RISK MANAGEMENT REPORT

RISK MANAGEMENT REPORT

One of the key missions of AfrAsia Bank Limited (the "Bank") is to identify, assess and manage the credit, operational, market and liquidity risks to which the Bank is exposed, thereby providing a sustainable environment to attract and promote business opportunities whilst improving the risk/return profile of its activities.

Through a robust internal control mechanism, together with comprehensive and up-to-date risk policies, reliable decision making support with strict adherence to the legal and regulatory requirements, our goals remain to maintain the confidence of the stakeholders by mitigating our risk through the management of current and potential credit, operational, market and liquidity risks.

RISK MANAGEMENT STRUCTURE

AfrAsia Bank Limited has clear risk management objectives and a well-established strategy to deliver them, through core risk management processes.

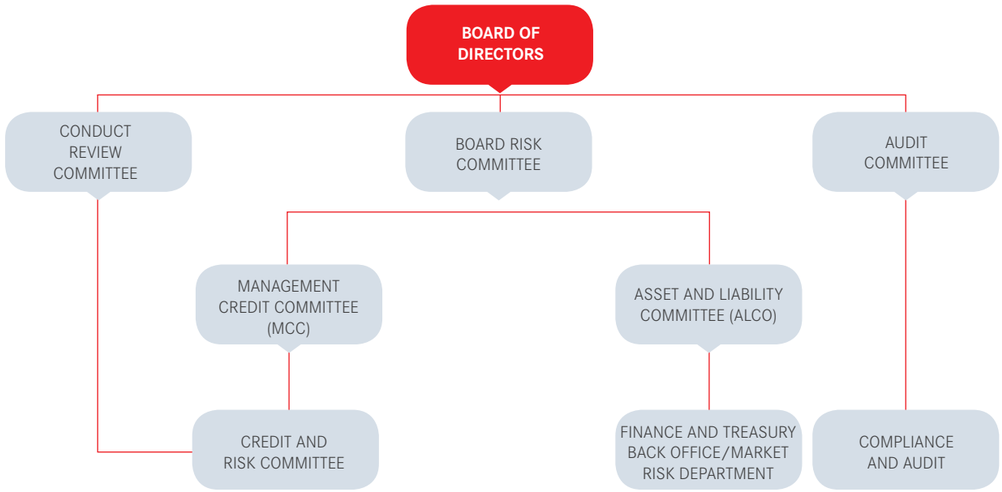
At a strategic level, the Bank's risk management objectives are to:

- identify the significant risks to the Bank;
- formulate the Bank's risk appetite and to ensure that business profiles and plans are consistent with it;
- establish strong and independent reviews in a dynamic structure; optimisation of risk and return decisions are taken as closely as possible to be in line with our core business;
- ensure business growth plans are properly supported by effective risk infrastructure; and
- ensure that the management of risk profile for specific financial deliverables remain possible under a range of adverse business conditions.

The Bank's main approach is to establish a solid and effective Risk Management infrastructure in terms of people, systems, policies, procedures, control and compliance and to recommend to the Board changes to meet the challenges of the dynamic market.

The Bank also has a clear organisational structure and comprehensive policies and procedures to identify, evaluate, monitor and control risks across the organisation. Reviews and modifications to these risk management policies and procedures are regularly carried out to reflect changes in markets and business strategies.

The Board has delegated some of its functions to a number of committees and departments as follows:



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RISK MANAGEMENT REPORT (CONTINUED)

The Board Risk Committee performs fundamental functions for the Bank which include:

- approving the delegation of credit limits to management and approving any transactions exceeding those delegated authorities;
- reviewing and recommending for Board approval the Bank's Risk Appetite Framework at least annually and reviewing the alignment of the Bank's strategic plan with the Risk Appetite Framework;
- reviewing and approving risk management policies recommended by Bank management for identifying, accepting, monitoring, managing and reporting on the significant risks to which the Bank is exposed; as part of such reviews, satisfy itself with the manner in which material exceptions to such policies are identified, monitored, measured and controlled, as well as the remedial actions taken when exceptions are identified;
- reviewing and recommending for Board approval the Bank's credit risk strategy at least annually;
- reviewing, monitoring and recommending to the Board the approval of risk related policies, procedures and standards as required by regulatory authorities;
- overseeing the risk management function, having regard to its independence, by periodically reviewing the results of independent reviews of the risk management function and reporting such results to the Board and overseeing that deficiencies identified related to the risk management function are remedied within an appropriate time frame and reporting to the Board on the progress of necessary corrective actions;
- reviewing on a quarterly basis management's report on the Bank's lending profile, and discuss with management identified material risks and emerging risk issues and trends;
- reviewing quarterly reports on the Bank's enterprise-wide risk profile (including credit, market, operational and liquidity risks) and reviewing against its risk appetite;
- reviewing and approving country limits in line with the Bank's strategy and country appetite; and
- reviewing and approving any other matters required by regulators from time to time.

Regular reporting enables the Board of Directors to monitor whether the overall risk policies and authorities are being complied with and whether they meet the Group's needs. In addition, the Board regularly reviews reports analysing the Group's portfolio, including data on industry concentrations.

RISK COMMITTEES ESTABLISHED BY THE BOARD OF DIRECTORS

BOARD RISK COMMITTEE

- The Board Risk Committee (BRC) is made up of three Independent Directors, one Non-Executive Director and the Chief Executive Officer. The Independent Directors are experienced risk professionals with extensive experience in emerging markets and Mauritius.
- The BRC is a consultative as well as an approval panel for facilities exceeding the Management Credit Committee's lending authority as defined in the Credit Risk Policy. In this capacity, the BRC examines and approves large credit applications where global exposures exceed MUR 50m.

AUDIT COMMITTEE

- The Audit Committee is composed of the three Non-Executive Independent Directors, which met four times during the year under review.
- The Audit Committee's principal responsibilities are to ensure that the Bank implements and maintains appropriate accounting, internal control and financial disclosure procedures, evaluating and approving the related procedures. It can also have consultations with both the Bank's internal and external auditors, as required.

