# 2021

## Bank Gaborone Limited
Registration No. BW00000015806
Bank Gaborone Pillar 3 Disclosures
For the year ended 30 June 2021

Bank Gaborone
a member of **Capricorn Group**

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# Bank Gaborone Pillar 3 Disclosures
For the year ended 30 June 2021

## Introduction

"The Bank of Botswana Directive on Revised International Convergence of Capital Measurement and Capital Standards for Botswana (Basel II Guidelines) (hereinafter referred to as "the Standards") read in conjunction with Sections 13, 18 and 48 of the Banking Act (CAP 46:04) effective 1st January 2016, outlines the need for banks to have a Pillar III disclosure (Market Discipline).

Section 12.1 and 12.2 of the directive stipulate the objectives of this disclosure as shown below;

- *The Primary purpose of Pillar III is to supplement the minimum capital requirements (Pillar II) by introducing a set of disclosure requirements, which allow market participants to influence the level of capital, risk assessment processes, capital adequacy and remuneration practices of a bank.*

- *Improved transparency, underpinned by high quality and timely market disclosures, will enhance market discipline, efficiency and confidence. The key objective is, therefore, to provide a market driven incentive for a bank to conduct business in a safe and sound manner. A bank is, therefore, responsible, beyond the disclosure requirements set out in this Directive, for Conveying adequate information regarding its actual risk profile and how these risks relate to capital."*

## Governance

### Board Oversight
Bank Gaborone Limited "the bank" in recognition of the importance of risk in its operations has adopted the bank`s Risk Internal Control and Assurance Framework (GRICAF) – "the framework" that was implemented across the Capricorn Group of Companies. The board of directors of Bank Gaborone is ultimately accountable for the adequacy of the GRICAF.

The board discharges its responsibilities for risk management through the bank's governance structures (refer to the governance section and bank governance document) and specifically the Board Audit Committee and the Board Risk and Compliance Committee respectively. The board is assured of the adequacy of the GRICAF through the second and third lines of defense consisting of the Risk, Compliance and Internal Audit functions. In addition to the internal functions, the board draws on the perspectives of external auditors and regulators who conduct regular reviews of the bank. The board is satisfied that the GRICAF was adequate during the period under review.

### Risk Capacity, Appetite and Tolerance (RCAT)
The RCAT is used to set the bank's capacity, appetite and tolerance thresholds for risk. The RCAT collectively refers to qualitative and quantitative statements. The board sets qualitative risk appetite as well as quantitative risk capacity and appetite. The executive, through principal risk owners (PROs), sets quantitative tolerance limits for each of the principal risks. Quantitative measures include thresholds which, if breached, trigger a change in status that attracts a higher level of monitoring and action. The capacity and appetite statements are regularly reviewed and reported to the risk committee, executive management team and the board risk and compliance committee (BRCC).

## Risk Overview

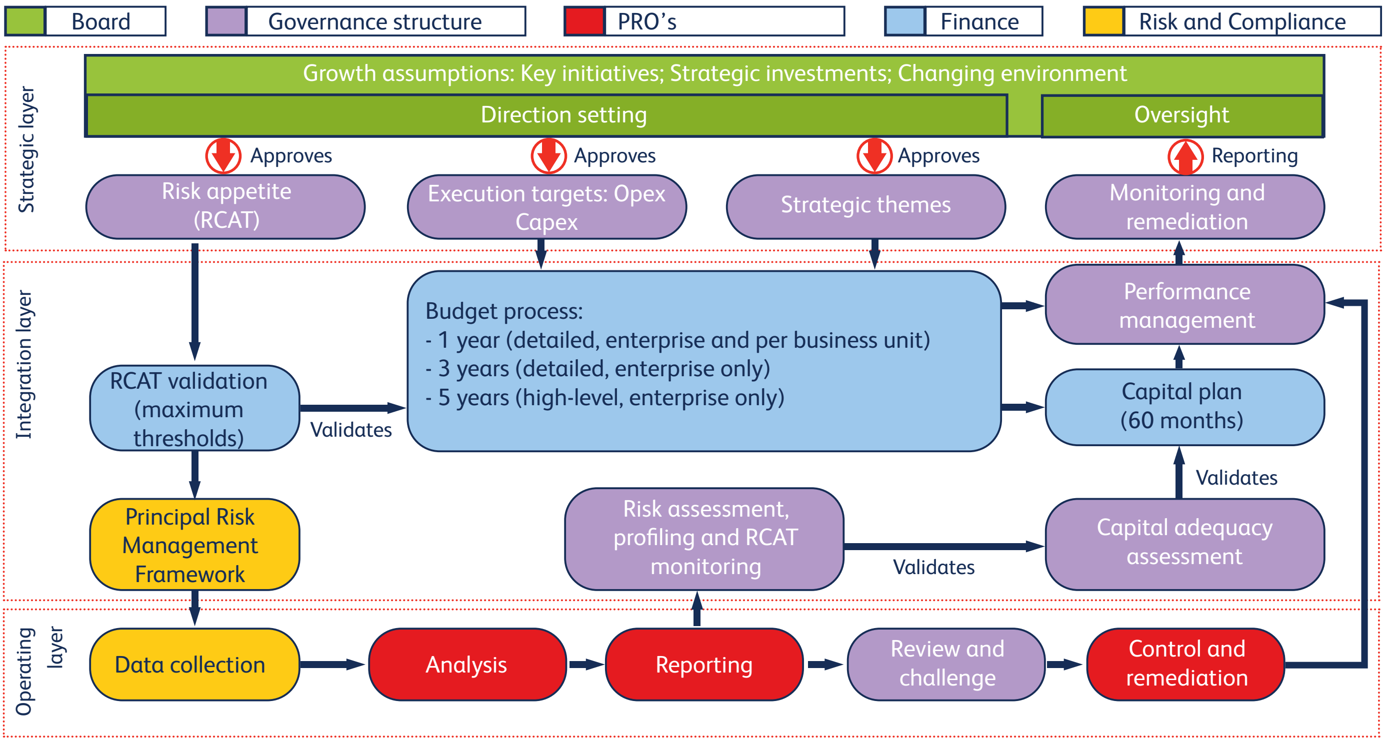
Bank Gaborone is a  financial services provider and it assumes risk exposure by the very nature of its business and its operations. The bank has identified 13 main risk categories. These risk categories have been defined as principal risks that are each managed according to a risk management framework. At a strategic level, risk management objectives are to:

- Optimise efficiency through effective use of risk resources in the bank.
- Directly contribute to the creation of end-customer value by eliminating unnecessary tasks in processes.
- Build standard risk management accountability, principles and processes into the business management process.
- Ensure risks are understood and pro-actively managed within the acceptable risk capacity, appetite and tolerance levels.

The bank maintains an effective risk, internal control and assurance framework based on the standard risk practices of the Committee of Sponsoring Organisations of the Treadway Commission (COSO) and Basel II, as set out below.

## Group Risk, Internal Control and Assurance Framework

**Integration of Strategic Planning, Risk Management and Capital Adequacy Assessment**




**RC: Regulatory Capital**

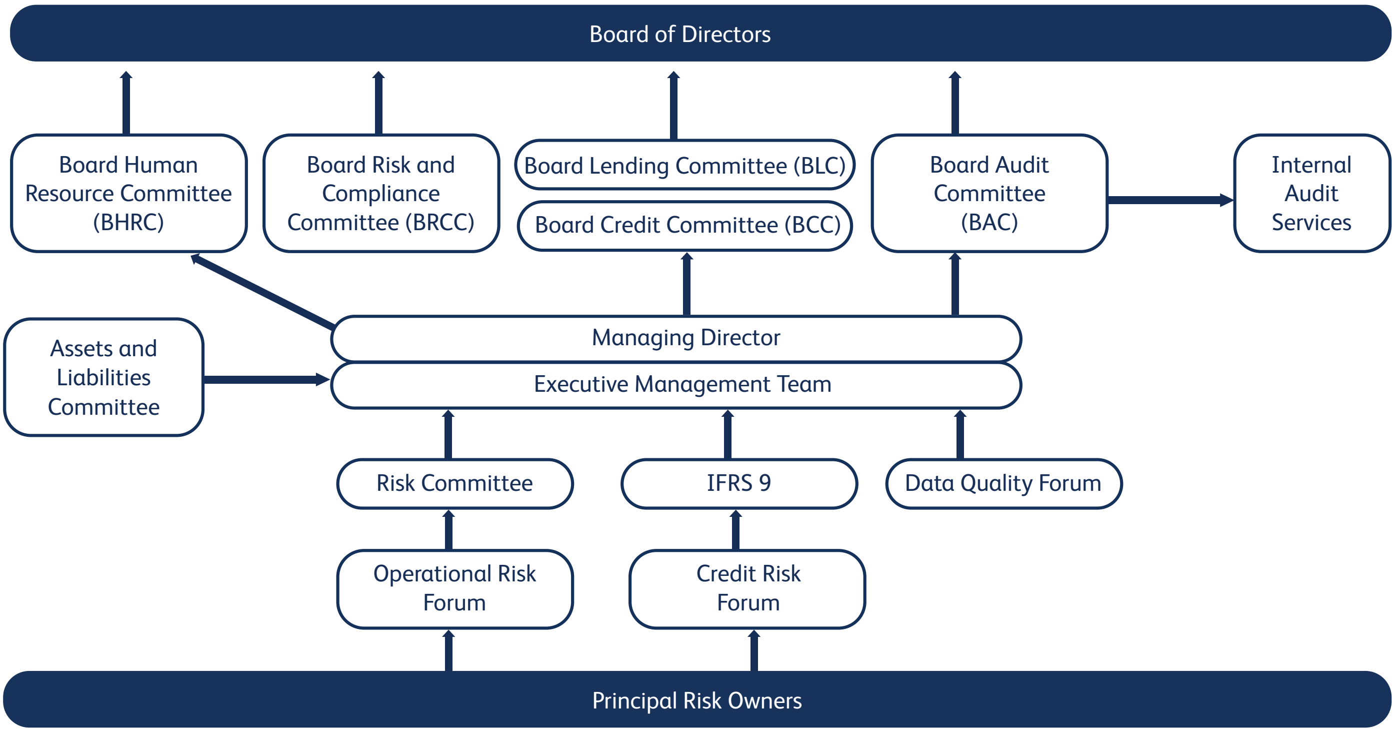
The bank has adopted standard practices for each of the principal risks. The standard practices of the GRICAF provide a common language and understanding of risk which allows the bank to standardise and aggregate risk managment and reporting which enables effective oversight by governance structures.

The board is ultimately accountable for effective risk management and responsibility is delegated to executive management to ensure that appropriate risk and control frameworks are designed and implemented. Each principal risk is assigned to an appropriate principal risk owner who is responsible for ensuring that an effective risk and control framework is designed, implemented and maintained for the principal risk. The principal risk owners are further responsible for the risk management frameworks within their respective business units, including their appropriateness, effectiveness and consistency. The bank's risk and compliance function is responsible for the overall infrastructure of the GRICAF and provides oversight and assurance in its second line of defense role.

