FMB

Annual Report 2009

First Merchant Bank

Contents

Senior management

Managing Director
Kashinath Chaturvedi

Deputy Chief Executive Officer
Ram Rastogi

Head, Information and Technology
E.P. Jacob

Head, International Banking and Corporate
Thomas Kadantot

Head of Finance, Operation and Administration
Mani Verma

Head, Human Resources
Indira Sharma-Surtee

Information and Technology Manager
D. Temperly

Senior Credit Control Manager
Agness Jazza

Senior Programme Manager – Makwacha
Nelson Njikho

Senior Audit Manager
Tiwonge Kalua

Senior Manager-Risk, Compliance and Security
George Kamvulumvulu

Finance Manager
Maxwell Banda

Branch management

BLANTYRE BRANCH

Branch Manager
Lexa Msowoya

Operations Manager
Bright Kadewere

LIMBE BRANCH

Branch Manager
Montfort Masinga

Operations Manager
Pamela Kasunda

LILONGWE BRANCH

Regional Manager
Prakash Kamath

Operations Manager
Kenneth Musonzo

Operations Manager
Eisenhower Mkaka

MZUZU BRANCH

Branch Manager
Evance Bamusi

Operations Officer
Harry Munthali

FIRST CORPORATE SERVICES BRANCH

Branch Manager
Emily Banda

Operations Officer
Mathews Phoso

LEASING AND FINANCE COMPANY

General Manager
Alex Chigwale

Lilongwe Branch Manager
Bessie Nsambo

CAPITAL CITY BRANCH

Branch Manager
Mary Nkando

Operations Manager
Jane Mphande

ZOMBA BRANCH

Officer In-charge
Rodney Mafunga

CROSSROADS AGENCY

Officer In-charge
Maliton Banda

KANENGO AGENCY

Officer In-charge
Geofrey Ng'oma

DEDZA AGENCY

Officer In-charge
Maxwell Kapezi

MCHINJI AGENCY

Officer In-charge
Alexander Kumchenga

MPONELA AGENCY

Officer In-charge
Mzondi Chimaliro

KASUNGU AGENCY

Officer In-charge
John Chipeta

DWANGWA AGENCY

Officer In-charge
Goodwin Ziyabu

KARONGA

Officer In-charge
Steve Kanyika

RUMPHI AGENCY

Officer In-charge
Timothy Munthali

MZIMBA AGENCY

Officer In-charge
Paul Munthali

NKHATA- BAY AGENCY

Officer In-charge
Frank Kawamba

LIWONDE AGENCY

Officer In-charge
Joseph Ching'ani

MANGOCHI AGENCY

Officer In-charge
Allison Amin

Chairman's statement

Although there were many challenges for the Malawi financial sector in 2009, in particular an acute foreign exchange shortage, the group achieved satisfactory results, recording a modest 5% growth in profit before tax. This was achieved despite a net loss of almost K200 million on our listed equity portfolio compared to K350 million profit in the prior year.

Net interest income grew by 37% and non interest income by 26% reflecting improved operating performance in all group companies. Our cost to income ratio worsened marginally to 54% as a result of an aggressive expansion of our service delivery infrastructure but remains broadly in line with expectations.

Capital Bank Limited, Botswana, which commenced operations in 2008 is now a modest contributor to group profits and the main driver of growth in the group's asset base. The Leasing and Finance Company of Malawi Limited also achieved a very commendable 47% and 60% growth in deposits and profit respectively. Our most recently established subsidiary, FMB Forex Bureau Limited, commenced business in November 2009 opening its first branch in Limbe, but is not yet a significant operation in the context of the overall group.

Economic Review

The Malawi economy continues to grow strongly with real GDP estimated to increase by 7.7% in 2009, following on from 9.8% and 8.6% growth in 2008 and 2007 respectively. The agricultural sector remains the main growth driver and once again the country registered a significant surplus of maize production due to favourable climatic conditions and the continuance of the universal fertilizer subsidy. 3.8 million tonnes were produced against a national requirement of 2.4 million tonnes.

Contribution from the key agricultural export crop, tobacco, was lower than 2008 despite production volumes increasing from 195,000 tonnes to 232,000 tonnes as the average price realized at auction fell from 242 US cents to 187 US cents per kilogramme. Nevertheless the total gross realization of US$433 million, while falling short of the 2008 record of US$472 million, remains more than double that achieved in any of the ten preceding years.

Following the commencement of uranium mining in the later part of 2009, robust growth of 8.8% is expected in the mining sector. However, the manufacturing sector which had begun to show signs of recovery with a 9.9% growth in 2008 was adversely affected by foreign exchange and fuel shortages and unreliable utility supplies and more modest growth of 4.7% is expected in this sector in 2009.

After maintaining commendable fiscal discipline for a number of years, concerns are beginning to arise over the re-emergence of fiscal deficits. Successive deficits of K19 billion, K35 billion and K27 billion have been experienced in the fiscal years ending 30 June 2007, 2008 and 2009, the latter approaching 4% of GDP. An ambitious target has been set to reduce the 2010 deficit to K12.5 billion or 1.6% of GDP but expenditure over runs have been incurred in the first half of the 2009/2010 fiscal year. These continuing fiscal deficits have resulted in increased resource to domestic borrowing by Government. The treasury bill stock closed the year just short of K140 billion up from K113 billion at end 2008 and K84 billion at end 2007.

Growth in money supply, M2, at 24.7% for 2009 continues to outstrip nominal GDP growth. It is perhaps encouraging that this gap is narrowing as the M2 growth rate has eased somewhat from previous annual rates in excess of 30%. The increase in broad money can be partially explained by a build up in private sector deposits of funds awaiting remittance due to the prevailing foreign exchange shortage. Nevertheless, inflationary pressures are likely to persist until broad money growth is curtailed further.

In 2009 the average annual inflation rate was contained at 8.4% which compares favourably with 8.7% recorded in 2008. The bumper food harvest saw food costs reduced significantly in the post harvest period before easing upwards again towards year end as the traditional 'lean season' commenced. Lower food cost inflation has helped offset somewhat higher non food inflation.

In view of the threat of inflation, the monetary authorities continued a policy of tight demand management and maintained the central intervention rate, the bank rate, unchanged at 15% throughout the year. As a consequence the banking industry generally did not adjust lending and savings rates though some upward movement in rates availed to wholesale and term depositors occurred in response to increased competition in the sector.

The country's foreign exchange position remained critical throughout 2009 and by year end gross official reserves had declined to US$127 million or one month of import cover. In addition there exists a sizeable backlog of unpaid foreign remittances. In 2009 foreign exchange reserves were depleted by the lagged effect of the 2008 surge in world fuel and fertilizer prices. Also a hiatus occurred in the disbursement of both bilateral and multilateral aid from the conclusion of the International Monetary Fund Exogenous Shock Facility through to the approval in early 2010 of a successor programme under the Extended Credit Facility.

The value of the Kwacha had remained pegged virtually unchanged against the US dollar from 2007 despite local inflation and significant growth in money supply over the same period. The resultant increasing dollar purchasing power of the local economy escalated demand for foreign currency. Eventually, in November 2009, the authorities allowed the value of the Kwacha to depreciate and by year end the currency had fallen in value by 3% against the benchmark US dollar.

Group Performance

The key highlights of the group performance for 2009 are:

- Deposits grew by 63% from K17.1 billion to K27.9 billion.

- Lending grew by 58% from K11.0 billion to K17.5 billion.

- Total assets grew by 55% from K24.9 billion to K38.7 billion.

- Profit before tax grew by 5% from K1.9 billion to K2.0 billion. However, operational profit before tax, excluding the performance of our investment portfolio, grew by a more impressive 42%.

- Shareholders' equity grew by 18% from K5.4 billion to K6.4 billion.

The market for bank deposits in Malawi was extremely competitive during the year and no growth was seen in the deposit base of First Merchant Bank itself. Our asset finance subsidiary, The Leasing and Finance Company of Malawi Limited, proved very successful in the term deposit market and achieved a 47% growth in its level of deposits. Capital Bank Limited, now in its second year of operations, has more than quadrupled its deposit base and is now responsible for some 40% of total group deposits.

We continue to grow our advances portfolio broadly in line with the growth in our deposit book and at year end our credit deposit ratio of 63% was virtually unchanged from a ratio of 64% at end 2008. The quality of our credit portfolio remains very satisfactory with a high proportion of blue chip and well secured lending. Continuous attention to credit monitoring and aggressive recovery procedures where required have kept the group impairment charge down to a very acceptable level of K15 million.

Some K17.4 billion or 45% of the group's total assets comprise low risk liquid assets in the form of cash and cash equivalents and money market investments such as government and central bank paper. As a result, all group companies comfortably comply with the prudential requirements for both capital adequacy and liquidity laid down by the regulators in Malawi and Botswana.

Our portfolio of Malawi listed equities which has performed poorly in recent years in line with a general downturn in the market now represents a much less significant 3% of total group assets. It is, however, worthwhile noting that the original cost of our residual portfolio is K185 million against a closing market value of K1.3 billion.

Net interest income grew by 33%, largely a reflection of the larger group deposit base as net interest margin on interest bearing assets declined reflecting the increasing influence of the lower spreads achievable in the Botswana market. Margins in Malawi were maintained although yields available on Malawi government paper declined over the course of the year. Non interest income also registered strong growth with fee and commission income growing by 27% to approach K1 billion and foreign exchange earnings growing by a very pleasing 27% in a very difficult trading environment.

The 22% recorded increase in the level of operating expenses incurred in the year is considerably higher than the rate of domestic inflation but was to be anticipated in light of the growth in business levels and the boll out of new infrastructure both in Malawi and Botswana where an additional branch was opened in Francistown. At 54% the overall cost to income ratio is in line with expectations but our goal remains to reduce this ratio back to historic levels of below 50%.

During the year dividends totaling K601 million were paid to shareholders against net group profit of K1,315 million. This resultant net retention of earnings together with a surplus of K200 million recorded on the periodic revaluation of fixed properties has seen group shareholders' equity grow to K6.4 billion, a level of capitalization with should further reinforce the confidence in the group of all its stakeholders.

Human Resources

Over the course of the year the staff numbers of First Merchant Bank grew from 496 to 572 mainly to service its expanded branch network and product range. Capital Bank now employs 78 persons in its head office and two branches while The Leasing and Finance Company remains with a lean staff complement of 16. Our main focus from the perspective of learning and growth continues to be mentoring and coaching employees on the job, backed up by generic banking courses and supervisory and management skills courses conducted at our in house training centre and other reputable training institutions within Malawi and abroad. In addition, we have invested considerable financial resources in developing capacity through supporting staff throughout

Chairman's statement

the group to obtain professional banking qualifications and through facilitating continuing professional development and relevant post graduate studies for our specialist and managerial staff.

Corporate Social Responsibility

The board of directors of First Merchant Bank is fully committed to ensuring that the group conducts its business affairs with integrity, maintains the highest ethical standards and complies with all legislation and regulation in force in the territories in which it operates. The group also seeks to make a positive contribution to the welfare of the community at large and provides financial support to numerous worthy causes with a particular focus on the areas of health, education and sports.

In accordance with the requirements of the Malawi Stock Exchange , a separate statement on corporate governance is also included within this annual report.

Outlook

Official estimates are that economic growth will remain robust at 6.3% in 2010, spurred by an expansion in the non agricultural sectors of the economy, Government investment in infrastructure and increased production from the Kayelekera uranium mine.

Agricultural output will be affected by the erratic weather patterns that have been experienced this season. Drought conditions will result in maize deficits in a number of districts but it is hoped that overall national production will be adequate to meet national demand. Additionally there remain significant significant carry over stocks from prior years and considerable volumes continue to be informally imported from neighbouring Mozambique.

The second round estimate of national tobacco production from Tobacco Control Commission is a total crop of 215,000 tonnes, 7.4% down on 2009. On the basis of the predicted crop throw (which cannot really be reliably established at this stage) the approved matrix of minimum prices for various tobacco grades should yield a total gross realization which compares favourably with 2009 despite the reduced crop size. Dry conditions in the early part of the crop growing season should be positive for crop quality but this may be mitigated somewhat by the detrimental effects of excessive rains during harvesting and curing of the crop.

The opening of the tobacco auctions should see an easing in the foreign exchange position, particularly now that dollars realized will be released to dealer banks rather than to RBM as has been the case in recent seasons. The approval by the IMF board in February 2010 of a macroeconomic programme for Malawi under the Extended Credit Facility should also unlock substantial donor inflows. Demand for foreign exchange may be dampened slightly due to the depreciation of the kwacha but it is unlikely that the modest 7% fall in value between November 2009 and March 2010 will be sufficient to have a meaningful impact. There remains some way to go to align the exchange rate with the economic fundamentals.

Inflationary pressures are likely to persist in the near term and the current IMF forecast is a 10.1% inflation rate for 2010. Against this background, RBM are likely to maintain a tight monetary stance and there would appear to be little scope for a reduction in the bank rate.

We anticipate that the Malawi financial market will remain highly competitive in 2010. This may well place pressure on interest margins and, until there is some improvement in the foreign exchange position, our foreign exchange earnings will remain depressed. However, we are confident that our investment in expanded geographical coverage and the planned introduction of a number of innovative products will enable us to grow our business through extending our banking outreach beyond our traditional customer base. Our two major subsidiaries, Capital Bank Limited and The Leasing and Finance Company of Malawi Limited are expected to make a much more significant contribution to group profits in 2010.

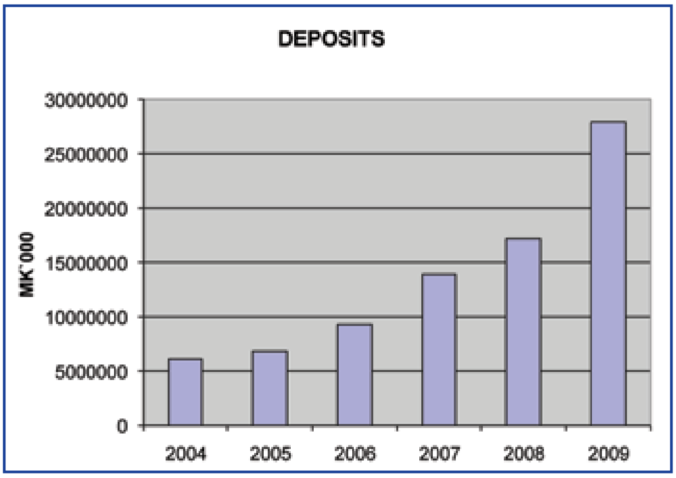
Acknowledgements

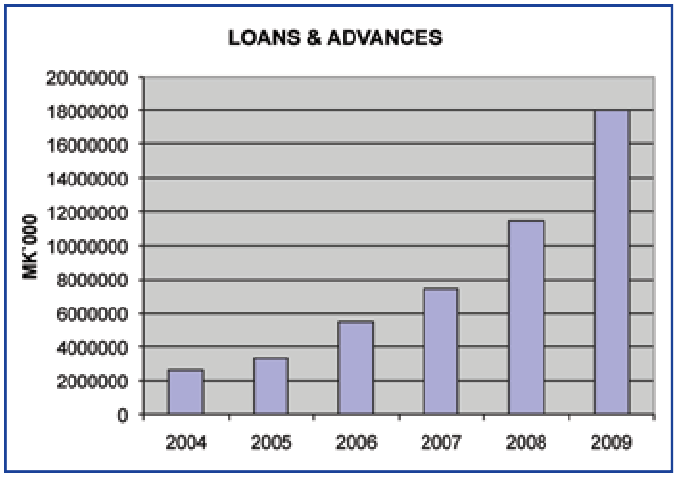
We gratefully acknowledge the continued support of our customers, shareholders and all other stakeholders over the past year and look forward to their continued support in the future. We also wish to record our appreciation of the support and guidance received from Reserve Bank of Malawi and Bank of Botswana. My sincere thanks also go to my fellow directors, management and staff for their dedicated service throughout the year.

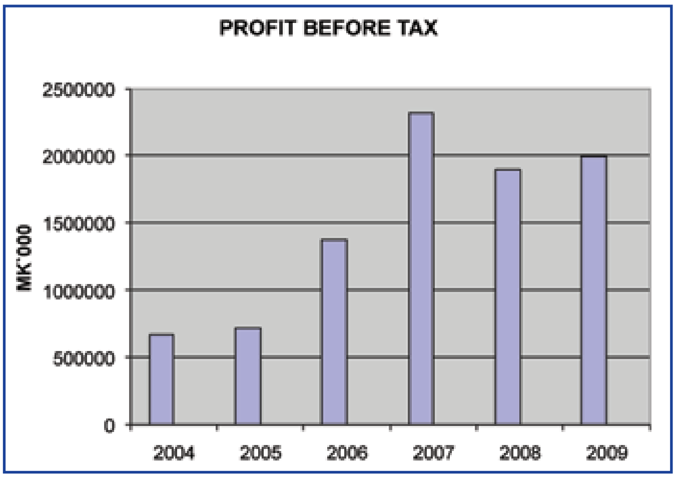
R.C. Kantaria

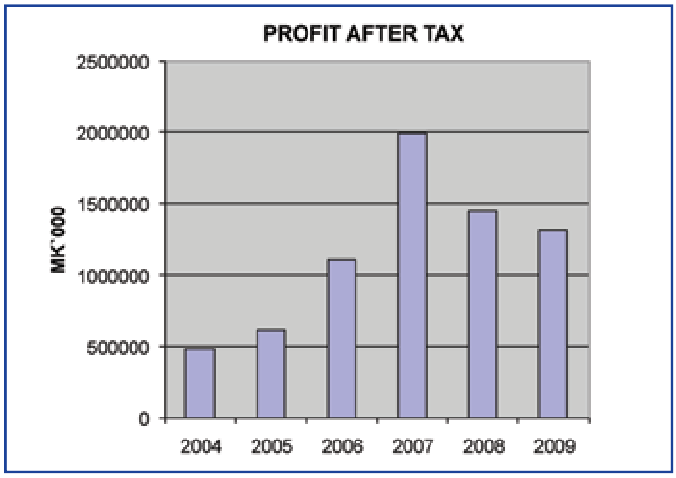
Chairman

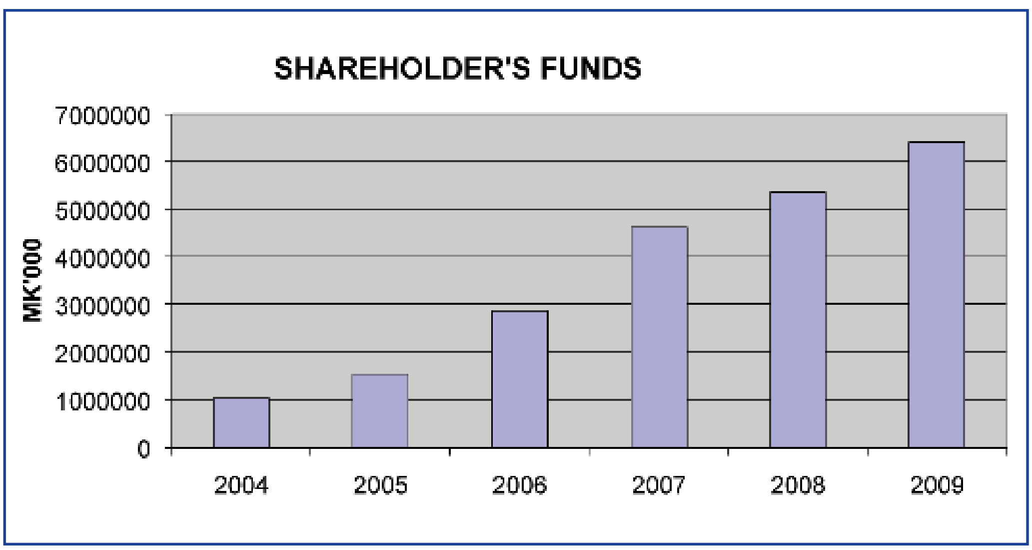
Performance











Important events

New Logo Launched - Blantyre

Winner of Kashi Kashi Promotion

1st Prize K1 Million - Chance Munthali, working at Machinga District Hospital

Corporate Social Responsibilities

Scholarship to Mzuzu University Students

Distribution of School Bags to Primary Pupils

Corporate Social Responsibilities

FMB Ladies Donating Blood

School Bag Distribution - Kasungu

Consolidated Financial Statements

For the year ended

31 DECEMBER 2009

Directors's Report

For the year ended 31 December 2009

The Directors have pleasure in submitting their report together with the audited consolidated financial statements of First Merchant Bank Limited for the year ended 31 December 2009.

