming in of the Joyce Banda administration. Key market reforms included the floatation of the Malawi Kwacha, removal of exchange controls on the current account and doing away with price controls and subsidies on utilities and fuel. These reforms were complemented with the implementation of an austerity budget to restore macroeconomic imbalances stemming from a long period of an overvalued exchange rate and widening budget deficit.

The Malawi Kwacha rate of exchange to the US dollar was devalued on 7th May 2012 from MK165/1USD to MK250/1USD and subsequently the authorities adopted a freely floating exchange rate regime. The floatation saw the currency closing at about MK340/1USD in the year. As a result of the adoption of a liberalized framework to economic management, an IMF program and donor support programs which were previously suspended due to poor economic management and bad governance respectively were restored.

The financial sector experienced liquidity challenges due to the settlement of significant external arrears accumulated in previous years due to the de facto pegging of the Malawi Kwacha to the US dollar.

INFLATION


Inflation was on an increasing trend in 2012, beginning the year at 10.3% and closing at 34.6% (annual average 21%). This was mainly due to the pass through effects of the exchange rate depreciation, removal of subsidies on fuel and utilities.

OUTLOOK FOR 2013

The economy is expected to rebound in 2013 registering real GDP growth of 5% mainly due to expected improvements in agriculture output, and in particular, tobacco production, the mainstay of the country's exports. The economy is also expected to benefit over the medium to long term from the market-oriented policies adopted by the government, which have generally boosted private sector confidence, especially the export sector.

The economy is expected to rebound in 2013 registering real GDP growth of 5% mainly due to expected improvements in agriculture output, and in particular, tobacco production...





CORPORATE GOVERNANCE STATEMENT	38 – 39
STATEMENT OF DIRECTORS’ RESPONSIBILITIES	40
INDEPENDENT AUDITOR’S REPORT	41
STATEMENTS OF FINANCIAL POSITION	42
STATEMENTS OF COMPREHENSIVE INCOME	43
STATEMENTS OF CHANGES IN EQUITY	44 – 45
STATEMENTS OF CASHFLOWS	46
NOTES TO THE FINANCIAL STATEMENTS	47– 105
CORRESPONDENT BANKS	106
HEAD OFFICE & SERVICE CENTRES	107
MAP OF MALAWI SHOWING NBM SERVICE CENTRES	108

Compliance with policies and achievement of objectives are monitored by the Board by holding management accountable for its activities through bi-monthly Board meetings...

CORPORATE GOVERNANCE STATEMENT

The Board of National Bank of Malawi is committed to good corporate governance and to this effect subscribes to the principles of openness, integrity and accountability as set out in the Malawi Corporate Governance Code, The Cadbury Report and the King Reports. These principles are key to the effective and satisfactory relationship between the shareholders, customers, strategic partners, suppliers of various goods and services, regulators and staff.

While the Board sets the strategic objectives of the Bank, determines investment policies, risk appetite and performance criteria, it delegates the detailed planning and implementation of these objectives to management in accordance with appropriate parameters.

Compliance with policies and achievement of objectives are monitored by the Board by holding management accountable for its activities through bi-monthly Board meetings at which performance is reported. Compliance is also monitored through the meetings of the Risk, Audit, Appointments & Remuneration and Credit Committees of the Board.

Each of these committees has specific terms of reference issued by the Board, which are in the custody of the company secretary. Each committee chairman reports on the proceedings of his committee at the next meeting of the Board.

The directors have the responsibility of maintaining a system of internal controls, which provides reasonable assurance that the Bank has effective and efficient systems with sound internal financial controls governing all the operations of the bank in line with best practice. The system of internal controls also ensures that there is compliance with laws and regulations. In this regard the Board supports investments in accounting, financial and risk management systems that enable the Bank to produce timely reports to its shareholders, the regulatory authorities and members of the general public.

Note 34 to the financial statements explains in detail the risk management processes that the Bank has embraced.

The approved maximum number of directors for the Bank is eleven, comprising two executive and nine non-executive directors. Five of the non-executive directors are nominated by Press Corporation Limited, two non-executive directors by the Old Mutual Companies and the rest by the Board in unison in line with the Articles of Association. The shareholders have the right to remove the directors they appoint. The chairman is chosen from among these directors. Four positions of non-executive directors were vacant at the end of the year and the process to fill them was underway.

All non-executive directors hold or have held senior leadership positions in financial services, public and private sectors which contribute to their strength of character, independence of judgement and opinion so that no individual or group has unfettered powers or unequal access to information.

Committees of The Board

Risk Committee

The Risk sub Committee is currently chaired by Mr. C. Kapanga. It has the overall responsibility for the strategic risk management of the Bank as delegated by the Board.

The Bank's Risk division provides the directors with risk management reports covering credit, market, liquidity, operational and compliance risks among other reports, which assist the directors to provide the necessary oversight and direction in relation to current and potential future risk exposures and future risk strategy. In particular the Committee is also providing oversight on the Bank's preparation for the implementation of Basel II.

Audit Committee

The chairman of the Audit Committee was Mr. Dye Mawindo who was in the course of the year appointed to public office and

by virtue of that appointment he automatically ceased to be a director of the bank by regulation. The position of committee chairman is currently vacant and the process of identifying a replacement independent director is underway. The Audit Committee exercises the full powers and authority of the Board in accounting and financial reporting matters as guided by its terms of reference.

The Committee has overall responsibility for the Bank's system of internal control and for reviewing its effectiveness. This is done through a review of the on-going processes for identifying, evaluating and managing the significant risks faced by the Bank and through an annual assessment of risk management systems.

The Bank's internal audit function provides the directors with information which assists the directors in assessing the effectiveness of internal controls in each business unit through a pre-arranged audit programme. This programme addresses the full spectrum of the Bank's potential risks.

The Audit Committee meets at least three times a year with the Bank's senior management and the external auditors to review among other things, accounting, auditing, internal controls, financial reporting matters and published financial statements of the Bank. The Head of the Bank's Internal Audit Division as well as the external auditors have unrestricted access to this Committee at all times.

Appointments and Remuneration Committee

This sub-committee of the Board is currently chaired by Mr E.J. Kambalame. Its principal functions are to ensure that there is a robust succession plan, that the Bank's human resources are best utilised, and that members of staff are remunerated commensurately with their responsibilities and effectiveness.

Credit Committee

This sub-committee is currently chaired by Mr P.P. Mulipa and meets at least four times a year, in line with its terms of reference.

Its principal functions are to review and approve the Bank's credit policy including provisioning, large loan exposures outside the mandate of management, counter-party lending and dealing lines. It also takes note of schedules of substandard debts and lists of facilities granted to sensitive customers and senior management.

Code of Ethics

The Bank is committed to a policy of fair dealing and integrity in the conduct of its business. This commitment is based on the fundamental belief that business should be conducted morally, honestly, fairly, legally and in a transparent manner.

Auditor Independence

The Board has in place systems for ensuring the independence, integrity, competence and professionalism of the Bank's external auditors and has satisfied itself that during the year, no aspect of their work was impaired on these grounds.

Board Information and Development

Under the stewardship of the Chairman, the Company Secretary is responsible for advising the Board on all governance issues, ensuring that board procedures are followed and applicable rules and regulations are complied with. Further, all the directors individually and as committees, have access to the advice and services of the Company Secretary. Training programmes are devised from time to time for the directors to keep up with knowledge levels required for their oversight responsibilities.

In 2012 the focus continued to be on Risk Management.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

31 December 2012

The Companies Act, 1984, requires the directors to prepare financial statements for each financial year, which give a true and fair view of the state of affairs of the Bank and the Group as at the end of the financial year and of the operating results for that year.

The Act also requires the directors to ensure that the Bank and the Group keep proper accounting records which disclose with reasonable accuracy at any time the financial position of the Bank and the Group and enable them to ensure that the financial statements comply with the Companies Act, 1984.

In preparing the financial statements the directors accept responsibility for ensuring the following:

- Maintenance of proper accounting records;
- Selection of suitable accounting policies and applying them consistently;
- Making judgements and estimates that are reasonable and prudent;
- Compliance with applicable Accounting Standards when preparing financial statements; and
- Preparation of financial statements on a going concern basis unless it is inappropriate to presume that the Bank and the Group will continue in business.

The directors also accept responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Bank and the Group and to maintain adequate systems of internal controls to prevent and detect fraud and other irregularities.

The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the Bank and the Group and of their operating results, so far as concerns the members of the company.



DIRECTOR:
Mr. G.B. Partridge



DIRECTOR:
Dr M.A.P Chikaonda

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF NATIONAL BANK OF MALAWI AND ITS SUBSIDIARIES

We have audited the consolidated and separate financial statements of National Bank of Malawi and its subsidiaries (the Group) as set out on pages 42 to 105, which comprise the statement of financial position as at 31 December 2012, and the statement of comprehensive income, statement of changes in equity and the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' Responsibility for the Financial Statements

The Group's directors are responsible for preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and in a manner required by the Companies Act, 1984 and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

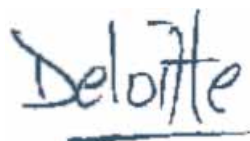
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank and the Group as of 31 December 2012, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards and in accordance with the provisions of the Companies Act, 1984, so far as concerns the members of the company.



27 March 2013

Audit • Tax • Consulting • Financial Advisory •

Resident Partners: N.T. Uka J.S. Melrose L.L. Katandula V.W. Beza C.A. Kapenda

A member of

Deloitte Touche Tohmatsu

STATEMENTS OF FINANCIAL POSITION

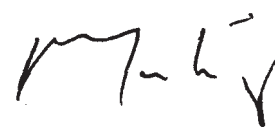
31 December 2012

	Notes	GROUP		COMPANY	
		2012 K'm	2011 K'm	2012 K'm	2011 K'm
ASSETS					
Cash and funds with Reserve Bank of Malawi	5	8,797	8,155	8,797	8,153
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	6	7,801	7,062	7,801	7,062
Government of Malawi local registered stock	7	372	467	372	467
Equity investments	8	732	695	731	683
Investment in associate	9	214	196	123	123
Investment in subsidiaries	10	-	-	142	125
Placements with other banks	11	19,347	8,753	19,347	8,753
Loans and advances	12	63,001	46,573	63,001	46,588
Other money market deposits	13	2,104	1,009	2,048	1,000
Assets held for sale	14	-	454	-	454
Other assets	15	8,539	4,201	8,486	4,181
Property, plant and equipment	16	15,366	12,685	15,321	12,655
Intangible assets	17	2,082	1,442	2,082	1,442
Deferred tax	18	1,134	417	1,134	417
Total assets		129,489	92,109	129,385	92,103
LIABILITIES AND EQUITY					
LIABILITIES					
Customer deposits	19	87,480	66,751	87,512	66,758
Amounts due to other banks	20	583	2,874	583	2,874
Current income tax liabilities	21	1,303	1,030	1,304	1,030
Loans	22	3,395	-	3,395	-
Other liabilities	23	15,161	5,166	15,099	5,133
Post-employment benefit obligation		-	585	-	585
Total liabilities		107,922	76,406	107,893	76,380
EQUITY					
Capital and reserves					
Share capital		467	467	467	467
Share premium		613	613	613	613
Loan loss reserve		632	466	632	466
Revaluation reserve		3,785	2,291	3,785	2,291
Retained earnings		16,051	11,859	15,995	11,886
Equity attributable to equity holders of the parent		21,548	15,696	21,492	15,723
Non-controlling interests		19	7	-	-
Total equity		21,567	15,703	21,492	15,723
Total equity and liabilities		129,489	92,109	129,385	92,103
Memorandum items					
Contingencies	33	5,551	4,215	5,551	4,215

The financial statements were approved and authorised for issue by the Board of Directors on 27 March, 2013 and were signed on its behalf by:



Chairman: Dr. M.A.P. Chikaonda



Director: Mr. G.B. Partridge

STATEMENTS OF COMPREHENSIVE INCOME

For the year ended 31 December 2012

	Notes	GROUP		COMPANY	
		2012 K'm	2011 K'm	2012 K'm	2011 K'm
Income					
Interest and similar income	25	12,270	9,116	12,274	9,089
Interest expense and similar charges	25	(2,407)	(956)	(2,408)	(956)
Net interest income	25	9,863	8,160	9,866	8,133
Commission and fee income	26	6,374	3,845	6,236	3,817
Gains less losses arising from dealing in foreign currencies		4,626	995	4,535	992
Income from operating leases		511	631	511	631
Fair value gain on equity investments	8	76	36	76	35
Profit/(loss) on disposal of equity investments		14	(1)	8	(2)
Share of profits of associate		26	1	-	-
Dividend income		51	40	50	39
Profit on disposal of property, plant and equipment		554	14	554	14
Total income		22,095	13,721	21,836	13,659
Expenditure					
Staff costs	27	5,552	2,243	5,476	2,206
Other operating expenditure	28	5,769	4,641	5,701	4,602
Properties fair value (gain)/loss	29	(838)	1,491	(838)	1,491
Total expenditure		10,483	8,375	10,339	8,299
Profit before recoveries and impairment losses on loans and advances		11,612	5,346	11,497	5,360
Recoveries on impaired loans and advances	12	253	207	253	207
Impairment losses on loans and advances	12	(860)	(317)	(860)	(317)
Profit before tax		11,005	5,236	10,890	5,250
Income tax expense	30	(3,418)	(1,678)	(3,399)	(1,671)
Profit for the year		7,587	3,558	7,491	3,579
Other comprehensive income					
Surplus on revaluation of properties	29	1,111	706	1,111	706
Deferred tax on revalued assets		762	(70)	762	(70)
Total other comprehensive income		1,873	636	1,873	636
Total comprehensive income for the year		9,460	4,194	9,364	4,215
Profit attributable to:					
Equity holders of the company	31	7,575	3,558	7,491	3,579
Non-controlling interests	12	-	-	-	-
		7,587	3,558	7,491	3,579
Comprehensive income attributable to:					
Equity holders of the company		9,448	4,194	9,364	4,215
Non-controlling interests	12	-	-	-	-
		9,460	4,194	9,364	4,215
Earnings per share (K)	31	16.22	7.62		
Diluted earnings per share (K)	31	16.22	7.62		
Dividend per share (K)	32	7.70	4.48		

STATEMENTS OF CHANGES IN EQUITY

For the year ended 31 December 2012

	Share capital K'm	Share premium K'm	Loan Loss reserve K'm	Revaluation reserve K'm	Retained earnings K'm	Equity attributable to equity holders of the parent K'm	Non-controlling interests K'm	Total K'm
GROUP								
2011								
As at 1 January 2011	467	597	411	1,671	10,431	13,577	7	13,584
Total comprehensive income	-	-	-	636	3,558	4,194	-	4,194
Transfer of excess depreciation	-	-	-	(16)	16	-	-	-
Transfer to loan loss reserve	-	-	55	-	(55)	-	-	-
2010 final dividend proposed and paid	-	-	-	-	(1,251)	(1,251)	-	(1,251)
2011 interim dividend proposed and paid	-	-	-	-	(840)	(840)	-	(840)
Issue of shares under ESOP	-	16	-	-	-	16	-	16
As at 31 December 2011	467	613	466	2,291	11,859	15,696	7	15,703
2012								
As at 1 January 2012	467	613	466	2,291	11,859	15,696	7	15,703
Total comprehensive income	-	-	-	1,873	7,575	9,448	12	9,460
Transfer on disposal of PPE	-	-	-	(325)	325	-	-	-
Transfer of excess depreciation	-	-	-	(54)	54	-	-	-
Transfer to loan loss reserve	-	-	166	-	(166)	-	-	-
2011 final dividend proposed and paid	-	-	-	-	(1,262)	(1,262)	-	(1,262)
2012 interim dividend proposed and paid	-	-	-	-	(2,334)	(2,334)	-	(2,334)
As at 31 December 2012	467	613	632	3,785	16,051	21,548	19	21,567

COMPANY

	Share capital K'm	Share premium K'm	Loan Loss reserve K'm	Revaluation reserve K'm	Retained earnings K'm	Total K'm
2011						
As at 1 January 2011	467	597	411	1,671	10,437	13,583
Total comprehensive income	-	-	-	636	3,579	4,215
Transfer of excess depreciation	-	-	-	(16)	16	-
Transfer to loan loss reserve	-	-	55	-	(55)	-
2010 final dividend proposed and paid	-	-	-	-	(1,251)	(1,251)
2011 interim dividend proposed and paid	-	-	-	-	(840)	(840)
Issue of shares under ESOP	-	16	-	-	-	16
As at 31 December 2011	467	613	466	2,291	11,886	15,723
2012						
As at 1 January 2012	467	613	466	2,291	11,886	15,723
Total comprehensive income	-	-	-	1,873	7,491	9,364
Transfer on disposal of PPE	-	-	-	(325)	325	-
Transfer of excess depreciation	-	-	-	(54)	54	-
Transfer to loan loss reserve	-	-	166	-	(166)	-
2011 final dividend proposed and paid	-	-	-	-	(1,261)	(1,261)
2012 interim dividend proposed and paid	-	-	-	-	(2,334)	(2,334)
As at 31 December 2012	467	613	632	3,785	15,995	21,492

STATEMENTS OF CHANGES IN EQUITY (Continued)

For the year ended 31 December 2012

	2012 K'm	2011 K'm
ANALYSIS OF SHARE CAPITAL		
Authorised		
500,000,000 Ordinary Shares of K1 each	500	500
Issued and fully paid		
466,931,738 Ordinary Shares of K1 each	467	467

GROUP & COMPANY

	2012 K'm	2011 K'm
LOAN LOSS RESERVE		
Loan loss reserve	632	466

The 1% general provision against risk assets as required by the Reserve Bank of Malawi cannot be offset against the gross value of the assets because IAS 39 *Financial Instruments: Recognition and Measurement* does not allow general provisions on anticipated future losses to be charged to the statement of comprehensive income.

