National Bank of Malawi plc

BASEL II PILLAR III (MARKET DISCLOSURE) REPORT

June 2019

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1. OVERVIEW

1.1. Performance and Financial Position

The Bank registered a 7.0% increase in Group after tax profit from K8.5bn in June 2018 to K9.1bn in June 2019. The performance took into consideration costs relating to a staff rationalization program amounting to K812m. Customer deposits and the loan book grew by 8% and 26% respectively contributing to an overall growth in the Statement of Financial Position of 9% from K405bn to K445bn in June 2019.

1.2. The Operating Environment

The overall macroeconomic environment in the first half of the year was generally stable. Average headline inflation at 8.8% was similar to that for the corresponding prior year period. Inflation is projected to marginally increase during the year due to lagging effects of the currency depreciation in the second quarter and pressure on maize prices. The Malawi Kwacha was stable against all its major trading currencies during the first quarter but lost ground during the second quarter, depreciating by 7% to the US dollar. This was due to front loading of import payments prior to the General Elections.

During the period, the Policy Rate was reduced to 13.5% from 16%. Similarly, the Liquidity Reserve Requirements (LRR) ratios were also reduced to 5% and 3.75 % for Malawi Kwacha and foreign currency liabilities respectively from a uniform 7.5% rate.

The business environment remained subdued in spite of the generally stable macroeconomic environment and the easing of monetary policy, largely on account of uncertainties pre and post the May 2019 General Elections.

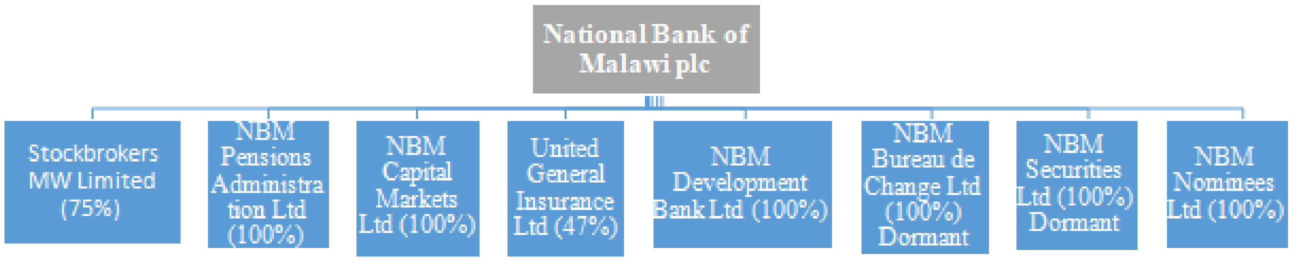
1.3. Report Scope

The Market Disclosure Report is mandated by the Reserve Bank of Malawi Guidelines on Market Disclosures under Basel II Pillar III. The Disclosures under Basel II complement the minimum capital requirements and the supervisory review process. It discloses the scope of application of Basel II, capital, particular risk exposures and risk assessment processes, and hence the capital adequacy of National Bank of Malawi plc. Disclosures consist of both quantitative and qualitative information and are provided at the consolidated level. National Bank of Malawi plc hereby presents this Market Disclosure report as at 30th June 2019 in line with Guidelines on Market Disclosures under Basel II Pillar III issued by the Reserve Bank of Malawi.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 and Directives of the RBM and other regulatory requirements.

1.4. National Bank of Malawi plc Group Structure

National Bank of Malawi plc was established on 1st July 1971 through an amalgamation of the interests of Standard Chartered Bank and Barclays Bank DCO. The Bank was listed on the Malawi Stock Exchange on 21st August 2000 with a total of 450,000,000 issued ordinary shares of K1 each. The Group provides retail, corporate, long-term/development and investment banking as well as Stock Broking, Asset Management, Insurance and Pension Administration services in Malawi through 8 subsidiaries and a network of 32 Service Centres in Malawi.

The subsidiary and associate companies of the Bank are shown below;



1.5. Enterprise Risk Group Structure and Oversight

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 following are the main governance structure for enterprise risk management:

1.5.1. The Board

The Board has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board develops the risk appetite, risk tolerance limits appropriate to the Group'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 five Board committees namely; the Risk Committee, the Credit Committee, the Audit Committee, the Appointments, Remuneration and Governance Committee, and the Related Parties Committee. The Board Committees comprise non-executive membership only and they report regularly to the Board on their activities.

1.5.2. The Board Risk Committee

The Board Risk Committee has responsibility for the risk management in the Group 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 Group may be exposed to in its course of business. It is also responsible for reviewing management performance in implementing the Group's strategic plan and ensures that the Group's activities are consistent with the policies agreed by the Group's Board and Directives of the RBM and other regulatory requirements.