NATURE OF BUSINESS, INCORPORATION AND REGISTERED OFFICE

First Merchant Bank Limited is a public limited liability company incorporated in Malawi under the Malawi Companies Act, 1984. It is listed on the Malawi Stock Exchange and is registered as a commercial bank under the Banking Act 1989. It has two wholly owned subsidiaries incorporated in Malawi, The Leasing and Finance Company of Malawi Limited, a licensed Financial Institution engaged in deposit taking and asset finance and FMB Forex Bureau, a licensed foreign exchange bureau. First Merchant Bank Limited also holds a 53.76% (2008:52.42%) shareholding in Capital Bank Limited, a licensed commercial bank incorporated in Botswana.

The physical address of the holding company's registered office is:-
Livingstone Towers,
Private Bag 122,
Glyn Jones Road,
Blantyre,
Malawi.

FINANCIAL PERFORMANCE

The results and state of affairs of the Group and Company are set out in the accompanying consolidated statement of financial position, statement of comprehensive income, statements of changes in equity, statements of cash flows and associated accounting policies and notes.

DIVIDENDS

Last year's second interim dividend of MK155.750 million (7 tambala per share) and final dividend of MK44.500 million (2 tambala per share) were paid during the year. On 28 May 2009 the directors declared a first interim dividend of MK400.500 million (18 tambala per share) for the year 2009 and a second interim dividend of MK140.175 million (6 tambala per share) was declared on 27 February 2010. The directors also propose a final dividend of MK46.725 million (2 tambala per share) for approval at the forthcoming annual general meeting.

DIRECTORATE AND SECRETARY

The following directors and secretary served during the year:

Mr. R.C. Kantaria	Chairman
Mr. H.N. Anadkat	Vice Chairman
Mr. K. N. Chaturvedi	Managing Director
Mr. S. Srinivasan	Deputy Managing Director and Company Secretary
Mr. J.M. O'Neill	Executive Director
Mr. N.G. Anadkat	Director
Mr. A. Abdallah	Director
Mr. B. Jani	Director – Member of Audit Committee
Mr. M. Msisha	Director – Chairman of Audit Committee
Mr. S.G. Malata	Director – Member of Audit Committee

In accordance with the Company's Articles of Association, Messrs. Messr's. A. Abdallah, S. Srinivasan, J.M. O'Neill and B. Jani retired by rotation at the last Annual General Meeting on 29 May 2009 and were re-appointed. Messr's. N.G. Anadkat, M. Msisha and K.N. Chaturvedi retire by rotation at the forthcoming Annual General Meeting but being eligible for re-appointment they offer themselves for re-election.

SHAREHOLDING ANALYSIS

Name	Holding (%)
Zambezi Investments Limited	44.94
Simsbury Holdings Limited	22.47
Prime Capital and Credit Limited	11.24
Prime Bank Limited	11.24
General Public	10.11
	100%

AUDITORS

A resolution will be proposed at the forthcoming Annual General Meeting to re-appoint Messrs. KPMG, Certified Public Accountants and Business Advisors (Malawi) as auditors in respect of the Company's 31 December 2010 financial statements.

....	....
K.N. Chaturvedi	M. Msisha
DIRECTOR	DIRECTOR

27 February 2010

Statement on Corporate Governance

For the year ended 31 December 2009

THE BOARD

The Bank has a unitary Board of Directors comprising a Non-Executive Chairman, 6 Non-Executive Directors and 3 Executive Directors.

The Board has adopted without modification the major principles of modern corporate governance as contained in the reports of Cadbury and King, and the Basel Committee on Banking Supervision.

The Board meets at least 3 times a year. There are adequate and efficient communication and monitoring systems in place to ensure that the Directors receive all relevant, accurate information to guide them in making necessary strategic decisions, and providing effective leadership, control and strategic direction over the Bank's operations, and in ensuring that the company fully complies with relevant legal, ethical and regulatory requirements.

BOARD AND MANAGEMENT COMMITTEES

There is one permanent management committee namely, the Asset and Liability Management Committee ("ALCO"), three permanent board committees, the Audit Committee, Credit Committee and the Appointments and Remuneration Committee and a Risk Committee comprising both directors and senior management. Additionally, there is an informal Business Promotion Committee which comprises branch managers, senior management, 2 non-executive directors and 3 executive directors. This committee meets regularly, usually once a month, and reviews the Bank's market position relative to its peers and sets operational strategy to maintain and grow market share.

Asset and Liability Management Committee (ALCO)

The primary objective of the ALCO is to ensure a proper balance in terms of maturity profile, cost and yield, risk exposure e.t.c. between funds mobilized and funds deployed. The ALCO seeks to manage risks in order to minimize the volatility of net interest income and protect the long term economic value of the Bank. The committee also monitors the capital adequacy of the Bank.

Key functions of the ALCO include setting pricing guidelines for assets and liabilities, setting limits and managing liquidity risk and interest rate risk and ensuring that contingency funding plans are in place to avert funding crises.

The ALCO is composed of 2 executive directors and 5 members of management and meets regularly, usually once a month. The members of the ALCO are:

Mr. K. N. Chaturvedi	Managing Director
Miss. A. Jazza	Senior Credit Control Manager
Mr. M. Banda	Finance Manager
Ms. M. Nyasulu	Treasury Manager
Mr. Thomas Kadantot	Head of International Banking
Mr. George Kamvulumvulu	Senior Manager – Risk Management, Compliance and Security

Audit Committee

The Audit Committee assists the Board in discharging its duties in relation to financial reporting, asset management, risk management, internal control systems, processes and procedures and monitors the quality of both the external and internal audit functions. The Bank's External Auditors and Internal Auditors report to the committee in their independent, private meetings to discuss risky exposure areas. Where the committee's monitoring and review activities reveal causes for concern or scope for improvement, it makes recommendations to the Board on required remedial actions.

The Audit Committee comprises 3 non-executive directors, 1 of whom acts as chairman. The committee meets at least 4 times a year. The members of the Audit Committee are:

Mr M. Msisha	Non-Executive Director (Chairman)
Mr B. Jani	Non-Executive Director
Mr S.G. Malata	Non-Executive Director

Credit Committee

The Credit Committee comprises 3 local directors with a good knowledge of the Malawi economy and business environment. Its overall responsibility is to ensure the soundness of the Bank's credit portfolio (including advances, guarantees and other facilities). Specific responsibilities include:

Ratification of terms and conditions of all credit facilities granted by management under its discretionary powers;
Approval of all credit facilities above the discretionary limits set for management save for those facilities requiring full board approval in accordance with Reserve Bank of Malawi directives; and
Review of non-performing assets and recovery procedures initiated in respect thereof and establishment of appropriate levels of provisioning where required.

The Managing Director, Deputy Managing Director, Senior Credit Control Manager and Branch Managers attend all Credit Committee meetings in a non-voting capacity.

The Credit Committee meets regularly, usually once a quarter and comprises the following members:

Mr H. N. Anadkat	Non-Executive Vice Chairman (Chairman)
Mr N. G. Anadkat	Non-Executive Director
Mr J. M. O'Neill	Executive Director

Appointments and Remuneration Committee

The Appointments and Remuneration Committee nominates persons to be appointed directors (subject to shareholders' approval) and recommends to the Board, executive and non-executive directors and senior management remuneration. The committee also approves overall human resource and remuneration policies and strategies.

The Appointments and Remuneration Committee meets twice a year and comprises the following members:-

Mr H. N. Anadkat	Non-Executive Vice Chairman (Chairman)
Mr M. Msisha	Non-Executive Director

Risk Committee

The risk management committee assists the board in relation to assessing the risks and to mitigate and control them. The committee reviews the risk, reveal causes of concern or scope of improvement. The committee makes recommendations to the board for remedial action.

The risk committee comprise of one non-executive director, who is chairman of the committee and two non-executive directors. The members of committee are:-

Mr. Stewart Malata	-	Non-Executive Director Chairman
Mr. K.N. Chaturvedi	-	Managing Director
Mr. G. Kamvulumvulu	-	Senior Manager, Risk Management, Compliance and Security.

Statement of Directors' Responsibilities

For the year ended 31 December 2009

ETHICAL STANDARDS

The Board is fully committed to ensuring the Group's affairs are conducted with integrity and that the highest ethical standards are maintained. All employees of the Group are required to abide by a code of conduct containing detailed guidelines governing ethics and integrity in the workplace.

The Companies Act, 1984, requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the group and company as at the end of the financial year and of the operating results for that year. Where a company has subsidiaries, the Companies Act requires the Group financial statements to give a true and fair view of the state of affairs of the group and company (normally as consolidated financial statements) and of its operating results and cashflows of the group and company so far as concerns the members of the company.

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

In preparing the group and company financial statements, the directors accept responsibility for the following:

Maintenance of proper accounting records;
Selection of suitable accounting policies and applying them consistently;
Making judgements and estimates that are reasonable and prudent;
Compliance with applicable accounting standards, when preparing financial statements, subject to any material departures being disclosed and explained in the financial statements; and
Preparation of financial statements on a going concern basis unless it is inappropriate to presume that the company will continue in business.

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

Nothing has come to the attention of the Directors to indicate that the Company and Group will not remain a going concern for at least the next twelve months from the date of this statement.

The Directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the Company and Group and of their operating results.

The financial statements of the Group and Company were approved for issue by the Board of Directors on 27 February 2010.

Director: ______________________________
K.N. Chaturvedi

Director: ______________________________
Modecai Msisha

Auditor’s Report

INDEPENDENT AUDITOR’S REPORT TO THE SHAREHOLDERS OF FIRST MERCHANT BANK LIMITED

Report on the financial statements

We have audited the accompanying consolidated and separate financial statements of First Merchant Bank Limited and its subsidiaries, which comprise the statements of financial position as at 31 December 2009, and the statements of comprehensive income, the statements of changes in equity and statements of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 20 to 83.

Directors’ responsibility for the financial statements

The company’s directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the Malawi Companies Act 1984. This responsibility includes: designing, implementing and maintaining internal control systems relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor’s responsibility

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

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

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

Opinion

In our opinion, these financial statements give a true and fair view in all material respects of the consolidated and separate financial position of First Merchant Bank Limited at 31 December 2009, and of its consolidated and separate financial performance and its consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards and with the provisions of the Malawi Companies Act 1984, so far as concerns members of the company.

KPMG
Certified Public Accountants and Business Advisors
Blantyre

27 February 2010

Consolidated and Separate Financial Statements

For the year ended 31 December 2009

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

In thousands of Malawi Kwacha

	Note	GROUP 2009	GROUP 2008	COMPANY 2009	COMPANY 2008
ASSETS			Restated		
Cash and cash equivalents	7	5,189,562	5,072,359	2,352,333	4,646,581
Money market investments	8	12,219,023	5,509,039	4,099,054	2,133,609
Loans and advances to customers	9	14,583,458	8,875,037	10,483,801	8,131,407
Finance lease receivables	10	2,889,213	2,153,526	-	-
Other assets	11	282,947	104,758	149,663	82,126
Investments in listed companies	12	1,312,969	1,602,650	1,312,969	1,602,650
Investment in subsidiaries	13	-	-	785,968	548,953
Property and equipment	14	2,071,972	1,484,080	1,727,151	1,209,017
Deferred tax assets	15	121,274	100,373	60,393	61,074
Total assets		38,670,418	24,901,822	20,971,332	18,415,417
LIABILITIES AND EQUITY					
Liabilities					
Customer deposits	16	27,895,094	17,113,667	11,607,977	11,539,513
Balances due to other Banks	17	2,308,913	670,403	2,308,913	670,403
Income tax payable		201,878	120,230	161,803	80,799
Other liabilities	18	980,983	1,030,854	914,275	874,587
Provisions	19	167,679	137,457	156,341	122,320
Deferred tax liabilities	15	223,336	101,430	159,498	76,297
Total liabilities		31,777,883	19,174,041	15,308,807	13,363,919
Equity					
Issued capital	20	116,813	111,250	116,813	111,250
Share premium	20	1,565,347	514,035	1,565,347	514,035
Property revaluation reserve	21	553,685	375,019	517,028	349,628
Investment revaluation reserve	22	1,127,626	1,400,970	1,127,626	1,400,970
Loan loss reserve	23	33,406	27,029	16,898	16,898
Non Distributable reserves		350,000	-	-	-
Translation reserve		(26,527)	(75,846)	-	-
Retained earnings		2,636,102	3,063,061	2,318,813	2,658,717
Total equity attributable to equity holders of the company		6,356,452	5,415,518	5,662,525	5,051,498
Non controlling interest		536,083	312,263	-	-
Total equity		6,892,535	5,727,781	5,662,525	5,051,498
Total equity and liabilities		38,670,418	24,901,822	20,971,332	18,415,417

The financial statements of the Group and Company were approved for issue by the Board of Directors on 27 February 2010 and were signed on its behalf by:

....Director
K.N. Chaturvedi

....Director
Modecai Msisha

The financial statements are to be read in conjunction with the notes from pages 27 to 83.

The independent auditor's report is on page 19.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

In thousands of Malawi Kwacha

		GROUP		COMPANY	
	Note	2009	2008	2009	2008
Interest income	24	3,735,034	2,521,594	2,284,767	1,874,678
Interest expense on deposits and other accounts		(949,130)	(497,898)	(200,847)	(230,065)
Net interest income		2,785,904	2,023,696	2,083,920	1,644,613
Fees and commissions		930,448	732,483	822,820	722,786
Income from investments	25	(194,265)	350,819	(194,265)	350,819
Gain on foreign exchange transactions		863,394	696,783	833,446	688,106
Net trading income		4,385,481	3,803,781	3,545,921	3,406,324
Other operating income	26	11,984	3,863	959	2,856
Total operating income		4,397,465	3,807,644	3,546,880	3,409,180
Staff and training costs	27	1,217,368	959,733	1,000,559	830,170
Premises and equipment costs		274,337	251,887	238,300	228,360
Depreciation	14	275,895	153,043	211,763	132,014
Other expenses	28	620,237	491,605	501,186	409,248
Impairment loss on financial assets		15,561	55,831	(5,149)	28,674
Total expenses		2,403,398	1,912,099	1,946,659	1,628,466
Profit before income tax expense		1,994,067	1,895,545	1,600,221	1,780,714
Income tax expense	29	(675,728)	(503,761)	(555,843)	(461,579)
PROFIT FOR THE YEAR		1,318,339	1,391,784	1,044,378	1,319,135
Other comprehensive Income					
Revaluation of property, plant and equipment		255,237	-	239,143	-
Tax on other comprehensive income		(76,571)	6,380	(71,743)	6,238
Translation difference for foreign operations		99,371	(140,053)	-	-
Total other comprehensive income for the year, net		278,037	(133,673)	167,400	6,238
Total comprehensive income for the year		1,596,376	1,258,111	1,211,778	1,325,373
Profit attributable to:					
Owners of the company		1,314,969	1,437,204	1,044,378	1,319,135
Non controlling interest		3,370	(45,420)	-	-
Profit for the year		1,318,339	1,391,784	1,044,378	1,319,135
Total comprehensive income attributable to:					
Owners of the company		1,544,893	1,305,616	1,211,778	1,325,373
Non controlling interest		51,483	(47,505)	-	-
Total comprehensive income for the year		1,596,376	1,258,111	1,211,778	1,325,373
Basic and diluted earnings per share (tambala)	30	56	62	-	-

The financial statements are to be read in conjunction with the notes from pages 27 to 83.