In order to comply with Reserve Bank of Malawi capital adequacy requirements, a non-distributable statutory general reserve is used.

STATEMENTS OF CASHFLOWS

For the year ended 31 December 2012

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Cash flows from operating activities				
Profit before tax	11,005	5,236	10,890	5,250
Adjustments for:				
• Depreciation	1,392	1,320	1,383	1,318
• Profit on disposal of property, plant and equipment	(554)	(14)	(554)	(14)
• Gain/(loss) on disposal of equity investments	(14)	1	(8)	2
• Fair value gain on equity investments	(76)	(36)	(76)	(35)
• Dividend receivable	(51)	(40)	(50)	(39)
• Properties fair value (gain)/loss	(838)	1,491	(838)	1,491
• Share of profits of associate	(26)	(1)	-	-
• Increase in customer deposits	20,728	7,728	20,754	7,728
• Increase/(decrease) in other liabilities	9,994	(1,600)	9,965	(1,552)
• Decrease in employment benefit obligations	(585)	(911)	(585)	(909)
• Increase in loans and advances	(16,428)	(4,043)	(16,413)	(4,059)
• (Increase)/decrease in other assets	(4,316)	1,432	(4,291)	1,433
Cash generated from operations	20,231	10,563	20,177	10,614
Taxation paid	(3,090)	(1,228)	(3,080)	(1,228)
Net cash flow from operating activities	17,141	9,335	17,097	9,386
Cash flows from investing activities				
Increase in investments with maturity over three months	(651)	(3,057)	(668)	(3,086)
Purchase of property, plant and equipment	(2,968)	(3,134)	(2,944)	(3,101)
Proceeds from disposal of property, plant and equipment	1,214	343	1,214	343
Purchase of equity investments	(15)	(130)	(15)	(130)
Proceeds from disposal of equity investments	50	109	43	109
Dividends received	51	40	50	39
Net cash flow from investing activities	(2,319)	(5,829)	(2,320)	(5,826)
Cash flows from financing activities				
Proceeds from issue of shares	-	16	-	16
Proceeds from borrowings	3,395	-	3,395	-
Dividends paid	(3,595)	(2,091)	(3,595)	(2,091)
Net cash flow from financing activities	(200)	(2,075)	(200)	(2,075)
Net increase in cash and cash equivalents	14,622	1,431	14,577	1,485
Cash and cash equivalents at beginning of the year	15,043	13,612	15,032	13,547
Cash and cash equivalents at end of the year (note 35)	29,665	15,043	29,609	15,032

1. GENERAL INFORMATION

National Bank of Malawi Group (the Group) provides retail, corporate and investment banking as well as stockbroking and insurance services in Malawi. The Group has a network of 29 (2011:28) service centres.

The Bank, which is licensed under the Banking Act, 2009, Part II, is a limited liability company incorporated and domiciled in Malawi. The Bank is listed on the Malawi Stock Exchange.

The address of its principal place of business and registered office is National Bank Head Office, 7 Henderson Street, Blantyre, Malawi.

The Group's parent company is Press Corporation Limited (PCL), which is a limited liability company, incorporated and domiciled in Malawi. PCL is listed on the Malawi and London Stock Exchanges.

2. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

2.1 Standards and Interpretations affecting amounts reported and/or disclosed in the financial statements

In the current year, the Group has adopted those new and revised Standards and Interpretations issued by the International Accounting Standards Board and the International Financial Reporting Interpretations Committee of the International Accounting Standards Board that are relevant to its operations and are effective for annual reporting periods beginning on 1 January 2012.

The adoption of these new and revised Standards and Interpretations did not have a significant impact on the financial statements of the Group.

2.2 Standards and Interpretations in issue, not yet effective

At the date of authorisation of these financial statements, the following Standards and Interpretations were in issue but not yet effective:

- 2.2.1 IFRS 7 *Financial Instruments: Disclosures* - Amendments enhancing disclosures about offsetting of financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2013 and interim periods within those periods).
- 2.2.2 IFRS 7 *Financial Instruments: Disclosures* - Amendments requiring disclosures about the initial application of IFRS 9 (effective for annual periods beginning on or after 1 January 2015 (or otherwise when IFRS 9 is first applied)).
- 2.2.3 IFRS 9 *Financial Instruments - Classification and Measurement* (effective for annual periods beginning on or after 1 January 2015 - mandatory application date amended December 2011).
- 2.2.4 IFRS 9 *Financial Instruments - Accounting for financial liabilities and derecognition* (effective for annual periods beginning on or after 1 January 2015 - mandatory application date amended December 2011).
- 2.2.5 IFRS 10 *Consolidated Financial Statements* (effective for annual periods beginning on or after 1 January 2013).
- 2.2.6 IFRS 11 *Joint Arrangements* (effective for annual periods beginning on or after 1 January 2013).
- 2.2.7 IFRS 12 *Disclosure of Interests in Other Entities* (effective for annual periods beginning on or after 1 January 2013).
- 2.2.8 IFRS 13 *Fair Value Measurement* (effective for annual periods beginning on or after 1 January 2013).
- 2.2.9 IAS 1 *Presentation of Financial Statements* - Amendments to revise the way other comprehensive income is presented (effective for annual periods beginning on or after 1 July 2012).
- 2.2.10 IAS 19 *Employee Benefits* - Amended Standard resulting from Post-Employment Benefits and Termination Benefits projects (effective for annual periods beginning on or after 1 January 2013).
- 2.2.11 IAS 27 *Consolidated and Separate Financial Statements* - Reissued as IAS 27 *Separate Financial Statements* (as amended in 2011) (effective for annual periods beginning on or after 1 January 2013).
- 2.2.12 IAS 28 *Investments in Associates* - Reissued as IAS 28 *Investments in Associates and Joint Ventures* (as amended in 2011) (effective for annual periods beginning on or after 1 January 2013).
- 2.2.13 IAS 32 *Financial Instruments: Presentation* - Amendments to application guidance on the offsetting of financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2014).
- 2.2.14 IFRIC 20 *Stripping Costs in the Production Phase of a Surface Mine* (effective for annual periods beginning on or after 1 January 2013).

The directors anticipate that other than IFRS 9 and 13, these Standards and Interpretations in future periods will have no significant impact on the financial statements of the company. IFRS 9 will impact the measurement of financial instruments and IFRS 13 will impact all fair value measurements in the financial statements.

3. ACCOUNTING POLICIES

Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards.

Basis of preparation

The consolidated financial statements have been prepared on the historical cost basis, except for the revaluation of certain non-current assets and financial instruments. No other procedures are adopted to reflect the impact on the financial statements of specific price changes or changes in the general level of prices. The principal accounting policies of the Group, which are set out below, have been consistently followed in all material respects, unless otherwise stated.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 4.

3.1 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Group and its subsidiaries, Stockbrokers Malawi Limited and NBM Bureau de Change Limited. The Group financial statements also incorporate results of associated companies.

National Bank of Malawi Nominees Limited, NBM Securities Limited and NBM Capital Markets Limited are dormant subsidiaries and are not consolidated.

a. Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Bank has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interests. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference (negative goodwill) is recognised directly in the statement of comprehensive income.

All intra-Group transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. The accounting policies of subsidiaries are changed where necessary to ensure consistency with policies adopted by the Group.

Non-controlling interests (previously referred to as 'minority' interests) in subsidiaries are identified separately from the Group's equity therein. The interest of non-controlling shareholders may be initially measured either at fair value or at the non-controlling interests' proportionate share of the fair value of the acquiree's identifiable net assets. The choice of measurement basis is made on an acquisition-by-acquisition basis. Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition plus the non-controlling interests' share of subsequent changes in equity. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interests having a deficit balance.

b. Associates

Associates are all entities over which the Group has significant influence but no control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition. The Group's share of its associates' post-acquisition profits or losses is recognised in the statement of comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associates, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associates.

3. ACCOUNTING POLICIES (Continued)

3.1 Basis of consolidation (Continued)

b. Associates (Continued)

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provided for evidence of an impairment of the assets transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

3.2 Comparatives

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

3.3 Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition depending on the nature and purpose of the financial assets.

i. Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired or incurred principally for the purpose of selling in the short term or if it is part of a portfolio of identified financial investments that are managed together and for which there is evidence of a recent actual pattern of short term profit taking. Derivatives are also categorised as held for trading unless they are designated and effective as hedging instruments.

Financial instruments included in this category are recognised initially at fair value; transaction costs are taken directly to the statement of comprehensive income. Gains and losses arising from changes in fair value are included directly in the statement of comprehensive income and are reported as 'Net gains/(losses) on financial instruments classified as held for trading'. Interest income and expense and dividend income and expenses on financial assets held for trading are included in 'Net interest income' or 'Dividend income', respectively. The instruments are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership and the transfer qualifies for derecognising.

ii. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- a. those that the Group intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;
- b. those that the Group upon initial recognition designates as available for sale; or
- c. those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable.

Loans and receivables are initially recognised at fair value – which is the cash consideration to originate or purchase the loan including any transaction costs – and measured subsequently at amortised cost using the effective interest rate method. Loans and receivables are reported in the statement of financial position as loans and advances to banks or customers or as investment securities. Interest on loans is included in the statement of comprehensive income and is reported as 'Interest and similar income'. In the case of impairment, the impairment loss is reported as a deduction from the carrying value of the loan and recognised in the statement of comprehensive income as 'Loan impairment charges'.

iii. Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity other than:

- a. those that the Group upon initial recognition designates as at fair value through profit or loss;
- b. those that the Group designates as available for sale; and
- c. those that meet the definition of loans and receivables.

Were the Group to sell other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available for sale.

3. ACCOUNTING POLICIES (Continued)

3.3 Financial assets (Continued)

iii. Held-to-maturity investments (Continued)

These are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method.

Interest on held-to-maturity investments is included in the statement of comprehensive income and reported as 'interest income'. In the case of an impairment, the impairment loss is reported as a deduction from the carrying value of the investment and recognised in the statement of comprehensive income as 'net gains/ (losses) on investment securities'. Held-to maturity investments are: Reserve Bank of Malawi Bonds; Malawi Government Treasury Bills; and Local Registered Stocks.

iv. Available-for-sale investments

Available-for-sale investments are financial assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices or that are not classified as loans and receivables, held to-maturity investments or financial assets at fair value through profit or loss.

Available-for-sale financial assets are initially recognised at fair value, which is the cash consideration including any transaction costs, and measured subsequently at fair value with gains and losses being recognised as other comprehensive income in the statement of comprehensive income, except for impairment losses and foreign exchange gains and losses which are recognised in profit or loss, until the financial asset is derecognised. If an available-for-sale financial asset is determined to be impaired, the cumulative gain or loss previously recognised as other comprehensive income in the statement of comprehensive income is recognised as profit or loss in the statement of comprehensive income. However, interest is calculated using the effective interest method, and foreign currency gains and losses on monetary assets classified as available for sale are recognised in the statement of comprehensive income. Dividends on available-for-sale equity instruments are recognised in the statement of comprehensive income in 'Dividend income' when the Group's right to receive payment is established.

v. Recognition

The Group uses trade date accounting for regular way contracts when recording financial asset transactions. Financial assets that are transferred to a third party but do not qualify for derecognition are presented in the statement of financial position as 'Assets pledged as collateral', if the transferee has the right to sell or repledge them.

vi. Derecognition

Financial assets are derecognised when the contractual rights to receive the cash flows from these assets have ceased to exist or the assets have been transferred and substantially all the risks and rewards of ownership of the assets are also transferred (that is, if substantially all the risks and rewards have not been transferred, the Group tests control to ensure that continuing involvement on the basis of any retained powers of control does not prevent derecognition). Financial liabilities are derecognised when they have been redeemed or otherwise extinguished.

Collateral (treasury bills and bonds) furnished by the Group under standard repurchase agreements and securities lending and borrowing transactions is not derecognised because the Group retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met. This also applies to certain securitisation transactions in which the Group retains a portion of the risks.

vii. Reclassification of financial assets

The Group may choose to reclassify a non-derivative financial asset held for trading out of the held-for-trading category if the financial asset is no longer held for the purpose of selling it in the near-term. Financial assets other than loans and receivables are permitted to be reclassified out of the held for trading category only in rare circumstances arising from a single event that is unusual and highly unlikely to recur in the near-term. In addition, the Group may choose to reclassify financial assets that would meet the definition of loans and receivables out of the held-for-trading or available-for-sale categories if the Group has the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification.

Reclassifications are made at fair value as of the reclassification date. Fair value becomes the new cost or amortised cost as applicable, and no reversals of fair value gains or losses recorded before reclassification date are subsequently made. Effective interest rates for financial assets reclassified to loans and receivables and held-to-maturity categories are determined at the reclassification date. Further increases in estimates of cash flows adjust effective interest rates prospectively.

On reclassification of a financial asset out of the 'at fair value through profit or loss' category, all embedded derivatives are re-assessed and, if necessary, separately accounted for.

3. ACCOUNTING POLICIES (Continued)

3.4 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

3.5 Sale and repurchase agreements

Securities sold subject to repurchase agreements ('repos') are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral; the counterparty liability is included in amounts due to other banks, deposits from banks, other deposits or deposits due to customers, as appropriate. Securities purchased under agreements to resell ('reverse repos') are recorded as loans and advances to other banks or customers, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest rate method. Securities lent to counterparties are also retained in the financial statements.

3.6 Impairment of financial assets

a. Assets carried at amortised cost

The Group assesses at each year-end date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of events that have an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about the following loss events:

- Significant financial difficulty of the issuer or obligor;
- 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;
- It becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- The disappearance of an active market for that financial asset because of financial difficulties; and
- Observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since 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; and
 - national or local economic conditions that correlate with defaults on the assets in the group.

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

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of comprehensive income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Group's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

3. ACCOUNTING POLICIES (Continued)

3.6 Impairment of financial assets (Continued)

a. Assets carried at amortised cost (Continued)

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Group and historical loss experience for assets with credit risk characteristics similar to those in the Group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in future cash flows for groups of assets should reflect and be consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the Group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the statement of comprehensive income.

b. Assets carried at fair value

The Group assesses at each year-end date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the statement of comprehensive income. Impairment losses recognised in the statement of comprehensive income on equity instruments are not reversed through the statement of comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the statement of comprehensive income, the impairment loss is reversed through the statement of comprehensive income.