CONDUCT REVIEW COMMITTEE

- The Conduct Review Committee (CRC) is composed of the three Non-Executive Independent Directors and one advisor, which met four times during the year under review.
- CRC reviews the Bank's transactions with related parties ensuring that the latter is in compliance with all reporting and/or approval procedures of the Bank of Mauritius. The CRC also reviews all related party transactions with any shareholder when said dealings are above 2% of Tier 1 capital ensuring that transactions which could materially affect the financial stability of the Bank are identified at source

ASSETS AND LIABILITIES COMMITTEE

- The Bank's Asset and Liability Committee's overall responsibility is to ensure that the Bank's overall asset and liability structure including its liquidity, currency and interest rate risks are managed within limits and targets set by the Board Risk Committee.
- This committee, which comprises the CEO, the Deputy CEO, Head of Global Banking, Treasury and Markets, the General Manager, Domestic Banking Relationships & Sales, the General Manager and Director of AfrAsia Private Banking, the Head of Finance & Treasury Back Office, the Head of Credit & Risk, the Money Market Executive, the Market Risk Executive and the Head of Global Business & Structured Trade meets at least once a month.

MANAGEMENT CREDIT COMMITTEE

- The Management Credit Committee (MCC) assists the Board to formulate, approve and implement loan policies, guidelines and credit practices of the Bank. It is also responsible for the implementation and maintenance of the Bank's credit risk management framework. Key objective of the MCC is to evaluate, review and sanction credit applications up to and including MUR 50m and those referred by lower mandates or, which cannot be sanctioned at lower levels.
- MCC reports to the BRC and comprises of eight permanent members among whom are three voting members (the CEO, the Head of Finance & Treasury Back Office and the Head of Credit & Risk). The other five members are "in attendance" (the General Manager, Head of Banking Treasury and Markets, the Head of Domestic Banking Relationships & Sales, the Head of Strategic Development and the Credit Risk Managers - International Business & Domestic Corporate)

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RISK MANAGEMENT REPORT (CONTINUED)

MANAGEMENT OF KEY RISK AREAS

Credit Risk Management Overview

Credit risk is the risk arising from any failure by a borrower or counterparty to fulfil its financial obligations as and when they fall due. The effective management of risk is fundamental to activities as the Group remains committed to manage the business in a way that is consistent with the agreed risk appetite.

The credit risk that the Bank faces arises mainly from direct lending (wholesale and retail loans and advances), trade finance activities including debt securities settlement balances with market counterparties, available-for-sale assets and reverse repurchase loans, together with the counterparty credit risk arising from derivative contracts entered into with our clients.

Credit risk management objectives are to:

- maintain a well-defined portfolio management;
- ensure that an effective risk management infrastructure is in place;
- monitor risk portfolio against agreed limits; and
- maximise the stakeholder's value.

Organisation And Structure

The Bank has structured the responsibilities of credit risk management so that decisions are taken as close as possible to the business, whilst ensuring that there is an adequate internal control mechanism and up-to-date and comprehensive risk policies which adhere to legal and regulatory requirements.

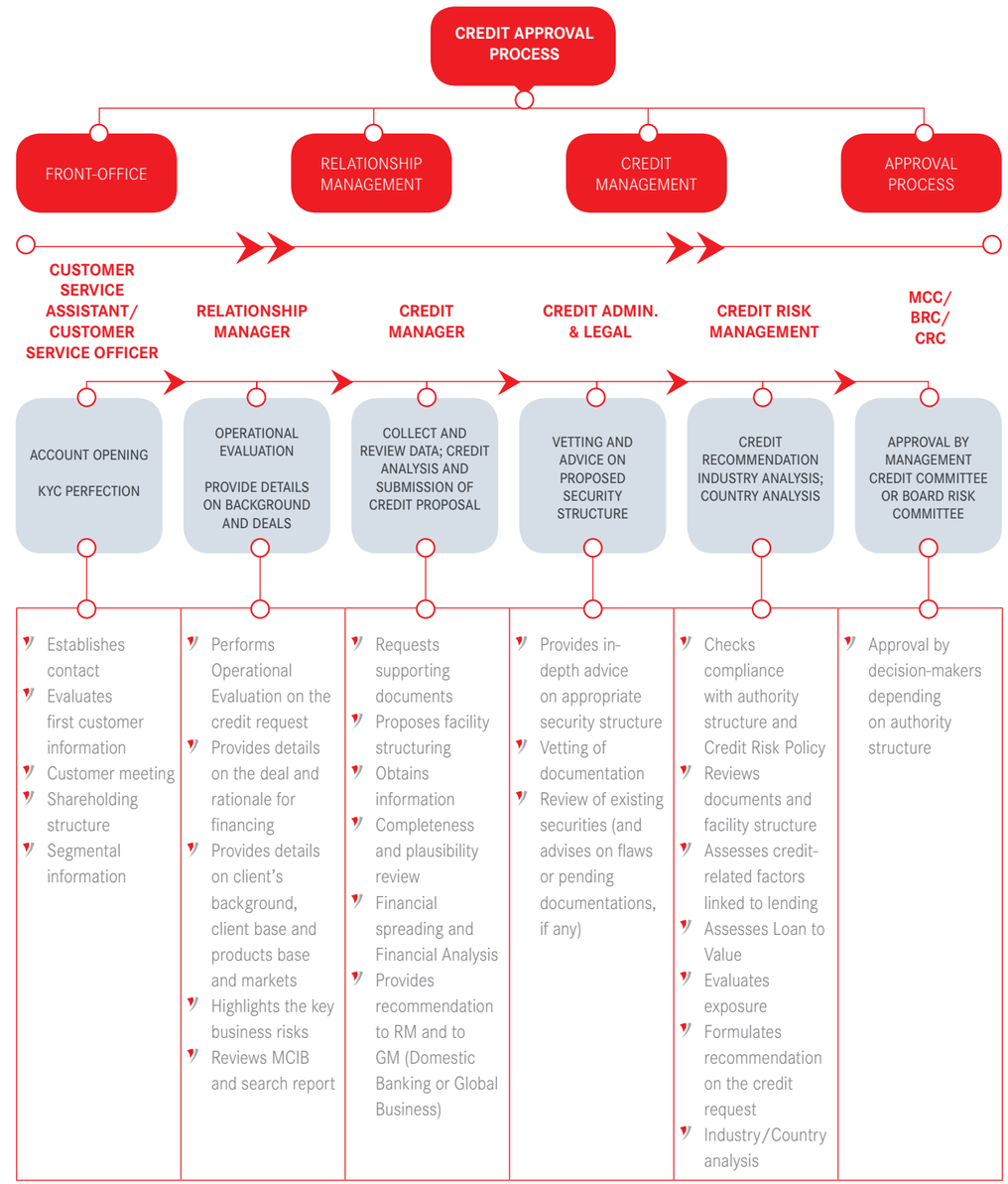
In designing credit policies and the credit process, due consideration is given to the Bank's commitment to:

- create, monitor and manage credit risk in a manner that complies with the Bank of Mauritius guidelines and AfrAsia Bank's credit risk policy;
- identify credit risk in each investment, loan or other activity of the Bank;
- utilise appropriate, accurate and timely tools to measure credit risk; and
- set acceptable risk parameters.