The independent auditor's report is on page 19.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

In thousands of Malawi Kwacha

	Share Capital	Share premium	Translation reserve	Property revaluation reserve	Investment revaluation reserve	Loan loss reserve	Retained earnings	Attributable to owners of the company	Non controlling interest	Total equity
GROUP										
Balance at 1 January 2008	111,250	514,035	(4,635)	389,906	1,489,897	66,606	2,054,586	4,621,645	229,721	4,851,366
Total comprehensive income for the year										
Profit for the year	-	-	-	-	-	-	1,437,204	1,437,204	(45,420)	1,391,784
Other Comprehensive income										
Depreciation on re-valued assets	-	-	-	(21,267)	-	-	21,267	-	-	-
Deferred tax on property revaluation	-	-	-	6,380	-	-	-	6,380	-	6,380
Arising on consolidation of subsidiary	-	-	(71,211)	-	-	-	-	(71,211)	(68,842)	(140,053)
Transfer from investment revaluation reserve	-	-	-	-	(313,244)	-	313,244	-	-	-
Transfer to loan loss reserve	-	-	-	-	-	559	(559)	-	-	-
Movement in loan loss reserve	-	-	-	-	-	(40,136)	40,136	-	-	-
Realised on disposals of shares	-	-	-	-	224,317	-	(224,317)	-	-	-
Total other comprehensive income	-	-	(71,211)	(14,887)	(88,927)	(39,577)	149,771	(64,831)	(68,842)	(133,673)
Total comprehensive income for the year	-	-	(71,211)	(14,887)	(88,927)	(39,577)	1,586,975	1,372,373	(114,262)	1,258,111
Transactions with owners, recorded directly in equity										
Contributions by and distributions to owners										
Non controlling interests' subscription for shares in subsidiary	-	-	-	-	-	-	-	-	196,804	196,804
Dividends to equity holders	-	-	-	-	-	-	(578,500)	(578,500)	-	(578,500)
Total Transactions with owners	-	-	-	-	-	-	(578,500)	(578,500)	196,804	(381,696)
Balance at 31 December 2008	111,250	514,035	(75,846)	375,019	1,400,970	27,029	3,063,061	5,415,518	312,263	5,727,781

The financial statements are to be read in conjunction with the notes from pages 27 to 83.
The independent auditor's report is on page 19.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

In thousands of Malawi Kwacha

	Share Capital	Share premium	Translation reserve	Property revaluation reserve	Investment revaluation reserve	Loan loss reserve	distributable reserve	Retained earnings	Attributable to owners of the company	Non controlling interest	Total equity
Balance at 1 January 2009 – restated *	111,250	514,035	(75,846)	375,019	1,400,970	27,029	-	3,063,061	5,415,518	312,263	5,727,781
Total comprehensive income for the year											
Profit for the year	-	-	-	-	-	-	-	1,314,969	1,314,969	3,370	1,318,339
Other Comprehensive income											
Deferred tax on property revaluation	-	-	-	(76,571)	14,832	-	-	(14,832)	(76,571)	-	(76,571)
Arising on consolidation of subsidiary	-	-	51,258	-	-	-	-	-	51,258	48,113	99,371
Transfer from investment revaluation reserve	-	-	-	-	(262,181)	-	-	262,181	-	-	-
Surplus on revaluation reserve of properties	-	-	-	255,237	-	-	-	-	255,237	-	255,237
Movement in loan loss reserve	-	-	-	-	-	6,377	-	(6,377)	-	-	-
Realised on disposals of shares	-	-	-	-	(25,995)	-	-	25,995	-	-	-
Total other comprehensive income	-	-	51,258	178,666	(273,344)	6,377	-	266,967	229,924	48,113	278,037
Total comprehensive income for the year	-	-	51,258	178,666	(273,344)	6,377	-	1,581,936	1,544,893	51,483	1,596,376
Transactions with owners, recorded directly in equity											
Contributions by and distributions to owners											
Dividends to equity holders	-	-	-	-	-	-	-	(600,751)	(600,751)	-	(600,751)
Dilution of minority interest on subscription	-		(1,939)	-	-	-	-	(1,269)	(3,208)	3,208	-
Non distributable reserve	-	-	-	-	-	-	350,000	(350,000)	-	-	-
Issue of shares	5,563	1,051,312	-	-	-	-	-	(1,056,875)	-	169,129	169,129
	5,563	1,051,312	(1,939)	-	-	-	350,000	(2,008,895)	(603,959)	172,337	(431,622)
Balance at 31 December 2009	116,813	1,565,347	(26,527)	553,685	1,127,626	33,406	350,000	2,636,102	6,356,452	536,083	6,892,535

* Restatement relates to the reclassification of translation differences arising on translation of the equity of Capital Bank Limited which had previously been attributed to non controlling interest.(Note 38)

The financial statements are to be read in conjunction with the notes from pages 27 to 83.

The independent auditor's report is on page 19.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

In thousands of Malawi Kwacha

COMPANY	Share capital	Share premium	Property revaluation reserve	Investment revaluation reserve	Loan loss reserve	Retained earnings	Total
Balance at 1 January 2008	111,250	514,035	364,183	1,489,897	57,034	1,768,226	4,304,625
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	1,319,135	1,319,135
Other comprehensive income							
Depreciation on revalued asset	-	-	(20,793)	-	-	20,793	-
Deferred tax on property revaluation	-	-	6,238	-	-	-	6,238
Movement in loan loss reserve	-	-	-	-	(40,136)	40,136	-
Realised on disposal of shares	-	-	-	224,317	-	(224,317)	-
Transfer from investment revaluation reserve	-	-	-	(313,244)	-	313,244	-
Total other comprehensive income	-	-	(14,555)	(88,927)	(40,136)	149,856	6,238
Total comprehensive income for the year	-	-	(14,555)	(88,927)	(40,136)	1,468,991	1,325,373
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Dividends paid	-	-	-	-	-	(578,500)	(578,500)
Balance at 31 December 2008	111,250	514,035	349,628	1,400,970	16,898	2,658,717	5,051,498

The financial statements are to be read in conjunction with the notes from pages 27 to 83.

The independent auditor's report is on page 19.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

In thousands of Malawi Kwacha

Share COMPANY	Share capital	Property revaluation premium	Investment revaluation reserve	Loan loss reserve	Retained reserve	earnings	Total
Balance at 1 January 2009	111,250	514,035	349,628	1,400,970	16,898	2,658,717	5,051,498
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	1,044,378	1,044,378
Other comprehensive income							
Surplus on revaluation of properties	-	-	239,143	-	-		239,143
Deferred tax on property revaluation	-	-	(71,743)	-	-	-	(71,743)
Deferred tax on revaluation of investments				14,832		(14,832)	-
Realised on disposal of shares	-	-	-	(25,995)	-	25,995	-
Transfer from investment revaluation reserve	-	-	-	(262,181)	-	262,181	-
Total other comprehensive income	-	-	167,400	(273,344)	-	273,344	167,400
Total comprehensive income for the year	-	-	167,400	(273,344)	-	1,317,722	1,211,778
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners	5,563	1,051,312	-	-	-	(1,056,875)	-
Dividends paid	-	-	-	-	-	(600,751)	(600,751)
Balance at 31 December 2009	116,813	1,565,347	517,028	1,127,626	16,898	2,318,813	5,662,525

The financial statements are to be read in conjunction with the notes from pages 27 to 83.

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CONSOLIDATED STATEMENTS OF CASH FLOWS

In thousands of Malawi Kwacha

	Note	GROUP 2009	GROUP 2008	COMPANY 2009	COMPANY 2008
CASH FLOWS FROM OPERATING ACTIVITIES					
Interest and fees received		5,539,419	3,952,450	3,940,551	3,294,370
Interest paid		(981,259)	(464,097)	(199,836)	(232,506)
Cash paid to suppliers and employees		(1,681,745)	(1,606,081)	(1,584,978)	(1,468,790)
		2,876,415	1,882,272	2,155,737	1,593,074
Increase/(decrease) in net customer balances		5,863,978	(838,271)	(368,321)	(2,668,663)
Cash generated from operations		8,740,393	1,044,001	1,787,416	(1,075,589)
Income taxes paid		(569,646)	(414,460)	(462,700)	(366,134)
Net cash from/(utilised in) operating activities		8,170,747	629,541	1,324,716	(1,441,723)
CASH FLOWS USED IN INVESTING ACTIVITIES					
(Purchases)/maturities of money market investments		(6,709,984)	(449,467)	(1,965,445)	1,795,665
Proceeds from sale of shares and other investments		27,177	384,684	27,177	384,684
Proceeds from sale of equipment		1,210	2,997	1,210	2,858
Acquisition of property and equipment	14	(617,774)	(495,468)	(521,589)	(299,521)
Acquisition of subsidiaries	13	-	-	(237,015)	(239,678)
Dividend received		68,239	66,245	68,239	66,245
Purchase of shares in listed companies	12	-	(77,077)	-	(77,077)
Net cash (used in)/from investing activities		(7,231,132)	(568,086)	(2,627,423)	1,633,176
CASH FLOWS TO FINANCING ACTIVITIES					
Increase in loans		220,500	-	220,500	-
Net proceeds of issue of shares		169,129	136,004	-	-
Dividend paid		(600,751)	(578,500)	(600,751)	(578,500)
Net cash used in financing activities		(211,122)	(442,496)	(380,251)	(578,500)
Net increase/(decrease) in cash and cash equivalents		728,493	(381,041)	(1,682,958)	(387,047)
Cash and cash equivalents at beginning of the year		4,401,956	4,782,997	3,976,178	4,363,225
Cash and cash equivalents at end of the period	7	5,130,449	4,401,956	2,293,220	3,976,178
ADDITIONAL STATUTORY DISCLOSURE					
Net movement in working capital		556,901	562,906	263,462	634,498

The financial statements are to be read in conjunction with the notes from pages 27 to 83.

The independent auditor's report is on page 19

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Reporting Entity

First Merchant Bank Limited is a public limited liability company incorporated in Malawi and is listed on the Malawi Stock Exchange. The consolidated financial statements as at and for the year ended 31 December 2009 comprise the Bank and its subsidiaries, The Leasing and Finance Company of Malawi Limited incorporated in Malawi, Capital Bank Limited incorporated in Botswana and FMB Forex Bureau Limited incorporated in Malawi (together referred to as the "Group"). The Group is involved in corporate and retail banking.

2. Basis of preparation

(i) Statement of compliance

The consolidated and separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB) and the provisions of the Malawi Companies Act 1984.

(ii) Basis of measurement

The consolidated and separate financial statements are prepared on the historical cost basis except for the following:

- land and buildings which are revalued;
- financial instruments at fair value through profit or loss are measured at fair value;
- available-for-sale financial assets are measured at fair value.

(iii) Functional and presentation currency

These consolidated and separate financial statements are presented in Malawi Kwacha, which is the Bank's functional and presentation currency. Except as indicated, financial information presented in Malawi Kwacha, has been rounded to the nearest thousand.

(iv) Use of estimates and judgements

The preparation of financial statements in conformity with IFRSs require management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in the following notes.

- Note 9 - Loans and advances to customers
- Note 10 - Finance leases
- Note 19 - Provisions - Severance pay liabilities.

3. Changes in accounting policies and new standards and interpretations not yet adopted

(a) Changes in accounting policies

With effect from 1 January 2009, the Group has changed its accounting policies in the following areas:

- Determination and presentation of operating segments
- Presentation of financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3. Changes in accounting policies and new standards and interpretations not yet adopted (cont'd)

Determination and presentation of operating segments

As of 1 January 2009 the Group determines and presents operating segments based on the information that is internally provided to the chief operating decision makers. This change in accounting policy is due to the adoption of IFRS 8 *Operating Segments*. The new accounting policy in respect of segment operating disclosures is presented as follows.

Comparative segment information has been re-presented in conformity with the transitional requirements of such standard. Since the change in accounting policy only impacts presentation and disclosure aspects, there is no impact on earnings per share.

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. An operating segment's operating results are reviewed regularly by the chief operating decision makers to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the chief operating decision makers include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly corporate assets (primarily the Company's headquarters), head office expenses, and income tax assets and liabilities.

Segment capital expenditure is the total cost incurred during the period to acquire property, plant and equipment, and intangible assets other than goodwill.

Presentation of financial statements

The Group applies revised IAS 1 *Presentation of Financial Statements* (2007), which became effective as of 1 January 2009. As a result, the Group presents in the consolidated statement of changes in equity all owner changes in equity, whereas all non-owner changes in equity are presented in the consolidated statement of comprehensive income.

Comparative information has been re-presented so that it is also in conformity with the revised standard. Since the change in accounting policy only impacts presentation aspects, there is no impact on earnings per share.

(b) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2009, and have not been applied in preparing these financial statements:

- Revised IFRS 3 *Business Combinations* (2008) incorporates the following changes:
  - The definition of a business has been broadened resulting in more acquisitions being treated as business combinations
  - All business combinations are accounted for by applying the acquisition method.
  - The acquirer can elect to measure any non-controlling interest at fair value at the acquisition date, or at its proportionate interest in the fair value of the identifiable assets and liabilities of the acquiree, on a transaction-by-transaction basis.
  - Subsequent recognition of deferred tax assets acquired in a business combination that did not satisfy the criteria for recognition at the acquisition date would be recognised in profit or loss.

  This standard applies prospectively to acquisitions with a date on or after the beginning of the first annual period beginning on or after 1 July 2009. This will have no impact on the company's financial statements.

- Amended IAS 27 *Consolidated and Separate Financial Statements* (2008) incorporates the following changes:

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3. Changes in accounting policies and new standards and interpretations not yet adopted (cont'd)

(b) New standards and interpretations not yet adopted (cont'd)

- Changes in a parent's ownership interest in a subsidiary after control is obtained that do not result in a loss of control are accounted for as equity transactions (i.e., transactions with owners in their capacity as owners). Accordingly, acquisitions of additional non-controlling interests are accounted for as equity transactions and disposals of equity interests while retaining control are accounted for as equity transactions;
- Transactions resulting in a loss of control would cause a gain or loss to be recognised in profit or loss; and
- Losses applicable to the non-controlling interests, including negative other comprehensive income, are allocated to non-controlling interests even if doing so causes the non-controlling interests to have a negative balance.

- This standard applies prospectively to acquisitions with a date on or after the beginning of the first annual period beginning on or after 1 July 2009. This will have no impact on the company's financial statements.

• Revised IFRS 1 *First-time Adoption of International Financial Reporting Standards* (2008)
  - The IASB issued a revised version of this standard with an improved structure but no changes to technical content. This is effective for period beginning on or after I July 2009. This will have no impact on the financial statements.

• Amended IAS 39– *Eligible Hedged Items*-Amendments clarify how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. This is effective for periods beginning on or after I July 2009. This will have no impact on the company's financial statements.

• IFRIC 17 *Distributions of Non-cash Assets to Owners* provides guidance in respect of distributions of non-cash assets to owners acting in their capacity as owners. Distributions within the scope of IFRIC 17 are measured at the fair value of the assets to be distributed. Any gain or loss on settlement of the liability for the dividend payable is recognised in profit or loss. The scope of IFRS 5 was expanded to include distributions of non-cash assets to owners. This is effective for period beginning on or after I July 2009 with prospective application. This will have no impact on the company's financial statements.

• Amended IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*
  The amendments specify that:
  - if an entity is committed to a plan to sell a subsidiary, then it would classify all of that subsidiary's assets and liabilities as held for sale when the held for sale criteria in paragraphs 6 to 8 of IFRS 5 are met; this applies regardless of the entity retaining an interest (other than control) in the subsidiary; and
  - disclosures for discontinued operations are required by the parent when a subsidiary meets the definition of a discontinued operation. If an entity applies the IFRS 5 amendments to periods beginning before 1 July 2009, then it also applies amended IAS 27 (2008) at the same time.
    The amendments apply prospectively from the date the entity first applied IFRS 5, subject to the transition requirements in paragraph 45 of IAS 27 (2008). This will have no impact on the company's financial statements.

• Amended IFRS 2 *Share-based Payments* and Revised IFRS 3 *Business Combinations* (2008) clarify that business combinations as defined in IFRS 3 (2008) are outside the scope of IFRS 2, notwithstanding that they may be outside the scope of IFRS 3. Therefore business combinations amongst entities under common control and the contribution of a business upon the formation of a joint venture will not be accounted for under IFRS 2. This is effective for period beginning on or after I July 2009. This will have no impact on the company's financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

- Amended IAS 38 *Intangible Assets* clarify that:

3. Changes in accounting policies and new standards and interpretations not yet adopted (cont'd)

(b) New standards and interpretations not yet adopted (cont'd)

- an intangible asset that is separable only together with a related contract, identifiable asset or liability is recognised separately from goodwill together with the related item; and
- complementary intangible assets with similar useful lives may be recognised as a single asset. The amendments also describe valuation techniques commonly used by entities when measuring the fair value of intangible assets acquired in a business combination for which no active market exists. These amendments apply prospectively for period beginning on or after I July 2009. Early application is required if IFRS 3 (2008) is adopted early. This will have no impact on the company's financial statements.

- IFRIC 9 *Reassessment of Embedded Derivatives* incorporates amendment to the scope so that embedded derivatives in contracts acquired in business combinations as defined in IFRS 3 (2008), joint venture formations and common control transactions remain outside the scope of IFRIC 9. This will have no impact on the company's financial statements.

- IFRIC 16 *Hedges of a Net Investment in a Foreign Operation*- The amendments remove the restriction that prevented a hedging instrument from being held by a foreign operation that itself is being hedged. These amendments apply prospectively for period beginning on or after I July 2009. This will have no impact on the company's financial statements.

- IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*- The amendments clarify that the required disclosures for non-current assets (or disposal groups) classified as held for sale or discontinued operations are specified in IFRS 5. The amendments apply prospectively for periods beginning on or after 1 January 2010. This will have no impact on the company's financial statements.

- Amended IFRS 8 *Operating Segment* -The amendments clarify that segment information with respect to total assets is required only if such information is regularly reported to the chief operating decision maker. The amendments apply for periods beginning on or after 1 January 2010. This will have no impact on the company's financial statements.

- Amended IAS 1 *Presentation of Financial Statements* -The amendments clarify that the classification of the liability component of a convertible instrument as current or non-current is not affected by terms that could, at the option of the holder of the instrument, result in settlement of the liability by the issue of equity instruments. The amendments apply for periods beginning on or after 1 January 2010. This will have no impact on the company's financial statements.

- Amended IAS 7 *Statement of Cash Flows* -The amendments clarify that only expenditures that result in the recognition of an asset can be classified as a cash flow from investing activities. The amendments apply for periods beginning on or after 1 January 2010. This will have no impact on the company's financial statements.

- Amended IAS 17 *Leases* -The amendments clarify that when a lease includes both the land and building elements, an entity should determine the classification of each element based on paragraphs 7 – 13 of IAS 17, taking account of the fact that land normally has an indefinite economic life. The amendments apply for periods beginning on or after 1 January 2010. This will have no significant impact on the company's financial statements.

- Amended IAS 36 *Impairment of Assets* -The amendments clarify that the largest unit to which goodwill should be allocated is the operating segment level as defined in IFRS 8 before applying the aggregation criteria of IFRS 8. The amendments apply prospectively for periods beginning on or after

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3. Changes in accounting policies and new standards and interpretations not yet adopted (cont'd)

(b) New standards and interpretations not yet adopted (cont'd)

1 January 2010. The company is currently in the process of evaluating the potential effect of this revision.

- Amended IAS 39 Financial Instruments: Recognition and Measurement -The amendments:
  - provide additional guidance on determining whether loan prepayment penalties result in an embedded derivative that needs to be separated;
  - clarify that the scope exemption in IAS 39 paragraph 2(g) is restricted to forward contracts, i.e., not options, between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination at a future acquisition date within a reasonable period normally necessary to obtain any required approvals and to complete the transaction; and
  - clarify that the gains or losses on a cash flow hedge should be reclassified from other comprehensive income to profit or loss during the period that the hedged forecast cash flows impact profit or loss. The amendments apply prospectively to all unexpired contracts from the date of adoption.

The amendments apply for periods beginning on or after 1 January 2010. This will have no impact on the company's financial statements.

- Amended IFRS 1 First-time Adoption of International Financial Reporting Standards – Additional Exemptions for First-time Adopters provide additional optional exemptions for first-time adopters of IFRSs that will:
  - permit entities not to reassess the determination of whether an arrangement contains a lease if the same assessment as that required by IFRIC 4 was made under previous GAAP; and
  - allow entities in the oil and gas industry to use their previous GAAP carrying amounts as deemed cost at the date of transition for oil and gas assets.