**The 13 principal risks identified by the bank are as follows:**

1. Credit
2. Market
3. Liquidity
4. Operations
5. Capital
6. Strategy
7. Compliance
8. Technology
9. People
10. Finance and tax
11. Legal
12. Financial Crime
13. Reputation

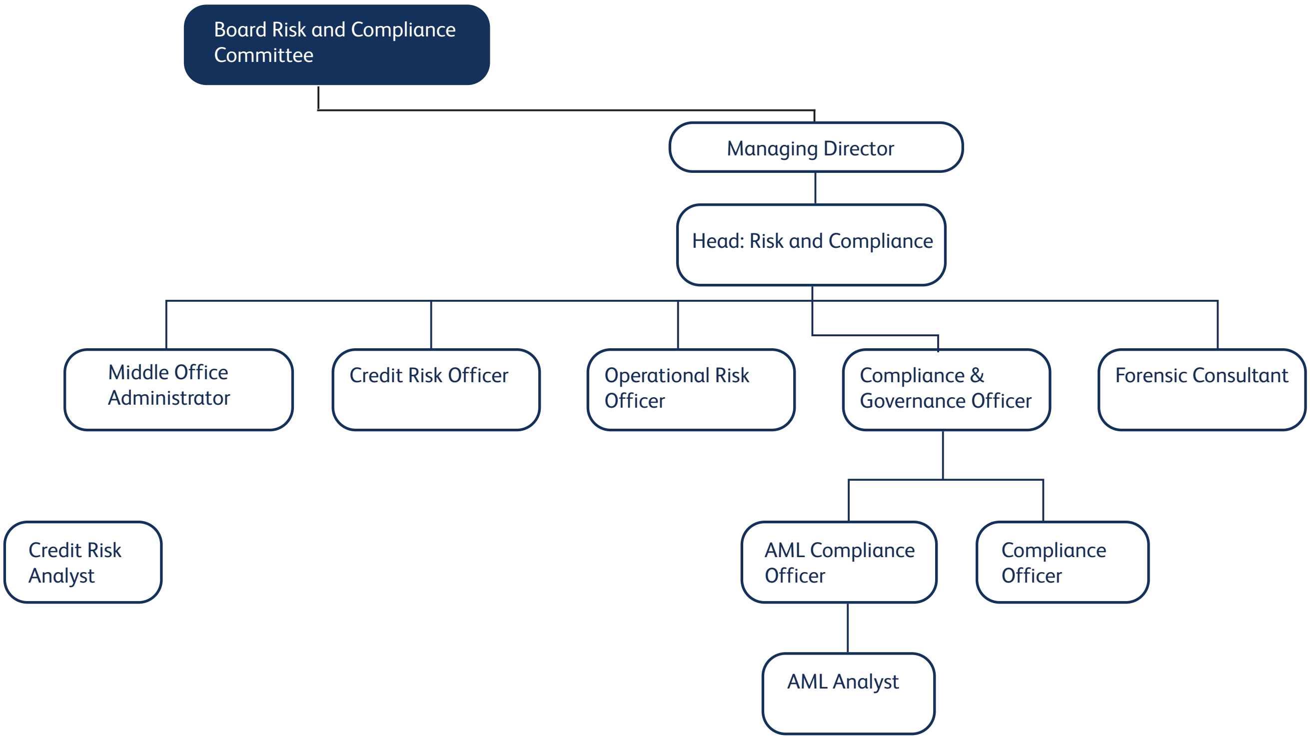
## The oversight structure of the bank is reflected below:




### Risk Management Function

The risk management function is headed by the Head: Risk and Compliance, who is a member of the executive management team. He/She has unrestricted access to the chairman of the Board Risk and Compliance Committee("BRCC"). The Compliance & Governance Officer is responsible for the practices which ensure compliance with the minimum requirements of the law and internal policy and is directly responsible for compliance to AML and sanctions. The Compliance & Governance Officer reports to the Head: Risk and Compliance.

The structure of a bank's risk management function is reflected below:



The bank has recognized that it is important that it sets out the outline within which risk management is conducted. Therefore, a Principal Risk Policy which is the overarching risk policy that sets out the identification of the "principal risks" that the banks faces was developed. A tabular summary of the scope of this policy are summarised below:

| | |
|---|---|
| **Direct** | 1. Understand the principal risks to achieve company strategy.<br>2. Define the risk system of control.<br>3. Set Risk Appetite.<br>4. Establish and communicate the risk and control framework, including accountabilities, responsibilities, authorities and key controls. |
| **Assess** | 1. Establish the process for identifying and analysing business-level risks and controls derived from the risk system of control through risk and control self-assessments (RCSAs).<br>2. Agree and implement measurement and reporting standards and methodologies.<br>3. Agree key risk indicators. |
| **Control** | 1. Set policies, tolerances, limits and authorities, monitor, and enforce.<br>2. Establish key control processes and practices, including limit structures, provisioning criteria and reporting requirements.<br>3. Monitor the operation of the controls and adherence to risk direction, tolerances and limits.<br>4. Provide early warning of limit or appetite breaches.<br>5. Ensure risk management practices and conditions are appropriate for the business environment. |
| **Report** | 1. Interpret and report on risk exposures, concentrations and risk-taking outcomes.<br>2. Interpret and report on sensitivities and key risk indicators.<br>3. Communicate with internal and external parties.<br>4. Contribute to principal risk profile reporting. |
| **Manage/ Challenge** | 1. Review and challenge all aspects of the company's risk profile and assessment of the adequacy of the risk and control framework.<br>2. Assess new risk-return opportunities.<br>3. Advise on optimizing the company's risk profile and risk framework.<br>4. Review and challenge risk management practices.<br>5. Oversee and challenge risk and control information. |

## Capital Risk

Capital risk is the risk that the bank is unable to meet its capital requirements and fund business expansion when needed. It includes the risk that regulatory requirements are not adhered to and the resultant costs of non-compliance, as well as the fact that insufficient capital will adversely affect the ability to raise funds.The bank appreciates that efficient capital management is critical to delivering on the bank's return on capital targets to ensure shareholders' expectations are met while making adequate capital available to support business growth. The impact of the trends on the various risk-weighted assets on capital are therefore assessed on a continuous basis.

## Capital Management Principles

Bank of Botswana requires each bank to hold the minimum level of the regulatory capital of P5 million, as well as to maintain the following capital adequacy ratios:

- Tier 1 and Tier 2 capital to risk weighted assets at a minimum of 12,5 %, referred to as capital adequacy ratio.
- Tier 2 capital to Tier 1 capital limited at a ratio of 50 % in the determination of capital adequacy.

The bank's regulatory (qualifying) capital is divided into two tiers:

- Tier 1 capital: stated capital and distributable reserves;
- Tier 2 capital: qualifying subordinated loan capital, collective impairment allowances and unrealised gains arising on the fair valuation of equity instruments held as available for sale.

The bank has adopted the standardized approach to Basel II effective from 1st January 2016, with risk-weighted assets being measured at three different levels: operational risk, market risk and credit risk. A summary of the banks capital elements, as well as the various risk weighted assets are discussed extensively in the following sections of this report.

In addition to the above minimum capital requirements, the Bank of Botswana requires the bank to perform an internal capital adequacy and assessment process (ICAAP) in terms of Pillar II of Basel II, which has been documented and approved by the board. The process results in:

- the identification of all significant risk exposures to the bank;
- the quantification of risk appetites for the major risks identified; and
- control measures to mitigate the major risks.

## ICAAP Process Flow

The ICAAP involves specific tasks and procedures that must be performed annually subsequent to the completion of the principal risk attestation process. The following table summarises the inputs and outputs of the ICAAP process:

| Input | Description | Source |
|---|---|---|
| Principal Risk Profile reports | Contains key information that describes the profile of every Principal Risk, including:<br>1. Overall Control Assessment<br>2. Risk and Control Self-Assessments<br>3. Key Risk Indicators<br>4. Risk and Loss Events<br>5. Risk Issue Tracking and Remediation<br>6. Waivers and Dispensations on policies and governance documents | Principal Risk Reporting process |
| Risk Capacity, Appetite and Thresholds Indicators | Details the status of key risk indicators that apply to the whole organisation and specific Principal Risks. This information assists PROs in assessing how well key risks are being managed. | Key Risk Indicator process |

## Outputs Generated by the ICAAP Process

| Output | Description | Frequency |
|---|---|---|
| ICAAP dashboard | This template summarizes the capital position for use in risk and business decision-making. | Annually |
| Annual ICAAP Report | The Annual ICAAP Report is submitted to BoB for purposes of the SREP review. The report is due no later than 31st December each year. | Annually |

**The table below summarises the composition of Bank Gaborone's regulatory capital for the year ended 30 June 2021.**

| | | |
|---|---|---|
| | **Common Equity Tier I capital: instruments and reserves** | |
| 1 | Directly issued qualifying common share (and equivalent for non-joint stock companies) capital plus related stock surplus. | 233,750 |
| 2 | Retained earnings | 225,447 |
| 3 | Accumulated other comprehensive income (and other reserves) | - |
| 4 | *Directly issued capital subject to phase out from CET1 CAPITAL (only applicable to non-joint stock companies)* | - |
| 5 | Common share capital issued by subsidiaries and held by third parties (amount allowed in bank CET1 CAPITAL) | - |
| 6 | **Common Equity Tier I capital before regulatory adjustments** | 459,197 |
| | **Common Equity Tier I capital: regulatory adjustments** | |
| 7 | Prudential valuation adjustments | - |
| 8 | Goodwill (net of related tax liability) | - |
| 9 | Other intangibles other than mortgage-servicing rights (net of related tax liability) | 4,316 |
| 10 | Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability) | - |
| 11 | Cash-flow hedge reserve | - |
| 12 | Shortfall of provisions to expected losses | - |
| 13 | Securitisation gain on sale (as set out in paragraph 562 of Basel II framework) | - |
| 14 | Gains and losses due to changes in own credit risk on fair valued liabilities | - |
| 15 | Defined-benefit pension fund net assets | - |
| 16 | Investments in own shares (if not already netted off paid-in capital on reported balance sheet) | - |
| 17 | Reciprocal cross-holdings in common equity | - |
| 18 | Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold) | - |
| 19 | Significant investments in the common stock of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold) | - |
| 20 | Mortgage servicing rights (amount above 10% threshold) | - |
| 21 | Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability) | - |
| 22 | Amount exceeding the 15% threshold | - |
| 23 | of which: significant investments in the common stock of financials | - |
| 24 | of which: mortgage servicing rights | - |
| 25 | of which: deferred tax assets arising from temporary differences | - |
| 26 | National specific regulatory adjustments | - |
| 27 | Regulatory adjustments applied to Common Equity Tier I due to insufficient Additional Tier I and Tier II to cover deductions | - |
| 28 | Total regulatory adjustments to Common equity Tier I | 4,316 |
| 28 (a) | **IFRS 9 Provisions Transitional Adjustments** | (19,970) |
| | a. Transitional Adjustment Amount Added Back to CET1 | 4,992 |
| 29 | **Common Equity Tier I capital (CET1 CAPITAL)** | **439,903** |
| | **Additional Tier I capital: instruments** | |
| 30 | Directly issued qualifying Additional Tier I instruments plus related stock surplus | - |
| 31 | of which: classified as equity under applicable accounting standards | - |
| 32 | of which: classified as liabilities under applicable accounting standards | - |
| 33 | *Directly issued capital instruments subject to phase out from Additional Tier I* | - |
| 34 | Additional Tier I instruments (and CET1 CAPITAL instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in bank AT1) | - |
| 35 | *of which: instruments issued by subsidiaries subject to phase out* | - |
| 36 | **Additional Tier I capital before regulatory adjustments** | - |
| | **Additional Tier I capital: regulatory adjustments** | |
| 37 | Investments in own Additional Tier I instruments | - |
| 38 | Reciprocal cross-holdings in Additional Tier I instruments | - |
| 39 | Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold) | - |
| 40 | Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions) | - |