3.7 Property, plant and equipment

Land and buildings are shown at valuation with subsequent additions at cost, less related depreciation and impairment losses. Revaluations of land and buildings are carried out with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the year-end date, as economic conditions dictate, by independent valuers. The basis of valuation used is current market value. Surpluses on revaluations are recognised and treated as other comprehensive income in the statement of comprehensive income and transferred to the non-distributable reserve; on realisation (either through use or disposal) of the asset, the appropriate portion of the reserve is transferred to retained earnings. Deficits on revaluations are charged to profit and loss, except to the extent that they relate to revaluation surpluses previously transferred to the revaluation reserve in which case they are treated as other comprehensive income. An amount equivalent to the additional depreciation arising from revaluations is transferred annually, net of deferred tax, from the revaluation reserve to retained earnings.

Land and buildings comprise mainly service centres and offices.

Motor vehicles and equipment are stated at historical cost less related depreciation and accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Properties in course of construction for administration or for purposes not yet determined are carried at cost less any recognised impairment loss. Cost includes professional fees.

3. ACCOUNTING POLICIES (Continued)

3.7 Property, plant and equipment (Continued)

Depreciation on assets is calculated using the straight-line method to write-off their cost to their residual values over their estimated useful lives.

The assets' residual values, useful lives, and depreciation method are reviewed, and adjusted if appropriate, at each year-end date.

Freehold land and capital work in progress are not depreciated.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the statement of comprehensive income.

3.8 Intangible assets

Intangible assets are reported at cost less accumulated amortisation and impairment losses. Amortisation is charged on a straight-line basis over their estimated useful lives. The estimated useful life and amortisation method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

3.9 Leases

Leases are classified as finance leases whenever the terms of a lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

a. The Group as lessor

Amounts due from lessees under finance leases are recorded as receivables at the amount of the Group's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant periodic rate of return on the Group's net investment outstanding in respect of the leases.

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

Assets held under finance leases are recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss.

b. The Group as lessee

Operating lease payments are recognised as an expense on a straight line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of the rental expenses on a straight line basis except where another more systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed.

3.10 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets.

Certain derivatives embedded in other financial instruments, such as the conversion option in a convertible bond, are treated

3. ACCOUNTING POLICIES (Continued)

3.10 Derivative financial instruments (Continued)

as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the statement of comprehensive income.

3.11 Impairment of tangible and intangible assets excluding goodwill and financial assets

At each year-end date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash generating units, or otherwise they are allocated to the smallest group of cash generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years.

A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

3.12 Non-current assets held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition.

Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of the assets' previous carrying amount and fair value less costs to sell.

3.13 Provisions

A provision is recognised in the statement of financial position when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

a. Restructuring

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Costs relating to the on-going activities of the Group are not provided for.

3. ACCOUNTING POLICIES (Continued)

3.13 Provisions (Continued)

b. **Onerous contracts**

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Group recognises any impairment loss on the assets associated with the contract.

c. **Warranties**

A provision for warranties is recognised when the underlying products or services are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities.

3.14 Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the year-end date.

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which these deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amounts of deferred tax assets are reviewed at each year-end date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantially enacted at the year-end date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow the manner in which the Group expects, at the year-end date, to recover or settle the carrying amount of its assets and liabilities. Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period

Current and deferred tax are recognised as an expense or income in profit or loss, except when they relate to items that are recognised outside profit or loss (whether in other comprehensive income or directly in equity), in which case the tax is also recognised outside profit or loss, or where they arise from the initial accounting for a business combination.

3.15 Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and balances with central banks, treasury bills and other eligible bills, loans and advances to banks, amounts due from other banks and short-term government securities.

3.16 Employee benefits

a. **Pension obligations - Defined Contribution Plan**

The Group contributes to a defined contribution pension plan for employees called the National Bank of Malawi Pension Fund. Contributions are charged to the statement of comprehensive income as incurred.

3. ACCOUNTING POLICIES (Continued)

3.16 Employee benefits (Continued)

a. Pension obligations - Defined Contribution Plan (Continued)

A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity. The Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employment service in the current and prior periods.

The plan has two funds: General Fund and Death Top up Fund (Special Fund). The Special Fund applies to additional funds that are made by the employer at 4% of salary to cover additional sums due on death-in-service and, the final salary underpin.

b. Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

3.17 Foreign currency translation

a. Functional and presentation currency

Items included in the financial statements are measured using Malawi Kwacha, the functional currency of the primary economic environment in which the entire Group operates. The financial statements are presented in Malawi Kwacha (rounded to the nearest million), which is the Group's functional and presentation currency.

b. Transactions and balances

Foreign currency transactions are translated into Malawi Kwacha using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income. Foreign exchange gains and losses arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognised directly in equity.

3.18 Financial liabilities and equity

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of the liabilities. The accounting policies adopted for specific financial liabilities and equity instruments are set out below;

i. Customer deposits and liabilities to other banks

Customer deposits and liabilities to other banks are recognised initially at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. These are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest rate method.

ii. Other liabilities

Other liabilities are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest rate method.

iii. Equity instruments

Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

3.19 Revenue recognition

Interest income and expense

Interest income and expense for all interest-bearing financial instruments except for those classified as held for trading or designated at fair value through profit and loss are recognised within "interest income" and "interest expense" in the statement of comprehensive income using the effective interest rate method.

The effective interest rate method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument (for

3. ACCOUNTING POLICIES (Continued)

3.19 Revenue recognition (Continued)

Interest income and expense (Continued)

example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. Loan syndication fees are recognised as revenue when the syndication has been completed and the bank retained no part of the loan package for itself or retained a part at the same effective interest rate for the other participants. Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party – such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction.

Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time apportionment basis. Asset management fees related to investment funds are recognised rateably over the period in which the service is provided. The same principle is applied to wealth management, financial planning and custody services that are continuously provided over an extended period of time. Performance linked fees or fee components are recognised when the performance criteria are fulfilled.

Dividend income

Dividends are recognised in the statement of comprehensive income when the Group's right to receive payment is established.

Premium on foreign exchange deals

Premium on foreign exchange deals are recognised as income when the deal is agreed and concluded.

3.20 Share capital

Share issue costs

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Company's shareholders.

Dividends for the year that are declared after the year-end date are dealt with in the subsequent events note.

Dividend per share

The calculation of dividend per share is based on the dividends paid to shareholders during the period divided by the number of ordinary shareholders on the register of shareholders as at year-end.

Earnings per share

The calculation of earnings per share is based on the net profit for the year and the weighted average number of shares in issue throughout the year. Where new equity shares have been issued by way of capitalisation or subdivision, the profit is apportioned over the shares in issue after the capitalisation or subdivision and the corresponding figures for all earlier periods are adjusted accordingly.

3.21 Fiduciary activities

The Group commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies described above (note 3) management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily available from other sources. The estimates and associated assumptions are based on historical experience and other factors that are relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future period if the revision affects both current and future periods.

4.1 Critical judgements in applying the Group's accounting policies

There were no critical judgements, apart from those involving estimations (note 4.2) that management has made in the process of applying the entity's accounting policies and that have significant effect on the amounts recognised in financial statements.

4.2 Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the year-end date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below:-

i. Impairment losses on loans and advances

The Group reviews its loan portfolios to assess impairment, at least, on a quarterly basis. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows.

The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Key assumptions used:

- a. Cash flows arising from repayment agreement are aggregated over yearly intervals and assumed to arise at the end of the period;
- b. Where there is an agreement but no security in place and cash flows in the subsequent years are doubtful, total future estimated cash flows are assumed to be nil;
- c. Unsupported guarantees are assumed to result in nil cash flows;
- d. No cash flows are assumed to arise where there is no repayment agreement and no security and repayments are erratic or unpredictable; and
- e. Cash flows arising from security realisation have been assumed to arise at the end of the calendar year in which they are expected.

ii. Held to maturity investments

The group follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held to maturity. This classification requires significant judgment. In making this judgment, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than for the specific circumstances- for example, selling an insignificant amount close to maturity- it will be required to reclassify the entire class as available for sale.

iii. Valuation of properties

The assumptions and methods of revaluing properties are disclosed in note 16.

iv. Residual values and useful lives of tangible assets

The residual values and useful lives of property, plant and equipment are reviewed and adjusted, if appropriate, at each financial position date to reflect current thinking on their remaining lives in the light of technological change, prospective economic utilisation and physical conditions of the assets concerned as described under note 3.6.

5. CASH AND FUNDS WITH RESERVE BANK OF MALAWI

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Cash	5,059	3,398	5,059	3,396
Balances with the Reserve Bank of Malawi	3,738	4,757	3,738	4,757
Total cash and funds with Reserve Bank of Malawi	8,797	8,155	8,797	8,153

The currency analysis of cash is in note 38(e).

Balances held at Reserve Bank of Malawi, which are denominated in Malawi Kwacha and United States Dollars, are non-interest bearing and regulated as disclosed in note 38(e) and 38(g).

6. GOVERNMENT OF MALAWI TREASURY BILLS AND RESERVE BANK OF MALAWI BONDS

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
	Average interest rate			
	<u>2012</u>	<u>2011</u>		
Government of Malawi treasury bills	16.8%	6.6%	3,741	5,969
Reserve Bank of Malawi bonds	15.5%	9.1%	4,060	1,093
	7,801	7,062	7,801	7,062
The bills and bonds are due to mature as follows:				
● Within three months	1,238	2,550	1,238	2,550
● Between three months and one year	3,355	3,419	3,355	3,419
● Over one year	3,208	1,093	3,208	1,093
	7,801	7,062	7,801	7,062

Government of Malawi treasury bills and Reserve Bank of Malawi bonds are denominated in Malawi Kwacha and are held to maturity.

7. GOVERNMENT OF MALAWI LOCAL REGISTERED STOCK

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
The stock is due to mature as follows:				
● Within three months	372	-	372	-
● Between three months and one year	-	63	-	63
● Between one and five years	-	404	-	404
	372	467	372	467

Government of Malawi local registered stock is denominated in Malawi Kwacha and is held to maturity. The stock earned an average interest rate of 15.5% (2011: 15.5%).

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

8. EQUITY INVESTMENTS

	2011 K'm	Additions /(disposals) K'm	Fair value adjustment K'm	2012 K'm	Cost K'm
GROUP - 2012					
First Merchant Bank Limited 7,209,720 (2011: 9,209,720) Ordinary shares of K2.50 each at a market value of K8.50 (2011: K7.00) per share	64	(14)	11	61	56
Illovo Sugar (Malawi) Limited 1,500,626 (2011: 1,500,626) Ordinary shares of K0.02 each at a market value of K153.35 (2011: K130.00) per share	195	-	35	230	172
NICO Holdings Limited 4,643,628 (2011: 5,667,790) Ordinary shares of K0.20 each at a market value of K14.30 (2011: K11.00) per share	62	(16)	20	66	8
Malawi Property Investment Company Limited 8,532,748 (2011: 8,574,393) Ordinary shares of K0.05 each at a market value of K2.40 (2011: K3.00) per share	26	-	(5)	21	28
National Investment Trust Limited 5,086,371 (2011: 4,946,371) Ordinary shares of K1.00 each at a market value of K17.00 (2011: K16.00) per share	79	2	6	87	121
NBS Bank Limited 10,282,645 (2011: 10,372,144) Ordinary shares of K0.50 each at a market value of K11.00 (2011: K10.00) per share	104	(1)	10	113	112
Standard Bank of Malawi Limited 740,929 (2011: 740,929) Ordinary shares of K1.00 each at market value of K128.23 (2011: K105.00) per share	78	-	17	95	65
Sunbird Malawi Limited 1,126,150 (2011: 1,126,150) Ordinary shares of K0.05 each at a market value of K6.50 (2011: K7.00) per share	8	-	(1)	7	10
Telekom Networks Malawi Limited 36,905,990 (2011: 40,664,191) Ordinary shares of K0.04 each at a market value of K1.40 (2011: K1.90) per share	77	(8)	(17)	52	74
Real Insurance Company Limited Nil (2011: 1,156,550) Ordinary shares of K0.40	2	(2)	-	-	-
Total equity investments	695	(39)	76	732	646

The above investments are listed on the Malawi Stock Exchange and are carried at market value.

8. EQUITY INVESTMENTS (Continued)

	2011 K'm	Additions /(disposals) K'm	Fair value adjustment K'm	2012 K'm	Cost K'm
COMPANY - 2012					
First Merchant Bank Limited 7,209,720 (2011: 9,209,720) Ordinary shares of K2.50 each at a market value of K8.50 (2011: K7.00) per share	64	(14)	11	61	56
Illovo Sugar (Malawi) Limited 1,500,626 (2011: 1,500,626) Ordinary shares of K0.02 each at a market value of K153.35 (2011: K130.00) per share	195	-	35	230	172
NICO Holdings Limited 4,643,628 (2011: 5,634,000) Ordinary shares of K0.20 each at a market value of K14.30 (2011: K11.00) per share	62	(16)	20	66	8
Malawi Property Investment Company Limited 8,532,748 (2011: 8,532,748) Ordinary shares of K0.05 each at a market value of K2.40 (2011: K3.00) per share	26	-	(5)	21	28
National Investment Trust Limited 5,086,371 (2011: 4,946,371) Ordinary shares of K1.00 each at a market value of K17.00 (2011: K16.00) per share	79	2	6	87	121
NBS Bank Limited 10,282,645 (2011: 10,282,645) Ordinary shares of K0.50 each at a market value of K11.00 (2011: K10.00) per share	103	-	10	113	112
Standard Bank of Malawi Limited 740,929 (2011: 740,929) Ordinary shares of K1.00 each at market value of K128.23 (2011: K105.00) per share	78	-	17	95	65
Sunbird Malawi Limited 1,000,000 (2011: 1,000,000) Ordinary shares of K0.05 each at a market value of K6.50 (2011: K7.00) per share	7	-	-	7	9
Telekom Networks Malawi Limited 36,592,400 (2011: 36,592,400) Ordinary shares of K0.04 each at a market value of K1.40 (2011: K1.90) per share	69	-	(18)	51	73
Total equity investments	683	(28)	76	731	644

The above investments are listed on the Malawi Stock Exchange and are carried at market value. Telekom Networks Malawi Limited is a related party.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

9. INVESTMENT IN ASSOCIATE

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Purchase consideration	123	123	123	123
Share of accumulated results	91	73	-	-
	<u>214</u>	<u>196</u>	<u>123</u>	<u>123</u>
Assets	1,762	1,403		
Liabilities	1,284	1,025		
Net assets	<u>478</u>	<u>378</u>		
Group's share of net assets of associates	<u>124</u>	<u>98</u>		
Total revenue	<u>1,991</u>	<u>1,536</u>		
Total profit for the period	<u>71</u>	<u>399</u>		

The Bank holds 26% (2011: 26%) of United General Insurance Limited share capital.

10. INVESTMENT IN SUBSIDIARIES

	COMPANY	
	2012 K'm	2011 K'm
Stockbrokers Malawi Limited	98	98
NBM Bureau de Change Limited	27	27
National Bank Capital Markets Limited	17	-
Total investment in subsidiaries	<u>142</u>	<u>125</u>

The Bank, through National Bank Nominees Limited, holds a 75% (2011: 75%) stake in Stockbrokers Malawi Limited. The Bank also holds a 100% (2011: 100%) stake in NBM Bureau de Change Limited and a 100% (2011: 100%) stake in NBM Capital Markets Limited.

11. PLACEMENTS WITH OTHER BANKS

	GROUP & COMPANY		
	2012 K'm	2011 K'm	
Money market placements with other banks	10,039	4,772	
Balances due from other banks	9,308	3,981	
Total placements with other banks	19,347	8,753	
Placements with other banks are denominated in the following currencies:			
	Average interest rate		
	2012	2011	
Malawi Kwacha denominated	-	11.75%	3,393
US Dollar denominated	2.00%	0.80%	2,755
GBP denominated	1.02%	0.59%	1,327
Euro denominated	1.00%	0.82%	1,150
ZAR denominated	4.50%	4.50%	3
Other	-	-	125
			8,753
	19,347		19,347

Money market placements with other banks are held to maturity and mature within one month (2011: three months).