The amendments apply for periods beginning on or after 1 January 2010. The amendment will have no impact on the 2010 group's financial statements. This will have no impact on the company's financial statements.

- Amended IFRS 2 Share-based Payment – Group Cash-settled Share based Payment Transactions The amendment will require an entity receiving goods or services (receiving entity) in either an equity-settled or a cash-settled share-based payment transaction to account for the transaction in its separate or individual financial statements. This principle even applies if another group entity or shareholder settles the transaction (settling entity) and the receiving entity has no obligation to settle the payment. Retrospective application is subject to the transitional requirements in IFRS 2. This will have no impact on the company's financial statements.

- Amended IAS 32 Financial Instruments: Presentation – Classification of Rights Issues -The amendment will allow rights, options or warrants to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency to be classified as equity instruments provided the entity offers the rights, options or warrants pro rata to all of its existing owners of the same class of its own non-derivative equity instruments. The amendments apply for periods beginning on or after 1 February 2010. This will have no impact on the Bank's financial statements.

- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments This interpretation provides guidance on the accounting for debt for equity swaps. The amendments apply for periods beginning on or after 1 July 2010. This will have no impact on the company's financial statements.

- Revised IAS 24 Related Party Disclosures (2009) - The revised standard amends the definition of a related party and modifies certain related party disclosure requirements for government-related entities. The amendments apply for periods beginning on or after 1 July 2011. This will have no impact on the company's financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3. Changes in accounting policies and new standards and interpretations not yet adopted (cont'd)

(b) New standards and interpretations not yet adopted (cont'd)

- Amendments to IFRIC 14 IAS 19 – The Limit on a Defined Benefit Assets, Minimum Funding Requirements and their Interaction. These amendments remove unintended consequences arising from the treatment of prepayments where there is a minimum funding requirement. These amendments result in prepayments of contributions in certain circumstances being recognised as an asset rather than an expense. The amendments apply for periods beginning on or after 1 July 2011. This will have no impact on the company's financial statements.

- IFRS 9 Financial Instruments -IFRS 9 replaces IAS 39 and retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortised cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply. The amendments apply for periods beginning on or after 1 July 2013.Prior periods need not be restated if an entity adopts the standard for reporting periods beginning before 1 January 2012. This will have no impact on the company's financial statements.

4. Significant accounting policies

The accounting policies have been consistently applied by the group and are consistent with those used in the previous year.

(a) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and its subsidiaries, the Leasing and Finance Company of Malawi Limited, FMB Forex Bureau Limited and Capital Bank Limited (together referred to as 'the Group').

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are presently exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Uniform accounting policies have been applied throughout the Group.

(ii) Funds management

The Group manages and administers assets held in investment vehicles on behalf of investors. The financial statements of these entities are not included in these consolidated financial statements except when the Group controls the entity.

(iii) Transactions eliminated on consolidation

Intra-group balances and transactions and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

(b) Foreign currency

Foreign currency transactions

Transactions in foreign currencies are translated to Malawi Kwacha at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(b) Foreign currency (cont'd)

date are translated to Malawi Kwacha at the foreign exchange rate (mid-rate) ruling at the reporting date. Foreign exchange differences arising on translation are recognised in the statement of comprehensive income.

Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Malawi Kwacha at foreign exchange rates ruling at the dates the fair values were determined.

Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to Malawi Kwacha at exchange rates (mid-rate) ruling at the reporting date. The income and expenses of foreign operations are translated to Malawi Kwacha at average exchange rates during the year.

Exchange difference arising on the translation of the assets and liabilities of foreign operations are recognised directly in other comprehensive income. When a foreign operation is disposed of in part or in full, the relevant amount in the foreign currency translation reserve is transferred to profit or loss.

Foreign exchange gains or losses arising from monetary items receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely in the foreseeable future and which in substance is considered to from a part of the net investment in foreign operation, are recognised directly in the foreign currency translation reserve.

(c) Financial assets and liabilities

(i) Recognition

A financial asset or liability is initially measured at fair value plus (for an item not classified at fair value through profit or loss) transaction costs that are directly attributable to its acquisition or issue.

(ii) Derecognition

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group also derecognises certain assets when they are deemed to be uncollectible.

(iii) Offsetting

Financial assets and liabilities are set off and the net amount presented in the balance sheet when, and only when, the Group has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by accounting standards, or for gains and losses arising from a group of similar transactions within the Group's trading activity.

(iv) Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method applied to the difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(c) Financial assets and liabilities (cont'd)

(v) Fair value measurement

The determination of fair values of financial assets and financial liabilities is based on quoted market prices for financial instruments traded in active markets. For all other financial instruments fair value is determined by using valuation techniques. Valuation techniques include net present value techniques, the discounted cash flow method, comparison to similar instruments for which market observable prices exist and valuation models.

The value produced by a model or other valuation technique is adjusted to take into account a number of factors as appropriate because valuation techniques cannot appropriately reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to take into account model risks, bid-ask spreads, liquidity risks as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments measured at fair value on the statement of financial position.

When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in profit or loss on an appropriate basis over the life of the instrument but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

(vi) Identification and measurement of impairment

At each balance sheet date the Group assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the financial asset and that the loss event has an impact on the future cash flows from the asset that can be estimated reliably.

The Group considers evidence of impairment at both a specific financial asset and collective level. All individually significant financial assets are assessed for specific impairment. All significant assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Financial assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortised cost) with similar risk characteristics.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

In assessing collective impairment (if applicable) the Group uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on financial assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted the financial assets' original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and advances.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(c) Financial assets and liabilities (cont'd)

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised out of other comprehensive income to profit or loss. When a

subsequent event causes the amount of impairment loss on an available-for-sale debt security to decrease, the impairment loss is reversed through profit or loss.

However, any subsequent recovery in the fair value of an impaired available-for-sale security is recognised directly in other comprehensive income. Any changes in impairment provisions attributable to time value are reflected as a component of interest income.

vii Designation at fair value through profit or loss

The Group has designated financial assets and liabilities at fair value through profit or loss when either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis;
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise.

Investments in listed companies (see note 12) have been described at fair value through profits or loss.

(d) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents are measured at amortised cost in the statement of financial position.

(e) Other assets

Other financial assets are subsequently measured at amortised cost using the effective interest method less impairment losses.

Other assets comprise interbranch accounts, interest receivables, prepayments, staff advances and office assets.

(f) Loans receivables

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Group does not intend to sell immediately or in the near term.

When the Group purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date ("reverse repo or stock borrowing"), the arrangement is accounted for as a loan to the other party, and the underlying asset is not recognised in the Group's financial statements.

Loans and advances are initially measured at fair value, and subsequently measured at their amortised cost using the effective interest method.

(g) Investments

Investment securities are initially measured at fair value plus incremental direct transaction costs, for investments not at fair value through profit and loss. Subsequent to initial recognition investment securities are accounted for depending on their classification as either held-to-maturity, fair value through profit or loss, or available-for-sale.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(g) Investments (cont'd)

(i) Held-to-maturity

- Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that the Group has the positive intent and ability to hold to maturity, and which are not designated at fair value through profit or loss or available-for-sale.

- Held-to-maturity investments are measured at amortised cost using the effective interest method. Any sale or reclassification of a significant amount of held-to-maturity investments not close to their maturity would result in the reclassification of all held-to-maturity investments as available- for-sale,

and prevent the Group from classifying investment securities as held-to-maturity for the current and the following two financial years.

(ii) Fair value through profit or loss

The Group recognises some investment securities at fair value, with fair value changes recognised immediately in profit or loss as described in accounting policy (c).

(iii) Available for sale

Available-for-sale investments are non-derivative investments that are designed available for sale or are not classified as another category of financial assets. Unquoted available for sale securities whose fair value cannot be reliably measured, are measured at cost. All other available-for-sale investments are measured at fair value.

Interest income is recognised in profit or loss using the effective interest method. Dividend income is recognised in profit or loss when the group becomes entitled to the dividend. Foreign exchange gains or losses on available for sale debt security investments are recognised in profit or loss.

Fair value changes are recognised directly in other comprehensive income until the investment is sold or impaired and the balance is recognised in profit or loss.

(h) Investment in subsidiaries

Investments in subsidiaries are recognised at cost in the company financial statements less any impairment losses.

(i) Property and equipment

(i) Owned assets

Items of property and equipment are stated at cost except for freehold property and leasehold improvements which are stated at latest valuation less accumulated depreciation and impairment losses as described in accounting policy (k).

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, qualifying borrowing costs, the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and are recognised

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(g) Investments (cont'd)

net within other income in profit or loss. When revalued assets are sold, the amounts included in the revaluation reserve are transferred to retained earnings.

All properties are subject to revaluation every two years, with surpluses on revaluation being transferred to a non-distributable property revaluation reserve.

(ii) Subsequent expenditure

Expenditure incurred to replace a component of an item of property and equipment that is accounted for separately, including major inspection and overhaul expenditure is capitalised. Other subsequent expenditure is capitalised only when it is probable that the future economic benefits embodied within the part will flow to the entity and its costs can be measured reliably. All other expenditure is recognised in the

profit and loss as an expense as incurred.

(iii) Depreciation

Property and equipment are depreciated on a straight-line basis at rates that would reduce carrying amounts to their residual values, estimated at the date of purchase, over the initially anticipated useful lives of the assets. The group re-assesses the useful lives, the depreciation method and the residual values of the assets at each reporting date. Any changes in the useful lives, depreciation method or estimated residual values is accounted for prospectively as a change in accounting estimate in accordance with IAS 8: *Accounting policies changes in accounting estimates and errors*.

Depreciation is recognised in profit or loss.
The depreciation rates for the current and comparative period are:

• leasehold properties	2.5% (or period of lease if shorter)
• freehold properties	2.5%
• motor vehicles	25%
• furniture, fixtures and fittings, computers, office equipment	20%

Freehold land is not depreciated.

(j) Capital work in progress

Capital work in progress represent gross amount spent to date in carrying out work of a capital nature. It is measured at cost recognised to date.

Capital work in progress is presented as part of property and equipment in the balance sheet. If the project is completed the expenditure is capitalised to the relevant items of plant and equipment. Capital work in progress is not depreciated.

(k) Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups of assets. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the units on a pro rata basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(k) Impairment of non-financial assets (cont'd)

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

An impairment loss is recognised in profit or loss unless it concerns property carried at revalued amount in which case it is treated as a revaluation decrease. If the impairment loss exceeds the revaluation reserve in

respect of the impaired asset, the excess is recognised in profit or loss.

A reversal of an impairment loss is recognised in profit or loss, unless it relates to property carried at revalued amounts, in which case the excess of the reversal over the amount recognised in profit or loss is treated as a revaluation increase.

(l) Liabilities to customers and other banks

When the Group sells a financial asset and simultaneously enters into a "repo" or "stock lending" agreement to repurchase the asset (or a similar asset) at a fixed price on a future date, the arrangement is accounted for as a deposit, and the underlying asset continues to be recognised in the Group's financial statements.

Deposits are initially measured at fair value plus directly attributable transaction costs, and subsequently measured at their amortised cost using the effective interest method, except where the Group chooses to account for the financial liabilities at fair value through profit or loss.

(m) Provisions

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

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

(n) Other payables

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

(o) Share capital

Share issue costs

Incremental costs directly attributable to the issue of an equity instrument are deducted from the initial measurement of the equity instruments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(p) Employee benefits

(i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in profit or loss when they are due.

(ii) Other long-term employee benefits

The Group's net obligation in respect of long-term employee benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any related assets is deducted.

(iii) Short-term benefits

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

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(q) Net interest income

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability.

When calculating the effective interest rate, the Group estimates future cash flows considering all contractual terms of the financial instrument but not future credit losses.

The calculation of the effective interest rate includes all fees and points paid or received transaction costs and discounts or premiums that are an integral part of the effective interest rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Interest income and expense presented in the profit or loss include:
- interest on financial assets and liabilities at amortised cost on an effective interest rate basis
- interest on available-for-sale investment securities on an effective interest rate basis.

Interest income is suspended and hence not included in net interest income when the collection of loans becomes doubtful.

Income from leasing is included in net interest income as further described in accounting policy (s).

(r) Leases

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

(i) The group as a lessor

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

(ii) The group as a lessee

Rentals payable under operating leases are recognised in profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(s) Fees and commissions income

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, account service fees, investment management fees, sales commission, placement fees and syndication fees are recognised as the related services are performed.

(t) Income from investments

Income from investments includes dividend income and increase in fair value of investments.

Dividend income is recognised when the right to receive income is established. Usually this is the ex-dividend date for available for sale securities.

Increase in fair value of investments designated at fair value through profit or loss includes all realised and unrealised fair value changes.

(u) Other income

Other income includes rentals receivable and net gains on the sale of assets and is recognised on the accruals basis.

(v) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the profit or loss except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is recognised for all temporary differences. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current assets, and they relate to income taxes levied in the same tax authority on the same taxable entity, or on different entities but they intend to settle current liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(w) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Group by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding after adjusting for the effects of all dilutive potential ordinary shares.

(x) Financial guarantees

Financial guarantee contracts require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. Significant accounting policies (cont'd)

(x) Financial guarantees (cont'd)

These financial guarantee contracts are classified as insurance contracts as defined in IFRS 4 Insurance Contracts. A liability is recognised when it is probable that an outflow of resources embodying economic benefits will be required to settle the contract and a reliable estimate can be made of the amount of the obligation. The amount recognised is the best estimate of the expenditure required to settle the contract at the statement of financial position date. Where the effect of discounting is material, the liability is discounted. The discount rate used is a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(y) Determination of fair values

- The fair values of investments in the listed equities are derived from price ruling at reporting date.

- The fair values of properties are estimated by a qualified valuer on an open market value basis.

5. Financial risk management

The board of directors of the Bank has ultimate responsibility for the level of risk taken by the bank and accordingly they have approved the overall business strategies and significant policies of the bank, including those related to managing and taking risk. Senior management in the bank is responsible for implementing strategies in a manner that limits risks associated with each strategy and that ensures compliance with applicable rules and regulation, both on a long term and day to day basis. The bank has a risk management department, which is independent of those who accept risks in the bank. The risk management department is tasked to:-

- identify current and emerging risks
- develop risk assessment and measurement systems
- establish policies, practices and other control mechanisms to manage risks
- develop risk tolerance limits for senior management and board approval
- monitor positions against approved risk tolerance limits
- report results of risk monitoring to senior management and the board.

To ensure that risk management is properly explained to and understood by all business lines the board has established the following risk management policies:-

- Credit Risk Management Policy
- Liquidity Risk Management Policy
- Operational Risk Management Policy
- Capital Risk Management Policy
- Market Risk Policy
    - Other comprehensive income
    - Interest Rate
    - Foreign Exchange

5(a) Credit risk

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5. Financial risk management (cont'd)

5(a) Credit risk (cont'd)

Management of credit risk

The Boards of Directors of the Group have delegated responsibility for the management of credit risk to their Credit Committees to whom separate Credit departments report. The Credit Committees are responsible for oversight of credit risk, including:-

- Formulating credit policies, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- Establishing the authorisation structure for the approval and renewal of credit facilities. Authorisation limits are allocated to Branch Managers. Larger facilities require approval by Head Office Management, The Credit Committee or the Board of Directors as appropriate.

- Reviewing and assessing credit risk. The Credit Department assesses all credit exposures in excess of designated limits, prior to facilities being committed to customers by the branches concerned. Renewals and reviews of facilities are subject to the same review process.
- Limiting concentrations of exposure to counterparties, geographies and industries (for loans and advances), and by issuer, credit rating band, market liquidity and country (for investment securities).
- Reviewing compliance of business units with agreed exposure limits.

Exposure to credit risk
The Group's exposure to credit risk comprises loans and advances to customers and finance lease receivable analysed as follows:

	Group		Company	
	2009	2008	2009	2008
Standard (fully performing)	16,728,049	10,773,461	10,397,619	8,090,647
Past due but not impaired	796,557	431,870	194,984	217,358
Impaired	492,302	250,594	331,479	188,461
	18,016,908	11,455,925	10,924,082	8,496,466
Past due but not impaired loans and advances comprise:				
30-60 days	307,402	87,698	72,110	56,783
61-90 days	349,846	344,172	26,729	160,575
>90 days	139,309	-	96,145	-
	796,557	431,870	194,984	217,358
An estimate of the fair value of collateral held against loans and advances to customers is shown below:				
Against individually impaired				
Property	114,294	249,140	-	238,640
Others	74,596	10,945	-	4,595
Against past due but not impaired				
Property	874,794	1,107,121	614,390	324,928
Others	1,206,301	749,580	873,100	146,976
Against neither past due nor impaired				
Property	11,948,925	13,424,706	8,050,996	12,691,756
Others	22,399,680	7,677,197	17,057,425	5,157,849
	36,618,590	23,218,689	26,595,911	18,564,744

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5. Financial risk management (cont'd)

5(a) Credit risk (cont'd)

Impaired loans and securities

Impaired loans and securities are loans and securities for which the Bank determines that it is probable that it will be unable to collect all principal and/or interest due according to the contractual terms of the loan / securities agreements.

Past due but not impaired loans

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

Allowances for impairment

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

Impairment policy

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

The Bank monitors concentrations of credit risk by sector. An analysis of concentrations of credit risk at the reporting date is shown below:

Economic sector risk concentrations within the customer loan portfolio were as follows:

	Group		Company	
	2009	2008	2009	2008
Agriculture	2,860,457	1,454,200	2,698,311	1,317,940
Mining	71,006	20,614	71,006	20,614
Finance and Insurance	6,268,961	2,408,606	105,332	93,409
Construction	673,201	1,706,555	349,408	308,843
Manufacturing	1,898,602	336,794	1,822,713	1,644,098
Wholesale and retail	3,428,489	3,128,824	3,240,595	3,083,907
Tourism and leisure	-	238,810	-	238,810
Transport	1,181,497	1,073,277	1,093,114	929,729
Others	1,634,695	1,088,245	1,543,603	859,116
	18,016,908	11,455,925	10,924,082	8,496,466

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

5. Financial risk management (Cont'd)

5(a) Credit risk (Cont'd)

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Bank using internal credit ratings. The table below shows the credit quality by class of financial asset for credit risk related items, based on the Bank's credit rating system.

GROUP 2009 Credit quality	Performing Loans Standard	 Special Mention	Non - Performing Loans Sub-Standard	 Doubtful	 Loss	 Total	Security against impaired loans	Net impaired loans
Loans and advances to customers	172,270	1,049	1,287	-	-	174,606	188,890	-
Personal and Business Banking								
- Instalment sales and finance leases	2,845,179	-	-	44,034	103,956	2,993,169	-	-
- Other loans and advances	8,066,763	72,110	66,008	749,609	328,565	9,283,055	465,000	328,565
Corporate and Investment Banking								
- Corporate lending	5,119,644	385,002	58,518	2,914	-	5,566,078	-	-
Total recognised financial instruments	16,203,856	458,161	125,813	796,557	432,521	18,016,908	653,890	328,565

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Bank using internal credit ratings. The table below shows the credit quality by class of financial asset for credit risk related items, based on the Bank's credit rating system.