| | | |
|---|---|---|
| 41 | National specific regulatory adjustments | - |
| 42 | Regulatory adjustments applied to Additional Tier I due to insufficient Tier II to cover deductions | - |
| 43 | Total regulatory adjustments to Additional Tier I capital | - |
| 44 | **Additional Tier I capital (AT1)** | - |
| 45 | **Tier I capital (T1 = CET1 CAPITAL + AT1)** | **439,903** |
| | **Tier II capital: instruments and provisions** | |
| 46 | Directly issued qualifying Tier II instruments plus related stock surplus | 266,000 |
| 47 | *Directly issued capital instruments subject to phase out from Tier II* | |
| 48 | Tier II instruments (and CET1 CAPITAL and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in bank Tier II) | - |
| 49 | of which: instruments issued by subsidiaries subject to phase out | - |
| 50 | Unpublished profits | 55,106 |
| 51 | Provisions | 58,921 |
| 52 | **Tier II capital before regulatory adjustments** | **380,027** |
| | **Tier II capital: regulatory adjustments** | P'000 |
| 53 | Investments in own Tier II instruments | - |
| 54 | Reciprocal cross-holdings in Tier II instruments | - |
| 55 | Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold). | - |
| 56 | Significant investments in the capital banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions). | - |
| 57 | National specific regulatory adjustments | - |
| 58 | **Total regulatory adjustments to Tier II capital** | - |
| 59 | **Tier II capital (T2)** | 380,027 |
| 60 | Total capital (TC = T1 + T2) | 819,930 |
| 61 | Total risk-weighted assets | 4,976,840 |
| | Capital ratios and buffers | |
| 62 | Common Equity Tier I (as a percentage of risk weighted assets) | 8.84% |
| 63 | *Tier I (as a percentage of risk-weighted assets)* | 8.84% |
| 64 | *Total capital (as a percentage of risk weighted assets)* | 16.47% |
| 65 | *Institution specific buffer requirement (minimum CET1 CAPITAL requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB buffer requirement, expressed as a percentage of risk weighted assets)* | - |
| 66 | *of which: capital conservation buffer requirement* | 2.5% |
| 67 | *of which: bank specific countercyclical buffer requirement* | - |
| 68 | *of which: G-SIB buffer requirement* | - |
| | Common Equity Tier I available to meet buffers (as a percentage of risk weighted assets) | |
| 69 | *National Common Equity Tier I minimum ratio (if different from Basel III minimum)* | 4.5% |
| 70 | *National Tier I minimum ratio (if different from Basel III minimum)* | 4.5% |
| 71 | *National total capital minimum ratio (if different from Basel III minimum)* | 12.5% |
| | Amounts below the thresholds for deduction (before risk-weighting) | |
| 72 | *Non-significant investments in the capital of other financials* | - |
| 73 | *Significant investments in the common stock of financials* | - |
| 74 | *Mortgage servicing rights (net of related tax liability)* | - |
| 75 | *Deferred tax assets arising from temporary differences (net of related tax liability)* | - |
| | Applicable caps on the inclusion of provisions in Tier II | |
| 76 | *Provisions eligible for inclusion in Tier II in respect of exposures subject to standardised approach (prior to application of cap)* | 58,921 |
| 77 | *Cap on inclusion of provisions in Tier II under standardised approach* | - |
| 78 | *Provisions eligible for inclusion in Tier II in respect of exposures subject to internal ratings-based approach (prior to application of cap)* | - |
| 79 | *Cap for inclusion of provisions in Tier II under internal ratings-based approach* | - |
| | Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2015 and 1 Jan 2020) | |
| 80 | *Current cap on CET1 CAPITAL instruments subject to phase out arrangements* | - |
| 81 | *Amount excluded from CET1 CAPITAL due to cap (excess over cap after redemptions and maturitie* | - |
| 82 | *Current cap on AT1 instruments subject to phase out arrangements* | - |
| 83 | *Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)* | - |
| 84 | *Current cap on T2 instruments subject to phase out arrangements* | - |
| 85 | *Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)* | - |

**Table 22 (c): Transitional Disclosures**

| | | a | b | c | d | e |
|---|---|---|---|---|---|---|
| | | June 21 | March 21 | Dec 20 | Sept 20 | June 20 |
| | **Available Capital (P'000)** | | | | | |
| 1 | Common Equity Tier 1 (CET1) | 459,197 | 419,847 | 416,047 | 372,216 | 372,216 |
| 1a | Fully loaded ECL accounting model | 439,903 | 405,014 | 400,596 | 356,270 | 358,971 |
| 2 | Tier 1 | 459,197 | 419,847 | 416,047 | 372,216 | 372,216 |
| 2a | Fully loaded ECL accounting model Tier 1 | 439,903 | 405,014 | 400,596 | 356,270 | 358,971 |
| 3 | Total capital | 839,224 | 719,980 | 710,242 | 694,728 | 629,705 |
| 3a | Fully loaded ECL accounting model total capital | 819,930 | 705,147 | 694,791 | 678,782 | 616,460 |
| | **Risk Weighted Asset (P'000)** | | | | | |
| 4 | Total risk-weighted assets (RWA) | 4,976,841 | 4,567,912 | 4,421,348 | 4,277,463 | 3,967,565 |
| 5 | Common Equity Tier 1 ratio | 9.23 % | 9.19 % | 9.40 % | 8.70 % | 9.38 % |
| 5a | Fully loaded ECL accounting model Common Equity Tier 1 | 8.84 % | 8.86 % | 9.06 % | 8.32 % | 9.04 % |
| 6 | Tier 1 ratio | 9.23 % | 9.19 % | 9.40 % | 8.70 % | 9.38 % |
| 6a | Fully loaded ECL accounting model Common Equity Tier 1 | 8.84 % | 8.86 % | 9.06 % | 8.32 % | 9.04 % |
| 7 | Total capital ratio | 16.86 % | 15.75 % | 16.06 % | 16.24 % | 15.87 % |
| 7a | Fully loaded ECL accounting model total capital ratio | 16.47 % | 15.44 % | 15.71 % | 15.86 % | 15.53 % |
| | **Additional CET1 buffer requirements as a percentage of RWA** | | | | | |
| 8 | Capital conservation buffer requirements (2.5 % from 2019) ( % ) | - | - | - | - | - |
| 9 | Countercyclical requirement ( % ) | - | - | - | - | - |
| 10 | Bank G-SIB and/or D-SIB additional requirements ( % ) | - | - | - | - | - |
| 11 | Total of bank CET1 specific buffer requirements ( % ) (row 8 + row 9 + row 10) | - | - | - | - | - |
| 12 | CET1 available after meeting the bank's minimum capital requirement (P'000) | - | - | - | - | - |

## 3.1 Qualitative Disclosures: Capital Ratios

For the Quarter Ended 30th June 2021, the bank's key capital ratios were above the minimum regulatory ratios. The ratio were as follows;

| Capital | Minimum prudential Ratio (Regulatory) | Reported Ratio |
|---|---|---|
| Common Equity Tier 1 Capital (CET 1) | 4.50 % | 8.84 % |
| Tier 1 | 7.50 % | 8.84 % |
| Total Unimpaired Capital (CAR) | 12.50 % | 16.47 % |

## 3.2 Quantitative Disclosures

Below is the breakdown of the bank's Risk Weighted Assets, followed by a detailed breakdown of the risk classes

| Risk Class | Methodology Used | Amount (P'000) |
|---|---|---|
| Credit Risk | Credit RWA (Simple Approach) | 4,713,703 |
| Market Risk | Market RWA | 11,424 |
| Operational Risk | Operational RWA (BIA) | 251,713 |
| **TOTAL RWA** | | **4,976,841** |

## Market Risk

Market risk is the exposure to adverse changes in the price or value of an instrument traded or held as an investment. Where market risk is a factor, and especially in volatile markets, the practice of marking to market on a regular basis is an important discipline.

From the above the following detailed risks arise:

- Interest rate risk: the risk of loss resulting from changes in interest rates, including changes in the shape of yield curves.
- Currency risk: also known as foreign exchange risk, which arises from fluctuations within the currency market.
- Basis risk: the change in price basis or spread between two rates or indices changes, e.g. the price of an asset does not change in the same manner as a change in a liability, or the spread between the funding and lending rate changes.

Market risks were actively monitored with emphasis on the impact of a stable interest rate cycle. The management of market risk will remain a key focus area given the probability of further decreasing interest rates, increased volatility in foreign currency markets and deterioration of the macroeconomic environment.

## Market Risk Management Process

Market risk is managed by closely monitoring the limits as set out in the Market Risk Framework. Models and stress tests are used to gain an increased understanding of the market risk environment. In addition, foreign exchange positions are managed via stop losses orders and closing or hedging out unwanted exposure via derivatives or in the spot market.

## Priorities for the next year

Explore and implement treasury and asset and liability management systems.

**The table below summarises the regulatory requirements for Bank Gaborone Limited's Market Risk Exposures for the year ended 30 June 2021:**

| | | |
|---|---|---|
| Interest Rate Risk | Risk weighted assets | - |
| | Capital required | |
| Foreign exchange risk | Risk weighted assets | 11,424 |
| | Capital required | 1,705 |

## Liquidity Risk

Liquidity risk is the risk that the bank will be unable to meet its obligations as they fall due. It is also the risk that the bank may not be able to liquidate assets quickly enough or without incurring excessive cost. Liquidity risk is inherent in the bank's business endeavours and represents its ability to fund increases in assets and meet its financial obligations, while complying with all statutory and regulatory requirements.

Against the backdrop of continuing challenges in the macroeconomic environment, the overall liquidity position remained well managed and met regulatory guidelines.

### Liquidity Risk Management Process

Liquidity risk is monitored and managed by means of a set of liquidity indicators and triggers that serve as early warning signs for effective liquidity management. The overall liquidity position is monitored and managed in conjunction with the funding action plan and ALCO strategies to ensure sound liquidity in the bank.

Liquidity risk is managed by monitoring various identified variables which include:

- the level of understanding of demand and supply for liquid assets;
- the level of adequacy and ability to access funding (established lines of funding) in a short period of time; and
- relationships with depositors.

**Priorities for the next year**

- Alternative sources of funding
- Improve concentration risk
- Build Stability and Cost Containment
- Entrench a liabilities driven culture

## Credit Risk

Credit risk is the risk of suffering financial loss, should any of the bank's customers, clients or market counterparties fail to fulfil their contractual obligations to the bank. Credit risk arises mainly from interbank, commercial and consumer loans and advances, and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as financial guarantees, letters of credit, endorsements and acceptances.

The bank is also exposed to other credit risks arising from investments in debt securities and other exposures arising from its trading activities ('trading exposures') including non-equity trading portfolio assets and derivatives as well as settlement balances with market counterparties and reverse repurchase agreements. Credit risk is the single largest risk for the bank 's business; management therefore carefully manages its exposure to credit risk and together with large exposures, is monitored by the BAC and BRCC.

## Credit Risk Highlights

Gross advances grew by 5.09 % to P5.0 billion compared to P4.6 billion recorded the previous financial year. NPLs as a percentage of gross loans and advances reduced slightly from 6.98 % recorded in June 2020 to 6.32 % recorded in June 2021. Provisions decreased by 6.74 % from P179.6 million in June 2020 to P167.5 million in 2021.

## Credit Risk Management Process

Credit risk remains well managed and within acceptable limits although the impact of the deterioration in the economic environment is evident in a slow increase in arrears and non-performing loans (NPLs). Credit risk is managed by monitoring the quality and concentration risk of the overall portfolio on an ongoing basis. Models and stress testing are used to enhance the understanding of the field and improve the management of the risks. Increased focus is placed on the loan application process to ensure responsible sustainable lending.On-going monitoring of loan performance is done to ensure effective quantification of credit risk exposure. Against the foregoing, loans and advances less than 90 days past due are not considered impaired, unless other information is available to indicate the contrary. Loans and advances less than 90 days past due are only considered impaired, if there is sufficient information available to indicate it. All loans past due more than 90 days are considered impaired.

The bank's loan book classification and provisioning methodology was effective 1 July 2018 with the adoption of IFRS 9 - Financial Instruments.