12. LOANS AND ADVANCES

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Gross loans and advances	63,951	46,943	63,951	46,958
Specific provisions	(950)	(370)	(950)	(370)
Net loans and advances	63,001	46,573	63,001	46,588
Due to mature as follows:				
● Within three months	24,539	12,252	24,539	12,252
● Between three months and one year	14,229	21,345	14,229	21,360
● After one year and not later than five years	25,404	13,506	25,404	13,506
● Interest in suspense	(221)	(160)	(221)	(160)
	63,951	46,943	63,951	46,958
Analysis of gross loans by currency				
Malawi Kwacha denominated	57,703	42,186	57,703	42,201
US Dollar denominated	6,248	4,757	6,248	4,757
	63,951	46,943	63,951	46,958

The Malawi Kwacha base lending rate for the bank as at 31 December 2012 was 35.0% (2011: 17.7%) and US Dollar denominated loans carried an average interest rate of 8.6% (2011: 8.6%).

12. LOANS AND ADVANCES (Continued)

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Movement on specific provisions				
At beginning of the year	370	351	370	351
Applied against advances	(262)	(284)	(262)	(284)
Charged to statements of comprehensive income	860	317	860	317
Recovered	(18)	(14)	(18)	(14)
At end of the year	950	370	950	370
Movement on interest in suspense				
At beginning of the year	160	248	160	248
Applied against advances	(510)	(497)	(510)	(497)
Suspended in the year	587	438	587	438
Recovered	(16)	(29)	(16)	(29)
At end of the year	221	160	221	160
Analysis of recoveries				
Specific provisions	18	14	18	14
Interest in suspense	16	29	16	29
Debts previously written off	219	164	219	164
Transferred to statement of comprehensive income	253	207	253	207

	GROUP AND COMPANY	
	2012 K'm	2011 K'm
Finance lease receivables		
Gross investment in finance lease receivable:		
● Within three months	48	65
● Between three months and one year	530	632
● After one year and not later than five years	6,919	3,733
	7,497	4,430
Unearned future income on finance leases	(2,486)	(816)
	5,011	3,614
Specific provisions	(9)	(1)
Net investment in finance leases	5,002	3,613
The net investment in finance leases matures as follows:		
● Within three months	46	58
● Between three months and one year	464	531
● After one year and not later than five years	4,492	3,024
	5,002	3,613

13. OTHER MONEY MARKET DEPOSITS

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Balances with discount houses	2,104	1,009	2,048	1,000

Balances with discount houses are held to maturity and mature within one month (2011: one month) after the year-end. The deposits earned an average interest rate of 28.0% (2011: 6.3%).

14. ASSETS HELD FOR SALE

	GROUP & COMPANY	
	2012 K'm	2011 K'm
Property	-	454

The bank sold two of its buildings, Henderson Street Branch building on plot BC 7A-8 in Blantyre and Churchill Road Branch building on plot LE 213/404 in Limbe. The sales were finalised during 2012.

15. OTHER ASSETS

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Letters of credit	7,397	875	7,397	875
Sundry receivables and prepayments	1,930	2,597	1,877	2,577
Due from local banks	410	1,932	410	1,932
Other investments	24	19	24	19
Provision for potential loss on other assets	(1,222)	(1,222)	(1,222)	(1,222)
Total other assets	8,539	4,201	8,486	4,181

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

16. PROPERTY, PLANT AND EQUIPMENT

	Freehold land and buildings K'm	Leasehold land and buildings K'm	Motor vehicles and equipment	Work in progress K'm	Total K'm
COMPANY					
COST OR VALUATION					
At 1 January 2011	2,480	1,299	5,720	5,669	15,168
Additions	-	29	852	1,917	2,798
Transfer from work in progress	7,330	3	253	(7,586)	-
Revaluation surplus	413	277	-	-	690
Fair value loss	(1,491)	-	-	-	(1,491)
Reclassified as held for sale	(465)	-	-	-	(465)
Elimination on disposal	-	-	(464)	-	(464)
At 31 December 2011	8,267	1,608	6,361	-	16,236
At 1 January 2012	8,267	1,608	6,361	-	16,236
Additions	658	5	1,297	186	2,146
Disposals	-	-	(968)	-	(968)
Revaluation surplus	1,384	504	-	-	1,888
At 31 December 2012	10,309	2,117	6,690	186	19,302
DEPRECIATION					
At 1 January 2011	-	-	2,812	-	2,812
Charge for the year	20	7	1,137	-	1,164
Elimination on revaluation	(9)	(7)	-	-	(16)
Reclassified as held for sale	(11)	-	-	-	(11)
Elimination on disposal	-	-	(368)	-	(368)
At 31 December 2011	-	-	3,581	-	3,581
At 1 January 2012	-	-	3,581	-	3,581
Charge for the year	52	9	1,163	-	1,224
Elimination on revaluation	(52)	(9)	-	-	(61)
Elimination on disposal	-	-	(763)	-	(763)
At 31 December 2012	-	-	3,981	-	3,981
CARRYING AMOUNT					
At 31 December 2012	10,309	2,117	2,709	186	15,321
At 31 December 2011	8,267	1,608	2,780	-	12,655

16. PROPERTY, PLANT AND EQUIPMENT (Continued)

	2012 K'm	2011 K'm
Carrying amount - GROUP		
Total property, plant and equipment	15,366	12,685

Land and buildings

Cost or valuation at end of the year (excluding capital work in progress) comprises the following:

Freehold	- at 2012 valuation	10,309	-
	- at 2011 valuation	-	8,267
Total freehold land and buildings		10,309	8,267
Leasehold	- at 2012 valuation	2,117	-
	- at 2011 valuation	-	1,608
Total leasehold land and buildings		2,117	1,608

Included in the property, plant and equipment in subsidiary companies are motor vehicles and office equipment with a gross value of K63m (2011: K43m).

Included in Group and Company property, plant and equipment are assets under operating leases with the following net book values:

	Related parties K'm	others K'm	2012 K'm	2011 K'm
Equipment	-	-	-	10
Motor vehicles	610	13	613	969
	610	13	613	979

Malawi Telecommunications Limited and the Bottling and Brewing Group Limited are related parties to whom the Bank is leasing out motor vehicles which were purchased at a cost of K121m (2011: K399m) and K1,427m (2011: K1,639m), respectively.

The following useful lives were used in the calculation of depreciation:

Freehold buildings	-	useful economic lives as determined by professional valuers
Leasehold property	-	lower of period of lease and useful economic lives as determined by professional valuers
Equipment	-	4 - 10 years
Motor vehicles	-	4 years

The register of land and buildings is open for inspection at the registered office of the Bank.

16. PROPERTY, PLANT AND EQUIPMENT (Continued)
Valuations in 2012

Land and buildings were fair valued as at 31 December 2012 by Chris Mullock, MRICS, MSIM, and Knight Frank, qualified independent valuers. The valuation of the Business Centre and Office Complex resulted in an increase in carrying value of K591m. The valuation of the Bank's other properties resulted in an increase in fair value of K1,358m. Out of the K1,949m total revaluation surplus, K838m was credited to the statement of comprehensive income to reverse decreases in fair values previously charged to the statement of comprehensive income and the balance of K1,111m was credited to the revaluation reserve through the statement of other comprehensive income (refer note 29). The basis of the valuations was current market value.

Had land and buildings been carried at historical cost less depreciation and accumulated impairment losses, their carrying value would have been approximately K9,171m (2011: K9,361m).

17. INTANGIBLE ASSETS

	Development costs K'm	Computer software K'm	Work in progress K'm	Total K'm
COMPANY AND GROUP				
COST OR VALUATION				
At 1 January 2011	326	1,061	115	1,502
Additions	-	114	189	303
At 31 December 2011	326	1,175	304	1,805
At 1 January 2012	326	1,175	304	1,805
Additions	-	203	596	799
At 31 December 2012	326	1,378	900	2,604
DEPRECIATION				
At 1 January 2011	167	42	-	209
Charge for the year	71	83	-	154
At 31 December 2011	238	125	-	363
At 1 January 2012	238	125	-	363
Charge for the year	80	79	-	159
At 31 December 2012	318	204	-	522
CARRYING AMOUNTS				
31 December 2012	8	1,174	900	2,082
31 December 2011	88	1,050	304	1,442

18. DEFERRED TAX

	Opening balance K'm	Charge to income K'm	Charged to equity K'm	Closing balance K'm
GROUP AND GROUP				
2011				
Accelerated capital allowances	(392)	5	-	(387)
Revaluation of fixed assets	(167)	448	(70)	211
Other temporary differences	566	27	-	593
Total deferred tax	7	480	(70)	417
2012				
Accelerated capital allowances	(387)	(34)	-	(421)
Revaluation of fixed assets	211	(252)	762	721
Other temporary differences	593	241	-	834
Total deferred tax	417	(45)	762	1,134

19. CUSTOMER DEPOSITS

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
	Average interest rate			
	2012	2011		
Analysis by account type:				
Current accounts	0.75%	0.10%	35,085	30,197
Foreign currency accounts	0.50%	1.69%	23,947	8,726
Savings accounts	7.50%	1.50%	12,635	11,559
Deposit accounts	10.68%	3.02%	15,813	16,269
Total customer deposits	87,480	66,751	87,512	66,758
Analysis by interest risk type:				
Interest bearing deposits	86,280	65,965	86,312	65,972
Non-interest bearing deposits	1,200	786	1,200	786
	87,480	66,751	87,512	66,758

All interest bearing accounts, excluding deposit accounts, are at floating rates that are adjusted at the Bank's discretion (note 34(d)).

Analysis by interest maturity:

Customer deposits are payable as follows:

● Within three months	86,346	65,878	86,378	65,885
● Between three months and one year	1,134	873	1,134	873
	87,480	66,751	87,512	66,758

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

19. CUSTOMER DEPOSITS (Continued)

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Analysis by sector:				
Agriculture	1,497	2,444	1,497	2,444
Manufacturing	4,976	2,999	4,976	2,999
Wholesale and retail	16,210	2,036	16,210	2,036
Finance and insurance	5,048	1,768	5,048	1,768
Personal accounts	48,294	53,624	48,294	53,631
Other	11,455	3,880	11,487	3,880
Total	87,480	66,751	87,512	66,758

The currency analysis of customer deposits is included in note 38(e).

20. AMOUNTS DUE TO OTHER BANKS

	GROUP AND COMPANY	
	2012 K'm	2011 K'm
Liabilities in Malawi Kwacha	52	1,423
Liabilities in foreign currency	203	912
Bills in suspense	328	539
Total amounts due to other banks	583	2,874

21. INCOME TAX LIABILITY

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Opening balance	1,030	125	1,030	123
Current charge	3,373	2,158	3,354	2,151
Amount paid	(3,090)	(1,228)	(3,080)	(1,228)
Prior period over provision	(10)	(25)	-	(16)
Closing balance	1,303	1,030	1,304	1,030

22. LOANS

The Bank signed an agreement for an unsecured facility of USD20 million from Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden (FMO) of the Netherlands for the purpose of on lending to exporting US Dollar earning small and medium-sized enterprises in sectors other than tobacco. As at 31 December 2012 USD10 million had been drawn down and this amount is repayable over a period of four years. The interest rate on the outstanding loan balance is adjustable quarterly and is at the rate of LIBOR plus 4%.

	GROUP AND COMPANY	
	2012 K'm	2011 K'm
Amounts repayable within one year	306	-
Amount repayable after one year	3,089	-
	<u>3,395</u>	<u>-</u>

23. OTHER LIABILITIES

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Letters of credit	7,397	875	7,397	875
Staff bonus	1,750	314	1,750	314
Unclaimed balances	915	368	915	368
Bank cheques	534	75	534	75
Office accounts	134	42	134	42
Other liabilities	4,431	3,492	4,369	3,459
Total other liabilities	<u>15,161</u>	<u>5,166</u>	<u>15,099</u>	<u>5,133</u>

The currency analysis of other liabilities is included in note 38(e).

24. PENSION SCHEME

The pension fund, which is managed internally, is a defined contribution scheme and the respective contributions by employees and the employer are 5.5% (2011: 5.5%) and 11% (2011: 11.0%) of the fund members' basic pensionable salaries, respectively. The employer contributes an additional 4% (2011: 4.0%) of the pensionable salary. Thus the total contribution by the employer is 15.0% of pensionable salary. The amount charged against income during the year was K363m (2011: K257m).

The Pension Fund operates two accounts: the General Fund and Death Top up Fund (Special Fund). The Special Fund applies to additional funds that are made by the employer at 4.0% of salary to cover additional sums due on death-in-service, the final salary underpin and severance pay liabilities. The Special Fund is also built up by investment income earned on the fund's assets and a percentage of the employer's contribution forfeited by resigning, dismissal and redundant employees in accordance with the rules of the Fund.

The General Fund represents a reserve from which all other benefits are paid including administration expenses and bonuses. The Pension Fund is a self-accounting Trust whose assets are not available to the Group. The Trustees of the Fund are employees of the Bank. The Bank rents some of the Fund's properties at commercial rates. The Group incurred K114m (2011: K99m) in rentals for such properties during the year.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
25. NET INTEREST INCOME				
Interest and similar income				
Interest on loans and advances and bills discounted	10,082	7,488	10,090	7,490
Income from investments	928	723	928	723
Income from lease financing	951	761	951	761
Interest on placements with other banks	309	144	305	115
	12,270	9,116	12,274	9,089
Interest expense and similar charges				
Banks and customers	1,666	619	1,667	619
Money market loans and repos	741	337	741	337
	2,407	956	2,408	956
Net interest income	9,863	8,160	9,866	8,133
26. COMMISSION AND FEE INCOME				
Commissions	2,949	1,997	2,817	1,972
Arrangement and other fee income	689	584	689	581
Premium on foreign exchange dealings	2,379	1,041	2,379	1,041
Other income	357	223	351	223
Total commission and fee income	6,374	3,845	6,236	3,817
27. STAFF COSTS				
Salaries and wages	2,466	1,925	2,423	1,894
Other staff costs	681	429	675	428
Staff bonus	1,962	438	1,941	438
Severance pay(write back)/expense	69	(884)	69	(884)
Pension costs - defined contribution plan	369	258	363	257
Contract gratuity expense	5	77	5	73
Total staff costs	5,552	2,243	5,476	2,206

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
28. OTHER OPERATING EXPENDITURE				
Other costs	2,988	1,316	2,462	1,295
Recurrent expenditure on premises and equipment	1,105	1,024	1,583	1,013
Depreciation	1,233	1,166	1,224	1,164
Amortisation of intangible assets	159	154	159	154
Increase in provision for potential loss on other assets	-	810	-	810
Legal charges	97	46	95	46
Auditor's remuneration including surtax and expenses:				
- current year	48	25	40	21
- prior year	-	4	-	4
Directors' remuneration:				
- fees for services as directors	13	11	12	10
- for managerial services	126	85	126	85
Total other operating expenditure	5,769	4,641	5,701	4,602
29. PROPERTIES FAIR VALUE GAINS/(LOSS)				
Fair value gains/(loss) on Business Centre and Office Complex	591	(1,693)	591	(1,693)
Fair value gains on other properties	247	202	247	202
Total fair value gains/(losses) through statement of comprehensive income	838	(1,491)	838	(1,491)
Fair value gains on properties included in other comprehensive income	1,111	706	1,111	706
Total properties fair value gains/(loss)	1,949	(785)	1,949	(785)
30. INCOME TAX EXPENSE				
Income tax	3,373	2,158	3,354	2,151
Deferred tax	45	(480)	45	(480)
Total income tax expense	3,418	1,678	3,399	1,671
<u>Reconciliation of rate of tax</u>	%	%	%	%
Standard rate of taxation	30	30	30	30
Permanent differences	1	2	1	2
Effective rate of taxation	31	32	31	32

31. EARNINGS PER SHARE
BASIC EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net profit attributable to equity holders of the Company by the weighted average number of Ordinary Shares in issue during the year.