COMPANY 2009 Credit quality	Performing Loans Standard	 Special Mention	Non - Performing Loans Sub-Standard	 Doubtful	 Loss	 Total	Security against impaired loans	Net impaired loans
Loans and advances to customers								
Personal and Business Banking:								
- Other loans and advances	8,066,763	72,110	66,008	192,070	328,565	8,725,516	465,000	328,565
Corporate and Investment Banking								
- Corporate lending	2,195,652	-	-	2,914	-	2,198,566	-	-
Total recognised financial instruments	10,262,415	72,110	66,008	194,984	328,565	10,924,082	465,000	328,565

Financial risk management (Cont'd)

5(a) Credit risk (Cont'd)

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Bank using internal credit ratings. The table below shows the credit quality by class of financial asset for credit risk related items, based on the Bank's credit rating system.

GROUP 2008 Credit quality	Performing Loans Standard	 Special Mention	Non - Performing Loans Sub-Standard	 Doubtful	 Loss	Total	Security against impaired loans	Net impaired loans
Loans and advances to customers	880,984	-	-	-	-	880,984	-	-
Personal and Business Banking								
- Mortgage Lending	170,352	2	63,836	-	-	234,190	-	-
- Instalment sales and finance leases	1,768,661	30,913	101,822	17,939	62,303	1,981,638	16,850	45,458
- Other loans and advances	5,994,930	115,271	114,068	217,358	188,815	6,630,442	243,235	187,796
Corporate and Investment Banking								
- Corporate lending	1,619,286	108,890	-	-	495	1,728,671	-	495
Total recognised financial instruments	10,434,213	255,076	279,726	235,297	251,613	11,455,925	260,085	233,749

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Bank using internal credit ratings. The table below shows the credit quality by class of financial asset for credit risk related items, based on the Bank's credit rating system.

COMPANY 2008 Credit quality	Performing Loans Standard	 Special Mention	Non - Performing Loans Sub-Standard	 Doubtful	 Loss	Total	Security against impaired loans	Net impaired loans
Loans and advances to customers								
Personal and Business Banking:								
- Other loans and advances	6,132,283	115,271	114,068	217,358	188,815	6,767,795	243,235	187,796
Corporate and Investment Banking								
- Corporate lending	1,619,286	108,890	-	-	495	1,728,671	-	495
Total recognised financial instruments	7,751,569	224,161	114,068	217,358	189,310	8,496,466	243,235	188,291

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5(a) Credit risk (Continued)

Maximum exposure to credit risk without taking into account any collateral.

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

GROUP	Gross maximum exposure	
	2009	2008
Balances with central banks	491,858	186,101
Balances with other banks	2,267,281	1,410,615
Balance with foreign banks	1,172,346	2,506,277
Bank of Botswana Certificates	6,570,005	1,830,289
Money market investments	5,649,018	3,678,750
Personal and Business Banking		
- Mortgage Lending	-	234,190
- Instalment sales and finance leases	2,993,169	1,981,638
- Other loans and advances	8,905,356	6,630,442
Corporate and Investment Banking		
- Corporate lending	6,118,383	2,843,845
Total recognised financial instruments	34,167,416	21,302,147
Letters of credit	1,300,473	805,023
Financial guarantees	8,477,308	4,359,029
Total unrecognised financial instruments	9,777,781	5,164,052
Total credit risk exposure	43,945,197	26,466,199

Maximum exposure to credit risk without taking into account any collateral or other credit enhancements.

COMPANY	Gross maximum exposure	
	2009	2008
Balances with central banks	201,715	148,393
Balances with other banks	1,868	1,300,103
Balance with foreign banks	1,038,520	2,431,884
Money market investments	4,099,054	2,133,609
Personal and Business Banking		
- Other loans and advances	8,725,516	6,767,795
Corporate and Investment Banking		
- Corporate lending	2,198,566	1,728,671
Total recognised financial instruments	16,265,239	14,510,455
Letters of credit	1,217,733	805,023
Financial guarantees	4,931,944	4,153,553
Total unrecognised financial instruments	6,149,677	4,958,576
Total credit risk exposure	22,414,916	19,469,031

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

Financial risk management (Continued)

5(a) Credit risk (Continued)

Description of collateral held as security and other credit enhancements, in respect of the exposure above

The Bank holds mortgages over property, registered securities and guarantees as collateral within the following classes:

	Group		Company	
	2009	2008	2009	2008
Personal and Business Banking				
- Mortgage Lending	1,742,796	234,190	-	-
- Instalment sales and finance leases	3,299,555	1,981,639	-	-
- Other loans and advances	24,067,800	18,895,860	19,087,472	16,457,744
Corporate and Investment Banking				
- Corporate lending	7,508,439	2,107,000	7,508,439	2,107,000
	36,618,590	23,218,689	26,595,911	18,564,744

It is the Bank's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the Bank does not occupy repossessed properties for business use.

The Bank has no repossessed collateral.

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

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

GROUP	At 31 December 2009	
	Carrying amount	Net exposure to credit risk
Cash and balances with banks	1,190,279	1,190,279
Loans and advances to banks	2,249,348	2,249,348
Loans and advances to customers	15,023,739	15,023,739
	18,463,366	18,463,366

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5(a) Credit risk (Continued)

GROUP

	At 31 December 2008	
	Carrying amount	Net exposure to credit risk
Cash and balances with banks	2,521,437	1,907,498
Loans and advances to banks	1,395,455	1,395,455
Loans and advances to customers	9,240,096	9,240,096
	13,156,988	12,543,049

COMPANY

	At 31 December 2009	
	Carrying amount	Net exposure to credit risk
Cash and balances with banks	1,040,388	1,040,388
Loans and advances to customers	10,924,082	10,924,082
	11,964,470	11,964,470

	At 31 December 2008	
	Carrying amount	Net exposure to credit risk
Cash and balances with banks	2,431,987	2,431,987
Loans and advances to banks	1,300,000	1,300,000
Loans and advances to customers	8,496,466	8,496,466
	12,228,453	12,228,453

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk

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

Management of liquidity risk

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

The daily liquidity position is monitored and regular stress testing is done under normal and severe, market conditions. However, it is assumed that under normal circumstances customer demand deposits will remain stable or increase in value and unrecognised loan/ overdraft commitments are not expected to be immediately drawn down in their entirety.

All liquidity policies and procedures are subject to review and approval by the Asset Liability Committees (ALCO). These are management committees which meet once a month or more often if necessary. The daily monitoring of liquidity is the responsibility of an integrated treasury department which monitors the level of mismatches in the maturity positions of assets and liabilities. The maturity gap analyses as at 31 December 2009 and 31 December 2008 are given below:-

Asset and Liability Management Committee (ALCO)

The primary objective of the ALCO is to ensure a proper balance in terms of maturity profile, cost and yield, risk exposure etc. between funds mobilized and funds deployed. The ALCO seeks to manage risks in order to minimize the volatility of net interest income and protect the long term economic value of the Bank. The committee also monitors the capital adequacy of the Bank.

Key functions of the ALCO include setting pricing guidelines for assets and liabilities, setting limits and managing liquidity risk and interest rate risk and ensuring that contingency funding plans are in place to avert funding crises.

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

Group - 31 December 2009

	Carrying amount	Up to 1 month	1-3 months	3-6 months	6-12 months	1-3 years	Over 5 years	Gross Nominal inflow/ (outflow)
ASSETS								
Cash and cash equivalents	5,189,562	5,189,562	-	-	-	-	-	5,189,562
Money market investments	12,219,023	7,285,865	763,403	2,169,518	1,524,577	475,660	-	12,219,023
Loans, advances and leases	17,472,671	783,487	2,161,690	1,974,256	7,902,993	4,398,457	251,788	17,472,671
Investment in listed companies	1,312,969	-	-	-	-	1,312,969	-	1,312,969
Other assets	282,948	223,081	-	-	-	-	59,867	282,948
Total assets	36,477,173	13,481,995	2,925,093	4,143,774	9,427,570	6,187,086	311,655	36,477,173
LIABILITIES								
Current and savings account	(11,325,847)	(2,265,169)	-	-	-	-	(9,060,678)	(11,325,847)
Foreign currency accounts	(2,391,866)	(478,373)	-	-	-	-	(1,913,493)	(2,391,866)
Term deposit accounts	(14,177,381)	(4,868,091)	(2,188,071)	(5,486,269)	(1,630,554)	(4,396)	-	(14,177,381)
Total liabilities to customers	(27,895,094)	(7,611,633)	(2,188,071)	(5,486,269)	(1,630,554)	(4,396)	(10,974,171)	(27,895,094)
Balances due to other banks	(2,308,913)	(1,132,913)	-	-	-	-	(1,176,000)	(2,308,913)
Other payables	(980,983)	(980,983)	-	-	-	-	-	(980,983)
Total liabilities	(31,184,990)	(9,725,529)	(2,188,071)	(5,486,269)	(1,630,554)	(4,396)	(12,150,171)	(31,184,990)
Net Liquidity Gap	5,292,183	3,756,466	737,022	(1,342,495)	7,797,016	6,182,690	(11,838,516)	5,292,183
Cumulative Liquidity Gap	5,292,183	3,756,466	4,493,488	3,150,993	10,948,009	17,130,699	5,292,183	-

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

Group - 31 December 2008

	Carrying amount	Up to 1 month	1-3 months	3-6 months	6-12 months	1-3 years	Over 5 years	Gross Nominal inflow/ (outflow)
ASSETS								
Cash and cash equivalents	5,072,359	5,072,359	-	-	-	-	-	5,072,359
Money market investments	5,509,039	2,737,655	1,384,611	549,999	330,624	461,150	45,000	5,509,039
Loans, advances and leases	11,028,563	612,593	1,256,681	6,774,667	290,804	1,713,456	380,362	11,028,563
Investment in listed companies	1,602,650	-	-	-	-	1,602,650	-	1,602,650
Other assets	104,758	82,125	-	-	-	22,292	341	104,758
Total assets	23,317,369	8,504,732	2,641,292	7,324,666	621,428	3,799,548	425,703	23,317,369
LIABILITIES								
Current and savings account	(8,678,934)	(1,720,825)	-	-	-	-	(6,958,109)	(8,678,934)
Foreign currency accounts	(2,412,388)	(482,478)	-	-	-	-	(1,929,910)	(2,412,388)
Term deposit accounts	(6,022,345)	(2,332,926)	(3,051,182)	(545,864)	(92,373)	-	-	(6,022,345)
Total liabilities to customers	(17,113,667)	(4,536,229)	(3,051,182)	(545,864)	(92,373)	-	(8,888,019)	(17,113,667)
Balances due to other banks	(670,403)	(670,403)	-	-	-	-	-	(670,403)
Other payables	(1,030,854)	(1,030,854)	-	-	-	-	-	(1,030,854)
Total liabilities	(18,814,924)	(6,237,486)	(3,051,182)	(545,864)	(92,373)	-	(8,888,019)	(18,814,924)
Net Liquidity Gap	4,502,445	2,267,246	(409,890)	6,778,802	529,055	3,799,548	(8,462,316)	4,502,445
Cumulative Liquidity Gap	4,502,445	2,267,246	1,857,356	8,636,158	9,165,213	12,964,761	4,502,445	-

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

Company - 31 December 2009

	Carrying amount	Up to 1 month	1-3 months	3-6 months	6-12 months	1-3 years	Over 5 years	Gross nominal inflow/ (outflow)
ASSETS								
Cash and cash equivalents	2,352,333	2,352,333	-	-	-	-	-	2,352,333
Money market investments	4,099,054	755,278		1,343,539	1,524,577	475,660	-	4,099,054
Loans, advances and leases	10,483,801	1,515	1,568,834	1,408,358	6,535,998	969,096	-	10,483,801
Investment in listed companies	1,312,969	-	-	-	-	1,312,969	-	1,312,969
Investment in subsidiaries	785,968	-	-	-	-	-	785,968	785,968
Other assets	149,663	149,663	-	-	-	-	-	149,663
Total assets	19,183,788	3,258,789	1,568,834	2,751,897	8,060,575	2,757,725	785,968	19,183,788
LIABILITIES								
Current and savings account	(8,714,575)	(1,742,915)	-	-	-	-	(6,971,660)	(8,714,575)
Foreign currency accounts	(1,661,610)	(332,322)	-	-	-	-	(1,329,288)	(1,661,610)
Term deposit accounts	(1,231,792)	-	(1,101,210)	(130,582)	-	-	-	(1,231,792)
Total liabilities to customers	(11,607,977)	(2,075,237)	(1,101,210)	(130,582)	-	-	(8,300,948)	(11,607,977)
Deposits from other banks	(2,308,913)	(1,132,913)	-	-	-	-	(1,176,000)	(2,308,913)
Other payables	(914,275)	(914,275)	-	-	-	-	-	(914,275)
Total liabilities	(14,831,165)	(4,122,425)	(1,101,210)	(130,582)	-	-	(9,476,948)	(14,831,165)
Net Liquidity Gap	4,352,623	(863,636)	467,624	2,621,315	8,060,575	2,757,725	(8,690,980)	4,352,623
Cumulative Liquidity Gap	4,352,623	(863,636)	(396,012)	2,225,303	10,285,878	13,043,603	4,352,623	-

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5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

Company - 31 December 2008

	Carrying amount	Up to 1 month	1-3 months	3-6 months	6-12 months	1-3 years	Over 5 years	Gross nominal inflow/ (outflow)
ASSETS								
Cash and cash equivalents	4,646,581	4,646,581	-	-	-	-	-	4,646,581
Money market investments	2,133,609	850,252	777,207	-	-	461,150	45,000	2,133,609
Loans, advances and leases	8,131,407	172,225	1,058,602	6,669,635	-	91,454	139,491	8,131,407
Investment in listed companies	1,602,650	-	-	-	-	1,602,650	-	1,602,650
Investment in subsidiaries	548,953	-	-	-	-	-	548,953	548,953
Other assets	82,126	82,126	-	-	-	-	-	82,126
Total assets	17,145,326	5,751,184	1,835,809	6,669,635	-	2,155,254	733,444	17,145,326
LIABILITIES								
Current and savings account	(8,120,944)	(1,624,189)	-	-	-	-	(6,496,755)	(8,120,944)
Foreign currency accounts	(2,346,451)	(469,291)				-	(1,877,160)	(2,346,451)
Term deposit accounts	(1,072,118)	-	(1,040,077)	(32,041)	-	-	-	(1,072,118)
Total liabilities to customers	(11,539,513)	(2,093,480)	(1,040,077)	(32,041)	-	-	(8,373,915)	(11,539,513)
Deposits from other banks	(670,403)	(670,403)	-	-	-	-	-	(670,403)
Other payables	(874,587)	(874,587)	-	-	-	-	-	(874,587)
Total liabilities	(13,084,503)	(3,638,470)	(1,040,077)	(32,041)	-	-	(8,373,915)	(13,084,503)
Net Liquidity Gap	4,060,823	2,112,714	795,732	6,637,594	-	2,155,254	(7,640,471)	4,060,823
Cumulative Liquidity Gap	4,060,823	2,112,714	2,908,446	9,546,040	9,546,040	11,701,294	4,060,823	-

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

The table below summarises the remaining contractual maturities of the Bank's financial assets and liabilities based on undiscounted cash flows:

GROUP

2009	Redeemable on Demand	Maturing within 1month	Maturing after 1month but within 6 months	Maturing after 6 months but within 12 months	Maturing after 12 months but within 5 years	Total
Financial Assets						
Balances with central bank	-	491,858	-	-	-	491,858
Cheques in course of clearing	-	262,297	-	-	-	262,297
Cash balances	-	995,780	-	-	-	995,780
Bank of Botswana Certificates	-	6,025,301	544,704	-	-	6,570,005
Treasury Bills and LRGS	-	1,260,564	2,388,217	1,524,577	475,660	5,649,018
Loans and advances to banks	-	3,439,627	-	-	-	3,439,627
Loans and advances to customers	563,491	219,996	4,135,946	7,902,993	4,650,245	17,472,671
Investment in listed companies					1,312,969	1,312,969
	563,491	12,695,423	7,068,867	9,427,570	6,438,874	36,194,225
Financial Liabilities						
Deposits from customers	(3,863,553)	(3,748,080)	(7,674,340)	(1,630,554)	(10,978,567)	(27,895,094)
Balances due to other banks	-	(1,132,913)	-	-	(1,176,000)	(2,308,913)
	(3,863,553)	(4,880,993)	(7,674,340)	(1,630,554)	(12,154,567)	(30,204,007)
Total recognised financial instruments	(3,300,062)	7,814,430	(605,473)	7,797,016	(5,715,693)	5,990,218
Letters of credit	-	190,583	1,109,890	-	-	1,300,473
Financial guarantees	-	5,466,331	813,304	877,270	1,320,403	8,477,308
Total Unrecognised financial assets	-	5,656,914	1,923,194	877,270	1,320,403	9,777,781
Letters of credit	-	(190,583)	(1,109,890)			(1,300,473)
Financial guarantees	-	(5,466,331)	(813,304)	(877,270)	(1,320,403)	(8,477,308)
Total Unrecognised financial liabilities	-	(5,656,914)	(1,923,194)	(877,270)	(1,320,403)	(9,777,781)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

The table below summarises the remaining contractual maturities of the Bank's financial assets and liabilities based on undiscounted cash flows:

COMPANY

2009	Redeemable on Demand	Maturing within 1month	Maturing after 1month but within 6 months	Maturing after 6 months but within 12 months	Maturing after 12 months but within 5 years	Total
Financial Assets						
Balances with central bank	-	201,715	-	-	-	201,715
Cheques in course of clearing	-	262,297	-	-	-	262,297
Cash balances	-	847,933	-	-	-	847,933
Treasury Bills and LRGS	-	755,278	1,343,539	1,524,577	475,660	4,099,054
Loans and advances to banks	-	1,040,388	-	-	-	1,040,388
Loans and advances to customers	1,515	1,568,834	1,408,358	6,535,998	969,096	10,483,801
Investment in listed companies	-	-	-	-	1,312,969	1,312,969
	1,515	4,676,445	2,751,897	8,060,575	2,757,725	18,248,157
Financial Liabilities						
Deposits from customers	(2,075,237)	(1,101,210)	(130,582)	-	(8,300,948)	(11,607,977)
Balances due to other banks	-	(1,132,913)	-	-	(1,176,000)	(2,308,913)
	(2,075,237)	(2,234,123)	(130,582)	-	(9,476,948)	(13,916,890)
Total recognised fincial instruments	(2,073,722)	2,442,322	2,621,315	8,060,575	(6,719,223)	4,331,267
Letters of credit	-	107,843	1,109,890	-	-	1,217,733
Financial guarantees	-	1,920,967	813,304	877,270	1,320,403	4,931,944
Total Unrecognised financial assets	-	2,028,810	1,923,194	877,270	1,320,403	6,149,677
Letters of credit	-	(107,843)	(1,109,890)			(1,217,733)
Financial guarantees	-	(1,920,967)	(813,304)	(877,270)	(1,320,403)	(4,931,944)
Total Unrecognised financial liabilities	-	(2,028,810)	(1,923,194)	(877,270)	(1,320,403)	(6,149,677)

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

The table below summarises the remaining contractual maturities of the Bank's financial assets and liabilities based on undiscounted cash flows:

GROUP

2008 Restated	Redeemable on Demand	Maturing within 1month	Maturing after 1month but within 6 months	Maturing after 6 months but within 12 months	Maturing after 12 months but within 5 years	Total
Financial Assets						
Balances with central bank	37,708	148,393	-	-	-	186,101
Cheques in course of clearing	-	154,620	-	-	-	154,620
Cash balances	-	814,746	-	-	-	814,746
Bank of Botswana Certificates	-	1,830,291	-	-	-	1,830,291
Treasury Bills and LRGS	-	907,364	1,934,610	330,624	506,150	3,678,748
Loans and advances to banks	-	3,916,892	-	-	-	3,916,892
Loans and advances to customers	365,714	1,503,560	6,774,667	2,004,260	380,362	11,028,563
Investment in listed companies	-	-	-	-	1,602,650	1,602,650
	403,422	9,275,866	8,709,277	2,334,884	2,489,162	23,212,611
Financial Liabilities						
Deposits from customers	(13,871,946)	(48,028)	(2,554,664)	(113,861)	(525,168)	(17,113,667)
Balances due to other banks	-	(670,403)	-	-	-	(670,403)
	(13,871,946)	(718,431)	(2,554,664)	(113,861)	(525,168)	(17,784,070)
Total Recognised financial instruments	(13,468,524)	8,557,435	6,154,613	2,221,023	1,963,994	5,428,541
Letters of credit	-	805,023	-	-	-	805,023
Financial guarantees	-	296,439	1,097,369	1,183,763	1,781,458	4,359,029
Total Unrecognised financial assets	-	1,101,462	1,097,369	1,183,763	1,781,458	5,164,052
Letters of credit	-	(805,023)	-	-	-	(805,023)
Financial guarantees	-	(296,439)	(1,097,369)	(1,183,763)	(1,781,458)	(4,359,029)
Total Unrecognised financial liabilities	-	(1,101,462)	(1,097,369)	(1,183,763)	(1,781,458)	(5,164,052)

The summarises of the remaining contractual maturities of the Bank's financial assets and liabilities based on undiscounted cash flows for the year ended 31 December 2008 have been restated due to a correction of an error in prior year.