## Credit Risk Measurement Techniques

The bank has developed statistical models to support the quantification of credit risk. These quantitative models are in use for all key credit portfolios and form the basis for measuring default risks. In measuring the credit risk of loans and advances at a counterparty level, the bank considers three components, namely:

i. the 'probability of default' (PD) by the client or counterparty on its contractual obligations;
ii. current exposures to the counterparty and its likely future development, from which the bank derives the 'exposure at default' (EAD); and
iii. the expected loss on the defaulted obligations (the 'loss given default') (LGD). This is similar to the approach used for the purpose of measuring Expected Credit Loss (ECL) under IFRS 9.

These credit risk measurements, which reflect expected loss (the 'expected loss model'), are required by the Basel committee on banking regulations and the supervisory practices (the Basel committee) and are embedded in the bank's daily operational management.

### i. Probability Of Default (PD)

The probability of default is an indication of the probability that a given loan will default. Under Basel II and IFRS 9 the elements that make up a loss are defined as economic loss and will include direct and indirect costs associated with collecting on the exposure such as allocations of internal overheads and other non-cash costs. The PD in Basel II and IFRS 9 is calculated using historical data of defaults.

### ii. Exposure At Default (EAD)

The exposure at default under Basel II and IFRS 9 will take into account an expectation of future draw-downs until the default event has occurred by utilising loan run down for amortizing products and a credit conversion factor for non-amortizing products. For example, for a loan this is the face value at the default date. For a commitment, the bank includes any amount already drawn plus the further amount that may have been drawn by the time of default, should it occur.

### iii. Loss Given Default (LGD)

Loss given default or loss severity represents the bank's expectation of the extent of loss on a claim should default occur (1 - recovery rate). It is expressed as percentage loss per unit of exposure. It typically varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. The measurement of exposure at default and loss given default is based on the risk parameters standard under Basel II and IFRS 9.

**Financial assets measured at amortised cost**

Assets in this category mainly relate to investments in financial instruments that have an external credit rating. Implied probability of defaults have been benchmarked against published estimates by external credit rating agencies. LGD's were benchmarked against Basel best practice. The implied PD's and LGD's are used to calculate expected credit losses for these assets.

## Expected credit loss measurement

IFRS 9 outlines a 'three-stage' model for impairment based on changes on credit quality since initial recognition as summarised below:

- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the bank.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit impaired. Please refer to 'Significant increase in credit risk (SICR)' note for a description of how the bank determines when a significant increase in credit risk has occurred.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Please refer to the 'definition of default and credit-impaired assets' note for a description of how the bank defines credit-impaired and default.
- Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis. Please refer to 'Measuring ECL' note for a description of inputs, assumptions and estimation techniques used in measuring the ECL.
- A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should be carried forward-looking information. The 'Forward –looking information incorporated in the ECL models' note includes an explanation of how the bank has incorporated this in its ECL models.

Further explanation is also provided of how the bank determines appropriate groupings when ECL is measured on a collective basis (refer to 'Grouping of instruments for losses measured on a collective basis' note).

The following diagram summarises the impairment requirements under IFRS 9:

**Change in credit quality since initial recognition**

| Stage 1 | Stage 2 | Stage 3 |
|---|---|---|
| (Initial recognition) | (Significant increase in credit risk since initial recognition) | (Credit-impaired assets) |
| 12-month expected credit losses | Lifetime expected credit losses | Lifetime expected credit losses |

The key judgements and assumptions adopted by the bank in addressing the requirements of the standard are discussed below:

### Significant Increase in Credit Risk (SICR)

The bank considers a financial instrument to have experienced an increase in credit risk when one or more of the of the following quantitative, qualitative or backstop criteria have been met:

#### Quantitative criteria

Accounts are classified on a watch list when there is qualitative information available on the client's credit risk increasing. These accounts are moved over to stage 2.

- Repayment ability of clients
- Collateral valuations
- Sector in which the client operates
- Natural events (i.e. drought)
- Debtors not paying across industries

The criteria used to identify SICR are monitored and reviewed periodically for the appropriateness by the independent Credit Risk team. Once the above matters improved sufficiently, an account can be moved back to stage 1.

#### Backstop

A backstop is applied and the financial instruments considered to have experienced a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payments.

The bank has not used the low credit risk exemption for any financial instruments in the year ended 30 June 2021.

### Definition of default and credit-impaired assets

The bank defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

#### Quantitative criteria

The borrower is more than 90 days past due on its contractual payments.

#### Qualitative criteria

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. These are instances where:

- The borrower is in long-term forbearance
- The borrower is deceased
- The borrower is insolvent
- The borrower is in breach of financial covenants
- It is becoming probable that the borrower will enter bankruptcy

The criteria above have been applied to all financial instruments held by the bank and are consistent with the definition of default used for internal credit risk management purposes.

The bank estimates provisions for impairments for stage 3 (non-performing loans) on an individual loan basis. Each loan's impairment is calculated as exposure less discounted value of collateral held.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria and it is fully paid up for a consecutive period of six months. This period of six months has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions. This is in line with regulatory requirements. When an account has been fully paid up for six months it is moved back to stage 1.

## Measuring ECL-Explanation of inputs, assumptions and estimates on techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or Lifetime basis depending on whether a significant increase in credit has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default, defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation, either over the next 12 months, or over the remaining lifetime of the obligation.
- EAD is based on the amount the bank expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For a revolving commitment, the bank includes the current drawn balance plus any further amount that is to be expected to be drawn up to the current contractual limit by the time of default, should it occur.
- Loss Given Default (LGD) represents the bank's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival. This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

The Lifetime PD is developed by applying a maturity profile to the current 12 month PD. The maturity profile looks at how defaults develop on a portfolio from the point of observation throughout the remainder of the lifetime of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio segment. This is supported by historical analysis.

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- The PD represents the likelihood of a borrower defaulting on its financial obligation, either over the next 12 months, or over the remaining lifetime of the obligation.
- EAD is based on the amount the group expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For a revolving commitment, the group includes the current drawn balance plus any further amount that is to be expected to be drawn up to the current contractual limit by the time of default, should it occur.
- Loss Given Default (LGD) represents the group's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

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The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type.

- For amortisation products and bullet repayment loans, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis. This will also be adjusted for any expected overpayments made by the borrower. Early repayment/refinance assumptions are also incorporated into the calculation.
- For revolving products, the exposure at default is predicted by taking current drawn balance and adding a "credit conversion factor" which allows for the expected drawdown of the remaining limit by the time of default. These assumptions vary by product type and current limit utilisation band, based on analysis of the bank's recent default data.

The 12-month and lifetime LGDs are determined based on the factors which impact the recoveries made post default. These vary by product type. This is supported by historical analysis of recoveries per portfolio segment, including the discounting of the recoveries to the default date as well as the recovery costs accounted for.

The assumptions underlying the ECL calculation are monitored and reviewed on a quarterly basis.

There have been no significant changes in estimation techniques or significant assumptions made during the reporting period.

### Forward – looking information incorporated in the ECL models

The measurement of the expected credit loss (ECL) allowance for financial assets requires the use of significant assumptions about future.

A number of significant judgements are required in applying the accounting requirements for measuring ECL, including:

- Determining criteria for significant increase in credit risk (SICR);
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL.

The assessment and calculation of forward-looking information (FLI)
Stage 1 and 2

As at 30 June 2021, the bank has granted loan deferments to exposures of P272.1 million.

### The assessment and calculation of Forward-looking information (FLI)

The bank did not identify the deferral scheme as a SICR event, and have thus not reclassified any of the loans where deferrals had been allowed to Stage 2. No deferrals were granted on loans already included in Stage 2, as while not yet in default such loans had already displayed indications of increased credit risk and thus did not qualify for the deferral scheme.

The bank applied historical PDs to determine the likely defaults (before impact of FLI) for those loans categorised as Stage 1 and Stage 2 at 30 June 2021. Such historical PDs were derived from periods of “normal” economic cycles, and thus do not reflect the likely impact of the severe economic downturn expected because of the COVID-19 pandemic.

Accordingly, these historical PDs were scaled upwards through application of forecasted economic variables, regression analysis and expert judgement to determine an appropriate forward looking view for the ECL calculation. While such statistical inference was used as base, the unique confluence of circumstances facing the global, regional and domestic economies required the bank to supplement this through qualitative judgment and input in determination of reasonable ECL outcomes.

This forecasting process was reviewed and approved by the bank’s management and governance structures, including the Executive Management Team, Board Credit Committee, Board Audit Committee and ultimately the Board of Directors. In order to determine how the recoverability of the bank loans and advances is impacted through periods of stress, the bank performed historical analysis of PD performance for different products:

The bank used regression and time series analysis techniques to determine the relationship between the movements in certain macroeconomic variables such as Gross Domestic Product (GDP), Unemployment rates, inflation etc., and increases in observed PDs for all loan portfolios during the observed historical period.

The bank also considered qualitative factors, which indicate that mitigations instituted in the current period will assist in limiting such impact, including the following:

i. The government reduced bank rate and increased significantly government spending on infrastructure and similar investment to assist economic recovery. These are expected to be repeated through the Government Economic and Transformation Recovery Plan, budgeted at P20billion, combined with a recurring budget deficit of P20billion over the upcoming fiscal years (to be financed from existing resources and available funding lines).
ii. Government loan guarantee scheme for 24 months for a total of P1billion. Also Agricultural revitalization through National Development Bank.
iii. Citizen empowerment initiatives to bolster local industry, including revised Citizen Entrepreneurial Development Agency (CEDA) loan schemes.

Based on the bank's assessment, these additional factors will mitigate the stress for the current forecast period more towards that of the 2015 outcomes than the 2009 outcomes.

Accordingly, after considering all factors, in estimating the impact of the forecasted economic downturn due to COVID 19 on the bank loan book, a probability weighting of 50:50 was to stress sensitivities from the 2009 and 2015 economic contractions.

Having considered a number of reputable economic forecasts, the bank applied the following GDP assumptions for ensuing financial years to determine the scaling factors to be applied to historical PDs in determining the FLI overlay for Stage 1 and Stage 2 ECL:

| | 2021 | 2020 |
|---|---|---|
| Growth in the next 12 months | 5.54 % | (6.80 % ) |
| Growth in the following 12 months | 7.51 % | 5.4 % |

Using the PD scalars determined as explained above, the Stage 1 and Stage 2 ECL was increased by P22 million from that indicated by historical PD and expert judgement.

**Sensitivity analysis**

Expected credit losses calculated for stage 1 and 2 after applying the sensitivity factor above was as follows:

| | 2021 | 2020 |
|---|---|---|
| | P'000 | P'000 |
| Base ECL for stage 1 and 2 | 65,732 | 63,660 |

Had the GDP forecast been 10 % better or 10 % worse, the ECL for stage 1 and 2 would be reflected as follows:

| | 2021 | 2020 |
|---|---|---|
| | P'000 | P'000 |
| GDP 10 % improvement | 57,515 | 60,076 |
| GDP 10 % deterioration | 70,602 | 104,076 |

## Significant Increase in Credit Risk

Even though COVID-19 had a negative impact on all the economy, it did not impact all industries and all clients equally. For this reason, COVID-19 was not seen as an indicator of SICR for the entire loan book. Clients seeking financial relief were assessed on an individual basis to determine if an indicator of SICR was present.

For the sensitivity analysis on the SICR rules the quantitative SICR rules were adjusted. The SICR movements per scenario is shown below:

Base – 2 credit grades move downwards since origination
Lower – 3 credit grades move downwards since origination (less stringent)
Upper – 1 credit grade move downwards since origination (more stringent)

| | Allowances for credit losses | |
|---|---|---|
| **Sensitivity Analysis** | **2021** | **2020** |
| | **P'000** | **P'000** |
| ECL | 167,515 | 179,627 |
| **SICR rules** | | |
| Lower | 126,956 | 160,262 |
| Upper | 159,551 | 185,574 |

## Grouping of instruments for losses measured on a collective basis

For expected credit loss provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous.