1.5.3. The Board Audit Committee

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

1.5.4. The Board Credit Committee

The Board Credit Committee is responsible for oversight of the Group's overall credit risk management issues. The committee is responsible for reviewing and approving the Group's credit policies including provisioning, large loan exposures, counter-party lending and interbank limits.

1.5.5. The Board Appointments, Remuneration and Governance Committee

The Appointments, Remuneration and Governance Committee is responsible for nominations and vetting of director appointments, good governance practices, ensuring that the Group has a robust succession plan, that the Group's human resources are best utilised, and that members of staff are remunerated commensurately with their responsibilities and effectiveness.

1.5.6. Enterprise Risk Committee

At management level, there is the Enterprise Risk Committee (ERCO), which provides a holistic oversight of the risks affecting the Group and the control measures that should be put in place to mitigate the risks and thereby reduce the potential losses. In addition, other Management Committees such as the Asset and Liability Committee (ALCO), Credit Committee (CREDCO) and IT Policy Committee (ITPC) are all responsible for developing and monitoring the Group's risk management policies in their specified areas.

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

2. RISK APPETITE

2.1. Definition

The Bank defines Risk Appetite as the amount and type of risk that the NBM plc Group is able and willing to accept in pursuit of its business objectives. The risk appetite therefore reflects the tolerance and willingness to accept risk and our ability to exploit business opportunities.

The Group's risk appetite includes qualitative statements as well as quantitative measures expressed relative to earnings, capital, liquidity and other relevant measures. Qualitatively, the Group expresses risk appetite in terms of policies, processes, procedures, statements and controls meant to limit risks that may or may not be quantified.

2.2. Approach to Risk Appetite Oversight

The Board has the overall responsibility for the establishment and oversight of the Bank's risk appetite. The Board has developed risk appetite and risk tolerance limits appropriate to the Bank's strategy and requires that Senior Management maintains an appropriate system of internal controls to ensure that these risks are managed within the agreed parameters.

Risk appetite across all risk types for the Bank is determined by the risk appetite statement and is apportioned to the various business units. Each business unit sub allocates its apportionment to various risk types in accordance with its business strategy. In developing the Risk Appetite Statement, the Bank's strategy and the desired balance between risk and return is taken into consideration.

2.3. Performance against Risk Appetite

During the review period, the Bank was generally within the approved risk appetite limits. The Bank has greatly improved the Non-Performing Loan ratio which was at 3.08% as compared to the 7.52% in June 2018. The NPL ratio was within the risk appetite range of 3-5%.

3. CAPITAL MANAGEMENT

3.1. Approach to Capital Management and Governance

The Bank's capital management strategy is designed to ensure that regulatory capital requirements are met at all times, and that the Bank and its principal subsidiaries and strategic associates are well capitalized in line with the group's risk appetite and target ratios approved by the Board.

3.2. Regulatory Capital

The Bank's capital management strategy is designed to ensure that regulatory capital requirements are met at all times, and that the Bank and its principal subsidiaries and strategic associates are well capitalized in line with the group's risk appetite and target ratios approved by the Board.

The Bank's Capital Management Policy (CMP) provides the processes for defining, measuring, raising and investing all types of capital in the Bank. The policy aims at optimizing the Bank's capital usage and to fulfil the requirements of the business and maintain an efficient capital structure with limited excesses. Capital adequacy is actively managed and forms a key component of the Bank's budget and forecasting process. The capital plan is tested under a range of stress scenarios as part of the Bank's annual Internal Capital Adequacy Assessment Process (ICAAP).

The main regulatory requirements to be complied with are those specified in the Financial Services Act 26 of 2010, The Reserve Bank of Malawi Directive on Capital Adequacy and related regulations, which are aligned with Basel II.

Regulatory capital adequacy is measured through the following two risk-based ratios:

Tier 1 (Core Capital) Ratio
The sum of share capital, paid-up, share premium, retained profits (prior years), 60% of after tax profit (current year-to-date) and in case of a loss, 100% and Other eligible core capital (Tier 1) elements as prescribed by the Registrar, less: investment in unconsolidated financial institutions.

Tier II (supplementary capital) ratio
The sum of revaluation reserves, subordinated debt; and the general provisions, which have received prior approval of the Registrar.

The table below shows the capital position of the Bank as at 30th June 2019 compared to a similar period last year.