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

Analysis of financial assets and liabilities by remaining contractual maturities

The table below summarises the remaining contractual maturities of the Bank's financial assets and liabilities based on undiscounted cash flows:

COMPANY

2008 Restated	Redeemable on Demand	Maturing within 1month	Maturing after 1month but within 6 months	Maturing after 6 months but within 12 months	Maturing after 12 months but within 5 years	Total
Financial Assets						
Balances with central bank	-	148,393	-	-	-	148,393
Cheques in course of clearing	-	148,585	-	-	-	148,585
Cash balances	-	617,616	-	-	-	617,616
Treasury Bills and LRGS	-	850,252	777,207	-	506,150	2,133,609
Loans and advances to banks	-	3,731,987	-	-	-	3,731,987
Loans and advances to customers	-	172,225	1,058,601	6,669,636	230,945	8,131,407
Investment in listed companies	-				1,602,650	1,602,650
	-	5,669,058	1,835,808	6,669,636	2,339,745	16,514,247
Financial Liabilities						
Deposits from customers	(10,435,354)	-	(1,072,118)	(32,041)	-	(11,539,513)
Balances due to other banks	-	(670,403)	-	-	-	(670,403)
	(10,435,354)	(670,403)	(1,072,118)	(32,041)	-	(12,209,916)
Total recognised financial instruments	(10,435,354)	4,998,655	763,690	6,637,595	2,339,745	4,304,331
Letters of credit	-	805,023	-	-	-	805,023
Financial guarantees	-	90,963	1,097,369	1,183,763	1,781,458	4,153,553
Total Unrecognised financial assets	-	895,986	1,097,369	1,183,763	1,781,458	4,958,576
Letters of credit	-	(805,023)	-	-	-	(805,023)
Financial guarantees	-	(90,963)	(1,097,369)	(1,183,763)	(1,781,458)	(4,153,553)
Total Unrecognised financial liabilities	-	(895,986)	(1,097,369)	(1,183,763)	(1,781,458)	(4,958,576)

The summarises of the remaining contractual maturities of the Bank's financial assets and liabilities based on undiscounted cash flows for the year ended 31 December 2008 have been restated due to a correction of an error in prior year.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (b) Liquidity risk (Continued)

The previous table shows the undiscounted cash flows on the group's financial assets and liabilities on the basis of their expected maturities as opposed to their earliest possible contractual maturity. Out of these, 20% are demand deposits and overdrafts, and are classified in the up to one month category with the balance in the over 5 years category as the Group's expected cash flows on these instruments varies significantly from their contractual maturity profile.

The Reserve Bank of Malawi has issued the following guidelines on the management of liquidity:

- Liquidity Ratio 1: Net liquidity (total liquid assets less suspense accounts in foreign currency) divided by total deposits must be at least 30 percent.

- Liquidity Ratio 2: Net liquidity (total liquid assets less suspense account in foreign currency and cheques in the course of collection) divided by total deposits must be at least 20 percent.

- Liquidity Ratios 1 and 2 were as specified below:-

First Merchant Bank Limited	31 December 2009	31 December 2008 Restated
Liquidity Ratio I	53.38%	49.99%
Liquidity Ratio II	50.74%	48.37%
The Leasing and Finance Company of Malawi Limited		
Liquidity Ratio I	53.00%	49.01%
Liquidity Ratio II	53.00%	49.04%
Capital Bank Limited		
Liquidity Ratio I	72.48%	85.47%
Liquidity Ratio II	72.48%	85.21%

The liquidity ratios for Capital Bank Limited have been restated as a result of a correction of an error in the prior year calculation.

5 (c) Operational risks

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the group's processes, personnel, technology and infrastructure and from external factors other than credit, liquidity, interest rate and market risks such as those arising from legal and regulatory requirements and the requirement to observe generally accepted standards of corporate behaviour. Operational risks arise from all of the bank's operations.

The objective of the group is to manage operational risks so as to balance the avoidance of financial losses and damages to the bank's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each branch. The responsibility is supported by the development of overall standards in the group for the management of operational risks in the following areas:-

- requirements for appropriate segregation of duties, including the independent authorisation of transactions
- requirements for the reconciliation and monitoring of transactions
- compliance with regulatory and other legal requirements
- documentation of controls and procedures

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (c) Operational risks (Continued)

- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified
- requirements for the reporting of operational losses and proposed remedial action
- development of contingency plans
- training and professional development
- ethical and business standards

Compliance with group standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the relevant Audit Committee.

5 (d) Capital management

Reserve Bank of Malawi sets and monitors the capital requirements for the group and requires the bank to maintain a minimum of 6 percent and 10 percent for core and total capital respectively. These requirements have remained consistent from prior year. The group's regulatory capital is analysed in two parts:-

- Tier I capital, which includes paid-up share capital, share premium, retained earnings, and other reserves less investment in subsidiaries
- Tier II capital, which includes investment revaluation reserve, property revaluation reserve and loan loss reserve.

The calculation of both the above ratios is given below:-

	Group		Company	
	2009	2008	2009	2008
Tier 1 capital		Restated		Restated
Share capital	116,813	111,250	116,813	111,250
Share premium	1,565,347	514,035	1,565,347	514,035
Retained earnings	2,636,103	3,065,062	2,318,813	2,658,717
Investment in unconsolidated subsidiaries	-	-	(785,968)	(548,953)
Investment in equities of financial institutions	(50,947)	(50,947)	(50,947)	(50,947)
	4,267,316	3,637,400	3,164,058	2,684,102
Tier 2 capital				
Reserves	2,038,190	1,727,172	1,661,552	1,767,496
Total regulatory capital	6,305,506	5,364,572	4,825,610	4,451,598
Risk weighted assets	28,291,944	17,530,828	15,961,935	13,768,802
Capital ratios				
Tier 1 capital expressed as a percentage of total risk-weighted assets	15.08	20.75	19.82	19.49
Total capital expressed as a percentage of total risk weighted assets.	22.29	30.60	30.23	32.33

Bank of Botswana sets and monitors the capital requirements for the Capital Bank Limited and requires the bank to maintain a minimum of 15 percent of risk weighted assets. The Bank's regulatory capital is analysed into two parts:-

- Tier I capital, which includes paid-up share capital, share premium, retained earnings, and other reserves less investment in subsidiaries
- Tier II capital, which includes investment revaluation reserve, property revaluation reserve and loan loss reserve.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (e) Market risk management policy

Market risk is the risk that changes in market prices, such as interest rates, foreign exchange rates and other available for sale financial assets prices will affect the group income or the value of its holding of financial instruments. The objective of the group's market risk management policy is to manage and control market risk exposures within acceptable parameters while optimizing the return on risk.

Investments in shares

The Board of Directors sets and regularly reviews exposure limits for investment in equity instruments. The performance of the equity market in general and the group's equity investments in particular are closely monitored and appropriate risk mitigation measures are implemented where necessary.

The group measures its investment in equities at fair value, with fair value changes recognized immediately in accordance with accounting policy (g).

Interest Rate Risk

Interest rate risk is the exposure of group's financial condition to adverse movements in interest rates. It basically arises from timing differences in the maturity of re-pricing of the group's assets and liabilities. Changes in interest rates can have adverse effects on the group's earnings and its economic value. The relevant Asset and Liability Committee (ALCO) monitors interest rate risk in the group. Interest rate sensitivity analysis as on the reporting date are set out below:-

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (e) Market risk management policy (Continued)

GROUP

31 December 2009	Zero rate	Floating rate	Fixed Rate Instruments 0-3 months	3-6 months	6-9 months	9-12 months	Over 12 months	Total
Total assets	8,978,724	17,472,671	7,753,732	2,465,054	200,055	1,324,522	475,660	38,670,418
Total liabilities and shareholders funds	8,466,411	20,640,121	2,188,071	5,486,269	1,630,554	252,409	6,583	38,670,418
Interest sensitivity gap	512,313	(3,167,450)	5,565,661	(3,021,215)	(1,430,499)	(1,072,113)	469,077	-
Impact on profit of increase of interest rate								
1%	-	17,223	286	12,210	(1,359)	10,721	4,691	43,772
2%	-	34,446	573	24,419	(2,719)	21,442	9,382	87,543
3%	-	51,670	858	36,629	(4,079)	32,164	14,072	131,314
Impact on profit of decrease of interest rate								
1%	-	(53,048)	(286)	(12,210)	1,359	(10,721)	(4,691)	(79,597)
2%	-	(158,538)	(573)	(24,419)	2,719	(21,442)	(9,382)	(211,635)
3%	-	(264,028)	(858)	(36,629)	4,079	(32,164)	(14,072)	(363,672)

GROUP

31 December 2008	Zero rate	Floating rate	Fixed Rate Instruments 0-3 months	3-6 months	6-9 months	9-12 months	Over 12 months	Total
Total assets	3,034,108	4,819,731	3,211,487	2,656,409	7,081,167	461,150	3,637,770	24,901,822
Total liabilities and shareholders funds	6,774,953	12,118,354	5,369,465	543,698	54,684	40,668	-	24,901,822
Interest sensitivity gap	(3,740,845)	(7,298,623)	(2,157,978)	2,112,711	7,026,483	420,482	3,637,770	-
Impact on profit of increase of interest rate								
1%	-	(72,986)	(21,580)	21,127	70,265	4,205	36,378	37,408
2%	-	(145,972)	(43,160)	42,254	140,530	8,410	72,755	74,817
3%	-	(218,959)	(64,739)	63,381	210,794	12,614	109,133	112,225
Impact on profit of decrease of interest rate								
1%	-	72,986	21,580	(21,127)	(70,265)	(4,205)	(36,378)	(37,408)
2%	-	145,972	43,160	(42,254)	(140,530)	(8,410)	(72,755)	(74,817)
3%	-	218,959	64,739	(63,381)	(210,794)	(12,614)	(109,133)	(112,225)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (e) Market risk management policy (Continued)

COMPANY
31 December 2009

	Zero rate	Floating rate	Fixed Rate Instruments 0-3 months	3-6 months	6-9 months	9-12 months	Over 12 months	Total
Total assets	6,388,477	10,483,801	755,278	1,343,539	200,055	1,324,522	475,660	20,971,332
Total liabilities and shareholders funds	7,054,442	12,685,098	1,101,210	130,582	-	-	-	20,971,332
Interest sensitivity gap	(665,965)	(2,201,297)	(345,932)	1,212,957	200,055	1,324,522	475,660	-
Impact on profit of increase of interest rate								
1%	-	1,076	(3,027)	7,581	2,001	13,245	4,757	25,633
2%	-	2,152	(6,054)	15,162	4,001	26,490	9,513	51,265
3%	-	3,228	(9,081)	22,743	6,002	39,736	14,270	76,898
Impact on profit of decrease of interest rate								
1%	-	(36,901)	3,027	(7,581)	(2,001)	(13,245)	(4,757)	(61,458)
2%	-	(126,244)	6,054	(15,162)	(4,001)	(26,490)	(9,513)	(175,357)
3%	-	(215,586)	9,081	(22,743)	(6,002)	(39,736)	(14,270)	(289,255)

COMPANY

31 December 2008

	Zero rate	Floating rate	Fixed Rate Instruments 0-3 months	3-6 months	6-9 months	9-12 months	Over 12 months	Total
Total assets	3,192,195	1,598,112	1,021,145	1,835,409	6,669,636	461,150	3,637,770	18,415,417
Total liabilities and shareholders funds	6,205,501	11,137,798	1,040,077	32,041	-	-	-	18,415,417
Interest sensitivity gap	(3,013,306)	(9,539,686)	(18,932)	1,803,368	6,669,636	461,150	3,637,770	-
Impact on profit of increase of interest rate								
1%	-	(95,397)	(189)	18,034	66,696	4,612	36,378	30,133
2%	-	(190,794)	(379)	36,067	133,393	9,223	72,755	60,266
3%	-	(286,191)	(568)	54,101	200,089	13,835	109,133	90,399
Impact on profit of decrease of interest rate								
1%	-	95,397	189	(18,034)	(66,696)	(4,612)	(36,378)	(30,133)
2%	-	190,794	379	(36,067)	(133,393)	(9,223)	(72,755)	(60,266)
3%	-	286,191	568	(54,101)	(200,089)	(13,835)	(109,133)	(90,399)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (e) Market risk management policy (Continued)

Effective interest rates of financial assets and liabilities

The effective interest rates for the principal financial assets and liabilities at 31 December 2009 and 2008 were in the following ranges:-

	2009	2008
	%	%
Assets:		
Government securities		
	7.14 – 11.2	13.15-16.93
Deposits with banking institutions	0.50 – 8.00	0.25-2.5
Loans and advances to customers (base rate)	19.50	19.5
Liabilities:		
Customer deposits	0.50 - 10	0.25-11.0

Foreign Exchange Rate Risk Management

The responsibilities of the Integrated Treasury Department include monitoring of foreign exchange risk. Foreign exchange rate risk is the potential impact of adverse currency rates movements on earnings and economic value. This involves the risks of the group incurring financial loss on settlement of foreign exchange positions taken in both the trading and banking books. The foreign exchange positions arise from the following activities:-

- Trading in foreign currencies through spot, forward and option transactions as a market maker or position taker, including the unhedged position arising from customer driven foreign exchange transactions.
- holding foreign currency position in the bank books (e.g. in the form of loans, deposits, cross border investments, etc)
- Engaging in derivative transactions that are denominated in foreign currency for trading or hedging purposes.

The treasury department is responsible for:-

- Setting the foreign exchange risk management strategy and tolerance levels.
- Ensuring that effective risk management systems and internal controls are in place.
- Monitoring significant foreign exchange exposure.
- Ensuring that foreign exchange operations are supported by adequate management information systems which complement the risk management strategy
- Reviewing the policies, procedures and currency limits regularly in line with changes in the economic environment.

The ALCO regularly monitors the controls put in place by the treasury department, which are approved and reviewed by the board from time to time.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

5. Financial risk management (Continued)

5 (e) Market risk management policy (Continued)

The group does not perform a sensitivity analysis on its foreign exchange exposure but manages its foreign exchange risk mainly by hedging assets in foreign exchange with liabilities in foreign exchange. The group's foreign exchange exposures at the reporting date were as follows:

GROUP	2009			2008		
	Assets	Liabilities	Net	Assets	Liabilities	Net
USD	41,184	37,231	3,953	21,736	13,952	7,784
GBP	3,979	3,341	638	2,612	2,178	434
EUR	4,222	3,525	697	4,140	1,513	2,627
ZAR	9,853	2,643	7,210	20,008	9,162	10,846
INR	81	-	81	-	-	-
JPY	319	-	319	-	-	-
COMPANY						
USD	13,477	10,512	2,965	17,845	12,122	5,723
GBP	993	671	322	1,764	1,582	182
EUR	2,027	1,502	525	3,224	952	2,272
ZAR	7,718	776	6,942	19,336	8,639	10,697

5 (f) Compliance risk

The office of Compliance Officer is an independent core risk management activity, which also has unrestricted access to the managing director and the chairman of the board. The Bank is subject to extensive supervisory and regulatory regimes, and the executive management remains responsible for overseeing the management of the bank's compliance risk.

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

The management of compliance risk has become a distinct discipline within the Bank's overall risk management framework. Ultimate responsibility for this risk lies with the Board of Directors. A combination of key activities are undertaken to manage the risk such as identifying the regulatory universe and developing compliance management plans, training staff and other stakeholders on relevant regulatory requirements, and monitoring compliance. Compliance with the Know-Your-Customer and Anti-money Laundering procedures and legislation became an area of major focus for the Bank especially in 2008. The Bank has a dedicated Money Laundering Control Officer who consults the country's newly established Financial Intelligence Unit on money laundering and anti-terrorist financing matters.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

6. Financial assets and liabilities

The estimated fair values of the group's financial assets and liabilities are summarised below:-

	Group		Company	
	2009	2008	2009	2008
Financial assets				
Cash and cash equivalents	5,189,562	5,072,359	2,352,333	4,646,581
Money market investments	12,219,023	5,509,039	4,099,054	2,133,609
Loans and advances to customers	14,583,458	8,875,037	10,483,801	8,131,407
Finance lease receivables	2,889,213	2,153,526	-	-
Investment in listed companies	1,312,969	1,602,650	1,312,969	1,602,650
	36,194,225	23,212,611	18,248,157	16,514,247
Financial liabilities				
Deposits from banks	2,308,913	670,403	2,308,913	670,403
Deposits from customers	27,895,094	17,113,667	11,607,977	11,539,513
	30,204,007	17,784,070	13,916,890	12,209,916

In the opinion of directors, the fair values of the group's financial assets and liabilities approximate the respective carrying amounts, due to the generally short period to contractual repricing or maturity dates. Fair values are based on discounted cash flows using a discount rate based upon the borrowing rate that directors expect would be available to the group at the balance sheet date.