In performing this grouping, there must be sufficient information for the group to be statistically credible. Where sufficient information is not available internally, the bank has considered benchmarking internal/external supplementary data to use for modelling purposes. The characteristics and any supplementary data used to determine groupings are outlined below:

- Product type
- Repayment type
- Collateral type

The groupings above only apply to stage 1 and stage 2 credit impairments. All stage 3 exposures are assessed individually. The appropriateness of groupings is monitored and reviewed on a periodic basis.

## Credit risk (continued)

### Loss allowance

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period

The following table explain the changes in the loss allowance between the beginning and the end of the annual period due to these factors:

| As at 30 June 2021 | Opening ECL 1 July 2020 | Total transfer from prior year staff impairment | Total transfer between stages | Net impairments raised | Impaired accounts written off | Exchange and other movements | Closing ECL 30 June 2021 |
|---|---|---|---|---|---|---|---|
| **Overdrafts** | **11,014** | **-** | **-** | **12,894** | **(986)** | **(1,671)** | **21,251** |
| Stage 1 | 10,891 | - | (386) | 247 | - | (2,864) | 7,888 |
| Stage 2 | 631 | - | 246 | 2,417 | - | (12) | 3,282 |
| Stage 3 | (508) | - | 140 | 10,230 | (986) | 1,205 | 10,081 |
| **Term loans** | **122,009** | **-** | **-** | **16,482** | **(46,419)** | **(3,595)** | **88,477** |
| Stage 1 | 34,305 | - | 254 | (3,909) | - | (2,434) | 28,216 |
| Stage 2 | 4,518 | - | (1,640) | 7,013 | - | (263) | 9,628 |
| Stage 3 | 83,186 | - | 1,386 | 13,378 | (46,419) | (898) | 50,633 |
| **Mortgages** | **29,081** | **-** | **-** | **12,380** | **(4,108)** | **1,317** | **38,670** |
| Stage 1 | 2,526 | - | 225 | 744 | - | 888 | 4,383 |
| Stage 2 | 1 | - | (522) | 1,548 | - | 65 | 1,092 |
| Stage 3 | 26,554 | - | 297 | 10,088 | (4,108) | 364 | 33,195 |
| **Instalment finance** | **17,524** | **-** | **-** | **1,966** | **(3,716)** | **3,343** | **19,117** |
| Stage 1 | 10,354 | - | (355) | (578) | 0 | 521 | 9,942 |
| Stage 2 | 434 | - | 48 | 883 | 0 | (64) | 1,301 |
| Stage 3 | 6,736 | - | 307 | 1,661 | (3,716) | 2,886 | 7,874 |
| **Total loans and advances** | **179,628** | **-** | **-** | **43,722** | **(55,229)** | **(606)** | **167,515** |

| As at 30 June 2020 | Opening ECL 1 July 2019 | Total transfer from prior year staff impairment | Total transfer between stages | Net impairments raised | Impaired accounts written off | Exchange and other movements | Closing ECL 30 June 2020 |
|---|---|---|---|---|---|---|---|
| **Overdrafts** | **5,308** | **-** | **1,541** | **(291)** | **(510)** | **4,966** | **11,014** |
| Stage 1 | 4,675 | - | (1) | 3,484 | 0 | 2,733 | 10,891 |
| Stage 2 | 633 | - | 42 | (60) | (2) | 18 | 631 |
| Stage 3 | - | - | 1,500 | (3,715) | (508) | 2,215 | (508) |
| Term loans | 93,949 | 19 | 15,058 | 10,961 | (5,138) | 7,160 | 122,009 |
| Stage 1 | 19,250 | 19 | (553) | 9,704 | 373 | 5,512 | 34,305 |
| Stage 2 | 6,241 | - | 1,618 | (3,951) | 360 | 250 | 4,518 |
| Stage 3 | 68,458 | - | 13,993 | 5,208 | (5,871) | 1,398 | 83,186 |
| Mortgages | 14,720 | 342 | 844 | 10,676 | (220) | 2,719 | 29,081 |
| Stage 1 | (1,395) | 342 | (348) | 3,420 | - | 507 | 2,526 |
| Stage 2 | 1,348 | - | (260) | (1,103) | - | 16 | 1 |
| Stage 3 | 14,767 | - | 1,452 | 8,359 | (220) | 2,196 | 26,554 |
| Instalment finance | 12,039 | 46 | 757 | 5,986 | (1,117) | (187) | 17,524 |
| Stage 1 | 6,104 | 46 | (190) | 4,777 | 1 | (384) | 10,354 |
| Stage 2 | 747 | - | (6) | (306) | (1) | 0 | 434 |
| Stage 3 | 5,188 | - | 953 | 1,515 | (1,117) | 197 | 6,736 |
| **Total loans and advances** | **126,016** | **407** | **18,200** | **27,332** | **(6,985)** | **14,658** | **179,628** |
| Other financial instruments | - | - | - | - | - | - | - |
| Stage 1 | - | - | - | - | - | - | - |
| Stage 2 | - | - | - | - | - | - | - |
| **Total** | **126,016** | **407** | **18,200** | **27,332** | **(6,985)** | **14,658** | **179,628** |

## Maximum exposure to credit risk before collateral held or other credit enhancements-All Financial instruments

| | 2021 | 2020 |
|---|---|---|
| | P'000 | P'000 |
| *Credit risk exposures relating to on-statement-of-financial-position assets are as follows:* | | |
| Cash and balances with the central bank | 75,617 | 59,223 |
| Bank of Botswana Certificates | 229,954 | 171,857 |
| Investment in equity instruments | 3,962 | 3,037 |
| Due from other banks and other financial institutions | 1,470,315 | 1,237,091 |
| Gross loans and advances to customers* | 4,991,037 | 4,749,198 |
| Other assets | 59,717 | 49,194 |
| **Total on-statement of financial position exposure** | **6,830,602** | **6,269,600** |

**Credit risk exposure relating to off-statement-of-financial-position items are as follows:**

| | 2021 | 2020 |
|---|---|---|
| | P'000 | P'000 |
| Liabilities under guarantee | 188,772 | 137,958 |
| Loan commitments | 86,292 | 64,667 |
| **Total off-statement-of-financial position exposure** | **275,064** | **202,625** |
| **Total credit risk exposure** | **7,105,666** | **6,472,225** |

*Excluded the impact of interest in suspense and the IFRS 9 effective interest rate.

The above table represents a worst case scenario of credit risk exposure to the bank at 30 June 2021 and 2020, without taking account of any collateral held or other credit enhancements attached. For all assets listed on the statement of financial position, the exposures set out above are based on carrying amounts as reported.

The most significant exposures are derived from loans and advances to customers.

Management is confident in its ability to continue to control and sustain minimal exposure of credit risk to the bank resulting from both its loans and advances portfolio and other securities based on the following:

- The bank employs a range of policies and practices to mitigate credit risk.
- Mortgage loans and Commercial loans, which represent the biggest group in the loans and advances to customers portfolio, are backed by collateral.
- All financial assets, other than special mention and non-performing loans and advances, are neither past due nor impaired.

## Maximum exposure to credit risk - Financial instruments subject to impairment

The following table contains an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount of financial assets below also represents the bank's maximum exposure to credit risk on these assets.

| As at 30 June 2021<br>All products | Stage 1<br>12-month<br>ECL | Stage 2<br>Lifetime ECL | Stage 3<br>Lifetime ECL | Total |
|---|---|---|---|---|
| **Loans and advances** | **P'000** | **P'000** | **P'000** | **P'000** |
| **Credit grade** | | | | |
| Not rated | 50,427 | 15,305 | 101,783 | 167,515 |
| Gross carrying amount* | 4,549,977 | 125,518 | 315,542 | 4,991,037 |
| Loss allowances | (50,427) | (15,305) | (101,783) | (167,515) |
| **Carrying amount** | **4,499,550** | **110,213** | **213,759** | **4,823,522** |
| Other Financial instruments | | | | |
| Credit grade | | | | |
| Non-rated | - | - | - | - |
| Gross carrying amount* | 1,818,775 | - | - | 1,818,775 |
| **Carrying amount** | **1,818,775** | **-** | **-** | **1,818,775** |

| As at 30 June 2020<br>All products | Stage 1<br>12-month<br>ECL | Stage 2<br>Lifetime ECL | Stage 3<br>Lifetime ECL | Total |
|---|---|---|---|---|
| **Loans and advances** | **P'000** | **P'000** | **P'000** | **P'000** |
| **Credit grade** | | | | |
| Not rated | 58,076 | 5,584 | 115,968 | 179,628 |
| Gross carrying amount* | 4,373,251 | 44,379 | 331,569 | 4,749,199 |
| Loss allowances | (58,076) | (5,584) | (115,968) | (179,628) |
| **Carrying amount** | **4,315,175** | **38,795** | **215,601** | **4,569,571** |

*Excludes the impact of interest in suspense and the IFRS 9 effective interest rate adjust

| | | | | |
|---|---|---|---|---|
| **Other Financial instruments** | | | | |
| **Credit grade** | | | | |
| Non-rated | - | - | - | - |
| Gross carrying amount* | 1,517,185 | - | - | 1,517,185 |
| **Carrying amount** | **1,517,185** | **-** | **-** | **1,517,185** |

### Credit risk weighting for Regulatory Purposes

Bank Gaborone employs the standardised approach to quantify credit risk. Under this approach, the banks are required to use ratings from External Credit Rating Agencies to quantify required capital for credit risk. Fitch ratings are utilised as far as possible. If Fitch ratings are not available, Moody and Standard & Poor's ratings are used for classification. If there are no ratings available, these exposures are classified as unrated. The bank applies credit ratings in 'Country Risk Management' to reflect the credit risk of financial instruments. External credit ratings for agencies are utilised for cross-border exposures, this is augmented with thorough internal credit and financial analyses in the determination and setting of exposure limits. Distinction between two broad credit quality classes is made, i.e. investment grade (AAA to BBB) and speculative / high-yield (BB and lower). For the period under review most of the bank's exposures were unrated, however, external credit ratings were employed for balances with foreign banks and asset managers.

The table below summarises the banks credit exposures subject to the standardised approach:

| Counterparties | Exposure P'000 | Impairment P'000 | Risk-weighted amounts | Write Offs |
|---|---|---|---|---|
| Sovereign and Central Bank | 378,009 | - | - | - |
| Security Firms | 8,696 | - | 8,696 | - |
| Banks | 695,673 | - | 430,251 | - |
| Corporate | 1,637,640 | 15,922 | 1,634,778 | 1,315 |
| Retail | 1,365,934 | 55,131 | 1,017,343 | 49,806 |
| Residential mortgage properties | 849,394 | 18,727 | 347,807 | 1,725 |
| Commercial Real Estate | 1,068,476 | 12,003 | 1,138,703 | 2,383 |
| Others | 839,545 | - | 89,444 | - |
| **Total** | **6,843,367** | **101,783** | **4,667,022** | **55,229** |

### Priorities for the next year

- Specific focus will be placed on the modelling and methodology for implementing the impairment calculations for IFRS 9.
- Improvement in the collection processes and arrears management processes.
- Selective lending with a view to managing non - performing loans and controlling exposures to certain sectors.