The responsibilities of the credit risk management teams in the businesses include: sanctioning new sources of risk; monitoring risk against limits and other parameters; ensuring all elements of post sanction fulfilment are completed in line with terms of the sanction; maintaining robust systems, data gathering, quality, storage and reporting methods for effective credit risk management; and performing effective turnaround and workout scenarios via dedicated restructuring and recoveries teams.

Credit risk approval is undertaken by experienced credit risk professionals operating within a clearly defined delegated authority framework, with only the head of the department entrusted with the higher levels of delegated authority.

An overview of the credit approval process and procedures is depicted below:



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RISK MANAGEMENT REPORT (CONTINUED)

CREDIT RISK

Credit Policies

The Board has ultimate control and oversight of the credit risk policies for the Bank and these policies are reviewed on at least an annual basis. The policies are designed to provide effective internal control within the Bank. Any development in the customers' financial situation is closely monitored by the Bank, thus enabling it to assess whether the basis for granting the credit facility has changed. However, a new review is triggered when changes happen in regulations and guidelines. Credit facilities are generally granted on the basis of an understanding of customers' individual financial circumstances, cash flow assessment of market conditions and security procedures. The facilities should match the customers' creditworthiness, capital position and assets to a reasonable degree, and customers should be able to substantiate their repayment ability. In order to reduce credit risk, the Bank generally requires collateral that corresponds to the risk for the product segment.

Credit Rating

As per Basel II Capital Accord, a Rating System must have 2-Dimensions and provide for a separate assessment of borrower and transaction characteristics to provide for a meaningful differentiation of risk. In that respect, over the reporting financial period, the Bank implemented CRISIL Risk Solutions which provide a suite of software that is critical for ensuring compliance with regulatory guidelines, such as Basel II. CRISIL's Risk Assessment Model (RAM) is the largest deployed internal risk rating solution in India. This model as well as CRISIL Retail Scoring Solution (CRESS) has been implemented to assist the Bank in complying with the requirements under the internal ratings-based approach of the Basel II Accord. Both models now facilitate credit risk appraisal of a borrower through a judicious mix of objective and subjective methodologies and act as a comprehensive database for all borrower-specific information.

CRISIL's rating grades and description for each grade are as follows:

Rating Grades	Description	Definition
AAA	Investment Grade - Highest safety	Borrowers rated AAA are judged to offer highest safety of timely payment.
AA+	Investment Grade - High safety	Borrowers rated AA+ are judged to offer high safety of timely payment.
AA	Investment Grade - High safety	Borrowers rated AA are judged to offer high safety of timely payment. They differ in safety from AA+ only marginally.
A	Investment Grade - Adequate safety	Borrowers rated A are judged to offer adequate safety of timely payment.
BBB	Investment Grade - Moderate safety	Borrowers rated BBB are judged to offer moderate safety of timely payment of interest and principal for the present.
BB	Investment Grade - Moderate safety	Borrowers rated BB are judged to offer moderate safety of timely payment of interest and principal for the present. There is only a marginal difference in the degree of safety provided by borrowers rated BBB.
B	Investment Grade - Minimum safety	Borrowers rated B are judged to carry minimum safety of timely payment of interest and principal for the present.
CC	Sub-Investment Grade - Inadequate safety	Borrowers rated CC are judged to carry inadequate safety of timely payment.
C	Sub-Investment Grade - High risk	Borrowers rated C have a greater susceptibility to default.
D	Highly susceptible to Default/Default	Borrowers rated D are in default or are expected to default on maturity.

CREDIT MONITORING

Monitoring weaknesses in portfolios

Credit risk exposures and weaknesses are managed through the robust credit assessment, structuring and regular monitoring process. The latter under the responsibility of the Credit Recovery Unit, involves the monitoring of daily credit excesses on accounts as well as the review of all potential credit losses on a timely basis. Those exposures showing signs of deterioration are put on a watch list (WL), the files are reviewed at least monthly to ensure prompt action is taken. The basis for provisioning and loan assessment is based on the Guideline on Credit Impairment and Income Recognition issued by the Bank of Mauritius.

Corporate portfolios

Corporate accounts that are showing signs of deterioration or a likelihood of potential credit losses risk are recorded on the WL comprising two categories graded in line with the perceived severity of the risk attached to the lending, and its probability of default.

These lists are updated monthly and circulated to the relevant recovery manager. Once an account has been placed on WL, the exposure is carefully monitored and, where appropriate, exposure reductions are effected. When an account becomes impaired, it will normally, but not necessarily, have passed through each of the two categories, which reflect the need for increasing caution and control. Where a borrower's financial health gives grounds for concern, it is immediately placed into the appropriate category. While all borrowers, regardless of financial health, are subject to a full review of all facilities on at least an annual basis, more frequent interim reviews may be undertaken should circumstances dictate.

Retail portfolios

Within the retail portfolios, the approach is consistent with the Bank's policy of raising a collective impairment allowance as soon as objective evidence of impairment is identified. Retail accounts can be classified according to specified categories of arrears status, which reflects the level of contractual payments which are overdue. The probability of default increases with the number of contractual payments missed, thus raising the associated impairment requirement. Once a loan has passed through a prescribed number of statuses and downgrades, it will enter recovery status where the file will be classified and monitored by the recovery unit.