Capital adequacy	Jun-2019	Jun-2018	Change (%)
Core Capital	54,245,008	46,366,876	17.0%
Total Capital	65,607,312	61,049,481	7.5%
Credit Risk Weighted Assets	253,011,128	229,109,533	10.4%
Operational Risk Weighted Assets	103,671,258	95,463,263	8.6%
Market Risk Weighted Assets	8,777,030	8,540,359	2.8%
Total Risk Weighted Assets	365,459,416	333,113,155	9.7%
Risk Based capital ratio I (Basel II approach)	14.84%	13.92%	6.6%
Risk Based capital ratio II (Basel II approach)	19.60%	18.33%	6.9%

Total Risk Weighted Assets (RWA) increased by 9.7% from K333.11bn to K365.46bn. This change was largely attributed to an increase in the operational risk and credit risk components which increased by 8.6% and 10.4%, respectively. The increase in the Bank's RWAs is significantly lower as compared to the 35.73% change experienced between 2017 and 2018 during the same period.

4. CREDIT RISK

Credit Risk means the likelihood that a debtor or financial instrument issuer is unwilling or unable to pay interest and/or repay the principal according to the terms specified in a credit agreement resulting in economic loss to the Bank. The risk arises from direct lending, trade finance and leasing business, but also from off-balance sheet activities such as guarantees, letters of credits and from holding of debt securities.

4.1. Approach to Managing Credit Risk

The Bank's credit risk arises mainly from wholesale and retail loans and advances. The Board of Directors has the responsibility for approving and periodically reviewing the credit risk strategy and significant credit risk policies or departures there from of the Bank as well as sanctioning facilities beyond Management's delegated limits. The Board of Directors delegates this responsibility to its Board Credit Committee. A Management Credit Committee was set up to be 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 oversees development, maintenance and review of the Group's risk grades in order to categorize 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 reviews credit concentrations vis-à-vis the Bank's capital in the form of single borrowers or counter parties, 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. 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.

4.2. Credit Risk Measurement

The Bank measures the credit risk capital requirements by applying appropriate risk weights to both on-balance sheet and off-balance sheet exposures in line with Basel II and the Guidelines on Standardized Approach to Credit Risk issued by the Reserve Bank of Malawi (RBM).

Recognision of Loss Allowance for Expected Credit Losses(ECLs)

The Bank analyses all data collected using statistical models and estimates the remaining lifetime Probability of Default (PD) of exposures and how these are expected to change over time. The factors taken into account in this process include macro-economic data such as GDP growth, unemployment, benchmark interest rates and house prices. The Bank then uses these forecasts, which are probability-weighted, to adjust its estimates for PDs, Exposure At Default (EADs) and the eventual Loss Given Defualt (LGDs).

The Group uses different criteria to determine whether credit risk has increased significantly per portfolio of assets. The criteria used are both quantitative changes in PDs as well as qualitative. The Bank assesses whether the credit risk on a financial instrument has increased significantly at reporting date since initial recognition. It does this by; -

1. Use of all reasonable and supportive information without undue cost to conduct the assessment.

2. Use of Significant Increase in Credit Risk (SICR) triggers in a more forward-looking manner than past due status, i.e. the Bank tries to anticipate default before past due (backstop) occurs.
3. The Bank also reviews and applies SICR rules on an individual as well as on collective basis.

The table below summarises per sector of asset the PDs as at 30th June 2019 and those of 31st December 2018.