	GROUP	
	2012	2011
Profit attributable to equity holders of the Company (K millions)	7,575	3,558
Net profit used to determine diluted earnings per share (K millions)	7,575	3,558
Weighted average number of Ordinary Shares in issue (millions)	467	467
Weighted average number of Ordinary Shares for diluted earnings per share (millions)	467	467
Basic earnings per share (expressed in K per share)	16.22	7.62

Diluted earnings per share

Diluted earnings per share is calculated by adjusting the weighted average number of Ordinary Shares outstanding to assume conversion of all dilutive potential ordinary shares. The Bank has outstanding share options which are dilutive potential ordinary shares. A calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	GROUP	
	2012	2011
Profit attributable to equity holders of the Company (K millions)	7,575	3,558
Net profit used to determine diluted earnings per share (K millions)	7,575	3,558
Weighted average number of Ordinary Shares in issue	467	467
Weighted average number of Ordinary Shares for diluted earnings per share (millions)	467	467
Diluted earnings per share (expressed in K per share)	16.22	7.62

32. DIVIDEND PER SHARE

Dividend per share is calculated by dividing the total dividends paid in the year by the weighted average number of Ordinary Shares in issue during the year.

	GROUP	
	2012 K'm	2011 K'm
Interim dividend paid (for current year)	2,334	840
Final dividend paid (for previous year)	1,261	1,251
	3,595	2,091
Weighted average number of Ordinary Shares in issue (millions)	467	467
Dividend per share	7.70	4.48

The proposed current year final dividend is K1,500 million (2011: K1,261 million) representing K3.21 per share (2011: K2.70 per share).

33. CONTINGENCIES

	GROUP & COMPANY	
	2012 K'm	2011 K'm
Guarantees		
Foreign guarantees	988	972
Local guarantees and performance bonds	4,563	3,243
Total contingencies from guarantees	5,551	4,215
Other contingencies		
Legal claims	248	265

Guarantees and performance bonds represent acceptances, guarantees, indemnities and credits which will crystallise into an asset and a liability only in the event of default on the part of the relevant counterparty.

Legal claims represent outstanding legal cases against the Group in the ordinary course of business, the outcome of which is uncertain. The amount disclosed represents an estimate of the cost to the Group in the event that legal proceedings find the Group to be in the wrong. In the opinion of the directors the claims are not expected to give rise to a cost to the Group. Legal claims in favour of the Group as at the end of the year were nil (2011: K320m).

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
34. COMMITMENTS				
Expenditure contracted but not incurred	2,844	775	2,844	775
Expenditure approved by the Board but not contracted	-	2,925	-	2,925
Total capital expenditure	2,844	3,700	2,844	3,700
35. CASH AND CASH EQUIVALENTS				
Cash and funds with Reserve Bank of Malawi (note 5)	8,797	8,155	8,797	8,153
Placements with other banks (note 11)	19,347	8,753	19,347	8,753
Other money market deposits (note 13)	2,104	1,009	2,048	1,000
Amounts due to other banks	(583)	(2,874)	(583)	(2,874)
Total cash and cash equivalents	29,665	15,043	29,609	15,032
36. CUSTOMER BALANCES				
Customer funds	3,067	1,855	-	-
Funds at call and on deposit	(3,067)	(1,855)	-	-
Total customer balances	-	-	-	-

Funds held by Stockbrokers Malawi Limited (SML), a subsidiary of the Group, on behalf of its clients are invested in Malawi Government securities or placed on call with reputable financial institutions. The funds are managed separately from SML's own funds.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

37. FINANCIAL ASSETS AND LIABILITIES

ACCOUNTING CATEGORIES AND FAIR VALUES

	Notes	Held for trading K'000	Held to maturity K'000	Loans and receivables K'000	Amortised Cost K'000	Total carrying amount K'000	Fair value K'000
GROUP							
<u>As at 31 December 2011</u>							
Assets							
Cash and bank balances with Reserve Bank of Malawi	5	8,155	-	-	-	8,155	8,155
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	6	-	7,062	-	-	7,062	7,062
Government of Malawi local registered stocks	7	-	467	-	-	467	467
Equity investments	8	695	-	-	-	695	695
Placements with other banks	10	-	-	8,753	-	8,753	8,753
Loans and advances to customers	11	-	-	46,573	-	46,573	46,573
Other money market deposits	12	-	-	1,009	-	1,009	1,009
Other assets	14	-	-	4,201	-	4,201	4,201
Total financial assets		8,850	7,529	60,536	-	76,915	76,915
Liabilities and equity							
Customer deposits	18	-	-	-	66,751	66,751	66,751
Amounts due to other banks		-	-	-	2,874	2,874	2,874
Other liabilities	19	-	-	-	5,166	5,166	5,166
Total financial liabilities		-	-	-	74,791	74,791	74,791
GROUP							
<u>As at 31 December 2012</u>							
Assets							
Cash and bank balances with Reserve Bank of Malawi	5	8,797	-	-	-	8,797	8,797
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	6	-	7,801	-	-	7,801	7,801
Government of Malawi local registered stocks	7	-	372	-	-	372	373
Equity investments	8	732	-	-	-	732	732
Placements with other banks	10	-	-	19,347	-	19,347	19,347
Loans and advances to customers	11	-	-	63,001	-	63,001	63,001
Other money market deposits	12	-	-	2,104	-	2,104	2,104
Other assets	14	-	-	8,539	-	8,539	8,539
Total financial assets		9,529	8,173	92,991	-	110,693	110,694
Liabilities and equity							
Long-term borrowing		-	-	-	3,395	3,395	3,395
Customer deposits	18	-	-	-	87,480	87,480	87,480
Amounts due to other banks		-	-	-	583	583	583
Other liabilities	19	-	-	-	15,161	15,161	15,161
Total financial liabilities		-	-	-	106,619	106,619	106,619

37. FINANCIAL ASSETS AND LIABILITIES (Continued)

ACCOUNTING CATEGORIES AND FAIR VALUES (Continued)

	Notes	Held for trading K'000	Held for maturity K'000	Loans and receivables K'000	Amortised Cost K'000	Total carrying amount K'000	Fair value K'000
COMPANY							
At 31 December 2011							
Assets							
Cash and bank balances with Reserve Bank of Malawi	5	8,153	-	-	-	8,153	8,153
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	6	-	7,062	-	-	7,062	7,062
Government of Malawi local registered stocks	7	-	467	-	-	467	467
Equity investments	8	683	-	-	-	683	683
Placements with other banks	10	-	-	8,754	-	8,754	8,754
Loans and advances to customers	11	-	-	46,588	-	46,588	46,588
Other money market deposits	12	-	-	1,000	-	1,000	1,000
Other assets	14	-	-	4,181	-	4,181	4,181
Total financial assets		8,836	7,529	60,523	-	76,888	76,888
Liabilities and equity							
Customer deposits	18	-	-	-	66,758	66,758	66,758
Amounts due to other banks		-	-	-	2,874	2,874	2,874
Other liabilities	19	-	-	-	5,133	5,133	5,133
Total financial liabilities		-	-	-	74,765	74,765	74,765
COMPANY							
At 31 December 2012							
Assets							
Cash and bank balances with Reserve Bank of Malawi	5	8,797	-	-	-	8,797	8,797
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	6	-	7,801	-	-	7,801	7,801
Government of Malawi local registered stocks	7	-	372	-	-	372	372
Equity investments	8	731	-	-	-	731	731
Placements with other banks	10	-	-	19,347	-	19,347	19,347
Loans and advances to customers	11	-	-	63,001	-	63,001	63,001
Other money market deposits	12	-	-	2,048	-	2,048	2,048
Other assets	14	-	-	8,486	-	8,486	8,486
Total financial assets		9,528	8,173	92,882	-	110,583	110,583
Liabilities and equity							
Long term borrowing		-	-	-	3,395	3,395	3,395
Customer deposits	18	-	-	-	87,512	87,512	87,512
Amounts due to other banks		-	-	-	583	583	583
Other liabilities	19	-	-	-	15,099	15,099	15,099
Total financial liabilities		-	-	-	106,589	106,589	106,589

37. FINANCIAL ASSETS AND LIABILITIES (Continued)

37.1 Valuation techniques and assumptions applied for the purposes of measuring fair value

The directors consider that the carrying amounts of financial assets and financial liabilities recognised at amortised cost in the financial statements approximate their fair values.

The fair values of financial assets and financial liabilities are determined as follows:

- The fair values of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices (includes listed redeemable notes, bills of exchange, debentures and perpetual notes).
- The fair values of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments.

37.2 Fair value measurements recognised in the statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	GROUP	
	2012 K'000	2011 K'000
<i>Financial assets at fair value through profit or loss</i>		
Non-derivative financial assets held for trading		
Level 1	732	695

	COMPANY	
	2012 K'000	2011 K'000
<i>Financial assets at fair value through profit or loss</i>		
Non-derivative financial assets held for trading		
Level 1	731	683

38. FINANCIAL RISK MANAGEMENT

a. Introduction and overview

The Group has exposure to the following risks arising from its transactions in financial instruments:

- Strategic risk;
- Credit risk;
- Liquidity risk;
- Market risk;
- Currency risk;
- Operational risks;
- Compliance risk;
- Capital adequacy; and
- Environmental and social risks.

38. FINANCIAL RISK MANAGEMENT (Continued)

a. Introduction and overview (Continued)

This note presents information about the Group’s exposure to each of the above risks, the Group’s objectives, policies and processes for identification, measurement, monitoring and controlling risk, and the Group’s management of capital.

Risk management framework

The Group’s approach to risk management is based on a well-established governance process and relies both on individual responsibility and collective oversight, supported by comprehensive reporting. This approach balances stringent corporate oversight with independent risk management structures within the business units.

The Board has overall responsibility for the establishment and oversight of the Bank’s risk management framework. The Board develops the risk appetite and risk tolerance limits appropriate to the Bank’s strategy and requires that management maintains an appropriate system of internal controls to ensure that these risks are managed within the agreed parameters. The Board delegates risk related responsibilities to four Board committees, the Risk Committee, the Credit Committee, the Audit Committee and the Appointments and Remuneration Committee. All the Board Committees have non-executive members and report regularly to the Board on their activities.

The Board Risk Committee has the overall responsibility for the risk management in the Bank as delegated by the Board. Its main responsibility is to have the overall oversight in the credit, market, liquidity and operational risks management as well as any other risks that the Bank may be exposed to in its course of business. It is also responsible for reviewing management performance in implementing the Bank’s strategic plan and ensures that the Bank’s activities are consistent with the policies agreed by the Bank’s Board as well as Directives of the Reserve Bank of Malawi (RBM) and other regulatory requirements.

The Board Audit Committee is responsible for conducting an independent check to ensure compliance with the Bank’s risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Board Risk and Audit Committees are assisted in these functions by the Risk Division which undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Board Risk Committee.

At management level, there is the Enterprise Risk Committee (ERCO) to allow the Bank have a holistic picture of the integrated risks affecting it and the control measures that should be put in place to mitigate the risks and thereby reduce the potential losses and maximise the sustainable shareholders’ value. In addition, the other management Committees such as the Asset and Liability Committee (ALCO), Credit, Operational Risk and IT Policy, are all responsible for developing and monitoring the Bank’s risk management policies in their specified areas.

The Group’s risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank strives to maintain a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Group has adopted three lines of defence in mitigation of the risk exposures namely: business unit management, risk and internal audit. This has been illustrated below:

First line of defence	Second line of defence	Third line of defence
This includes the Business Unit management	Risk management function including compliance	Internal Audit Provides independent assessment
Assesses, evaluates, measures and controls risk exposures through the day-to-day activities of the business within the framework set by the second line of defence.	Sets frameworks within the parameters set by the Board. Provides independent oversight of the first line of defence.	of the adequacy and effectiveness of the frameworks and thereby providing the overall assurance.
Reports to management	Reports to management and Board Risk Committee	Reports to Board Audit Committee

38. FINANCIAL RISK MANAGEMENT (Continued)**b. Credit risk**

Credit risk is the likelihood of financial loss to the Group if customer or counterparty to financial instrument fails to meet its contractual obligations, and arises principally from the Group's loans and advances to customers. For risk management reporting purposes, the Group considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Management of credit risk

The Board has the responsibility for approving and periodically reviewing the credit risk strategy and significant credit risk policies or departures there from of the Group as well as sanctioning facilities beyond management's delegated limits. The Board of Directors has delegated this responsibility to its Board Credit Committee.

Additionally, there is a Management Credit Committee which is comprised of some members of senior management. The Management Credit Committee has the responsibility of implementing the credit risk strategy approved by the Board and for formulating and developing policies and procedures for identifying, measuring, monitoring and controlling credit risk in existing as well as new products, activities and procedures in order to ascertain quality of the Bank's credit portfolio. The committee is also responsible for establishing the authorisation structure for the approval and renewal of credit facilities.

It also oversees development, maintenance and review of the Group's risk gradings in order to categorise exposures according to the degree of risk of potential financial loss and focus management on the attendant risk. The risk grading system helps in determining where impairment provisions may be required against specific credit exposures. The current risk grading framework consists of ten grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. Risk grades are subject to regular reviews.

The committee also reviews credit concentrations vis-à-vis the Bank's capital be they in form of single borrowers or counter parties, a group of connected counter parties, sectors and products to ensure aggregate credit commitments to arrest widespread losses that can arise out of close linkages and correlated factors.

A separate Credit Management Division reporting to the Chief Executive and the Board Credit Committee is responsible for oversight of the Group's overall credit risk management issues including:

- Formulating credit policies and procedures as a general guide to lending in order to maintain credit risk exposure within acceptable parameters and in compliance with the Bank's risk strategy, legal, regulatory and statutory requirements;
- Overseeing the granting and administration of credit i.e. assessment, approval, sanctioning, security perfection, monitoring, review, classification etc;
- Managing exposures to ensure aggregate credit commitments be they in form of single borrowers or counter parties, a group of connected counter parties are maintained within acceptable concentration vis-à-vis the Bank's capital;
- Monitoring compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types; and
- Providing advice, guidance and specialist skills to business units to promote best practice throughout the Bank in the management of credit risk.

Each Business Unit (BU) is required to implement the Bank's credit policies and procedures, within delegated credit approval authorities. Each business unit has a Head or Manager who is accountable for all credit related matters and reports as appropriate to Credit Management Division or the Credit Committee through Credit Management Division. Regular audits of business units and Credit processes are undertaken by the Internal Audit Division.

Basel II approach to credit risk

In accordance with the Bank's strategic plan, the Bank is currently implementing Misys Almonde, a risk management solution for computation of required Basel II capital for credit, operational and market risks.

The Basel II framework permits banks to choose among the three broad methodologies for calculating their capital requirements for credit risk. One method is Standardized Approach for Credit Risk which requires banks providing the external credit assessments for its counterparties. The alternative methodologies, which require explicit approval from the Central Bank of the country, are Internal Rating Based (IRB) Foundation and Advanced IRB approaches which require internal rating assessment for credit risk.

38. FINANCIAL RISK MANAGEMENT (Continued)**b. Credit risk** (Continued)**Basel II approach to credit risk** (Continued)

The RBM recognises all the three approaches for assessing minimum regulatory capital for credit risk. The Bank will adopt the Standardised Approach this year and migrate to the IRB Foundation Approach within the next two years.

Misys Almonde supports all the three methodologies for credit risk. It will be configured for the Standardized approach to compute the credit risk capital with the RBM national discretions incorporated.

The Basel II framework recommends that the Standardised Approach should be based on ratings assigned by eligible External Credit Assessment Institutions (ECAIs) or Export Credit Agencies (ECAs) to determine risk weights for a bank's exposures to counterparties in order to set regulatory capital for credit risk. The Bank will use:

- First the risk weights that have been adopted by the RBM
- Then, if any, the External Rating provided by the ECAIs especially the multi-national companies; and
- Finally the "unrated" exposures will be used.