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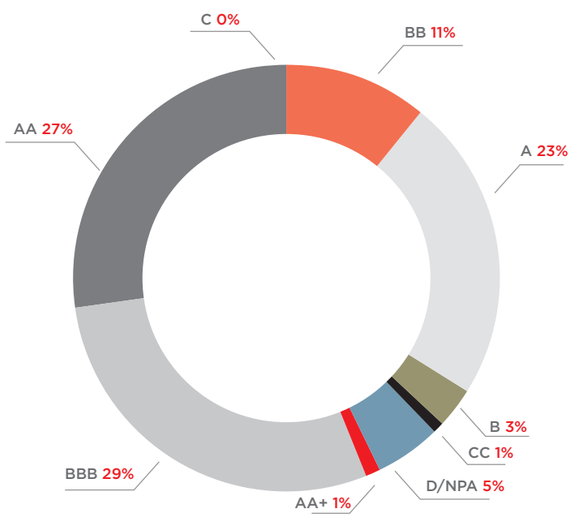
RISK MANAGEMENT REPORT (CONTINUED)

ASSET CREDIT QUALITY

CRISIL Rating	Description	Overall CRISIL Rating	%
		MUR	MUR
AAA	Investment Grade - Highest safety	-	0%
AA+	Investment Grade - High safety	282,033,466	1%
AA	Investment Grade - High safety	5,908338,338	27%
A	Investment Grade - Adequate safety	5,110,077,910	23%
BBB	Investment Grade - Moderate safety	6,466,497,190	29%
BB	Investment Grade - Moderate safety	2,319,876,482	11%
B	Investment Grade - Minimum safety	592,961,582	3%
CC	Sub-Investment Grade - Inadequate safety	142,602,886	1%
C	Sub-Investment Grade - High risk	6,769,953	0%
D/NPA	Default	1,140,731,822	5%
Sub-Total		21,969,889,630	
Credit Card		123,967,610	1%
Grand-Total		22,093,857,240	100%

CRISIL RATING



All loans and advances are categorised as neither past due nor impaired; past due but not impaired; or impaired, which includes restructured loans.

- A loan is considered past due when the borrower has failed to make a payment when due under the terms of the loan contract.
- The impairment allowance includes allowances against financial assets that have been individually impaired and that are subject to collective impairment.
- Loans neither past due nor impaired consist predominantly of loans that are performing.

In carrying out credit transactions, AfrAsia Bank Limited strives not only to improve its volume growth, but also keeps in mind the quality of its loan portfolio.

As at 30 June 2015, 94% of the Bank's asset book (excluding Credit Cards) was in the range AA+ to B, thus, reflective of investment grade status of the borrowers. The remaining 6% were either sub-investment grade (facilities being on the watchlist where there are arrears and borrowings classified as non-performing).

Total Non-Performing Assets (including credit cards NPA of MUR 7,401,921) were at MUR 1,148,133,743 representing 5.20% of total asset book. This has increased from last financial year from 2.66%. The Bank has classified as NPA few large corporates over this financial year.

CREDIT EXPOSURE

The Bank manages portfolios for individual industries by determining the credit appetite and limit for each industry on the basis of total exposure, credit quality and industry outlook. The portfolio monitoring and reporting system enables the Group to manage portfolios and to focus on specific industries and business units.

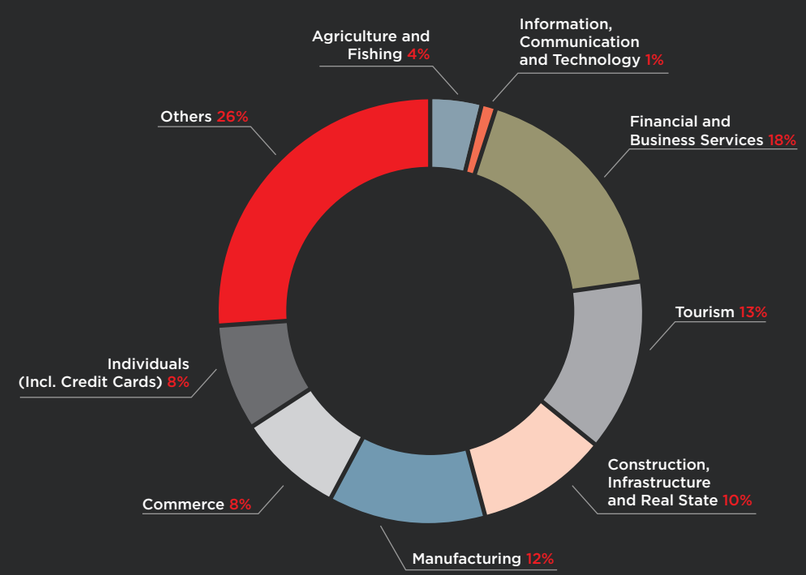
Exposure risk arises due to the over-dependency on a particular sector of the economy, geographical area, industry and currency. Exposure for a single party or a group is managed through sector limits with monitoring and approval on a monthly basis to the MCC and BRC.

The Bank's key portfolio concentrations by industry are set out below:

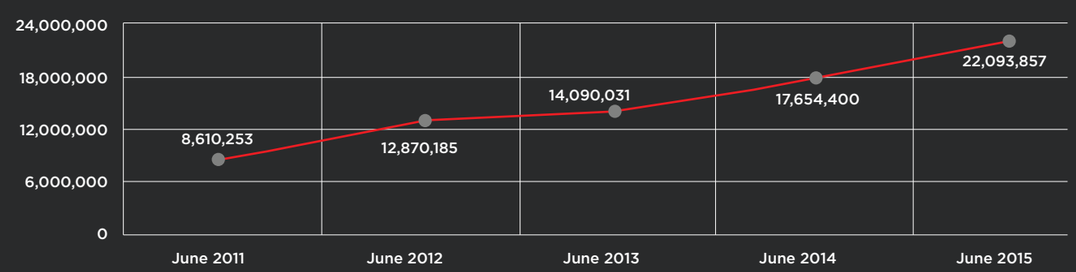
SECTOR	OUTSTANDING BALANCE	
	30 June 2015 (MUR'000)	30 June 2014 (MUR'000)
Financial and Business Services	3,856,234	2,670,704
Tourism	2,800,971	2,097,708
Construction, Infrastructure and Real Estate	2,288,266	2,329,744
Manufacturing	2,636,013	2,669,042
Commerce	1,803,152	1,659,370
Individuals (incl. Credit Cards)	1,847,212	1,548,075
Others	5,772,814	3,813,644
Agriculture and Fishing	927,736	675,507
Information, Communication and Technology	161,460	190,606
Total Exposure	22,093,857	17,654,400

RISK MANAGEMENT REPORT (CONTINUED)

UTILISATION LEVEL



OUTSTANDING BALANCE - PAST 5 YEARS



During the Financial Year 2014/15, AfrAsia Bank Limited has taken active steps in prudently managing its exposures and ensuring that its loan book is judiciously diversified, while periodically conducting stress tests to assess the resilience of its portfolio in case of unfavourable events. Over the years, the Bank has been keeping close attention to its credit concentration to ensure it meets regulatory requirements.