SUMMARY OF AVERAGE PDs, LGDs, AND EADs AS AT 30TH JUNE 2019											
	STAGE ONE					STAGE TWO					STAGE THREE
INDUSTRY	PD_12	LGD_12	EAD_12	ECL_12	DF_12	PD_life	EAD_life	LGD_life	ECL_life	DF_life	LGD_NPL
AGRICULTURE FORESTRY FISHING AND HUNTING	0.1512	0.2375	0.8022	0.0269	0.9382	0.1512	0.8022	0.2375	0.0269	0.9382	0.0057
COMMUNITY SOCIAL AND PERSONAL SERVICES	0.2033	0.1864	0.9064	0.0329	0.8467	0.2040	0.9061	0.1864	0.0330	0.8465	0.0506
CONSTRUCTION	0.2105	0.1805	0.8553	0.0349	0.7992	0.2110	0.8550	0.1805	0.0349	0.7991	0.1028
ELECTRICITY GAS WATER AND ENERGY	0.1288	0.2327	0.9117	0.0220	0.8490	0.1298	0.9108	0.2327	0.0221	0.8489	0.0293
FINANCIAL SERVICES	0.2068	0.1893	0.8612	0.0324	0.8454	0.2071	0.8610	0.1893	0.0324	0.8453	0.0495
MANUFACTURING	0.1760	0.2055	0.8701	0.0312	0.8266	0.1774	0.8691	0.2055	0.0314	0.8264	0.0643
MINING AND QUARRYING	0.1242	0.2094	1.0279	0.0203	0.9499	0.1242	1.0279	0.2094	0.0203	0.9499	0.0000
PERSONAL SECTOR - ORDINARY	0.0976	0.2982	20.8575	0.5125	0.8658	0.0993	21.1315	0.2982	0.7308	0.8653	0.0288
PERSONAL SECTOR STAFF	0.0107	0.3346	1.0194	0.0026	0.9713	0.0107	1.0193	0.3346	0.0026	0.9713	0.0000
REAL ESTATE	0.1711	0.2361	0.9303	0.0303	0.8882	0.1711	0.9303	0.2361	0.0303	0.8882	0.0048
RESTAURANTS AND HOTELS	0.1761	0.2093	0.8856	0.0305	0.8376	0.1792	0.8845	0.2093	0.0310	0.8369	0.0564
TRANSPORT STORAGE AND COMMUNICATION	0.1570	0.2015	0.1222	0.2154	0.7718	0.1583	0.1208	0.2015	0.2393	0.7716	0.1312
WHOLESALE AND RETAIL TRADE	0.1811	0.1910	0.8304	0.0299	0.7964	0.1816	0.8300	0.1910	0.0299	0.7963	0.0824

SUMMARY OF AVERAGE PDS, LGDS, EADS, AS AT 30 JUNE 2018											
	STAGE ONE					STAGE TWO					STAGE THREE
INDUSTRY	PD_12	EAD_12	LGD_12	DF_12	ECL_12	PD_life	DF_life	ECL_life	EAD_life	LGD_life	LGD_NPL
AGRICULTURE FORESTRY FISHING AND F	0.19620	0.66550	0.19863	0.82495	0.03407	0.19645	0.82480	0.03410	0.66555	0.19863	0.02679
COMMUNITY SOCIAL AND PERSONAL SER	0.16762	0.48410	0.13213	0.52490	0.03384	0.16845	0.52484	0.03386	0.48346	0.13213	0.09294
CONSTRUCTION	0.15074	0.43305	0.12238	0.48337	0.02907	0.15110	0.48337	0.02907	0.43288	0.12238	0.09370
ELECTRICITY GAS WATER AND ENERGY	0.12352	0.64525	0.16866	0.67384	0.02398	0.12352	0.67384	0.02398	0.64525	0.16866	0.04001
FINANCIAL SERVICES	0.15515	0.43343	0.12247	0.47567	0.02990	0.15515	0.47567	0.02990	0.43343	0.12247	0.09900
MANUFACTURING	0.15221	0.50243	0.15105	0.60247	0.02744	0.15290	0.60246	0.02744	0.50175	0.15105	0.07045
MINING AND QUARRYING	0.40494	0.60000	0.13793	0.57879	0.08963	0.40494	0.57879	0.08963	0.60000	0.13793	0.09467
PERSONAL SECTOR - ORDINARY	0.14064	0.35204	0.15672	0.59372	0.01656	0.14143	0.59365	0.01658	0.35113	0.15672	0.05846
PERSONAL SECTOR STAFF	0.01885	0.66814	0.22966	0.94311	0.00271	0.01885	0.94311	0.00271	0.66814	0.22966	0.00013
REAL ESTATE	0.12007	0.50457	0.14056	0.55920	0.02336	0.12010	0.55920	0.02336	0.50454	0.14056	0.07946
RESTAURANTS AND HOTELS	0.16929	0.60303	0.17264	0.68643	0.03261	0.16929	0.68643	0.03261	0.60303	0.17264	0.05458
TRANSPORT STORAGE AND COMMUNICAT	0.11639	0.39552	0.12149	0.48575	0.02118	0.11812	0.48550	0.02123	0.39558	0.12149	0.12609
WHOLESALE AND RETAIL TRADE	0.12605	0.41738	0.13981	0.55779	0.02152	0.12874	0.55763	0.02158	0.41524	0.13981	0.07376

Except for Personal Sector -staff and Real Estate there has been an improvement in the probability of default (PDs) for the six months ending 30th June 2019. There have been significant changes in the economic environment for the borrower especially in the lowering of applicable interest rates on loans rendering the loans more affordable. The applicable rate has gone down by at least 5% within six months.