Under this approach, the assets classification of the RBM is similar to the Basel II standard one, except that the Past Due Loans are risk weighted at 100%. All the non-performing loans (past dues) for each category should be reported on a separate line. The exposure amounts to be risk weighted therefore should be net amounts i.e. less the non-performing loans to avoid double counting.

Exposure to credit risk**Maximum exposure to credit risk without taking into account any collateral or other credit Enhancements**

The table below shows the maximum exposure to credit risk by class of financial instrument. Financial instruments include financial instruments defined and recognised under IAS 39 *Financial Instruments: Recognition and Measurement* as well as other financial instruments not recognised. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

Gross maximum exposure

	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Balances with the Reserve Bank of Malawi	3,738	4,757	3,738	4,757
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	7,801	7,062	7,801	7,062
Government of Malawi local registered stocks	372	467	372	467
Placements with other banks	19,347	8,753	19,347	8,753
Loans and advances to customers	63,001	46,573	63,001	46,588
Other money market deposits	2,104	1,009	2,048	1,000
Other assets	8,539	4,201	8,486	4,181
Total recognised financial instruments	104,902	72,822	104,793	72,808
Guarantees and performance bonds	5,551	4,215	5,551	4,215
Loan commitments and other credit facilities	12,256	10,122	12,256	10,122
Total unrecognised financial instruments	17,807	14,337	17,807	14,337
Total credit exposure	122,709	87,159	122,600	87,145

38. FINANCIAL RISK MANAGEMENT (Continued)

b. Credit risk (Continued)

Net exposure to credit risk without taking into account any collateral or other credit

In respect of certain financial assets, the bank has legally enforceable rights to offset them with financial liabilities. However, in normal circumstances, there would be no intention of settling net, or of realising the financial assets and settling the financial liabilities simultaneously. Consequently, the financial assets are not offset against the respective financial liabilities for financial reporting purposes. However, the exposure to credit risk relating to the respective financial assets is mitigated as follows:

GROUP

	Carrying Amount K'm	Offset K'm	Net exposure to credit risk K'm
31 December 2011			
Balances with the Reserve Bank of Malawi	4,757	-	4,757
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	7,062	-	7,062
Government of Malawi local registered stock	467	-	467
Placements with other banks	8,753	-	8,753
Loans and advances to customers	46,573	-	46,573
Other money market deposits	1,009	-	1,009
Other assets	4,201	-	4,201
	72,822	-	72,822
31 December 2012			
Balances with the Reserve Bank of Malawi	3,738	-	3,738
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	7,801	-	7,801
Government of Malawi local registered stock	372	-	372
Placements with other banks	19,347	-	19,347
Loans and advances to customers	63,001	-	63,001
Other money market deposits	2,104	-	2,104
Other assets	8,539	-	8,539
	104,902	-	104,902

38. FINANCIAL RISK MANAGEMENT (Continued)

b. Credit risk (Continued)

COMPANY

	Carrying Amount K'm	Offset K'm	Net exposure to credit risk K'm
31 December 2011			
Balances with the Reserve Bank of Malawi	4,757	-	4,757
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	7,062	-	7,062
Government of Malawi local registered stock	467	-	467
Placements with other banks	8,753	-	8,753
Loans and advances to customers	46,588	-	46,588
Other money market deposits	1,000	-	1,000
Other assets	4,306	-	4,306
	72,933	-	72,933
31 December 2012			
Balances with the Reserve Bank of Malawi	3,738	-	3,738
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	7,801	-	7,801
Government of Malawi local registered stock	372	-	372
Placements with other banks	19,347	-	19,347
Loans and advances to customers	63,001	-	63,001
Other money market deposits	2,048	-	2,048
Other assets	8,628	-	8,628
	104,935	-	104,935

The Group's credit risk is primarily attributed to overdraft and other loan facilities extended to its customers. The amounts presented in the statement of financial position are net of provisions for doubtful debts as shown above. The specific provision represents allowances for estimated irrecoverable amounts when there is objective evidence that the asset is impaired.

The credit risks on balances with banks, treasury bills, bonds and local registered stocks are limited because the counterparties are institutions with high credit ratings.

38. FINANCIAL RISK MANAGEMENT (Continued)

b. Credit risk (Continued)

There is one significant concentration of credit risk, for K11.2 billion (2011: K8.9 billion) due from SFFRFM which was guaranteed by the Government of Malawi. The remainder of the book is spread over a relatively large number of counterparties and customers.

During the year the Government of Malawi proposed to issue promissory notes to settle this exposure and several other Government Guaranteed loans, including interest, up to the effective date of the promissory notes. The total exposure of NBM to these Government Guarantee loans as at 31 December 2012 was K16.5 billion, including the K11.2 billion owed by SFFRFM mentioned above. The Bank has since accepted the promissory notes to settle the Government Guaranteed loans effective 1 February 2013.

Credit quality of loans and advances

The credit quality of loans and advances is managed by the Group using internal credit ratings. The analysis below shows the credit quality of the loans and advances based on the Group's credit rating system.

	GROUP & COMPANY	
	2012 K'm	2011 K'm
Individually impaired:		
Grade 8: Impaired	508	171
Grade 9: Impaired	487	406
Gross amount	995	577
Allowance for impairment	(190)	(60)
Carrying amount	805	517
Past due but not impaired:		
Grade 7: Watch list	16,227	14,549
Neither past due nor impaired:		
Grade 1 – 3 Low risk	17,560	5,182
Grade 4 – 6 Fair risk	28,409	26,325
Total carrying amount	63,001	46,573

Impaired loans and advances

Impaired loans and advances are loans and advances for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan/advances agreement(s). These loans are graded 8 to 9 in the bank's internal credit risk grading system.

Past due but not impaired loans

These are loans and advances where contractual interest or principal payments are past due but the Group believes that impairment is not appropriate on the basis of the level of security/collateral available and/or the stage of collection of amounts owed to the Group.

38. FINANCIAL RISK MANAGEMENT (Continued)**b. Credit risk (Continued)****Allowance for impairment**

The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individual significant exposures.

Write-off policy

The Group writes off a loan balance (and any related allowances for impairment losses) when it has determined that the loans are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower/issuer's financial position such that the borrower/issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

Set out below is an analysis of the gross and net (of allowances for impairment) amounts of individually impaired assets by risk grade.

GROUP AND COMPANY**Loans and advances to customers**

	Gross K'm	Allowance for Impairment K'm	Net K'm
<u>31 December 2011</u>			
Grade 8: Individually impaired	171	(14)	157
Grade 9: Individually impaired	406	(46)	360
Total	577	(60)	517
<u>31 December 2012</u>			
Grade 8: Individually impaired	508	(130)	378
Grade 9: Individually impaired	487	(60)	427
Total	995	(190)	805

The Group holds collateral against loans and advances to customers in the form of mortgage interests over property, cash, equities, registered securities over assets, guarantees and other forms of collateral. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are only updated when performing the annual review except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to banks, except when securities are held as part of reverse repurchase and securities borrowing activity.

38. FINANCIAL RISK MANAGEMENT (Continued)

b. Credit risk (Continued)

An estimate of the fair value of collateral and other security enhancements held against financial assets is shown below:

	GROUP AND COMPANY	
	2012 K'm	2011 K'm
<u>Against individually impaired</u>		
Motor vehicles	48	36
Commercial property	315	235
Residential property	221	164
Total	584	435
<u>Against the rest of the loan book</u>		
Motor vehicles	6,083	4,042
Commercial property	7,063	7,564
Residential property	11,778	10,559
Cash	2,666	2,843
Equities	112	181
Government guarantees	11,965	11,463
Treasury Bills	728	-
Mortgages over farmland	1,546	-
Bank guarantees	302	275
Total	42,243	36,927
Grand total	42,827	37,362

Collateral repossessed

It is the Group's policy to dispose of repossessed collateral in an orderly fashion. The proceeds are used to reduce or repay the outstanding loan balance. In general the Group does not use repossessed assets for its business.

The Group monitors concentrations of credit risk by sector. An analysis of concentrations of credit risk at the year-end date is shown below:

	Loans and advances to customers			
	GROUP		COMPANY	
	2012 K'm	2011 K'm	2012 K'm	2011 K'm
Concentration by sector				
Agriculture	7,436	7,158	7,436	7,158
Finance and Insurance	1,044	36	1,044	51
Manufacturing	5,758	4,323	5,758	4,323
Other	15,459	7,180	15,459	7,180
Transport and communication	3,957	2,369	3,957	2,369
Real estate	4,355	5,109	4,355	5,109
Personal	4,306	3,847	4,306	3,847
Wholesale and Retail	20,686	16,551	20,686	16,551
	63,001	46,573	63,001	46,588

The risk that counterparties to trading instruments might default on their obligations is monitored on an on-going basis. In monitoring credit risk exposure, consideration is given to trading instruments with a positive fair value and the volatility of the fair value of trading instruments.

To manage the level of credit risk, the Group deals with counterparties of good credit standing, enters into master netting agreements wherever possible, and when appropriate, obtains collateral. Master netting agreements provide for the net settlement of contracts with the same counterparty in the event of default.

38. FINANCIAL RISK MANAGEMENT (Continued)

c. Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations from its financial liabilities.

Management of liquidity risk

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The daily management of liquidity is entrusted with the Treasury and Financial Institutions Division (TFID) at Head Office. The TFID receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. The TFID then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Group as a whole. The liquidity requirements of business units are funded through deposits from customers. Any short-term fluctuations are funded through treasury activities such as inter-bank facilities, repurchase agreements and others.

The TFID monitors compliance of all operating units of the Group with local regulatory limits on a daily basis.

The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions. All liquidity policies and procedures are subject to review and approval by ALCO. Daily reports cover the liquidity position of both the Group and operating units. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO.

Basel II approach to liquidity risk

The Misys Almonde includes modules for Asset and Liability Management (ALM) and Funds Transfer Pricing (FTP).

The ALM module enables the multi-currency balance sheet management including interest rate risk management, balance sheet modelling and forecasting, income simulation, market value sensitivity, liquidity analysis, foreign exchange risk and behaviour modelling such as prepayments.

The FTP allows the Group to calculate the true profitability or cost of any financial contract within the context of the Group's overall business. Through the FTP the Bank can analyse more efficiently its net interest margin, because fund transfer pricing allows for quantifying the variances caused by imbalance of funds provided and funds used by the Bank.

Exposure to liquidity risk

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets are considered as including cash and cash equivalents and investment securities for which there is an active and liquid market less any deposits from banks, other borrowings and commitments maturing within the next month. A similar, but not identical, calculation is used to measure the Group's compliance with the liquidity limit established by the Reserve Bank of Malawi. Details of the reported Group ratio of net liquid assets to deposits from customers at the year-end date and during the reporting period were as follows: 44% (2011: 26%)

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

38. FINANCIAL RISK MANAGEMENT (Continued)

c. Liquidity risk (Continued)

	2012	2011
At 31 December	44%	26%
Average of the period	41%	25%
Maximum for the period	44%	27%
Minimum for the period	38%	23%

The table below analyses assets and liabilities into relevant maturity profiles based on the remaining period to the contractual maturity date.

GROUP

	Less than 1 month K'm	1 - 3 months K'm	3 - 12 months K'm	Over 1 year K'm	Total K'm	Carrying amount K'm
At 31 December 2011						
Financial assets						
Cash and funds with Reserve Bank of Malawi	8,155	-	-	-	8,155	8,155
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	2,056	506	3,600	1,050	7,212	7,062
Local registered stocks	-	-	60	350	410	467
Equity investments	-	695	-	-	695	695
Placements with other banks	7,953	800	-	-	8,753	8,753
Loans and advances to customers	6,923	5,699	21,059	13,262	46,943	46,573
Other money markets deposits	700	309	-	-	1,009	1,009
Other assets	4,583	313	508	19	5,423	4,201
Total financial assets	30,370	8,322	25,227	14,681	78,600	76,915
Financial liabilities						
Customer deposits	62,719	3,550	104	378	66,751	66,751
Amounts due to other banks	2,055	-	819	-	2,874	2,874
Other liabilities	4,345	313	508	-	5,166	5,166
Total financial liabilities	69,119	3,863	1,431	378	74,791	74,791
Contractual liquidity mismatch	(38,749)	4,459	23,796	14,303	3,809	2,124
Cumulative mismatch	(38,749)	(34,290)	(10,494)	3,809	-	-

Included in group balances are gross assets/liabilities and equity for the subsidiary company with carrying amounts totaling K112.5m (before elimination of group balances). As such, the separate analyses of the above are not materially different from the group analyses.

38. FINANCIAL RISK MANAGEMENT (Continued)

c. Liquidity risk (Continued)

GROUP

	Less than 1 month K'm	1 - 3 months K'm	3 - 12 months K'm	Over 1 year K'm	Total K'm	Carrying amount K'm
At 31 December 2012						
Financial assets						
Cash and funds with Reserve Bank of Malawi	8,797	-	-	-	8,797	8,797
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	1,238	-	3,356	3,207	7,801	7,801
Local registered stocks	-	372	-	-	372	372
Equity investments	-	732	-	-	732	732
Placements with other banks	19,347	-	-	-	19,347	19,347
Loans and advances to customers	19,394	4,924	14,229	25,404	63,951	63,001
Other money markets deposits	2,104	-	-	-	2,104	2,104
Other assets	8,515	-	-	24	8,539	8,539
Total financial assets	59,395	6,028	17,585	28,635	111,643	110,693
Financial liabilities						
Long term borrowing	-	25	281	3,089	3,395	3,395
Customer deposits	74,474	11,872	1,063	71	87,480	87,480
Amounts due to other banks	583	-	-	-	583	583
Other liabilities	13,411	1,750	-	-	15,161	15,161
Total financial liabilities	88,468	13,647	1,344	3,160	106,619	106,619
Contractual liquidity mismatch	(29,073)	(7,619)	16,241	25,475	5,024	4,074
Cumulative mismatch	(29,073)	(36,692)	(20,451)	5,024	-	-

Included in group balances are gross assets/liabilities and equity for subsidiary companies with carrying amounts totaling K88.6m (before elimination of group balances). As such, the separate analyses of the above are not materially different from the group analyses.

The contractual liquidity mismatch shows the mismatch before any adjustments are made for product and customer behavioural assumptions. The Group's Asset and Liability Committee manages this mismatch by setting guidelines and limits for anticipated liquidity gaps and monitors these gaps daily. The committee reviews the product and customer behavioural assumptions when there is indication that there is a shift in one or more variables.

38. FINANCIAL RISK MANAGEMENT (Continued)**d. Market risks**

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control risk exposures within acceptable parameters, while optimising the return on risk.

Management of market risks

The Group separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios mainly are held by the Treasury and Financial Institutions Division, and include positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

Overall authority for market risk is vested in ALCO. Treasury and Financial Institutions Division is responsible for the development of detailed risk management policies (subject to review and approval by ALCO) and for the day-to-day review of their implementation.

Basel II approach to market risk

The Basel II framework permits banks to choose among the two methodologies for calculating their capital requirements for market risk. The first method is the Standardized Measurement Method (STD), It uses a 'building block' approach for interest rate-related and equity instruments which differentiates capital requirements for specific risk from those for general market risk. The second method is the Internal Models Method (IMM). It allows banks to use risk measures derived from their own internal risk management models.

The Bank will adopt the STD this year and it will use the Misys Almonde to satisfy the requirements. It will cover all the four types of market risk as shown below:

- Foreign exchange risk—the risk incurred by the Bank because of foreign exchange rate variations.
- Interest rate risk— the risk incurred by the Bank because of interest rate variations.
- Equity risk—the risk incurred by the bank because of stock prices variations; and
- Commodity risk— the risk incurred by the Bank because of commodity prices (i.e. grains, metals, etc.) variations.

Exposure of interest rate risk: non-trading portfolio

The principal risk to which non-trading portfolio are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands. The ALCO is the monitoring body for compliance with these limits and is assisted by Treasury and Financial Institutions Division in its day-today monitoring activities. The table below summarises the exposure to interest rate risks. Included in the table are the Group's assets and liabilities at carrying amounts, categorised by earlier of contractual re-pricing or maturity dates.