CONCENTRATION OF RISK / LARGE EXPOSURES

The Bank of Mauritius Guidelines on Credit Concentration (revised November 2013) restrict the granting of credit facilities to non-financial institutions and other related parties, to:

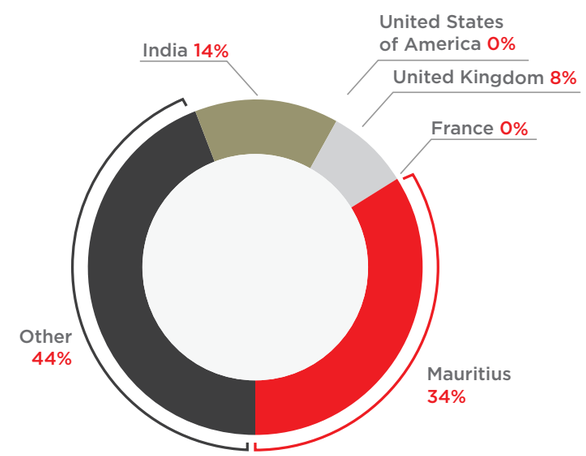
- a maximum exposure to any single customer of 25%;
- a maximum exposure to a related group of companies to 40% of the Bank's capital base;
- in aggregate, any individual exposure of 15% above the Bank's capital base shall not exceed 600% of its capital base.

The key focus of the Bank's macro credit risk management approach is to avoid any undue concentrations in its credit portfolio, whether in terms of counterparty, group, portfolio, product, country, sovereign, or currency. The Bank has always kept its large exposures within these limits. For instance, our concentration ratio of large exposures above 15% was 139% as at 30 June 2015, well within the regulatory limit of 600% as shown below:

CAPITAL BASE AS AT 30 JUNE 2015	MUR'000
Tier I	4,016,507
Tier II	896,799
Capital Base	4,913,306
Total Large Exposures (15% above)	6,833,167
% Large exposure v/s Capital Base (Limitation 600%)	139%

The Bank's portfolio management supports a comprehensive assessment of concentrations within its credit risk portfolio for provision of subsequent risk mitigating actions and diversification across various geographical boundaries, sectors, borrower groups and products, with the main objectives of maximising shareholder value. To manage industry risk, the Bank also prepares economic and industry reports, which are submitted to the Board Risk Committee, that highlight industry developments and risks to the Bank's credit portfolio. These reports are used to define strategies for both our industry portfolio and individual counterparties within the portfolio.

COUNTRY RISK



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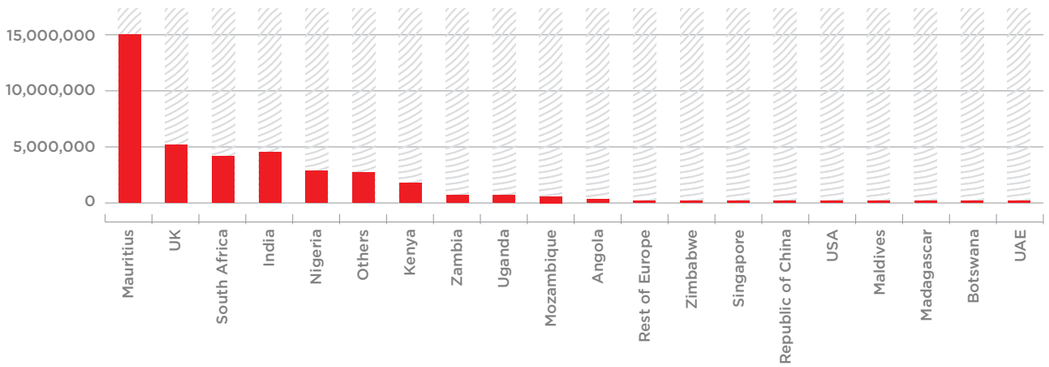
RISK MANAGEMENT REPORT (CONTINUED)

The Board of Directors is responsible for setting the Bank's tolerance for country risk. It has delegated authority for the day-to-day management of the country risk policy to MCC.

This policy will also ensure effective oversight by the Board of Directors and Senior Management in ensuring that country risk is managed satisfactorily.

LOANS AND PLACEMENTS AS OF 30 JUNE 2015

COUNTRY EXPOSURE: LOANS AND PLACEMENTS



The Bank regularly compares its internal risk ratings with the ratings of the major international rating agencies. Country risk limits are reviewed regularly, in conjunction with the review of country risk ratings. Country risk limits are set by the Board Risk Committee.

RISK ASSESSMENT

Assessment of country risk involves the determination of the nature of risks associated with individual country exposure and the evaluation of country conditions. In this connection, the Bank conducts a thorough evaluation of risks associated with its cross-border operation and which have the potential to adversely affect its risk profile.

The aim is to identify the risk of a shock, such as an economic crisis or a sudden change in the political environment that would affect those conducting business within a country.

The Bank utilizes two types of approach:

- a bottom-up approach analysis of the country risk pertaining to each cross-border credit files, placements, financial products (among others)
- a top-down approach:
  - analysis of the concentration/diversification of country risk in the Bank's portfolio
  - analysis of the global or regional economic and political movements and their adverse impacts on the country risk profiles

Risk team analyses the following elements:

- the short and long term Economic Risk: the aim is to assess the degree to which the country approximates the ideal of non-inflationary growth, contained fiscal and external deficits, and manageable debt ratios. The analysis takes into account GDP growth, unemployment, inflation, real interest rates, exchange rates, the fiscal balance, the current account balance, external debt and a number of other structural factors; and
- the short and long term Political Risk: the political risk assessment compares the state against a theoretical ideal state, essentially a liberal state and a homogenous society in terms of ethnicity and income equality, with the premise that democracies are more able to contain and manage direct threats to the political system and offer a template for greater long-term stability.

LIMITS

An appropriate structure of limits is set for each individual country exposure.