INDUSTRY	30-Jun-18 EXPOSURE AS AT 30 JUNE 2018	AVERAGE PD_12	IFRS9 Provision	30-Jun-19 EXPOSURE AS AT 30 JUNE 2019	AVERAGE PD_12	IFRS9 Provision
AGRICULTURE FORESTRY FISHING AND HUNTIN	30,577,348	0.19620	130,488	38,020,372	0.15117	1,193,275
COMMUNITY SOCIAL AND PERSONAL SERVICES	96	0.16762	22	2,684,963	0.20334	253,579
CONSTRUCTION	39,139,473	0.15074	429,850	2,188,155	0.21051	417,988
ELECTRICITY GAS WATER AND ENERGY	11,028,846	0.12352	16,746	23,956,775	0.12884	993,996
FINANCIAL SERVICES	2,498,299	0.15515	68,503	3,016,701	0.20678	33,000
MANUFACTURING	34,056,587	0.15221	4,937,272	27,189,806	0.17604	860,704
MINING AND QUARRYING	8,007,775	0.40494	11,412	97,670	0.12419	323
PERSONAL SECTOR	6,355,409	0.07974	57,186	30,096,565	0.05413	853,569
REAL ESTATE	1,526,552	0.12007	17,149	3,144,276	0.17110	131,184
RESTAURANTS AND HOTELS	3,984,102	0.16929	101,277	14,786,229	0.17612	282,431
TRANSPORT STORAGE AND COMMUNICATION	6,813,885	0.11639	175	9,085,842	0.15703	328,029
WHOLESALE AND RETAIL TRADE	23,858,944	0.12605	366,434	46,774,197	0.18106	1,718,438
TOTAL	**167,847,316**		**6,136,514**	**201,041,551**		**7,066,515**

The Bank does conduct timely assessment credit risk at each reporting date to determine if:

a) Credit-impaired: It is reported as Stage 3 and recognised lifetime Expected Credit Loss (ECL).
b) Not credit impaired and Significant Increase in Credit Risk (SICR) occurred since origination: It is reported as Stage 2 and recognizedlifetime ECL.
c) Not credit-impaired & SICR has not occurred since origination: It is reported as Stage 1 and recognised 12-month ECL.

4.3. The Nature and Extent of Credit Risk Exposures

The Bank measures the credit risk capital requirements by applying appropriate risk weights to both on-balance sheet and off-balance sheet exposures in line with Basel II and the Guidelines on Standardized Approach to Credit Risk issued by the Reserve Bank of Malawi (RBM).

Total loans and advances increased by 20.9% from K156.53bn to K189.22bn as at 30th June 2019. This increase was attributed mainly to an increase in the corporate loans.

Indicators	Jun-2019	Jun-2018	Change(%)
	K'm	K'm	
Net Loans and Advances	189,220	156,533	20.9%
Non-Performing loans	6,196	12,614	-50.9%
Specific Provisions	0	0	0
IFRS9 Provision	7,066	8,984	-21.35%
Non-Performing loans to total loans and advances	3.08%	7.52%	-59.0%

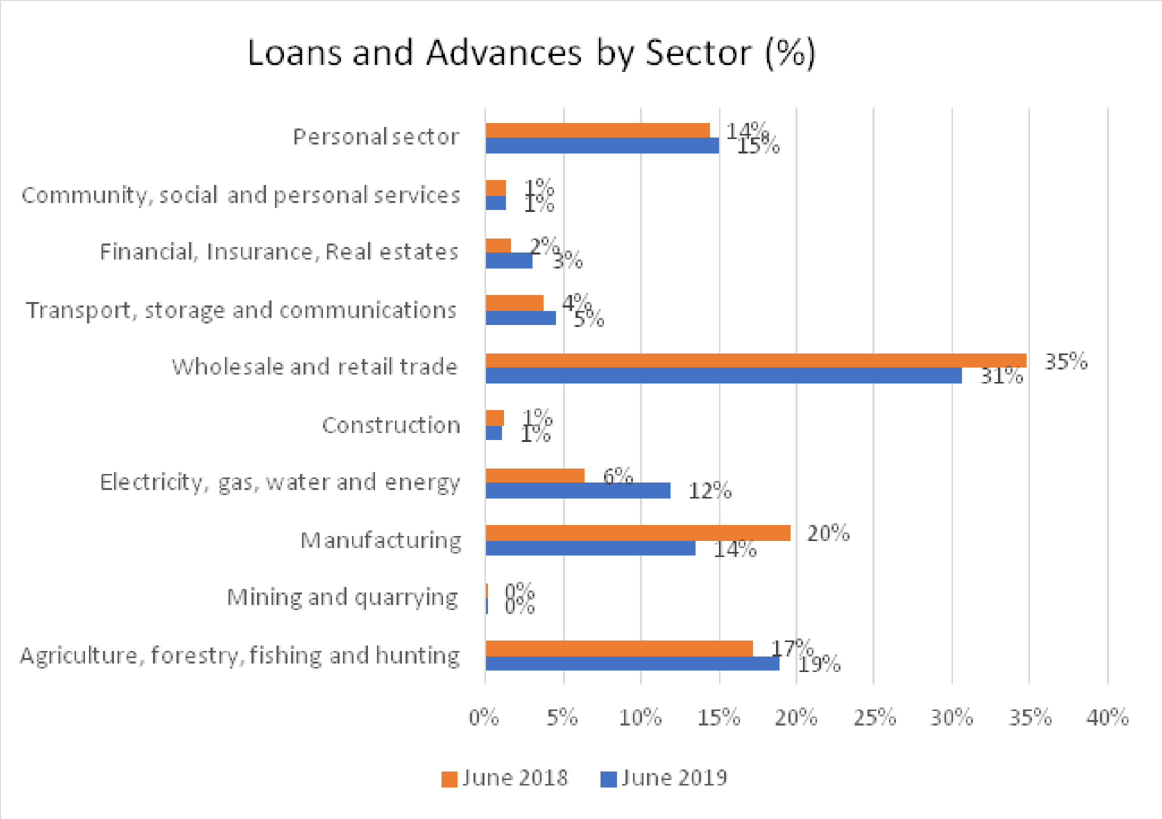
Total non-performing loans decreased by 50.9% from K12.61bn to K6.20bn which led to a decreased NPL ratio from 7.52% to 3.08%. The Bank was on track in implementing strategies to maintain the NPL ratio to be within 3-5% range as stated in the risk appetite.