### Operational Risk

Operational Risk is the risk of the bank suffering financial losses directly or indirectly due to failed internal processes or systems, human error or from external events. This includes the following non-financial principal risks:

- Compliance risk – The risk of failure to comply with applicable rules and regulations, and in so doing, exposing the bank to penalties and reputation damage. Penalties received or due to non-compliance is an example of this risk.
- Operations risk – The risk of failure to deliver the intended outcome with respect to customers, products and services, facilities, data, processes, business continuity, physical cash management, payment management and change execution and delivery. Data entry, maintenance or loading errors that result in data quality issues, is an example of this risk.
- Technology risk – The risk that the strategic technology investment is not aligned to the bank's vision or business strategy, or catastrophic failure of technology to deliver secure IT services which provide critical business services. System break-downs or systems being offline are an example of this risk.
- People risk – The risk of failure to achieve the bank's business objectives through problems which may arise from people-related issues. Misuse of confidential information is an example of this risk.
- Finance and tax risk – The risk of failure to monitor and report on statutory financial requirements in line with the bank's requirements. The restatement of the annual financial statements is an example of this risk.
- Legal risk – The risk of exposure due to a failure to conduct business in accordance with laws or contractual obligations. Planned and potential litigation is an example of this risk.
- Financial crime risk – The risk of fraud or dishonesty, misconduct or misuse of information relating to a financial market, handling the proceeds of crime or the financing of terrorism. Financial crimes may involve fraud (cheque fraud or credit card fraud), theft, scams or confidence tricks, tax evasion, bribery, embezzlement, identity theft, forgery and counterfeiting, computer crime, phishing, burglary and armed robbery. Phishing attacks are an example of this risk.
- Reputation risk – This is mainly a consequence of the realisation of other risks and is the risk of failure to understand, identify or manage events that impact negatively on the bank's reputation. Loss of customers and revenue due to negative publicity is an example of this risk.

## Operational Risk Management Framework

The bank has adopted the standardised approach to operational risk management under Basel II as the foundation for its operational risk management framework. Operational risk is managed through the Operational Risk Management Framework, read in conjuction with the Bank of Botswana Guidelines on Risk Management (issued May 2018) . Within the framework qualitative and quantitative tools are applied to identify and assess operational risks, as well as managing the mitigation of identified control weaknesses. The prime responsibility for the management of operational risk rests with the management of business units where the risk arises.

The operational risk management framework establishes the operational infrastructure that enables Principal Risk Owners (PROs) to collect, interpret and act on risk information, thereby discharging their responsibilities in terms of the GRICAF. The components of the operational risk management framework are:

## Risk and Control Self-Assessments (RCSAS)

As part of the systems of control developed for every principal risk, a number of key internal controls are identified and documented. The aim of the RCSA process is for management to assess the design and operation of these controls to determine if they are functioning effectively or not and to perform semi-annual risk attestations. For an internal control to be effective, evidence must exist that supports this conclusion.

### Key Risk Indicators (KRIs)

KRIs are quantitative measurements specifically used for the following:

- Measurement of risk exposure (via the RCAT statement and thresholds); and
- Assessing the effectiveness of internal controls.

### Risk Incident and Loss Event Reporting

Losses and risk incidents are included in monthly risk reports through the collection of information from business units. The bank has built up an internal database of risk incidents and losses stretching over more than eight years. The data is used for trend analysis, risk modelling and capital adequacy assessment.

## Risk Issue Remediation and Closure Process

The process consists of recording, tracking and reporting on the bank's performance in terms of resolving risk issues raised by risk service providers such as internal and external audit, management assurance services and regulators.

### Priorities for the next year

- Enhancing the existing operational risk management infrastructure to support the bank's strategy.
- Embedding of new procedures for enhanced risk assessment of new products or material changes to existing products.
- Embedding the bank's intergrated Governance, Risk and Compliance system that was implemented in the previous financial year.

## Financial Crime

The bank makes use of a full time forensic function with qualified staff to monitor, investigate and report on financial crime.

### Factors that influenced Financial crime risk

The frequency and sophistication of cyber related fraud were addressed with the introduction of EMV compliant chip cards, improved proactive fraud monitoring and increased fraud awareness.

### Priorities for the next year

Continued focus on preventative and pro-active fraud risk management. This includes internal and external fraud awareness.

## Compliance Risk Management

As a leading financial services bank, the bank faces complex challenges to ensure that its activities comply with local legislation, regulations and supervisory requirements and relevant international standards and requirements.

The compliance function identifies, assesses, advises, monitors and reports on the compliance risk and governance of the bank and its subsidiaries, as well as legal risk in terms of the potential impact of changes in laws and regulations. The management of compliance risk forms part of the GRICAF.

The compliance function consists of general compliance, compliance monitoring,corporate governance and money laundering compliance. The methodology followed by the compliance function has been developed and benchmarked against the standards prescribed by the Compliance Institute Southern Africa.

### Key activities undertaken by general compliance

The key activities undertaken by general compliance to support the directors, executive officers, management and employees in discharging the relevant compliance responsibilities include the following:

- **Compliance risk management framework** – The framework sets out the minimum requirements for the management and control of compliance risk at different levels within the bank.
- **Compliance risk identification, assessment and prioritisation** – Compliance risks, once assessed, are consolidated into a compliance risk profile known as the Compliance Universe. Given that the bank is a dynamic corporate entity and that the regulatory landscape is evolving and becoming increasingly stringent, the regulatory risk profile is reviewed and updated at least annually or as and when new regulatory requirements are introduced, to ensure any possible risk of non-compliance with applicable laws, regulations and supervisory requirements are addressed.
- **Compliance risk management plans (CRMPs)** – The CRMPs serve as a management tool, outlining the compliance risks that the business units or support functions are exposed to and controls that are implemented to manage and mitigate those risks. These plans have been developed and are updated on an ongoing basis or as and when compliance risk changes or when new regulation or legislation is introduced.
- **Compliance risk monitoring** – Monitoring of compliance risk is currently only conducted for CRMP's implemented for high risk requirements. During the financial year there were no financial penalties, or public reprimands imposed on the bank.
- **Compliance risk reporting** – Compliance reports are submitted to governance committees attended by directors, executive officers and management. Compliance awareness is also an important component of compliance risk reporting.

### Key activities undertaken by money laundering compliance

The key activities undertaken by money laundering compliance are to support the directors, executive officers, management and employees in discharging their responsibilities in respect of the risk of money laundering and terrorist financing including the following:

- **Governance and oversight** – Money laundering compliance sets policies and provides guidance and training relating to anti-money laundering and anti-terrorist financing regulatory requirements.
- **Regulatory or policy breaches** – Money laundering compliance reports any breaches to the various governance forums and, if required, to the regulators.
- **Automated money laundering prevention solution** – The bank's automated money laundering prevention solution provides a mechanism to efficiently counter money laundering risks and events.
- **Sanctions screening** – The bank has key controls and procedures in place to conduct sanctions screening and minimum screening standards are maintained by the compliance function who are ultimately responsible for money laundering compliance.
- **Training** – The bank has developed and maintains ongoing training programmes for employees on money laundering, combating of terrorist financing activities and sanctions laws.

### Factors that influenced Compliance risk

Human error and non-compliance with policies and procedures were addressed with increased compliance awareness.

New legislation and ammendments to existing legislation as well as goAML compliance

### Priorities for the next year

- Establishing a compliance risk monitoring capability to effectively report on the results of compliance risk monitoring with the aim of ensuring the quick and effective resolution of regulatory issues.
- Incorporating an ethics component into the compliance risk management framework.
- Conducting an external health check on the money laundering compliance structure and processes.
- Increase integration and interaction between the various enterprise risk management capabilities in order to ensure a comprehensive overall risk capability.

## Human Capital Management

Human capital remains a very important source of the Bank' sustainable competitive advantage. The remuneration and reward system therefore plays a critical role in attracting, motivating and retaining high-performing employees who can contribute to sustained business growth. The bank recognizes individual ability and effort and to provide all the support needed to keep employees motivated to deliver excellent performance while under-achievements are managed through the Performance Improvement Programme, remuneration is fully integrated into other management processes, such as the performance management process, and the overall Banks Human Resources policies. The policies aim to ensure that individuals with the necessary skills and competencies are attracted and retained by the Bank , as well as create fair and equitable practices in terms of employee remuneration. Bank Gaborone continues to ensure that our remuneration practices and policies adhere to global best practice and align executive interest strongly to those of our shareholders.

Bank Gaborone just as other Capricorn Group entities, utilizes PricewaterhouseCoopers through RemChannels annually to review and advise the bank on remuneration. Particular attention is paid to the setting of the performance conditions for the long-term incentives and, consistent with the previous year, we have taken the decision to disclose the performance conditions in this report. We have seen, after the introduction of our new 5Cs performance development methodology, has added stretch management, which required strong company performance to unlock rewards for participants.

The following roles are considered as Material Risk Takers i.e. the employees in these roles can make decisions that can affect the Bank's financials; Managing Director, Chief Financial Officer, Treasurer and Head: Credit. Other Executive Management Team Members who also take decisions that affect the Bank's operations are Head: Retail Banking, Head: Wholesale Banking, Head: Risk & Compliance, Head: Human Resources, Head: Brand and Communications and Chief Operating Officer.

All Bank employees are required to adhere to a strict Group Ethics and Conduct Policy that guides employee behavior and as our operations are prone to bribery; there is no differentiation between categories of employees, e.g. Risk and Compliance, on salaries to ensure employees do not succumb to unethical conduct. We believe our remuneration is competitive and as such expect all employees to serve at the highest levels of ethical conduct required of them. For the past year, we experienced no major fraud cases.

Consistent with previous years, we strive for appropriate transparency of our executive remuneration policies and practices and again present a two-part report. The two-part report contains our forward-looking remuneration policy in the first section and the actual implementation of our policy for the year under review in the second section. This allows shareholders to observe the manner in which our stated policies translate into actual outcomes for senior management and executives.

**Governance of Remuneration**

The Capricorn group has a centralized board remuneration committee (Remco) which governs remuneration. Executive directors attend committee meetings by invitation, but are requested to recuse themselves when matters are discussed that concern them. Local matters are governed by the Board Human Resources Committee, which is mandated to oversee and decide on the appointment, remuneration, promotion, benefits, terms, conditions, succession and performance of employees other than directors and executive officers of Bank Gaborone. The Committee is responsible for policy formulation and review and approval of the remuneration philosophy, principles and policy and the broad framework of remuneration. As at June 30, 2021, the committee composed: M Mothibatsela (Chairperson), M. Chilisa (Member), S Coetzee (Member) . The committee met 4 times in the year under review and they were compensated for this function.

**The key activities and recommendations of the committee with regard to remuneration during 2021 included the:**

- approval of changes in Remuneration Policies
- benchmarking of employees total reward packages with other organisation using REMChannel
- benchmarking of employee remuneration packages and the recommendation to the main board and shareholders
- consideration of annual total guaranteed pay increases
- approval of short-and long-term incentive allocations
- approval of Job Grades Audit Outcome

**Remuneration philosophy and policy**

The bank's remuneration philosophy aims to ensure that all employees are rewarded fairly and appropriately for their contribution. In setting remuneration levels, the human resources and remuneration committees consider appropriate market benchmarks, while ensuring sufficient emphasis is placed on pay for performance. This approach helps to attract, engage, retain and motivate key employees while ensuring their behavior remains consistent with the bank's values. The guiding principles for managing remuneration are as follows:

- **Total rewards mindset** – Reward is viewed in a holistic manner comprising a range of monetary (fixed and variable) and non-monetary components.
- **Performance differentiation** – There is strong differentiation based on performance, particularly for senior, specialist and leadership roles where line of sight to strategic choices are evident.
- **Manager discretion** – Management discretion is central to Bank Gaborone's remuneration philosophy and is based on the requirement that reward must always be based on merit.
- **Variable pay component** – The variable pay component of total reward increases with seniority (organisational level), as the ability to impact business results increases.
- **Performance aligned with strategy** – Performance is the cornerstone of reward practices and there is clear differentiation between performers and non-performers.
- **Risk containment** – Reward plans are structured to mitigate against excessive risk-taking.
- **Consistency** – The reward philosophy strives to be both consistent and transparent. Benchmarking is performed annually using consistent and recognised methodologies.
- **Attraction and retention** – The focus is on competitive remuneration practices that attract, engage and retain talent to deliver on the business strategy.