7. Cash and cash equivalents

	Group		Company	
	2009	2008	2009	2008
Liquidity Reserve Deposits:				
- Central Banks	491,858	186,101	201,715	148,393
Placements with other banks	2,249,348	1,395,455	-	1,300,000
Balances with banks abroad	1,172,346	2,506,277	1,038,520	2,431,884
Balances with local banks	17,933	15,160	1,868	103
Cheques in course of clearing	262,297	154,620	262,297	148,585
Cash balances	995,780	814,746	847,933	617,616
Total cash and cash equivalents	5,189,562	5,072,359	2,352,333	4,646,581
Balances due to banks abroad (17)	(59,113)	(670,403)	(59,113)	(670,403)
Cash and cash equivalents as per statement of cash flows	5,130,449	4,401,956	2,293,220	3,976,178

8. Money market investments

Bank of Botswana Certificates	6,570,005	1,830,291	-	-
Malawi Government Treasury Bills	5,504,018	3,533,748	3,954,054	1,988,609
Local Registered Stocks	145,000	145,000	145,000	145,000
	12,219,023	5,509,039	4,099,054	2,133,609

The interest rate on local registered stock approximates the market interest rate and hence the carrying amount approximates the fair value. All money market investments mature between 2 and 12 months except for local registered stocks which mature after 12 months.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

9. Loans and advances to customers

	Group		Company	
	2009	2008	2009	2008
Loans and advances are receivable as follows:				
Maturing within 3 months	2,829,575	225,540	1,570,349	175,912
Maturing between 3 and 12 months	9,894,002	8,770,508	8,384,636	8,089,439
Maturing after 12 months	2,300,162	244,048	969,097	231,115
	15,023,739	9,240,096	10,924,082	8,496,466
Segmental analysis by industry:				
Agriculture	2,860,457	1,454,200	2,698,311	1,317,940
Mining	71,006	20,614	71,006	20,614
Finance and insurance	3,275,792	192,777	105,332	93,409
Construction	673,201	1,706,555	349,408	308,843
Manufacturing	1,898,602	336,794	1,822,713	1,644,098
Wholesale and retail	3,428,489	3,128,824	3,240,595	3,083,907
Tourism and leisure	-	238,810	-	238,810
Transport	1,181,497	1,073,277	1,093,114	929,729
Others	1,634,695	1,088,245	1,543,603	859,116
	15,023,739	9,240,096	10,924,082	8,496,466
Specific allowances for impairment:				
Balance at 1 January	(210,717)	(189,810)	(210,717)	(189,810)
Charge for the year	(108,771)	(106,268)	(108,771)	(106,268)
Write offs	8,662	7,767	8,662	7,767
Recoveries	113,920	77,594	113,920	77,594
Balance at 31 December	(196,906)	(210,717)	(196,906)	(210,717)
Interest in suspense:				
Balance at 1st January	(154,342)	(101,782)	(154,342)	(101,782)
Charge for the year	(89,033)	(52,560)	(89,033)	(52,560)
Balance at 31st December	(243,375)	(154,342)	(243,375)	(154,342)
Net loans and advances	14,583,458	8,875,037	10,483,801	8,131,407

The directors consider that the carrying amount of loans and advances approximates to their fair value. Impairment of loans and advances has been calculated as disclosed in note 5a.

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10. Finance leases

	Group		Company	
	2009	2008	2009	2008
Investment in finance leases, receivable:				
Less than one year	650,092	525,484	-	-
Between one and five years	2,195,087	1,679,641	-	-
More than five years	147,990	10,704	-	-
Balance at 31 December	2,993,169	2,215,829	-	-
Specific allowances for impairment:				
Balance at 1 January	(45,458)	(19,360)	-	-
Charge for the year	(20,843)	(29,419)	-	-
Writeoffs	5,263	1,059	-	-
Recoveries	455	2,262	-	-
Balance at 31 December	(60,583)	(45,458)	-	-
Unearned finance income:				
Balance at 1 January	(16,845)	(6,978)	-	-
Charge for the year /recoveries	(26,528)	(9,867)	-	-
Balance at 31 December	(43,373)	(16,845)	-	-
Net finance lease receivables	2,889,213	2,153,526	-	-

The directors consider that the carrying amount of lease receivables approximates to their fair value.

11. Other assets

	Group		Company	
	2009	2008	2009	2008
Items in transit	4,383	215	4,383	215
Interest receivable	14,860	14,378	14,860	14,378
Prepayments	16,461	13,511	9,453	1,520
Stock of consumable stationery	32,328	30,173	29,768	28,770
FMB Forex Bureau Limited	-	-	8,672	-
Clearing accounts	122,161	-	-	-
Others	92,754	46,481	82,527	37,243
	282,947	104,758	149,663	82,126

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12. Investments in listed companies

	Group and Company			
	2009		2008	
	Valuation	Cost	Valuation	Cost
Balance brought forward	1,602,650	186,847	1,625,683	127,990
Shares bought during the year	-	-	77,077	77,077
(Decrease)/increase in fair value	(262,181)	-	231,354	-
Shares disposed	(27,500)	(1,505)	(331,464)	(18,220)
	1,312,969	185,342	1,602,650	186,847

All investments in quoted companies are held for trading. The increase in fair value is taken to income statement. The investments have been designated at fair value through profit and loss upon initial recognition.

13. Investment in subsidiaries

	Shareholding		Company	
At cost	2009	2008	2009	2008
		Restated		
The Leasing and Finance Company of Malawi Limited	100%	100%	65,911	65,911
Capital Bank Limited	53.76%	52.64%	710,057	483,042
FMB Forex Bureau Limited	100%	100%	10,000	-
Total investment in subsidiaries			785,968	548,953
Movement during the year:				
Balance at 1 January			548,953	309,275
FMB Forex Bureau Limited			10,000	-
Increase in shareholding of Capital Bank Limited			227,015	239,678
Balance at 31 December			785,968	548,953

The shareholding percentage in Capital Bank Limited has been restated due to correction of an error in the computation in prior year.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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14. Property and equipment

GROUP	Freehold property	Leasehold improvements	Motor vehicles	Equipment fixture & fittings	Capital work in progress	Total
Cost or valuation						
Balance at 1 January 2008	465,343	403,812	64,561	674,608	64,449	1,672,773
Additions	245	-	54,880	327,188	113,155	495,468
Transfers	-	20,035	-	63,847	(83,882)	-
Disposals	-	-	(4,390)	(1,232)	(7,214)	(12,836)
Impairments	-	-	-	(56,240)	(10,706)	(66,946)
Balance at 31 December 2008	465,588	423,847	115,051	1,008,171	75,802	2,088,459
Accumulated depreciation and impairment losses						
Balance at 1 January 2008	-	-	36,959	419,916	-	456,875
Charge for the year	10,223	9,841	15,613	117,366	-	153,043
Released on disposals	-	-	(4,389)	(1,150)	-	(5,539)
Balance at 31 December 2008	10,223	9,841	48,183	536,132	-	604,379
Cost or valuation						
Balance at 1 January 2009	465,588	423,847	115,051	1,008,171	75,802	2,088,459
Additions	7,115	9,707	22,052	305,036	273,864	617,774
Transfers	-	24,328	-	66,181	(90,509)	-
Revaluation surplus	152,390	61,813	-	-	-	214,203
Retranslation gain/(loss)	-	-	19	21,592	-	21,611
Disposals	-	-	-	(1,201)	-	(1,201)
Impairments	-	-	-	(982)	(29,602)	(30,584)
Balance at 31 December 2009	625,093	519,695	137,122	1,398,797	229,555	2,910,262
Accumulated depreciation and impairment losses						
Balance at 1 January 2009	10,223	9,841	48,183	536,132	-	604,379
Charge for the year	10,489	10,481	21,218	233,707	-	275,895
Eliminated on revaluation	(20,712)	(20,322)	-	-	-	(41,034)
Released on disposals	-	-	-	(950)	-	(950)
Balance at 31 December 2009	-	-	69,401	768,889	-	838,290
Carrying amount						
At 31 December 2009	625,093	519,695	67,721	629,908	229,555	2,071,972
At 31 December 2008	455,365	414,006	66,868	472,039	75,802	1,484,080

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14. Property, plant and equipment (Continued)

COMPANY	Freehold property	Leasehold improvements	Motor vehicles	Equipment fixture & fittings	Capital work in progress	Total
Cost or valuation						
Balance at 1st January 2008	427,203	403,812	48,970	657,576	24,162	1,561,723
Additions	-	-	49,846	136,520	113,155	299,521
Transfers	-	20,035	-	31,513	(51,548)	-
Disposals	-	-	(4,390)	(1,093)	(7,214)	(12,697)
Impairments	-	-	-	(56,240)	(10,706)	(66,946)
Balance at 31 December 2008	427,203	423,847	94,426	768,276	67,849	1,781,601
Accumulated depreciation						
Balance at 1 January 2008	-	-	34,074	411,977	-	446,051
Charge for the year	9,505	9,841	12,030	100,638	-	132,014
Released on disposal	-	-	(4,389)	(1,092)	-	(5,481)
Balance at 31 December 2008	9,505	9,841	41,715	511,523	-	572,584
Cost or valuation						
Balance at 1st January 2009	427,203	423,847	94,426	768,276	67,849	1,781,601
Additions	7,115	9,707	21,174	209,729	273,864	521,589
Transfers	-	24,328	-	58,228	(82,556)	-
Revaluation surplus	137,732	61,813	-	-	-	199,545
Disposals	-	-	-	(1,201)	-	(1,201)
Impairments	-	-	-	(982	(29,602)	(30,584)
Balance at 31 December 2009	572,050	519,695	115.600	1,034,050	229,555	2,470,950
Accumulated depreciation and impairment						
Balance at 1 January 2009	9,505	9,841	41,715	511,523	-	572,584
Charge for the year	9,771	10,481	17,025	174,486		211,763
Elimination on revaluation	(19,276)	(20,322)	-	-	-	(39,598)
Released on disposal	-	-	-	(950)	-	(950)
Balance at 31 December 2009	-	-	58,740	685,059	-	743,799
Carrying amount						
At 31 December 2009	572,050	519,695	56,860	348,991	229,555	1,727,151
At 31 December 2008	417,698	414,006	52,711	256,753	67,849	1,209,017

Registers of land and buildings giving details as required under the Companies Act 1984, Schedule 3, Section 16 are maintained at the registered office of the company and are open for inspection by members or their duly authorised agents.

The freehold properties and leasehold improvements were last revalued on 31 December 2009 by Don Whayo BSc; MRICS; MSIM of Knight Frank Malawi Limited, independent valuers, not connected with the group, on an open market value basis. The resultant surplus of K255.237 million for the group and K239.143 million for the company were credited to revaluation reserve.

Capital work in progress represents development costs on the bank's various branches and Auto teller machines in the course of installation.

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15. Deferred tax

	Assets		Liabilities		Net	
	2009	2008	2009	2008	2009	2008
(i) GROUP						
Property and equipment	(14,644)	(18,906)	29,639	7,134	14,995	(11,772)
Accrued income	-	-	49,445	36,706	49,445	36,706
Revaluation of property	-	-	119,329	42,758	119,329	42,758
Tax losses	(60,881)	(34,601)	-	-	(60,881)	(34,601)
Operating Lease - accrual	-	(1,287)	381	-	381	(1,287)
Revaluation on investments	-	-	-	14,832	-	14,832
Gratuity and severance pay liabilities	(45,749)	(45,579)	-	-	(45,749)	(45,579)
Other company differences	-	-	19,865	-	19,865	-
Translation reserve	-	-	4,677	-	4,677	-
Tax (assets)/liabilities	(121,274)	(100,373)	223,336	101,430	102,062	1,057
(ii) COMPANY						
Property and equipment	(14,644)	(18,906)	-	-	(14,644)	(18,906)
Accrued income	-	-	49,445	23,155	49,445	23,155
Revaluation of property	-	-	110,053	38,310	110,053	38,310
Revaluation of investments	-	-	-	14,832	-	14,832
Gratuity and severance pay liabilities	(45,749)	(42,168)	-	-	(45,749)	(42,168)
Tax (assets)/liabilities	(60,393)	(61,074)	159,498	76,297	99,105	15,223

Movements in temporary differences during the year
GROUP

	Opening balance	Recognised in profit or loss	Recognised in equity	Closing balance
2009				
Property and equipment	(11,772)	26,767	-	14,995
Accrued income	36,706	12,739	-	49,445
Revaluation of property	42,758	-	76,571	119,329
Tax losses	(34,601)	(26,280)	-	(60,881)
Operating lease	(1,287)	1,668	-	381
Revaluation of investments	14,832	(14,832)	-	-
Gratuity and severance pay provisions	(45,579	(170)	-	(45,749)
Other differences	-	19,865	-	19,865
Translation reserve	-	4,677	-	4,677
	1,057	24,434	76,571	102,062
2008				
Property and equipment	(16,234)	4,462	-	(11,772)
Accrued income	71,246	(34,540)	-	36,706
Revaluation of property	49,138	-	(6,380)	42,758
Tax losses	-	(34,601)	-	(34,601)
Operating lease	-	(1,287)	-	(1,287)
Revaluation of investments	7,796	7,036	-	14,832
Gratuity and severance pay provisions	(34,715)	(10,864)	-	(45,579)
	77,231	(69,794)	6,380	1,057

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

15. Deferred tax liabilities (Continued)

COMPANY

	Opening balance	Recognised in profit or loss	Recognised in equity	Closing balance
2009				
Property and equipment	(18,906)	4,262	-	(14,644)
Accrued income	23,155	26,290	-	49,445
Revaluation of property	38,310	-	71,743	110,053
Revaluation of investments	14,832	(14,832)	-	-
Gratuity and severance pay provisions	(42,168)	(3,581)	-	(45,749)
Tax (assets)/liabilities	15,223	12,139	71,743	99,105
2008				
Property and equipment	(17,615)	(1,291)	-	(18,906)
Accrued income	57,908	(34,753)	-	23,155
Revaluation of property	44,548	-	(6,238)	38,310
Revaluation of investments	7,796	7,036	-	14,832
Gratuity and severance pay provisions	(31,304)	(10,864)	-	(42,168)
Tax (assets)/liabilities	61,333	(39,872)	(6,238)	15,223

	Group		Company	
16. Customer deposits	2009	2008	2009	2008
Current and savings accounts	11,325,847	8,678,934	8,714,575	8,120,944
Foreign currency accounts	2,391,866	2,412,388	1,661,610	2,346,451
Term deposit accounts	14,177,381	6,022,345	1,231,792	1,072,118
	27,895,094	17,113,667	11,607,977	11,539,513
Payable as follows:				
Maturing within 3 months	9,799,704	7,587,411	3,176,447	3,133,557
Maturing after 3 months and above	18,095,390	9,526,256	8,431,530	8,405,956
	27,895,094	17,113,667	11,607,977	11,539,513

For information about interest rates refer to note 5.

17. Balances due to other banks

Local banks	700,000	-	700,000	-
European Investment Bank loan	1,176,000	-	1,176,000	-
Loans due to foreign banks	373,800	-	373,800	-
Other foreign banks (note 7)	59,113	670,403	59,113	670,403
	2,308,913	670,403	2,308,913	670,403

18. Other liabilities

Interest payable	6,074	38,203	6,074	5,063
Bankers cheques issued and uncleared	207,076	175,543	175,330	166,346
Margins on letters of credit and forward Contracts	104,342	251,639	104,342	251,639
Bills payable	93,365	73,892	93,365	73,892
Trade payables	488,816	165,234	489,004	165,234
Accrued expenses	38,416	222,980	32,932	184,383
FMB Forex Bureau Limited	-	-	5,620	-
Others	42,894	103,363	7,608	28,030
	980,983	1,030,854	914,275	874,587

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19. Provisions

	Group 2009	Group 2008	Company 2009	Company 2008
Severance pay liabilities				
Balance at 1 January	137,457	106,610	122,320	95,240
Current year charge	31,441	33,025	35,240	29,258
Payment made	(1,219)	(2,178)	(1,219)	(2,178)
Balance at 31 December	167,679	137,457	156,341	122,320

In terms of the current interpretation by the courts of the Employment Act, severance allowance is payable in full to employees on termination of employment by mutual agreement, death, retirement, voluntary retirement, retrenchment or redundancy without allowing any set off of employer's pension scheme contributions against severance allowance due.

In preparing the financial statements, the directors have considered the matter and have prepared these financial statements on the basis of the existing interpretation of the law. The amount has not been subject to actuarial valuation as in the directors' opinion; it represents the best estimate based on assumptions.

20 (a) Share capital

	2009	2008
Authorised	120,000	111,250
Authorised, issued fully paid brought forward	111,250	111,250
Bonus shares issued during the year	5,563	-
	116,813	111,250

During the year, by creation of bonus shares, the company increased both its authorised and issued capital from 2,225,000,000 to 2,336,250,000 of 5 tambala each. As a result, the earnings per share as at 31 December 2008 has been restated (see note 30).

(b). Share premium

	2009	2008
Authorised, issued fully paid brought forward	514,035	514,035
Arising on bonus issue	1,051,312	-
	1,565,347	514,035

On 19 June 2006, following an offer to the public, 2,225,000,000 ordinary shares of 5 tambala each were allotted at a premium of 245 tambala per share.

Five tambala 111,250 thousand bonus shares were issued at 950 tambala per share giving rise to a share premium of K1,051,312,000 which was credited to the share premium account.

21. Property revaluation reserve

This represents the increase in fair value of property, plant and equipment net of the related deferred taxation provision and is not available for distribution to the Bank's shareholders.

22. Investment revaluation reserve

This represents the unrealized increase in fair value of investments at fair value through profit and loss net of the related deferred taxation provision transferred from retained earnings and is not available for distribution to the Bank's shareholders.