4.4. Loans and Advances to Customers by IFRS9 Stages

Stage	June 2019 K'm	June 2018 K'm	Change (%)
Stage 1	177,844,178	149,479,488	+19%
Stage 2	17,001,252	5,753,121	+196%
Stage 3	6,196,121	12,614,707	-51%
Total Gross Carrying Amount	**201,041,551**	**167,847,316**	**+20%**
Less Loss Allowance	(8,311,744)	(9,664,980)	-14%
Net Carrying amount	**192,729,807**	**158,182,336**	**+22%**

4.5. Loans and Advances to Customers by Sector

Sector	June 2019	June 2018
Agriculture, forestry, fishing and hunting	38,020,372	28,801,527
Mining and quarrying	97,670	96
Manufacturing	27,189,806	32,791,809
Electricity, gas, water and energy	23,956,775	10,637,941
Construction	2,188,155	1,920,978
Wholesale and retail trade	61,560,427	58,430,540
Transport, storage and communications	9,085,842	6,257,060
Financial, Insurance, Real estates	6,160,977	2,663,590
Community, social and personal services	2,684,962	2,242,477
Personal sector	30,096,565	24,101,328
Total	**201,041,551**	**167,847,316**



5. LIQUIDITY RISK AND FUNDING

The Bank defines Liquidity Risk as the potential for loss to the Bank arising from either its inability to meet obligations as they fall due or to fund increases in assets without incurring unacceptable cost or losses (funding or market liquidity risk).

5.1. Approach and Management of Liquidity Risk

The primary role of a bank in terms of financial intermediation is to transform short-term deposits into longer-term loans. 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 Group has a Liquidity and Funds Management Policy that provides guidance in the management of liquidity. The daily management of liquidity is entrusted to the Treasury and Investment Banking Division (TIBD) at Head Office. The TIBD 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.

5.2. Regulatory Liquidity Limits

The Bank experienced a steady decrease in liquidity ratios during the first half of 2019. Liquidity ratio I decreased from 61.99% to 46.42%. in June 2019. Liquidity ratio II decreased from 61.90%.to 45.37%.