38. FINANCIAL RISK MANAGEMENT (Continued)

d. Market risks (Continued)

Exposure of interest rate risk: non-trading portfolio (Continued)

The Group does not bear an interest rate risk on off statement of financial position items. A summary of the Group's maturity profile gap position on non-trading portfolio is as follows:

GROUP

	Less than 1 month K'm	1 - 3 months K'm	3 - 12 months K'm	Over 1 year K'm	Non- interest sensitive K'm	Total K'm
At 31 December 2011						
Financial assets						
Cash and funds with Reserve Bank of Malawi	-	-	-	-	8,155	8,155
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	2,049	501	3,419	1,093	-	7,062
Government of Malawi local registered stocks	-	-	63	404	-	467
Equity investments	-	695	-	-	-	695
Placements with other banks	8,753	-	-	-	-	8,753
Loans and advances to customers	6,553	5,699	21,059	13,262	-	46,573
Other money market deposits	700	309	-	-	-	1,009
Other assets	-	-	-	-	4,201	4,201
Total financial assets	18,055	7,204	24,541	14,759	12,356	76,915
Financial liabilities						
Customer deposits	61,933	3,550	104	378	786	66,751
Amounts due to other banks	2,055	-	819	-	-	2,874
Other liabilities	-	-	-	-	5,166	5,166
Total financial liabilities	63,988	3,550	923	378	5,952	74,791
Interest sensitivity gap	(45,933)	3,654	23,618	14,381	6,404	2,124
Cumulative gap	(45,933)	(42,279)	(18,661)	(4,280)	2,124	-
<i>Impact on profit of an increase in interest rates +1%</i>	(459)	37	236	144	-	(42) +2%
<i>Impact on profit of a decrease in interest rates -1%</i>	459	(37)	(236)	(144)	-	42 -2%

Included in group balances are gross assets/liabilities and equity for the subsidiary company with carrying amounts totaling K88.6m (before elimination of group balances). As such, the separate analyses of the above are not materially different from the group analyses.

38. FINANCIAL RISK MANAGEMENT (Continued)

d. Market risks (Continued)

Exposure of interest rate risk: non-trading portfolio (Continued)

GROUP

	Less than 1 month K'm	1 - 3 months K'm	3 - 12 months K'm	Over 1 year K'm	Non- interest sensitive K'm	Total K'm
At 31 December 2012						
Financial assets						
Cash and funds with Reserve Bank of Malawi	-	-	-	-	8,797	8,797
Government of Malawi treasury bills and Reserve Bank of Malawi bonds	1,238	-	3,356	3,207	-	7,801
Government of Malawi local registered stocks	-	372	-	-	-	372
Equity investments	-	732	-	-	-	732
Placements with other banks	19,347	-	-	-	-	19,347
Loans and advances to customers	18,444	4,924	14,229	25,404	-	63,001
Other money market deposits	2,104	-	-	-	-	2,104
Other assets	-	-	-	-	8,539	8,539
Total financial assets	41,133	6,028	17,585	28,611	17,336	110,693
Financial liabilities						
Long term borrowing	-	25	281	3,089	-	3,395
Customer deposits	73,274	11,872	1,063	71	1,200	87,480
Amounts due to other banks	583	-	-	-	-	583
Other liabilities	-	-	-	-	15,161	15,161
Total financial liabilities	73,857	11,897	1,344	3,160	16,361	106,619
Interest sensitivity gap	(32,724)	(5,869)	16,241	25,451	975	4,074
Cumulative gap	(32,724)	(38,593)	(22,352)	3,099	4,074	-
<i>Impact on profit of an increase in interest rates +1%</i>	(327)	(59)	162	255	-	31 +2%
<i>Impact on profit of a decrease in interest rates -1%</i>	327	59	(162)	(255)	-	(31) -2%

Included in group balances are gross assets/liabilities and equity for the subsidiary company with carrying amounts totaling K217.3m (before elimination of group balances). As such, the separate analyses of the above are not materially different from the group analyses.

38. FINANCIAL RISK MANAGEMENT (Continued)

e. Currency risk

The Group had the following significant foreign currency positions:

GROUP

	MK K'm	USD K'm	GBP K'm	EURO K'm	ZAR K'm	OTHER K'm	TOTAL K'm
At 31 December 2011							
Financial assets							
Cash and funds with Reserve Bank of Malawi	6,698	1,452	3	1	1	-	8,155
Government of Malawi Treasury Bills and Reserve Bank of Malawi Bonds	7,062	-	-	-	-	-	7,062
Government of Malawi local registered stocks	467	-	-	-	-	-	467
Equity investments	695	-	-	-	-	-	695
Placements with other banks	3,393	2,755	1,327	1,150	3	125	8,753
Loans and advances to customer	41,816	4,757	-	-	-	-	46,573
Other money market deposits	1,009	-	-	-	-	-	1,009
Other assets	3,326	436	-	308	131	-	4,201
Total financial assets	64,466	9,400	1,330	1,459	135	125	76,915
Financial liabilities							
Customer deposits	58,026	6,230	1,385	1,023	13	74	66,751
Amounts due to other banks	1,411	1,349	9	10	95	-	2,874
Other liabilities	1,973	2,660	-	308	224	1	5,166
Total financial liabilities	61,410	10,239	1,394	1,341	332	75	74,791
Net balance open position	3,056	(839)	(64)	118	(197)	50	2,124
<i>Impact of a 10% strengthening of the Malawi Kwacha against other currencies on profit</i>	-	84	6	(12)	20	(5)	93
<i>Impact of a 10% weakening of the Malawi Kwacha against other currencies on profit</i>	-	(84)	(6)	12	(20)	5	(93)

Included in group balances are gross assets/liabilities and equity for the subsidiary company with carrying amounts totaling K88.6m (before elimination of group balances). As such, the separate analyses of the above are not materially different from the group analyses.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

38. FINANCIAL RISK MANAGEMENT (Continued)

e. Currency risk (Continued)

GROUP

	MK K'm	USD K'm	GBP K'm	EURO K'm	ZAR K'm	OTHER K'm	TOTAL K'm
At 31 December 2012							
Financial assets							
Cash and funds with Reserve Bank of Malawi	5,061	3,627	13	60	36	-	8,797
Government of Malawi Treasury Bills and Reserve Bank of Malawi Bonds	7,801	-	-	-	-	-	7,801
Government of Malawi local registered stocks	372	-	-	-	-	-	372
Equity investments	732	-	-	-	-	-	732
Placements with other banks	-	13,033	3,271	2,296	650	97	19,347
Loans and advances to customer	56,753	6,247	1	-	-	-	63,001
Other money market deposits	2,104	-	-	-	-	-	2,104
Other assets	929	6,425	65	438	518	164	8,539
Total financial assets	73,752	29,332	3,350	2,794	1,204	261	110,693
Financial liabilities							
Loans and borrowings	-	3,395	-	-	-	-	3,395
Customer deposits	63,259	18,635	3,196	2,283	58	49	87,480
Liabilities to other banks	380	4	-	-	199	-	583
Other liabilities	6,958	6,719	159	399	761	165	15,161
Total financial liabilities	70,597	28,753	3,355	2,682	1,018	214	106,619
Net balance open position	3,155	579	(5)	112	186	47	4,074
<i>Impact of a 10% strengthening of the Malawi Kwacha against other currencies on profit</i>							
	-	(58)	1	(11)	(19)	(5)	(92)
<i>Impact of a 10% weakening of the Malawi Kwacha against other currencies on profit</i>							
	-	58	(1)	11	19	5	92

Included in group balances are gross assets/liabilities and equity for the subsidiary company with carrying amounts totaling K217.3m (before elimination of group balances). As such, the separate analyses of the above are not materially different from the group analyses.

38. FINANCIAL RISK MANAGEMENT (Continued)**f. Operational risk**

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Group's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Group's operations and are faced by all business entities.

The Group's objectives is to manage operational risk so as to balance the avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness and avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the Risk Division by the development of overall Group standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- requirements for the reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial action;
- prevention of business disruption and system failures and development of contingency plans;
- ethical and business standards;
- risk mitigation, including insurance where this is effective; and
- safeguarding assets against loss or damage.

Compliance with Group standards is supported by a programme of periodic reviews undertaken by Risk Division. The results of Internal Audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the management Operational Risk Committee and Board Risk Committee and senior management of the Group.

Basel approach to operational risk

The Basel II framework permits banks to choose among the three broad methodologies for calculating their capital requirements for operational risk. One method is the Basic Indicator Approach (BIA) which requires a bank to use the average gross income for the previous three years for the calculation of the risk weighted assets (RWA). The alternative methodologies, which require explicit approval from the Central Bank of the country, are the Standardised Approach and Advanced Measurement Approach (AMA).

The RBM recognises all the three approaches for assessing minimum regulatory capital for operational risk. The Bank, using the Misys Almonde, will adopt the BIA this year and migrate to the Standardised Approach within the next two years.

For the BIA, the regulatory capital charge calculations will be based on gross income by business line over the last 3 financial years.

In the Standardised Approach, banking activities will be divided into the following eight business lines: corporate finance, trading and sales, retail banking, commercial banking, payment and settlement, agency services, asset management, and retail brokerage.

The capital charge for each business line will be calculated by multiplying gross income by a fixed factor (denoted beta) assigned to that business line. The total capital charge is calculated as the three-year average of the simple summation of the regulatory capital charges across each of the business lines in each year.

38. FINANCIAL RISK MANAGEMENT (Continued)

f. Operational risk (Continued)

Beta values applicable to the gross income for each of the eight business lines, are set by the Basel II Committee. The values of the betas are detailed below:

Business Lines	Beta Factors
Corporate finance	18%
Trading and sales	18%
Retail banking	12%
Commercial banking	15%
Payment and settlement	18%
Agency services	15%
Asset management	12%
Retail brokerage	12%

g. Compliance risk

The risk of non-compliance with any statutory requirements of central or local government, including regulations imposed by the Reserve Bank of Malawi and other regulatory bodies.

The management of compliance risk has become a distinct discipline within the Group’s overall risk management framework. Ultimate responsibility for this risk lies with the Board of Directors. A combination of key activities are undertaken to manage the risk such as identifying the regulatory universe and developing compliance management plans, training staff and other stakeholders on relevant regulatory requirements, and monitoring compliance. The Group has a dedicated Compliance Officer who consults the country’s Financial Intelligence Unit on money laundering and anti-terrorist financing matters.

Money laundering control and occupational health and safety (including aspects of environment risk management) are managed within the compliance function and there are increasingly onerous legislative requirements being imposed in both areas. The Group has adopted anti-money laundering policies including Know Your Customer policies, and procedures, and adheres to the country’s anti-money laundering legislation and Reserve Bank of Malawi regulations and directives.

Statutory requirements

In accordance with the Section 38 of Banking Act, 2009, the Reserve Bank of Malawi has established the following requirements as at the year-end date:

Liquidity reserve requirement

The Bank is required to maintain a liquidity reserve with the Reserve Bank of Malawi equivalent to no less than 15.5% (2011: 15.5%) of total customer deposits. At the end of the year the liquidity reserve was equivalent to 43.6% (2011: 26.0%) of total customer deposits.

Capital adequacy requirement as per Section 10(1) of the Banking Act, 2009

The Bank’s available capital is required to be a minimum of 10.0% (2011: 10.0%) of its risk bearing assets and contingent liabilities. At the end of the year the Bank’s available capital was 23.4% (2011: 25.5%) of its risk bearing assets and contingent liabilities.

Prudential aspects of bank liquidity

As a complement to the Section 38 of the Banking Act, 2009, the Reserve Bank of Malawi had issued the following guidelines on the management of liquidity as at the year-end date:

- Liquidity Ratio I - Net liquidity (total liquid asset less suspense accounts in foreign currency) divided by total deposits must be at least 30%; and
- Liquidity Ratio II - Net liquidity (total liquid assets less suspense accounts in foreign currency and cheques in the course of collection) divided by total deposits must be at least 20%.

Liquidity ratios

At the end of the year, the Bank’s liquidity ratio I was 43.7% (2011: 32.1%) and liquidity ratio II was 43.6% (2011: 32.1%).

38. FINANCIAL RISK MANAGEMENT (Continued)

h. Capital management

Regulatory capital

The Reserve Bank of Malawi sets and monitors capital requirements for the Group as a whole. Regulatory capital requirement is the minimum amount of capital required by the Reserve Bank of Malawi, which if not maintained will usually require supervisory intervention.

In implementing current capital requirements the Reserve Bank of Malawi requires the Group to maintain a prescribed ratio of total capital to total risk-weighted assets. The minimum capital ratios are as follows:

- A core (tier 1) capital of not less than 6% of total risk-weighted on statement of financial position assets plus risk-weighted off-statement of financial position items
- A total capital (tier 2) of not less than 10% of its total risk-weighted on statement of financial position assets plus risk-weighted off-statement of financial position items.

The regulatory capital is analysed into the two tiers as follows:

- Core capital (Tier 1) consists of ordinary share capital, share premium, retained profits, 60% of after-tax profits in the current year (or less 100% of current year loss), less any unconsolidated investment in financial companies.
- Total capital (Tier 2), consists of revaluation reserves and general provisions, when such general provisions have received prior approval of the Reserve Bank of Malawi plus tier 1 capital. Supplementary capital must not exceed core capital i.e. shall be limited to 100% of total core capital.

Banking operations are categorised as either trading book or banking book and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-statement of financial position exposures.

The Board of Directors is responsible for establishing and maintaining at all times an adequate level of capital. The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Group recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a lower gearing position.

The Group and individually regulated operations have complied with all externally imposed capital requirements throughout the period.

There have been no material changes in the Group's management of capital during the period.

38. FINANCIAL RISK MANAGEMENT (Continued)

h. Capital management (Continued)

Regulatory capital (Continued)

The Bank's regulatory capital position at 31 December 2012 was as follows:

	2012	2011
Tier 1 capital		
Ordinary share capital	467	467
Share premium	613	613
Retained earnings	12,997	10,454
Unconsolidated investments	(142)	(142)
Total regulatory (tier 1) capital	13,935	11,392
Supplementary capital		
Loan loss reserve	632	466
Revaluation reserve	3,785	2,291
Total regulatory (tier 2) capital	18,352	14,149
Risk-weighted assets		
Retail bank, corporate bank and treasury	78,379	55,002
Total risk-weighted assets	78,379	55,002
Capital ratios		
Total regulatory capital expressed as a percentage of total risk-weighted assets	23.4%	25.5%
Total tier 1 capital expressed as a percentage of risk-weighted assets	17.8%	20.5%

38. FINANCIAL RISK MANAGEMENT (Continued)**i) Basel II implementation**

The Reserve Bank of Malawi announced in 2011 that all the banks in Malawi must be Basel II compliant by 1 January 2014. The main objective for the Basel II implementation is to strengthen the prudential elements of capital framework and improve the banking sector's ability to absorb shocks arising from financial and economic stress and thereby contain any possible systemic risks in the economy.

The Group is fully committed to be compliant with the Basel II requirements by 2014. The Basel II implementation has been set as one of the milestones to be achieved in the Group's Strategic Plan for the five-year period from 2013 to 2017. The activities that have already been completed by the Group include the following: the Basel II implementation gap analysis and an action plan (road map); setting up of the steering committee and project team; Appointment of the representatives to the Reserve Bank of Malawi Basel II sub committees; Providing training on Basel II to some of the Group's Directors, management and staff; Conducting an assessment of the Basel II solutions and the selection process; Adopting the stress testing and scenario analysis policy and guidelines document; Approving the Basel II capital and revenue expenditures in the years 2012 and 2013 budgets; Participating in the first and second Reserve Bank of Malawi's Basel II Quantitative Impact Studies; and participating in the Reserve Bank of Malawi's Basel II self-assessments.

The Group continues to assess the impact of these proposals on its capital position to arrive at an appropriately calibrated total level of risk-weighted assets, qualifying capital and leverage ratio, and has factored the proposals into its strategic business plans.