23. Loan loss reserve

Arising from the changes to IAS 39: Financial Instruments: Recognition and Measurement, the 1% general provision against risk assets as required by the Reserve Bank of Malawi may no longer be offset against the gross value of the assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

24. Interest income

	Group		Company	
	2009	2008	2009	2008
Loans and advances	2,216,842	1,440,470	1,867,352	1,399,958
Lease finance	586,199	363,109	-	-
Treasury bills	515,912	438,662	343,532	310,807
Bank of Botswana certificates	274,336	85,460		
Local registered stocks	26,975	27,079	26,975	27,079
Placements with other banks	114,770	166,814	46,908	136,834
Total interest income	3,735,034	2,521,594	2,284,767	1,874,678

25. Income from investments

Dividend income	68,239	66,245	68,239	66,245
Movement in fair value of investments:				
-Unrealised	(262,181)	231,353	(262,181)	231,353
-Realised	(323)	53,221	(323)	53,221
	(194,265)	350,819	(194,265)	350,819

26. Other operating income

Profit on disposal of motor vehicles and equipment	959	2,914	959	2,856
Other	11,025	949	-	-
	11,984	3,863	959	2,856

27. Staff and training costs

Salaries and wages	691,573	786,621	474,692	699,135
Training costs and other staff costs	458,992	107,062	456,967	75,354
Provision for severance pay	31,441	33,025	35,240	29,258
Contributions to defined contribution plans	35,362	33,025	33,660	26,423
	1,217,368	959,733	1,000,559	830,170

28. Other costs

Other costs include:

Auditor's remuneration				
- Current audit fees	11,921	17,036	10,915	11,030
- Under provision in previous year	-	812	-	-
- Other services and VAT	4,018	4,122	3,285	3,544
Directors' fee	25,519	23,124	24,624	23,004
Others	578,779	446,511	462,362	371,670
Total other costs	620,237	491,605	501,186	409,248

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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29. Income tax expense

	Group		Company	
	2009	2008	2009	2008
Recognised in the income statement				
Current tax expense				
Current year at 30% (2008: 30%) based on profits	644,998	556,943	537,408	484,839
Dividend tax expense	6,296	6,234	6,296	6,234
Deferred tax (credit)/expense				
Origination and reversal of temporary differences (Note 15)	24,434	(69,794)	12,139	(39,872)
Underprovision in previous year	-	10,378	-	10,378
Total income tax expense in income statement	675,728	503,761	555,843	461,579
Reconciliation of effective tax rate				
Profit before income tax	1,994,067	1,895,545	1,600,221	1,780,714
Income tax using the domestic corporation tax rate 30% (2008:30%) Capital Bank Limited rate 25%	598,220	575,419	480,066	534,214
Non-deductible expenses	29,166	20,829	27,435	19,852
Tax exempt income	43,447	(98,210)	43,447	(98,210)
Tax incentives	(1,401)	(511)	(1,401)	(511)
Dividend tax	6,296	6,234	6,296	6,234
Total income tax expense in income statement	675,728	503,761	555,843	461,579

30. Basic and diluted earnings per share

	Group	
	2009	2008 Restated
Profit attributable to ordinary shareholders	1,314,696	1,437,204
Weighted average number of ordinary shares in issue (thousands)	2,336,250	2,336,250
Basic earnings per share (tambala)	56	62
Diluted earnings per share (tambala)	56	62

There are no potential dilutive ordinary shares.

31. Dividends

Last year's second interim dividend of MK155.75 million, final dividend of MK44.5 million and an interim dividend for the year of MK400.5 million were declared and paid during the year.

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In thousands of Malawi Kwacha

32. Related party transactions

The Group transacts part of its business with related parties including directors and parties related to or under the control of the directors. Details of related party transactions of the Group are set out below:

	Directors and their related parties	Employees	FMB Pension Fund	Total
2009				
Advances	652	199,669	-	200,321
Deposits	(74,631)	26,730	24,579	(23,322)
Net balances	73,979	226,399	24,579	176,999
Interest received	40,879	420	-	41,299
Fees and commission received	-	-	30	30
Interest paid	(892)	543	(26)	(375)
Operating expenditure	-	-	-	-
Capital expenditure	-	-	-	-
	39,987	963	4	40,954
2008				
Advances	6,912	143,018	-	149,930
Deposits	(11,634)	(29,351)	(5,417)	(46,402)
Net balances	(4,722)	113,667	(5,417)	103,528
Interest received	845	9,307	-	10,152
Fees and commission received	170	-	26	196
Interest paid	(183)	(320)	(16)	(519)
Operating expenditure	(3,631)	-	-	(3,631)
Capital expenditure	(1,957)	-	-	(1,957)

Advances to directors and parties related thereto are in the normal course of business and considered to be adequately secured.

Advances to employees include MK4,089,000 (2008: MK2,975,000) of interest free advances and MK119,586,000 (2008: MK73,065,000) of advances which carry interest at one quarter of the prevailing prime lending rate of the Bank. All other transactions with related parties are carried out on an arms length basis on normal commercial terms.

In accordance with the Group's accounting policy, advances to related parties at concessionary rates of interest are valued at the present value of expected future repayments of the advances discounted at a pre-tax discount rate that equates to the interest rate charged by the Bank on similar loans to non-related parties. As a result an allowance for impairment losses of MK23,192,000 (2008: MK23,192,000) has been made

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32. Related party transactions (Cont'd)

against concessionary advances to related parties. No other impairment losses have been recorded against loans to related parties.

Details of related party transactions between the Bank and its wholly owned subsidiary, The Leasing and Finance Company of Malawi Limited (LFC), Capital Bank Limited and FMB Forex Bureau Limited, which have been eliminated on consolidation, are as follows:

	2009	2008
	MK'000	MK'000
Deposits by LFC with FMB	1,695	187,703
Loan syndications	(90,988)	(137,183)
Fees and commissions received	2,328	1,953
Interest received	14,880	7,380
Interest paid	804	708
Management fees (Capital Bank Limited)	13,000	20,281

Key management personnel compensation:

	Executive Directors		Non-Executive Directors	
	2009	2008	2009	2008
Salaries	47,969	43,921	-	-
Bonuses	48,000	56,500	-	-
Fees	-	-	25,320	24,282
	95,969	100,421	25,320	24,282

In addition to their salaries, the Group also provides non-cash benefits to executive directors. The estimated value of total non-cash benefits to directors amounts to MK8.2 million (2008: MK7.1 million).

Directors' interests

As at 31 December 2009, the total direct and indirect interests of the directors and parties related thereto in the issued share capital of the company were as follows:

R. C. Kantaria	1,050,000,000 ordinary shares
H. N. and N. G. Anadkat	1,050,000,000 ordinary shares
K. N. Chaturvedi	2,444,400 ordinary shares
J. M. O'Neill	4,649,422 ordinary shares
M. Msisha	1,050,000 ordinary shares
S.G. Malata	42,000 ordinary shares

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

33. Capital commitments and contingent liabilities

In common with other banks, the Bank conducts business involving acceptances, guarantees, performance bonds and indemnities. The majority of these facilities are offset by corresponding obligations of third parties.

The contractual amounts of the Bank's off balance sheet financial instruments that commit it to extend credit to customers are as follows:

	Group		Company	
	2009	2008	2009	2008
Contingent liabilities		Restated		
Acceptances and letters of credit	1,300,473	805,023	1,217,733	805,023
Financial guarantees	8,477,308	4,359,029	4,931,944	4,153,553
Civil litigation and labour matters	5,266	-	-	-
	9,783,047	5,164,052	6,149,677	4,958,576

Contingencies in respect of letters of credit will only crystallise into an asset or a liability when bills are presented in accordance with the terms and conditions of payment of the individual letters of credit.

Contingencies in respect of guarantees and performance bonds issued will only crystallise into an asset and a liability in the event of default by the relevant counterparty.

Contingencies in respect of civil litigation and labour matters will cystalise into a liability only in the unlikely event of an unfavourable judgement.

Financial guarantees for the group have been restated due to a correction of an error in prior year

Commitments

Undrawn formal stand-by facilities,
credit lines and other commitments to lend:

	Group		Company	
	2009	2008	2009	2008
Authorised and contracted capital commitments	60,139	77,715	60,139	77,715

As at 31 December 2009, the authorised but not yet contracted capital commitments were MK160.0 million (2008: MK76.5 million).

34. Statutory requirements

In accordance with Section 27 of the Banking Act 1989, the Reserve Bank of Malawi has established the following requirements as at the financial reporting date:

(i) Liquidity Reserve Requirement
The Bank is required to maintain a liquidity reserve as defined by the Reserve Bank of Malawi, calculated on a weekly average basis, of not less than 15.5% (2008: 15.5%) of the preceding weeks total deposit liabilities. In the last week of December 2009, the liquidity reserve was 17.44% (2008: 21.8%) of total customer deposits.

(ii) Capital Adequacy Requirement
The Bank's available capital is required to be a minimum of 10% of its risk bearing assets and contingent liabilities. At 31 December 2009, the Bank's available capital was 15.08% (2008: 20.75%) of its risk bearing assets and contingent liabilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

35. Exchange rates and inflation

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

Exchange rates	2009 MK	2008 MK	2007 MK
Kwacha/GBP	237.0	216.5	285.9
Kwacha/Rand	19.9	15.9	21.1
Kwacha/US Dollar	146.0	141.5	140.3
Kwacha/Euro	211.8	210.1	209.7
Inflation rate %	7.6%	9.9	8.0

At the time of signing these financial statements the exchange rates moved as under

Kwacha/GBP	237.4
Kwacha/Rand	20.2
Kwacha/US Dollar	150.8
Kwacha/Euro	211.2

36. Effective interest rates of financial assets and liabilities

The effective interest rates for the principal financial assets and liabilities at 31 December were in the following ranges:

	2009
Assets	
Government securities	7.14% -11.2%
Deposits with banking institutions	0.50% -8.0%
Loans and advances to customers	19.5%
Liabilities	
Customer deposits	0.50% - 12%

	2008 Restated
Assets	
Government securities	13.15%-16.95%
Deposits with banking institutions	0.25%-2.50%
Loans and advances to customers	19.5%
Liabilities	
Customer deposits	0.5%-12%

The effective interest rate range for liabilities from customer deposits has been restated due to correction of an error in the prior year computation.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

In thousands of Malawi Kwacha

37. Segmental Reporting

Separate financial information is presented to the Group's chief operating decision makers in respect of the individual legal entities comprised in the Group, namely:

- First Merchant Bank Limited – corporate and retail banking in Malawi
- The Leasing and Finance Company of Malawi Limited - deposit taking and asset finance in Malawi
- FMB Forex Bureau Limited – operation of foreign exchange bureaux in Malawi
- Capital Bank Limited – corporate and retail banking in Botswana

In the case of First Merchant Bank Limited information on income and expenditure, assets and liabilities is further disaggregated between its various individual branches and agencies and its head office operations. Head office income includes group treasury income from dealing in foreign currency and trading in financial instruments and income from funds management, corporate advisory and transfer secretarial services. Head office expenditure includes all head office staff, premises and overhead costs including the costs of group treasury and capital market operations which are not separately identified in internal reports.

Branches and agencies of First Merchant Bank are all engaged in corporate and retail banking, offer similar products and services to similar classes of customer and are governed by the same regulatory environment. Given their common economic characteristics, these individual segments are aggregated and presented in a single segment, Malawi corporate and retail banking, in these financial statements.

FMB Forex Bureau Limited does not meet any of the quantitative thresholds set out in IFRS 8 for separate disclosure and reporting and this segment has been aggregated into the Malawi corporate and retail banking segment information presented below.

Income tax expense, assets and liabilities are not disaggregated but allocated in full to head office.

Included in external interest income is income from placements with banks abroad of K23.011 million (2008:K101.917 million). All other revenues are attributable to the country in which the respective operating segment is domiciled.

During the year the Group earned K817.222 million (2008:K535.431 million) interest on Government of Malawi treasury bills, Bank of Botswana Certificates and local registered stock; Knil (2008: K15.770 million) interest on Reserve Bank of Malawi bills; K143.73 million (2008: K0.025 million) interest on loans and advances to enterprises controlled by Government of Malawi and Government of Botswana; and fees and commissions of K19.363 million (2008: K13.901 million) from accounts of enterprises controlled by Government of Malawi and Government of Botswana.

GEOGRAPHICAL SEGMENT

From 2007 the group conducts its business operations in Malawi and Botswana

	Malawi Head Office	Malawi Corporate and Retail banking	Malawi asset finance and deposit taking	FMB Forex Bureau	Total Malawi	Botswana Corporation and Retail Banking	Total before adjustments	Intersegment	Total
	K'000	K'000	K'000	K'000	K'000	K'000	K'000	K'000	K'000
Interest Income - External	-	1,844,341	615,627	-	2,459,968	349,240	2,809,208	(29,178)	2,780,030
Interest Expense - External	23,011	-	-	-	23,011	-	23,011	-	23,011
Other operating segments	417,415	-	197,437	2	614,854	317,153	932,007	(14)	931,993
Total interest income	440,426	1,844,341	813,064	2	3,097,833	666,393	3,764,226	(29,192)	3,735,034
Interest expense	-	(180,456)	(355,411)	(12)	(535,879)	(422,052)	(957,931)	29,192	(928,739)
External	-	-	-	-	-	-	-	-	-
Other operating segments	(20,391)	-	-	-	(20,391)	-	(20,391)	-	(20,391)
Total interest expense	(20,391)	(180,456)	(355,411)	(12)	(556,270)	(422,052)	(978,322)	-	(949,130)
Net interest income	420,035	1,663,885	457,653	(10)	2,541,563	244,341	2,785,904	-	2,785,904
Fees and commissions	117,259	695,501	24,020	-	836,780	101,595	938,375	(17,987)	920,388
External capital market fees	9,966	-	-	-	9,966	-	9,966	-	9,966
Other external fees and commission	-	-	-	-	-	-	-	-	-
Other operating segments	94	-	-	-	94	-	94	-	94
Total fees and commissions	127,319	695,501	24,020	-	846,840	101,595	948,435	(17,987)	930,448
Income from investments	(194,265)	-	-	-	(194,265)	-	(194,265)	-	(194,265)
Gains on foreign exchange transactions	488,077	345,368	-	978	834,423	28,971	863,394	-	863,394
Other operating income	959	-	40	-	999	10,985	11,984	-	11,984
Total operating income	842,125	2,704,754	481,713	968	4,029,560	385,892	4,415,452	(17,987)	4,397,465
Staff and training costs	544,377	456,182	38,657	-	1,039,216	178,152	1,217,368	-	1,217,368
Premises and equipment costs	99,612	138,688	-	2,197	240,497	33,840	274,337	-	274,337
Depreciation	116,090	95,673	4,587	325	216,675	59,220	275,895	-	275,895
Other expenses	292,905	208,281	37,171	368	538,725	99,499	638,224	(17,987)	620,237
Impairment of financial assets	(5,149)	-	15,984	-	10,835	4,726	15,561	-	15,561
Total expenditure	1,047,835	898,824	96,399	2,890	2,045,948	375,437	2,421,385	(17,987)	2,403,398

GEOGRAPHICAL SEGMENT (Continued)

	Malawi Head Office	Malawi Corporate and Retail banking	Malawi asset finance and deposit taking	FMB Forex Bureau	Total Malawi	Botswana Corporation and Retail Banking	Total before adjustments	Intersegment	Total
	K'000	K'000	K'000	K'000	K'000	K'000	K'000	K'000	K'000
Profit before income tax expense	(205,710)	1,805,930	385,314	(1,923)	1,983,612	10,455	1,994,067	-	1,994,067
Income tax expense	(555,843)	-	(116,719)	-	(672,562)	(3,166)	(675,728)	-	(675,728)
Profit for the year	(761,553)	1,805,930	268,595	(1,923)	1,311,050	7,289	1,318,339	-	1,318,339
Reportable segment assets	20,963,978	-	5,930,820	15,493	26,910,291	12,652,956	39,563,247	(892,829)	38,670,418
Reportable segment liabilities	15,284,946	-	5,091,871	6,838	20,383,655	11,475,661	31,859,316	(81,433)	31,777,883

38. Comparative information

Comparative information has been restated in order to account for an error in the classification of translation differences arising on translation of the equity of a foreign subsidiary which had previously been attributed to the non controlling interest as follows:

	Retained earnings	Translation reserve	Non controlling interest
As previously stated	3,065,146	(144,688)	379,020
Reclassification	(2,085)	68,842	(66,757)
As at 31 December 2008 - restated	3,063,061	(75,846)	312,263

In addition, certain prior year comparative numbers may not agree to the numbers presented in the prior year due to reclassifications for better presentation in the current year.

There is no impact on income tax and earnings per share.

39. Subsequent events

Subsequent to year end, no significant events have occurred necessitating adjustments to or disclosure in these group financial statements.

Statistics for First Merchant Bank

As at 31 December 2009

INDUSTRY CODES	Shares		Holders	
INVESTMENT COMPANIES & TRUSTS	1,054,225,450	45.12%	21	1.00%
LOCAL COMPANIES	553,654,63723.	70%	64	3.05%
FOREIGN COMPANIES	537,175,658	22.99%	6	0.29%
CITIZEN RESIDENT INDIVIDUALS	122,496,525	5.24%	1,685	80.20%
PENSION FUNDS	37,619,109	1.61%	35	1.67%
EMPLOYEES	13,475,100	0.58%	202	9.61%
NOMINEES LOCAL	5,046,826	0.22%	34	1.62%
NON RESIDENTS	4,096,771	0.18%	21	1.00%
OTHER ORGANISATIONS	2,474,195	0.11%	11	0.52%
INSURANCE COMPANIES	2,454,621	0.11%	5	0.24%
DIRECTORS	2,444,400	0.10%	1	0.05%
LEASING AND FINANCE	847,150	0.04%	10	0.48%
NON RESIDENT CITIZENS	120,383	0.01%	1	0.05%
OTHER RESIDENT INDIVIDUALS	108,675	0.00%	4	0.19%
NOMINEES FOREIGN	10,500	0.00%	1	0.05%
TOTALS	2,336,250,000		2,101	

COUNTRIES	Shares		Holders	
MALAWI	1,798,052,221	76.96%	2,070	98.52
KENYA	525,073,500	22.48%	4	0.19%
BERMUDA	8,797,362	0.38%	1	0.05%
PORTUGAL	2,335,200	0.10%	8	0.38%
UNITED KINGDOM	855,896	0.04%	2	0.10%
USA	659,268	0.03%	5	0.24%
SOUTH AFRICA	298,515	0.01%	3	0.14%
BOTSWANA	121,247	0.01%	1	0.05%
WARRANT NOT PRESENTABLE	35,581	0.00%	5	0.24%
CAYMAN ISLANDS	20,790	0.00%	1	0.05%
ZIMBABWE	420	0.00%	1	0.05%
TOTALS	2,336,250,000		2,101	

SHARE HOLDING DISTRIBUTION	Share		Holders	
1 - 5000	1,015,955	0.04%	318	15.14%
5001 - 10000	1,923,422	0.08%	289	13.76%
10001 - 25000	9,074,466	0.39%	572	27.23%
25001 - 50000	9,652,370	0.41%	255	12.14%
50001 - 100000	13,277,735	0.57%	195	9.28%
100001 - 200000	22,966,437	0.98%	188	8.95%
200001 - 500000	60,136,714	2.57%	207	9.85%
500000 - 1000000	27,326,901	1.17%	42	2.00%
1000000 +	2,190,876,000	93.78%	35	1.67%
	2,336,250,000		2,101	

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Notes