The determination of limits is based on the following:

- the overall strategy and commercial opportunities;
- the relation with Bank's capital base;
- the perceived economic strength and stability of the borrowing country;
- the degree of perceived risk; and
- the diversification of the Bank's international lending and investment portfolio.

The Board of Directors validates the structure and value of the limits.

The Bank's operations are performed strictly within the approved limits

CREDIT RISK MITIGATION

As a fundamental credit principle, the Bank does not generally grant credit facilities solely on the basis of the collateral provided. All credit facilities are also based on the credit rating, source of repayment and debt servicing ability of the borrower. Collateral is taken whenever possible to mitigate the credit risk. The collateral is monitored on a regular basis with the frequency of the valuation depending on the liquidity and volatility of the collateral value enforcement. Legal certainty of enforceability and effectiveness is another technique used to enforce the risk mitigation.

COLLATERAL CHART	MUR'000
Cash Security	738,896
Unsecured Loans and Advances	3,281,990
Claims on Bank	282,795
Tangible Assets	17,790,175
Total Loans and Advances	22,093,857

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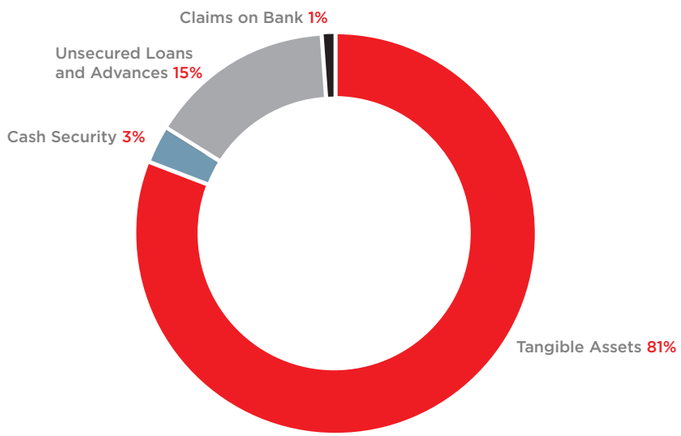
RISK MANAGEMENT REPORT (CONTINUED)

COLLATERAL COVER



Where a claim on counterparty is secured against eligible collateral, the secured portion of the claim is weighted according to the risk weight of the collateral and the unsecured portion against the risk weight of the counterparty. To mitigate counterparty risk, the Bank also requires closeout netting agreements. This enables the Bank to net the positive and negative replacement values of contracts if the counterparty defaults. The Bank's policy is to promote the use of closeout netting agreements and mutual collateral management agreements with an increasing number of products and counterparties in order to reduce counterparty risk.

As an indication, claims secured by cash which has been netted off against exposure are 3% of the asset book, whilst 1% of total asset book was for claims on banks.

MARKET AND LIQUIDITY RISK

Asset And Liability Committee

The objective of the Asset and Liability Committee is to ensure that the Bank's overall asset and liability structure and market risk including liquidity, currency and interest rate risks are managed within the prudential limits and targets delegated by its Board Risk Committee and in accordance with the Guidelines set by the Bank of Mauritius.

On a monthly basis, the Asset and Liability Committee (ALCO) reviews the risk ratios and limits for these areas wherein the Bank has exposure together with sensitivity analysis/stress tests done to monitor impact of potential changes in interest rates or currency movements.

The Bank's Board Risk Committee delegates the implementation and monitoring of the Bank's ALCO strategy, policies and procedures to management. ALCO, is composed of some of the Executive Committee members and meets at least once monthly to review the ALCO risk ratios, financials and other relevant information.

A sub-committee of the ALCO is the Treasury Committee; the main purpose of which is to monitor on a weekly basis the Bank's liquidity position and decide on its investment in Government securities and bank placements.

MARKET RISK MANAGEMENT

Market Risk Management is an independent risk management function that works in close partnership with the lines of business, mainly Treasury desk, to identify and monitor market risks throughout the Bank and to define market risk policies and procedures. The Market Risk function reports to the Bank's Head of Risk.

Market Risk Management seeks to control risks, facilitate efficient risk/return decisions, reduce volatility in operating performance and provide transparency into the Bank's market risk profile for senior management, the Board of Directors and regulators.

Although primary responsibility for managing risk exposure lies with the front office managers, the supervision system is based on an independent structure, the Market Risk Department of the Risk Division. This Department carries out the following tasks:

- establishment of a market risk policy framework;
- independent measurement, monitoring and control of Bank wide market risk;
- definition, approval and monitoring of limits;
- qualitative risk assessments; and
- definition of risk measurement methods, approval of the valuation models used to calculate risks and results.

MARKET RISK

Market risk is the potential for adverse changes in the value of the Bank's assets and liabilities resulting from changes in market variables such as interest rates, foreign exchange rates, equity prices or commodity prices.

INTEREST RATE RISK

With regards to its commercial activities, AfrAsia Bank Limited is exposed to rate fluctuations in several currencies.

This structural interest rate risk arises mainly from the residual gaps (surplus or deficit) of the Money Market & Fixed Income Desk fixed-rate forecasted positions.

AfrAsia Bank Limited uses several indicators to measure its interest rate risk. The three most important indicators are:

- interest rate gap analysis (the difference between outstanding fixed-rate assets and liabilities by maturity): the schedule of fixed rate positions is the main indicator for assessing the characteristics of the hedging operations required. It is calculated on a static basis;
- the net interest income sensitivity to variations in interest rates in various stress scenarios over a 1-year rolling horizon; and
- the economic value sensitivity is a supplementary and synthetic indicator. It is calculated as the sensitivity of the economic value of the statement of financial position to variations in interest rates. This measurement is calculated for all currencies to which the Group and the Bank are exposed.

The following observations can be made with regards to the business structural interest rate risk:

- treasury redirects mainly the funds into Government securities, Nostro, banks placements and margin accounts and invests a non-significant part into corporate bonds. Loans granted to clients represent almost one third of Interest-Bearing Asset;

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RISK MANAGEMENT REPORT (CONTINUED)

- the funding stems mainly from clients' current accounts, time deposits and saving accounts; and
- the impact of interest rate fluctuations on the Bank's Net Interest Income (NII) over a one year period is limited. The most significant sensitivities for NII are for a further decrease of MUR rate and an increase Federal Reserves Bank. See Note 38(d) for Interest Rate Risk Analysis.