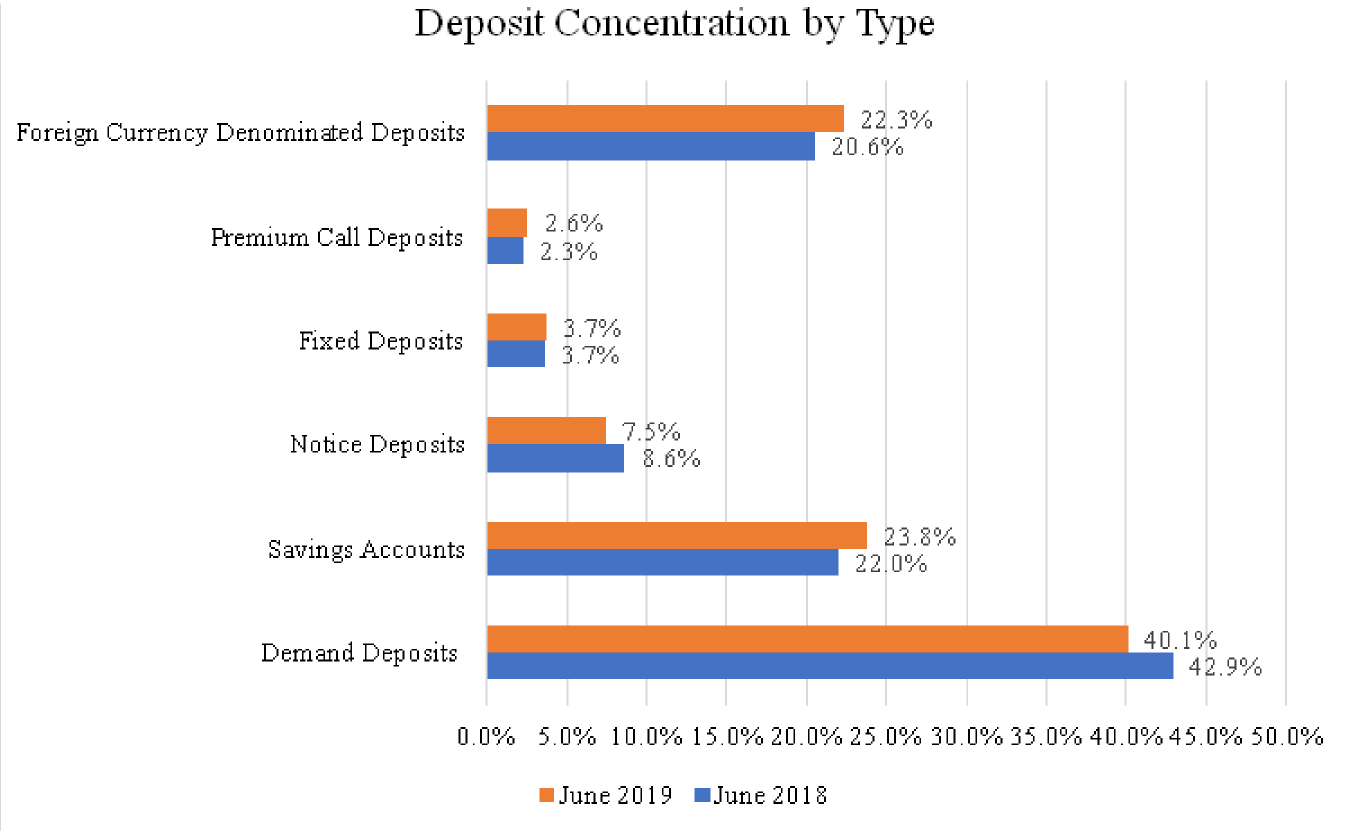
The Table below shows that the Liquidity ratios were within regulatory limit and risk appetite.

	Jun-2019	Jun-2018
Liquidity Ratio I	46.42%	61.99%
RBM Limit	25.00%	25.00%
NBM Limit	45.00%	45.00%
Liquidity Ratio II	45.37%	61.90%
RBM Limit	25.00%	20.00%
NBM Limit	35.00%	30.00%

5.3. Deposit Concentration Risk

In normal times, the deposit concentration may not pose a problem and instead prove to be profitable, but in unforeseen circumstances, sudden withdrawal of funds by the category of deposits can pose a serious challenge and, therefore expose the Bank to un-quantified risk.

The total deposits increased by 9.55% from K263.29bn to K288.44bn in June 2019. The deposits were largely made up of Demand Deposits (40.1%), Savings Accounts (23.8%), Foreign Currency Denominated Deposits 22.3% and the rest of the deposits accounted for 13.8% as depicted in the graph below;
The total Top 10 Deposits were at K35. 72bn.The ratio of Top 10 Depositors to total deposits



decreased from 14.59% to 12.38% as at 30th June 2019. The ratio was within the 25% threshold limit.