The bottom line of our remuneration philosophy is to reward performance. Annually, the Bank awards management discretionary bonuses and salary increments to employees who have at least met the expectations of their jobs and display behaviors that are in line with The Capricorn Way. Due to the negative financial impact of Covid-19 the Bank delayed in the implementation of increments however an agreement with the union was reached and incremnets as well as backpays were made in April 2021. Our increase distribution is illustrated as below;

| Perfomance Descriptor | Bonus Awarded? | Salary Increment Awarded? |
|---|---|---|
| Exceptional | Yes | Yes |
| Exceeds Expectation | Yes | Yes |
| Meets Expectation | Yes | Yes |
| Inconsistent Performer | No | No |
| Does not Meet Expectations | No | No |

For inconsistent performers and those who do not meet performance objectives, measures are put in place to ensure they improve through performance improvement plans and an exit for those who do not improve after interventions. There is currently no malus (negative bonus) or clawbacks as these are not permissible under Botswana Labour Laws.

**Elements of pay**

The table below sets out an overview of the elements of pay applicable to Bank Gaborone employees:

| | Element | Detail |
|---|---|---|
| Fixed remuneration and Benefits | Basic Salary | The fixed element of remuneration is referred to as basic salary. |
| | Benefits | Benefits include membership of a pension fund and medical aid, to which contributions are made by both the employee and the company, except for medical aid which is 100 % company contribution, and may also include mortgage bond interest subsidies as well as housing, car, entertainment or other allowances,depending on the job level of the employee. Company contributions are calculated as part of the employee's costs to company. |
| Variable remuneration | Short -term incentives (STI) | The bank has a short-term incentive plan which aligns with best market practice within the industry and operates in the same manner for all employees within the bank. A bonus pool from which all Short Term Incentivess are paid is calculated based on consolidated bank profit. |
| | Long-term incentives (LTI) | LTI awards take the form of share appreciation rights, conditional shares or a combination of both. Most awards are subject to vesting conditions relating to company performance, measured over a three-year performance period. In instances where retention is required, conditional shares are awarded which are subject to a vesting condition of continued tenure within the group. In addition, employees from a specified grade level may participate in the group's share purchase scheme to purchase Capricorn Investment Holdings Botswana(CIHB) shares at the volume-weighted average price over the previous 12 months with the option of an interest-free loan repayable over nine years.Full ownership of these shares vests after three to five years. |

### Remuneration Paid

Annual remuneration reviews are effective on 1 September and as alluded to before, the increases are not guaranteed. During this process, remuneration structures and pay ranges are evaluated and adjusted where necessary, based on each individual's salary compared to the salary scales, considering the:

- employee's performance review
- formal salary survey conducted to determine local and regional pay practices
- adjustment of salary scales to reflect any market movement
- performance of the business

### Remuneration Structure

General Staff Remuneration for the 2021 financial year is summarised below:

| | Total value of remuneration awards for the current fiscal year | Unrestricted |
|---|---|---|
| Fixed Remuneration | Cash Based | 34,004,983 |
| Variable Remuneration | Performance Bonus | 1,058,100 |
| | Guaranteed 13th Cheque | 3,090,789 |
| | Severance Payments | 175,032 |

Senior Management Remuneration for the 2021 year is summarised below:

| | Total value of remuneration awards for the current fiscal year | Unrestricted |
|---|---|---|
| Fixed Remuneration | Cash Based | 42,654,476 |
| Variable Remuneration | Performance Bonus | 6,574,000 |
| | Shares and share-linked instruments | 2,400 |

## Annexure 1: Credit Risk

### Past Due Loans

| As at 30 June 2021 | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| | P'000 | P'000 | P'000 | P'000 |
| Article finance | 307,044 | 6,369 | 24,759 | 338,172 |
| Commercial loans | 1,710,948 | 70,752 | 38,116 | 1,819,816 |
| Individual loans | 313,663 | 2,725 | 53,800 | 370,188 |
| Mortgage loans | 1,728,595 | 24,407 | 164,868 | 1,917,870 |
| Overdrafts | 489,728 | 21,265 | 33,999 | 544,992 |
| **Total gross loans and advances*** | **4,549,978** | **125,518** | **315,542** | **4,991,038** |
| Impairments raised | (50,429) | (15,303) | (101,783) | (167,515) |
| **Net loans and advance*** | **4,499,549** | **110,215** | **213,759** | **4,823,523** |

| Non Performing Loans | Article finance | Commercial loans | Mortgages | Individual loans | Overdrafts | Total |
|---|---|---|---|---|---|---|
| | P'000 | P'000 | P'000 | P'000 | P'000 | P'000 |
| 30 June 2021 | | | | | | |
| Past due up to 30 days | 3,103 | 5,095 | 19,156 | 855 | 844 | 29,053 |
| Past due 31 - 60 days | 175 | 1,111 | 5,614 | 252 | 155 | 7,307 |
| Past due 61 - 90 days | 411 | 33 | 6,388 | 1,251 | - | 8,083 |
| Past due 91-180 days | 7,631 | 7,910 | 20,795 | 4,150 | 721 | 41,207 |
| Past due more than 180 days | 13,440 | 31,250 | 112,915 | 40,009 | 32,279 | 229,893 |
| **Total** | **24,760** | **45,399** | **164,868** | **46,517** | **33,999** | **315,543** |
| Fair value of collateral | (16,885) | (35,017) | (131,674) | (7,959) | (22,225) | (213,760) |
| **Total** | **7,875** | **10,382** | **33,194** | **38,558** | **11,774** | **101,783** |
| **Impairment raised against unsecured amounts** | **7,875** | **10,382** | **33,194** | **38,558** | **11,774** | **101,783** |
| **Net exposure** | **-** | **-** | **-** | **-** | **-** | **-** |

**Note: All Exposures are Domestic.**

Residual contractual maturity breakdown of the whole portfolio, broken down by major types of credit exposure.

| As at 30 June 2021 | P '000 | P '000 | P '000 | P '000 | P '000 | P '000 |
|---|---|---|---|---|---|---|
| | Up to 1 month | 1 - 3 months | 3 - 12 months | 1 - 5 years | Over 5 years | Total |
| **Financial Assets** | | | | | | |
| Cash and balances with Central bank | 75,617 | - | - | - | - | 75,617 |
| Bank of Botswana Certificates | 229,954 | - | - | - | - | 229,954 |
| Due from other banks | 1,470,315 | - | - | - | - | 1,470,315 |
| Loans and advances to customers | 574,188 | 7,599 | 55,296 | 968,612 | 3,385,342 | 4,991,037 |
| Investment in equity instruments | - | - | - | 3,962 | - | 3,962 |
| Loans and advances to staff | - | - | - | - | - | - |
| Other assets | 59,717 | - | - | - | - | 59,717 |
| **Total assets (contractual maturity dates)** | **2,409,791** | **7,599** | **55,296** | **972,574** | **3,385,342** | **6,830,602** |

Industry or counter-party type distribution of exposures, broken down by major types of credit exposure.

| | Cash and balances with the Central Bank | Financial asset at fair value through profit and loss | Due from other banks | Loans and advances to customers | Other assets | Total |
|---|---|---|---|---|---|---|
| **As at 30 June 2021** | **P'000** | **P'000** | **P'000** | **P'000** | **P'000** | **P'000** |
| Agriculture and forestry | - | - | - | 261,287 | - | 261,287 |
| Mining | - | - | - | 6,246 | - | 6,246 |
| Manufacturing | - | - | - | 64,423 | - | 64,423 |
| Building and construction | - | - | - | 95,757 | - | 95,757 |
| Electricity, gas and water | | | | 5,537 | | 5,537 |
| Trade and accommodation | - | - | - | 124,460 | - | 124,460 |
| Transport and communication | - | - | - | 59,392 | - | 59,392 |
| Finance and insurance | - | - | 1,470,315 | 15,197 | - | 1,485,512 |
| Business services | - | - | - | 1,876,734 | - | 1,876,734 |
| Commercial Real Estate | - | - | - | 1,124,910 | - | 1,124,910 |
| Government | - | 229,954 | - | 52,725 | - | 282,679 |
| Individuals | - | - | - | 1,246,367 | - | 1,246,367 |
| Other | 75,617 | 3,962 | - | 58,002 | 115,644 | 253,225 |
| | **75,617** | **233,916** | **1,470,315** | **4,991,037** | **115,644** | **6,886,530** |

**Total gross credit risk exposures, plus average gross exposure over the period broken down by major types of credit exposure**

| Assets | Month End | Average |
|---|---|---|
| | **P'000** | **P'000** |
| As at 30 June 2021 | | |
| Current account | 21,581 | 10,790 |
| Reserve requirement account | 11,491 | 69,703 |
| Repurchase agreement | 617,891 | 339,944 |
| Bank of Botswana Certificates | 229,954 | 339,942 |
| Balances due from domestic banks | 468,055 | 333,476 |
| Balances due from foreign banks | 375,673 | 381,569 |
| Balances due from related parties | - | 2,784 |
| Loans and advances | 4,991,037 | 4,962,883 |
| Accounts receivable | 188,937 | 191,428 |
| Investment in Equity Instruments | 3,962 | 4,292 |
| Investments in asset managers | 8,696 | 252,401 |
| | **6,917,277** | **6,889,212** |

**Industry or counter-party type distribution of past due and non-performing loans**

| **Assets** | **Past due but not impaired** | **Individually Impaired** |
|---|---|---|
| | **P'000** | **P'000** |
| **As at 30 June 2021** | | |
| Agriculture and forestry | - | 18 |
| Mining | 33 | - |
| Manufacturing | - | 1,050 |
| Building and construction | 114 | 12,253 |
| Trade and accommodation | 3,270 | 2,341 |
| Transport and communication | - | 2,978 |
| Finance and insurance | - | 2,873 |
| Business services | 28,434 | 84,160 |
| Commercial Real Estate | 2,328 | 55,481 |
| Government | - | 110 |
| Individuals | 34,737 | 148,912 |
| Other | 231 | 5,475 |
| | **69,147** | **315,651** |

**Reconciliation of changes in the allowances for loan impairment.**

| Assets | 2021 | 2020 |
|---|---|---|
| | **P'000** | **P'000** |
| Movement in impairment for the bank is as follows: | | |
| **Balance at the beginning of the year** | **179,628** | **126,016** |
| Stage 1 | 58,076 | 28,634 |
| Stage 2 | 5,584 | 8,969 |
| Stage 3 | 115,968 | 88,413 |
| **Transfer from prior year staff loan impairements** | **0** | **407** |
| • Staff loan impairements | 0 | 407 |
| **Provision/(Recovery) for loan impairment** | **43,116** | **60,190** |
| • Specific impairment | 41,044 | 35,271 |
| • Portfolio impairment | 2,072 | 24,919 |
| **Amounts written-off during the year as uncollectible** | **(55,229)** | **(6,985)** |
| • Specific impairment | (55,229) | (6,985) |
| • Portfolio impairment | - | - |
| **Balance at the end of the year** | **167,515** | **179,628** |
| Stage 1 | 50,427 | 58,076 |
| Stage 2 | 15,305 | 5,584 |
| Stage 3 | 101,783 | 115,968 |
| • Specific impairment | | |
| • Portfolio impairment | | |