CURRENCY RISK

Currency risk or foreign exchange risk is defined as the risk that the value of the Bank's foreign currency positions may be adversely affected by movements in foreign exchange rates.

The Bank does not actively take foreign exchange risk in its core deposit taking and lending operations.

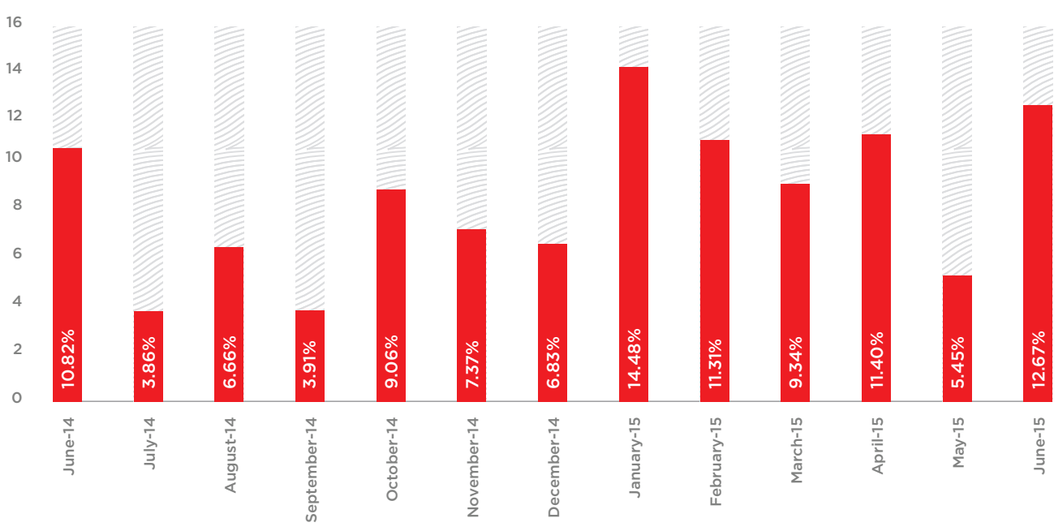
However, the Bank services clients' activity in products across foreign exchange and structured foreign exchange products and acting as a market maker dealer for corporate and institutional clients does require the management of "open positions" from foreign exchange transactions with these counterparties.

These positions are monitored daily according to prudential trading limits that have been delegated to dealers by the Board Risk Management Committee on intra-day and overnight open exposures. Transactions are mostly micro hedged or back-to-back with other banks.

The following observations can be made with regards to the Bank's currency risk:

- the Bank's net open, either overbought/oversold, position against the Mauritian Rupee has been no more than 15% of Tier I capital, throughout the financial year ended 30 June 2015, which is in compliance with the Bank of Mauritius requirements.

FOREIGN EXCHANGE EXPOSURE FROM JUNE 2014 to JUNE 2015 on a monthly basis



- the following table presents the sensitivity of net profit to the fluctuation of the major currencies traded by the Bank. A 5% movement has been used against each currency.

CURRENCY	% change in currency rate	Assets	Liabilities	EFFECT ON PROFIT OF CHANGE IN CURRENCY ON Assets	EFFECT ON PROFIT OF CHANGE IN CURRENCY ON Liabilities	SENSITIVITY OF NET INCOME AND EQUITY
		MUR'000	MUR'000	MUR'000	MUR'000	MUR'000
AUD	+5%	633,079	631,064	31,654	(31,553)	101
	-5%			(31,654)	31,553	(101)
EUR	+5%	13,287,577	13,156,548	664,379	(657,827)	6,551
	-5%			(664,379)	657,827	(6,551)
GBP	+5%	3,897,727	3,892,020	194,886	(194,601)	285
	-5%			(194,886)	194,601	(285)
USD	+5%	41,410,619	41,168,418	2,070,531	(2,058,421)	12,110
	-5%			(2,070,531)	2,058,421	(12,110)
OTHERS - FCY	+5%	1,989,017	1,957,935	99,451	(97,897)	1,554
	-5%			(99,451)	97,897	(1,554)

LIMITS

Market risk is controlled primarily through a series of limits, whether set internally by management in the context of the market environment and business strategy and/or set by regulators.

In setting limits, the Bank takes into consideration factors such as market volatility, product liquidity and accommodation of client business and management experience.

The Bank maintains different levels of limits:

Dealers' limits

- Dealers operate within limits approved and are tightly monitored by Back Office
- Dealers request for sign-off from approved signatories ahead of a deal that triggers their dealing limits.

Counterparty limits

- Exposure is determined according to the nature of the contract and its maturity.

RISK MANAGEMENT REPORT (CONTINUED)

Products limits

- Dealers can only transact in products that have been approved by Board Risk Committee;
- Product limits are tightly monitored by the Treasury Back Office.

Forex Exposure limits

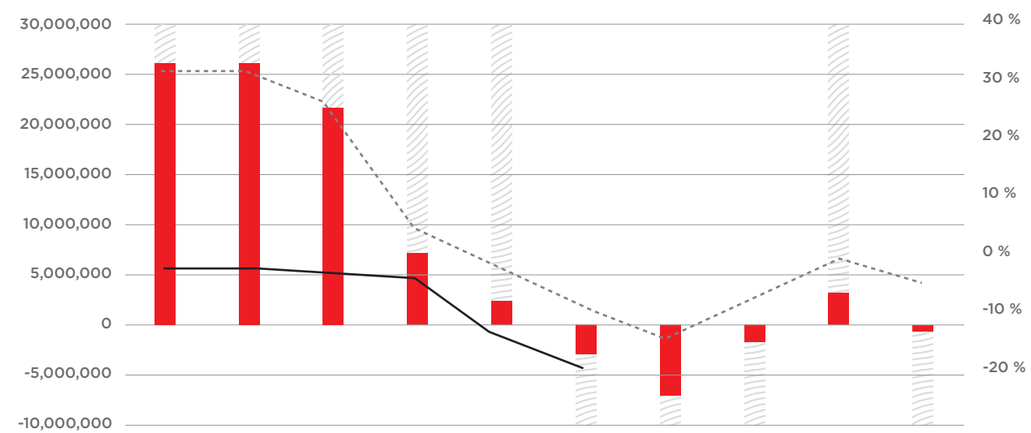
- Foreign exposure is monitored daily and a report is sent to the Bank of Mauritius every day;
- Overall currency exposure may not exceed 15% of Tier 1 Capital and single currency limit is set at 10% of Tier 1 Capital.