5.4. Liquidity Maturity Profiles

The Bank ensures adequate management of liquidity maturity mismatch which is a financial situation whereby assets held to meet future liabilities are not aligned in terms of maturity time. The Liquidity and Funds Management Policy provides guidance and mitigation strategies in case of a material maturity mismatch which could lead to liquidity squeeze. Below are the maturity profiles as at 30th June 2019;

	Up to 1 Month	1 - 3 Months	3 - 6 Months	6 - 12 Months	1 - 3 Years	3 - 6 Years	Over 6 Years	Total
Total Assets	92,524	20,693	34,257	62,605	58,921	85,640	21,922	376,562
Total Liabilities	248,814	64,337	1,410	2,142	16,392	-	209	333,305
Net Liquidity Gap	(156,291)	(43,645)	32,847	60,463	42,529	85,640	21,712	43,257

6. MARKET RISKS

6.1. Approach and Management of Market Risks

The Group separates its exposure to market risk between trading and non-trading portfolios. Basel II's market risk standardized approach has pre-specified and standardized methods for all the four types of risks covered: Interest rate risk, equity risk, exchange rate risk and commodity risk. The accord specifically states that eligible capital can only be calculated after the bank has calculated minimum capital requirement for credit risk and also operational risks then only can it be established how much Tier I and Tier II capital is available to support market risk. The Group's trading portfolios mainly are held by the TIBD, 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. TIBD 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.

6.2. Interest rate risk

The principal risk to which non-trading portfolio are exposed to is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments 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 TIBD in its day-today monitoring activities. The table below summarizes the exposure to interest rate risks. Included in the table are the Group's assets and liabilities at carrying amounts, categorized by earlier of contractual re-pricing or maturity dates. The Group does not bear an interest rate risk on off balance sheet items.

6.3. Foreign exchange risk

Foreign currency risk is the risk of the group's assets losing value as a result of movements in exchange rates that adversely impact the Malawi Kwacha value.

6.4. Market Risk Exposures

The total capital set aside for market risk under the Standardized Approach was as follows;

Capital Charge	June 2019 (K'm)	June 2018 (K'm)
Foreign Exchange Risk	93	16
Equity Risk	622	639
Total	**715**	**655**

The Bank has a comprehensive framework of limits that is used to control market risk exposures for different levels of reporting. The limits are reviewed at least annually or more frequently and adjusted when conditions of risk tolerances change. A summary of all breaches is reported to ALCO, ERCO and BRC.

7. 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 has an Operational Risk Management Framework that guides the management of operational risk.

7.1. Approach to Managing Operational Risk

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 Bank measures operational risk using the Basic Indicator Approach. In using this approach the Bank determines the gross income for 3 years and then multiplies it by a capital charge factor of 15% to determine the total operational risk capital charge

The total capital set aside for operational risk under the Basic Indicator Approach was as follows;

Capital Charge	June 2019 (K'm)	June 2018 (K'm)
Operational Risk	103,67	195,463

The capital charge increased by 8.6% as at 30th June 2019 as Gross Income for the review period generally increased at the same margin.

8. STRESS AND SCENARIO TESTING

8.1. Stress and Scenario Testing

The Bank has a comprehensive Stress and Scenario Testing Framework which is used, inter alia, to stress the base case projections and so assess the adequacy of the Bank's capital buffers and target ratios. The Bank conducts stress tests on a quarterly basis by applying various scenarios on its market risk exposures to ensure that the Bank is capable of withstanding any stressed conditions.

8.2. Stress frequency and scenarios

The Bank's stress and scenario testing recognizes and estimates the potential volatility of its capital requirements and the base-case (expected) three-year business plan projections, including the key assumptions and sensitivities contained therein, which themselves are subject to fluctuation, and ultimately the adequacy of the Bank's capital buffers and target capital ratios.

8.3. Mid-Year Stress Testing Results

Overall the Bank had a solid capital base during the year which was to sustain itself in a number of worst scenarios. Furthermore, overall the Bank improved in responding to a combination of macro-economic shocks during the year. On liquidity risk shocks, the Bank remained constant as it was able to survive for 3 days. The Bank continues to monitor the structure of the Assets and Liabilities to ensure minimal mismatch so as to improve the liquidity base and the number of days in which the Bank would be liquid in the event of a run on deposits.

Notwithstanding, the Bank was exposed to the impact of default of top five borrowers and increase in non-performing loans by sector which resulted in the ratios of regulatory requirement falling below the prescribed minimum. In order to manage capital risk, the Bank has embarked on implementation to Internal Rating Based (IRB) approach for credit risk. Implementation of this approach is expected to result in improvement in capital ratios and improvement in the quantum of credit extended to customers.

9. CONCLUSION

The Bank continues to closely monitor its core risks and ensure that they are properly mitigated. Supported by the sustained growth in retained earnings, exposures across risk types are generally assigned comfortable capital levels. Looking ahead, some fundamental changes that could potentially occur on the regulatory front over the course of the next few years would heighten prudential standards for capital requirements, leverage, liquidity and contingent capital applicable for the banking industry as a whole. Besides, the ramifications of the weakened economic and financial environments both domestically and internationally would invariably impact the market potential of banks over the foreseeable future.