Misys Almonde was selected as the Basel II solution that satisfied the Group's request for proposal (RFP) requirements and implementation had since commenced. The business analysis review was done and the data mapping exercise was being done. The key milestones in this exercise include the following:

- Updating the product attributes in T24 to comply with the Basel II (Almonde) format;
- Updating the ISIC codes in T24 by either editing the product screens or deleting the wrong product screens and creating the correct product screens;
- Creating the Basel II asset classes in T24;
- Creating the Basel II business lines in T24;
- Creating the permissible Basel II mitigating factors (i.e. qualifying collateral) in T24;
- Deployment of staff members for the exercise;
- Consideration of recruiting a third party (consultant), who is conversant with T24 and has some experience in implementing Basel II solutions, to assist in the data mapping exercise; and
- Training of all the relevant staff members.

The Misys Almonde solution is scheduled to go live on 30 June 2013

j. Environmental and social risks

The Group adopted the environmental and social management policy last year which was also consistent with its own corporate social responsibility (CSR) initiatives. It has taken an obligation to manage the environmental and social impacts that its activities, products and services have on society and to respond strategically to the risks which global environmental and social pressures have on its ability to create sustainable value for its stakeholders.

As a financial services group, it has both direct and indirect impacts on society and the environment. It manages its indirect impact by screening corporate banking loans to ensure that the customers who borrow from it manage their social and environmental risks that are associated with their activities. It is impacted directly on the environment in its daily business activities through its consumption of energy and other resources, and as such it has developed systems and processes to reduce its environmental footprint. In addition, it has raised environmental awareness among its stakeholders, particularly its employees and suppliers.

38. FINANCIAL RISK MANAGEMENT (Continued)

j. Environmental and social risks (Continued)

The major milestones that have been achieved include the following:

- Developed an E&S Policy and the Environmental and Social Management System (ESMS) framework including the exclusion activities list and the approach to E&S risk management;
- Categorised the Bank's existing portfolio and associated risks;
- Established precise procedures, tools and guidelines for review processes including classification, and follow-up (e.g. risk screening tool, client questionnaire etc.);
- Established a sector-based approach to enable effective allocation of the Bank's resources to the different sectors in their portfolio, bringing about specialization and efficiency in E&S risk analysis;
- Provided training to the appropriate bank officers in the E&S procedures. This involved building the business case to obtain both management-level and operational-level buy-in;
- Provided training to the risk and credit analysts;
- Developed strategies for inserting E&S analysis into the existing work flow;
- Developed strategies and tools for communicating E&S findings into the banks' credit decision framework;
- Developed client engagement/information tools;
- Conducted the pilot run of the ESMS;
- Going live of the ESMS; and
- Periodic ESMS monitoring and (internal) reporting.

The Group shall not invest in, lend to, or engage in activities that are detrimental to the environment, harmful, or dangerous to people or communities. In particular it will not support the following activities:

- Production or activities involving forced labour or child labour;
- Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements;
- Production or trade in: a) weapons and munitions, and b) hard liquor;
- Lending to gambling, casinos and equivalent enterprises;
- Any business relating to pornography or prostitution;
- Trade in wildlife or wildlife products regulated under CITES;
- Production or use of or trade in hazardous materials such as radioactive materials, unbounded asbestos and fibres and products containing PCBs;
- Cross-border trade in waste and waste products unless compliant to the Basel Convention and the underlying regulations;
- Drift net fishing in the marine environment using nets in excess of 2.5 km in length;
- Production, use of or trade in pharmaceuticals, pesticides/herbicides, chemicals, ozone depleting substances and other hazardous substances subject to international phase-outs or bans;
- Significant conversion or degradation of Critical Habitat;
- Production and distribution of racist and anti-democratic media;
- Significant alteration, damage, or removal of any critical cultural heritage; and
- Relocation of Indigenous Peoples from traditional or customary lands.

The environmental and social management system will enable the Group to track and manage environment and social aspects of its operations. It will protect the Group against financial, legal and/or reputational risks arising from activities that are not compliant with sustainable development.

39. RELATED PARTY TRANSACTIONS

The approval of the Reserve Bank of Malawi has been obtained for related party transactions in accordance with the terms of the Banking Act, 2009.

The Group transacts a portion of its business with organisations affiliated to the principal shareholders on an arm's length basis.

The Group is controlled by Press Corporation Limited (incorporated in Malawi), which owns 51.5% (2011: 51.5%) of the Ordinary Shares. The Old Mutual Group owns 24.5% (2011: 24.5%) of the Ordinary Shares and the remaining 24% (2011: 24%) of the Ordinary Shares are widely held by individuals, corporate and institutional investors and are publicly traded on the Malawi Stock Exchange.

The ultimate holding entity of the Group is Press Trust. Press Trust owns 44.47% (2011: 44.47%) of Press Corporation Limited.

Transactions between the Bank and its subsidiaries, which are related parties of the Group, have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Group and other related parties are disclosed below.

Net outstanding balances as at 31 December 2012 with the shareholders and other related parties are as follows:

GROUP AND COMPANY

	Loans K'm	Deposits K'm	Net 2012 K'm	Net 2011 K'm
Press Corporation Limited and its subsidiaries	3,393	(1,826)	1,567	457
Old Mutual Group	1	(257)	(256)	(268)
Bottling and Brewing Group Limited	503	(212)	291	968
Limbe Leaf Tobacco Company Limited	70	(246)	(176)	75
Press Trust	-	(14)	(14)	(5)
Directors	70	(19)	51	8
Employees	2,083	(273)	1,810	1,217
National Bank of Malawi Pension Fund	1	(41)	(40)	(17)
Total related party balances	6,121	(2,888)	3,233	2,435

Bottling and Brewing Group Limited and Limbe Leaf Tobacco Company Limited are associates of Press Corporation Limited.

Loans are granted and deposits accepted on normal banking terms. Loans are secured.

During the year no amount due from a related party was written off against interest in suspense and provision for loan losses. There were no provisions in respect of loans granted to related parties as at the end of the year (2011: nil).

There were no material related party transactions with the ultimate holding entity of the Group, Press Trust, during the year.

39. RELATED PARTY TRANSACTIONS (Continued)

The following transactions were conducted with related parties:

GROUP AND COMPANY	2012	2011
	K'm	K'm
Interest receivable		
Press Corporation Limited and its subsidiaries	765	398
Bottling and Brewing Group Limited	55	13
Limbe Leaf Tobacco Company Limited	8	2
Directors	6	-
Employees	377	208
Average interest rate (%)	24	19
Operating lease income		
Malawi Telecommunication Limited	100	129
Bottling and Brewing Group Limited	381	423
Interest payable		
Press Corporation Limited and its subsidiaries	10	7
Old Mutual Group	8	2
Employees	10	141
Purchases		
Press Corporation Limited and its subsidiaries	233	151

	GROUP		COMPANY	
	2012	2011	2012	2011
	K'm	K'm	K'm	K'm
Compensation of key management personnel				
Salaries, bonus and benefits	435	274	405	250
Severance pay	-	150	-	150

No specific share options were offered to key management personnel during the year 31 December 2012 (2011: Nil). No shares were exercised by key management during the year ended 31 December 2012 (2010: Nil).

40. BUSINESS SEGMENTS

A business segment is a group of assets and operations engaged in providing services that are subject to risks and returns that are different from those of other business segments.

The Group is organised on a national basis into three main business segments:

- i. Retail and corporate banking – incorporating, savings, deposits, investment savings products, consumer loans, current accounts, overdrafts, loan and other credit facilities, trade finance and corporate leasing;
- ii. Treasury – incorporating financial instruments trading, dealings in foreign currency, stock broking and derivative products; and
- iii. Other operations comprising fund management, custodial services and providing training services, none of which constitutes a separately reportable segment.

Transactions between the business segments are on normal commercial terms and conditions.

Funds are ordinarily allocated between segments, resulting in funding cost transfers disclosed in operating income. Interest charged for these funds is based on the Group's cost of capital. There are no other material items of income or expense between the business segments. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the statement of financial position, but exclude items such as taxation and borrowings.

40. BUSINESS SEGMENTS (Continued)

	Corporate banking K'm	Retail banking K'm	Treasury K'm	Other K'm	Total K'm
GROUP					
Statement of comprehensive income					
<u>December 2012</u>					
Total external income	12,019	2,581	8,908	993	24,501
Segment result	10,398	1,936	8,779	375	21,488
Unallocated income	-	-	-	-	-
Unallocated expenses	-	-	-	-	(10,483)
Profit before tax	-	-	-	-	11,005
Corporate tax	-	-	-	-	(3,418)
Group profit for the year	-	-	-	-	7,587
Other information					
Depreciation					
Unallocated depreciation	-	-	-	-	1,392
Revaluation surplus on property					
Unallocated fair value gain	-	-	-	-	838
GROUP					
Statement of financial position					
<u>December 2012</u>					
Assets					
Segment assets	44,468	15,286	40,576	29,159	129,489
Unallocated assets	-	-	-	-	-
Total consolidated assets	44,468	15,286	40,576	29,159	129,489
Liabilities and equity					
Segment liabilities	50,734	12,635	28,123	16,430	107,922
Unallocated liabilities and equity	-	-	-	-	-
Total consolidated liabilities and equity	50,734	12,635	28,123	16,430	107,922
Other information					
Capital additions	-	-	-	-	-
Unallocated capital additions	-	-	-	-	21,567
Total	-	-	-	-	129,489

NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 December 2012

40. BUSINESS SEGMENTS (Continued)

GROUP	Corporate banking K'm	Retail banking K'm	Treasury K'm	Other K'm	Total K'm
Statement of comprehensive income 2011					
Total external income	6,215	1,818	4,329	4,253	16,615
Segment result	5,697	1,285	2,487	4,142	13,611
Unallocated income	-	-	-	-	-
Unallocated expenses	-	-	-	-	(8,375)
Profit before tax	-	-	-	-	5,236
Corporate tax	-	-	-	-	(1,678)
Group profit for the year	-	-	-	-	3,558
Other information					
Depreciation					
Unallocated depreciation	-	-	-	-	1,320
Revaluation surplus on property					
Unallocated fair value loss	-	-	-	-	1,491
Statement of financial position December 2011					
Assets					
Segment assets	37,842	7,242	22,989	24,036	92,109
Unallocated assets	-	-	-	-	-
Total consolidated assets	37,842	7,242	22,989	24,036	92,109
Liabilities and equity					
Segment liabilities	46,474	11,559	11,599	6,774	76,406
Unallocated liabilities and equity	-	-	-	-	15,703
Total consolidated liabilities and equity	46,474	11,559	11,599	6,774	92,109
Other information					
Capital additions	-	-	-	-	-
Unallocated capital additions	-	-	-	-	-
Total	-	-	-	-	-

41. EXCHANGE RATES AND INFLATION

The average of the year-end buying and selling rates of the foreign currencies most affecting the performance of the Group are stated below, together with the increase in the National Consumer Price Index, which represents an official measure of inflation.

	2012	2011
Kwacha/GBP	414.96	249.20
Kwacha/Rand	32.45	21.30
Kwacha/US Dollar	255.81	157.50
Kwacha/Euro	337.20	214.60
Inflation (%) (December 2012)	34.6	7.6

At the date of approval of the financial statements, the above noted exchange rates had moved as follows:

Kwacha/GBP	623.76
Kwacha/Rand	45.16
Kwacha/US Dollar	404.35
Kwacha/Euro	530.56

CORRESPONDENT BANKS

The bank also has a network of correspondent banking relationships across the world. Some of these include:

-  Citibank, New York
-  Standard Chartered Bank, London
-  Deutsche Bank AG, Frankfurt
-  Deutsche Bank Trust Company Americas, New York (New)
-  ABSA Bank, Johannesburg
-  First National Bank, Johannesburg
-  Standard Bank, Johannesburg
-  Standard Chartered Bank, Tokyo
-  Bank of Montreal, Canada
-  Union Bank of Switzerland – Zurich
-  West Landsbank, Dusseldorf
-  Commerz Bank, Frankfurt
-  Credit Suisse, Zurich
-  Bank of China, Beijing

As well as banks in India, Sweden, Denmark, Australia, Swaziland, Botswana, Kenya, and Zambia.

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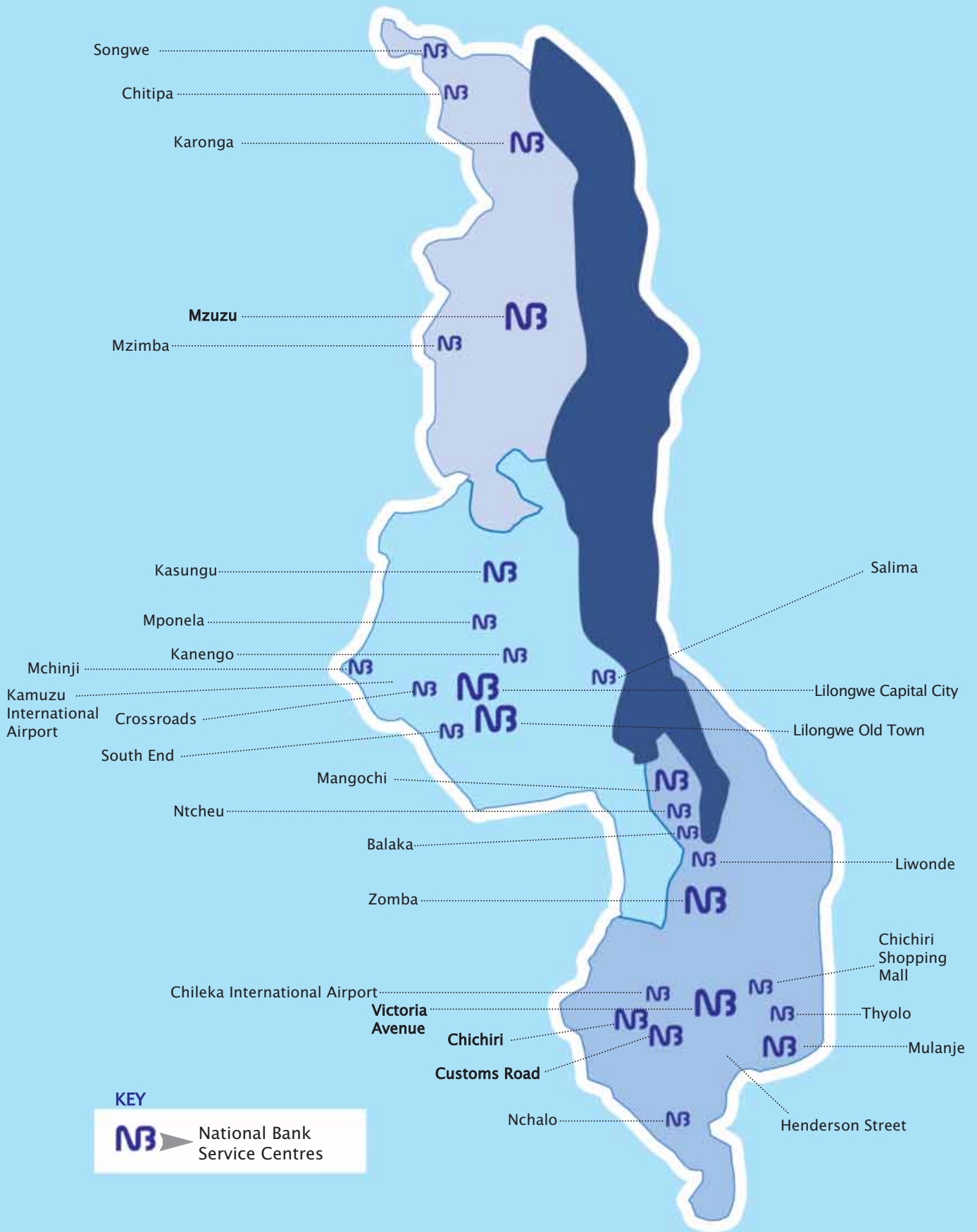
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MAP OF MALAWI – NB SERVICE CENTRES



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