**Table 25**
**Reconciliation of Financial Statements items to the statutory return**

| | Balance sheet as in published financial statements | Under regulatory scope of consolidation | |
|---|---|---|---|
| **Assets** | **P'000** | **P'000** | **Variance** |
| Cash and balances at central banks | 75,617 | 75,617 | - |
| Items in the course of collection from other banks | - | - | - |
| Trading portfolio assets | - | - | - |
| Financial assets designated at fair value | 229,954 | 229,954 | - |
| Derivative financial instruments | - | - | - |
| Loans and advances to banks | 1,470,315 | 852,424 | (617,891) |
| Loans and advances to customers | 4,804,989 | 4,822,923 | 17,934 |
| Reverse repurchase agreements and other similar secured lending | - | 617,891 | 617,891 |
| Available for sale financial investments | - | - | - |
| Current and deferred tax assets | 336 | - | (336) |
| Prepayments, accrued income and other assets | 59,717 | 31,090 | (28,627) |
| Investments in associates and joint ventures | 3,962 | 3,962 | (0) |
| Goodwill and intangible assets | - | - | - |
| of which goodwill | - | - | - |
| of which other intangibles (excluding MSRs) | 7,967 | 4,316 | (3,651) |
| of which MSRs | - | - | - |
| Property, plant and equipment | 107,341 | 110,985 | 3,644 |
| **Total Assets** | **6,760,198** | **6,749,163** | |
| **Liabilities** | | | |
| Deposits from banks | 171,034 | 171,000 | (34) |
| Items in the course of collection due to other banks | - | - | - |
| Customer accounts | 5,550,896 | 5,550,896 | - |
| Repurchase agreements and other similar secured borrowing | - | - | - |
| Trading portfolio liabilities | - | - | - |
| Financial liabilities designated at fair value | - | - | - |
| Derivative financial instruments | - | - | - |
| Debt securities in issue | 328,389 | 328,389 | - |
| Accruals, deferred income and other liabilities | 173,929 | 99,012 | (74,917) |
| Current and deferred tax liabilities | 644 | - | (644) |
| Of which DTLs related to goodwill | - | - | - |
| Of which DTLs related to intangible assets | - | - | - |
| (excluding MSRs) | - | - | - |
| Of which DTLs related to MSRs | - | - | - |
| Subordinated liabilities | 40,973 | 40,973 | (0) |
| Provisions | - | 54,382 | 54,382 |
| Retirement benefit liabilities | - | 10,182 | 10,182 |
| **Total liabilities** | **6,265,865** | **6,254,834** | **-** |
| **Shareholders' Equity** | | | |
| Paid-in share capital | | | - |
| of which amount eligible for CET1 CAPITAL | 233,750 | 233,750 | - |
| of which amount eligible for AT1 | | | - |
| Retained earnings | 260,583 | 211,902 | 48,681 |
| Accumulated other comprehensive income | | 48,678 | 48,678 |
| **Total shareholders' equity** | **494,333** | **494,330** | **3** |
| **Total Liabilities & Shareholders' Equity** | **6,760,198** | **6,749,164** | |

**Table 26**
**Reference of Financial Statements items to the statutory return**

| | Balance sheet as in published financial statements | Under regulatory scope of consolidation | |
|---|---|---|---|
| **Assets** | **P'000** | **P'000** | Notes |
| Cash and balances at central banks | 75,617 | 75,617 | 12 |
| Items in the course of collection from other banks | | | |
| Trading portfolio assets | | | |
| Financial assets designated at fair value | 229,954 | 229,954 | 14 |
| Derivative financial instruments | | | |
| Loans and advances to banks | 1,470,315 | 852,424 | 15 |
| Loans and advances to customers | 4,804,989 | 4,822,923 | 13 |
| Reverse repurchase agreements and other similar secured lending | - | 617,891 | 16 |
| Available for sale financial investments | | | |
| Current and deferred tax assets | 336 | - | 26 |
| Prepayments, accrued income and other assets | 59,717 | 31,090 | 16 |
| Investments in associates and joint ventures | 3,962 | 3,962 | 15 |
| Goodwill and intangible assets | | | |
| of which goodwill | | | |
| of which other intangibles (excluding MSRs) | 7,967 | 4,316 | 18 |
| of which MSRs | | | |
| Property, plant and equipment | 107,341 | 110,985 | 18 |
| **Total Assets** | **6,760,198** | **6,749,163** | |
| **Liabilities** | | | |
| Deposits from banks | 171,034 | 171,000 | 19 |
| Items in the course of collection due to other banks | | | |
| Customer accounts | 5,550,896 | 5,550,896 | 21 |
| Repurchase agreements and other similar secured borrowing | | | |
| Trading portfolio liabilities | | | |
| Financial liabilities designated at fair value | | | |
| Derivative financial instruments | | | |
| Debt securities in issue | 328,389 | 328,389 | 20 |
| Accruals, deferred income and other liabilities | 173,929 | 99,012 | 22 |
| Current and deferred tax liabilities | 644 | - | |
| Of which DTLs related to goodwill | | | |
| Of which DTLs related to intangible assets | | | |
| (excluding MSRs) | | | |
| Of which DTLs related to MSRs | | | |
| Subordinated liabilities | 40,973 | 40,973 | 29 |
| Provisions | | 54,382 | 22 |
| Retirement benefit liabilities | | 10,182 | 22 |
| **Total liabilities** | **6,265,866** | **6,254,834** | |
| **Shareholders' Equity** | | | |
| Paid-in share capital | | | |
| of which amount eligible for CET1 CAPITAL | 233,750 | 233,750 | 28 |
| of which amount eligible for AT1 | | | |
| Retained earnings | 260,583 | 211,902 | 28 |
| Accumulated other comprehensive income | | 48,678 | 28 |
| **Total shareholders' equity** | **494,333** | **494,330** | |
| **Total Liabilities & Shareholders' Equity** | **6,760,199** | **6,749,164** | |

**Table 27**
**Extract of Basel III common disclosure template**

| Common Equity Tier I capital: instruments and reserves | | | |
|---|---|---|---|
| | | Component of regulatory capital reported | Source based on Reference numbers |
| 1 | Directly issued qualifying common share (and equivalent for non-joint stock companies) capital plus related stock surplus. | 233,750 | h |
| 2 | Retained Earnings | 211,902 | |
| 3 | Accumulated other comprehensive income (and other reserves) | 48,678 | |
| 4 | Directly issued capital subject to phase out from CET1 CAPITAL (only applicable to non- joint stock companies) | - | |
| 5 | Common share capital issued by subsidiaries and held by third parties (amount) allowed in group CET1 CAPITAL) | - | |
| 6 | Common Equity Tier I capital before regulatory adjustments | 494,330 | |
| 7 | Prudential valuation adjustments | - | |
| 8 | Goodwill (net of related tax liability) | 4,316 | a-d |

**Table 28**
**Main feature of instruments issued by the Bank**

| | Pref Share | Pref Share | Pref Share | BG 001 | BG 002 | BG 003 |
|---|---|---|---|---|---|---|
| Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement) | n/a | n/a | n/a | n/a | n/a | n/a |
| Governing law(s) of the instrument | Botswana | Botswana | Botswana | Botswana | Botswana | Botswana |
| Regulatory treatment | Tier II | Tier II | Tier II | Tier II | Tier II | Tier II |
| Transitional Basel III rules | [Tier II] | [Tier II] | Disqualified | Disqualified | [Tier II] | [Tier II] |
| Post-transitional Basel III rules | [Tier II] | [Tier II] | [Deduction from Tier II] | [Deduction from Tier II] | [Tier II] | [Tier II] |
| Eligible at solo/group/group and solo | Solo | Solo | Solo | Solo | Solo | Solo |
| Instrument type (types to be specified by each jurisdiction) | Preference Shares | Preference Shares | Subordinated Term Debt | Subordinated Term Debt | Subordinated Term Debt | Subordinated Term Debt |
| Amount recognised in regulatory capital (Currency in mil, as of most recent reporting date) | 50,000 | 100,000 | 100,000 | - | 25,000 | 41,000 |
| Par value of instrument | 50,000 | 100,000 | 100,000 | 50,000 | 25,000 | 41,000 |
| Accounting classification | Preference Shares | Preference Shares | Debt | Debt | Debt | Debt |
| Original date of issuance | 16/09/2019 | 26/10/2019 | 24/06/2020 | 27/10/2011 | 30/06/2017 | 30/06/2018 |
| Perpetual or dated | Dated | Dated | Dated | Dated | Dated | Dated |
| Original maturity date | 15/09/2029 | 25/10/2029 | 23/06/2030 | 31/10/2021 | 30/06/2027 | 30/06/2028 |
| Issuer call subject to prior supervisory approval | Yes | Yes | Yes | Yes | Yes | Yes |
| Optional call date, contingent call dates and redemption amount | 5 year anniversary or after | 5 year anniversary or after | 5 year anniversary or after | 5 year anniversary or after | 5 year anniversary or after | 5 year anniversary or after |
| Subsequent call dates, if applicable | 5 year anniversary or after at the option of issuer | 5 year anniversary or after at the option of issuer | 5 year anniversary or after at the option of issuer | 5 year anniversary or after at the option of issuer | 5 year anniversary or after at the option of issuer | 5 year anniversary or after at the option of issuer |

| | | | | | | |
|---|---|---|---|---|---|---|
| Coupons / dividends | Dividends | Dividends | Coupon | Coupon | Coupon | Coupon |
| Fixed or floating dividend/ coupon | Floating | Floating | Floating | Floating | Floating | Floating |
| Coupon rate and any related index | Bank Rate+1.6% | Bank Rate+1.4% | Bank Rate+1.4% | 91 Day BOBC Rate+4% | Bank Rate+2.25% | Bank Rate+2.5% |
| Existence of a dividend stopper | None | None | None | None | None | None |
| Fully discretionary, partially discretionary or mandatory | Mandatory | Mandatory | Mandatory | Mandatory | Mandatory | Mandatory |
| Existence of step up or other incentive to redeem | None | None | None | None | None | None |
| Noncumulative or cumulative | Cumulative | Cumulative | Cumulative | Cumulative | Cumulative | Cumulative |
| Convertible or non-convertible | Non-convertible | Non-convertible | Non-convertible | Non-convertible | Non-convertible | Non-convertible |
| If convertible, conversion trigger (s) | n/a | n/a | n/a | n/a | n/a | n/a |
| If convertible, fully or partially | n/a | n/a | n/a | n/a | n/a | n/a |
| If convertible, conversion rate | n/a | n/a | n/a | n/a | n/a | n/a |
| If convertible, mandatory or optional conversion | n/a | n/a | n/a | n/a | n/a | n/a |
| If convertible, specify instrument type convertible into | n/a | n/a | n/a | n/a | n/a | n/a |
| If convertible, specify issuer of instrument it converts into | n/a | n/a | n/a | n/a | n/a | n/a |
| Write-down feature | n/a | n/a | n/a | n/a | n/a | n/a |
| If write-down, write-down trigger(s) | n/a | n/a | n/a | n/a | n/a | n/a |
| If write-down, full or partial | n/a | n/a | n/a | n/a | n/a | n/a |
| If write-down, permanent or temporary | n/a | n/a | n/a | n/a | n/a | n/a |
| If temporary write-down, description of write-up mechanism | n/a | n/a | n/a | n/a | n/a | n/a |
| Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument) | Subordinated Debt | Subordinated Debt | Subordinated Debt | Depositors and General Creditors | Depositors and General Creditors | Depositors and General Creditors |
| Non-compliant transitioned features | n/a | n/a | n/a | Yes | n/a | n/a |
| If yes, specify non-compliant features | n/a | n/a | n/a | Call option on the bond | n/a | n/a |