LIQUIDITY RISK

Liquidity risk is the risk of not being able to meet cash flow requirements when they fall due and at a reasonable price.

The Bank's Net Funding Ratio ("NFR") analysis requires the building of a maturity ladder to determine any fund excess or shortage at selected maturity dates on a day-to-day basis and on a much longer period. The Bank has, in this respect, prudently set its NFR Gap in line with the guideline on Liquidity Risk Management issued by the Bank of Mauritius. No excess is recorded as at 30 June 2015.

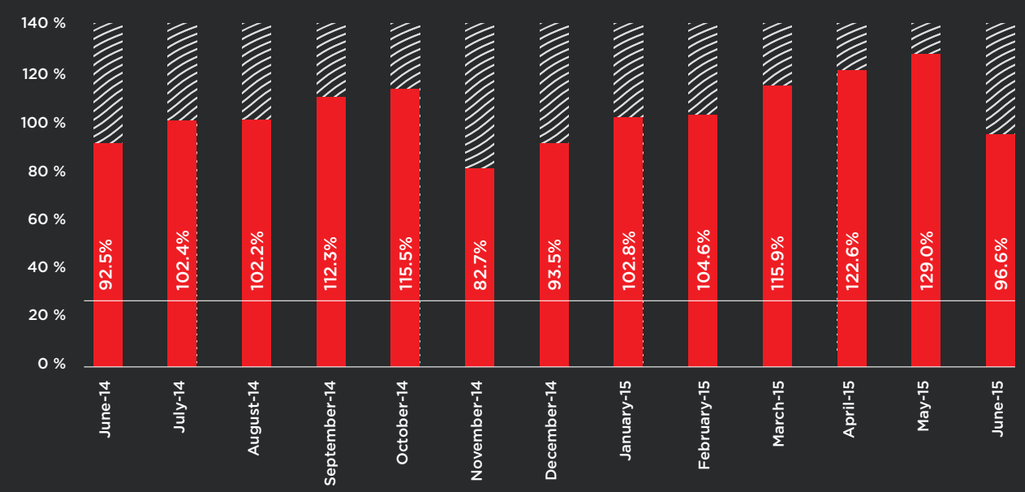
LIQUIDITY GAP ANALYSIS: MUR + FCY — JUNE 2015



	1 Day	2-7 Days	8-14 Days	15 Days to 1 Month	1-3 Months	3-6 Months	6-12 Months	1-3 years	>3 years	Non Maturity Items
Cum Gap	26,842,069	26,702,879	22,239,506	7,343,358	2,367,223	-2,924,207	-7,166,044	-1,861,587	3,058,656	-228,125
NFR Ratio	34.01%	33.83%	28.17%	9.30%	3.00%	-3.07%	-9.08%	-2.36%	3.87%	0.29%
BoM Limits	2%	2%	1%	1%	-10%	-15%				

The liquidity ratio assesses the extent to which assets can be readily converted into cash or cash substitutes to meet financial obligations. AfrAsia Bank Limited's liquidity ratio reflects a strong liquidity position, adequate to absorb the impact of a stressed liquidity and funding environment. The table on the following page shows the month end liquidity ratio maintained during the financial year ended 30 June 2015 against the limit approved by the Board Risk Committee.

LIQUIDITY RATIO - JUNE 2014 TO JUNE 2015



OPERATIONAL RISKS INFORMATION

Operational risks include risks of losses resulting from defects in IT systems, legal disputes, inadequate or erroneous procedures and fraud. The Bank limits its operational risks with business procedures and internal controls that are updated and adjusted to its current business conditions on an on-going basis. The Bank has been computing its operational risks capital computation in line with the Bank of Mauritius Guidelines under the Basel II Basic Indicator Approach where the capital charge for Operational Risk is taken at 15% of average gross income over the past 3 years.

The Bank's operational risk management process involves a structured and uniform approach across the Bank. It includes risk identification and assessments, the monitoring of risk indicators, controls and risk mitigation plans for key operational risks.

RISK MANAGEMENT REPORT (CONTINUED)

On an annual basis, the Bank performs a complete review of all its processes and its procedures across all the areas of operation to mitigate the risk arising from the fast growing operations. Each subsidiary, business unit and resource area is now responsible for the day-to-day monitoring of its operational risks and for reducing and preventing losses caused by operational risks. To that end, all Heads of Department have participated in this review and each department has nominated an Operational Risk Business Coordinator (ORBC) who works closely with risk management. Procedures and processes have been updated accordingly and action plans designed for each area.

The review conducted during the financial year ended June 2015 showed that risk ranges from 'low' to 'low to medium'. The overall results were unchanged from last financial year end. Additional controls have been put in place and additional staff have been recruited as well as restructuring of some departments happened in financial year 2014 to ensure higher controls.

Department	Average Rating
Strategic Development/AIL	C
Credit & Risk Management	C
Domestic Sales	C
Treasury	C
Finance	C
Marketing	C
Global Business	C
Human Resources	C
Information Technology	C
Administration	C
Business Operations	C

A - High B - Medium to High C - Low to Medium D - Low

Where, the Risk Matrix/Measurement at the Bank being

Absolute/ Inherent Level of Risk	Exposure				
	1	2	3	4	5
>10	C	B	B	A	A
8 to 10	C	C	B	B	A
5 to 7	C	C	C	B	B
3 to 4	D	C	C	C	B
0 to 2	D	D	C	C	C

A - High B - Medium to High C - Low to Medium D - Low

We note improvements in the Business Operations department in the various Inherent Level of Risk, overall. In another area where we have seen some Inherent Level of Risk increasing, namely the Treasury Department, the Bank tested several systems and a new Treasury system (Front Office) is currently being implemented to cater for the higher volume of trades and also based on new products we are offering to clients. A new ALM (Asset & Liability Management) system is under testing for implementation. The two systems will enhance the level of controls and risk monitoring capabilities. A new system for higher controls has also been implemented for AML monitoring and detection.

BUSINESS CONTINUITY MANAGEMENT (BCM)

Business Continuity Management Policy has been put in place, with appropriate plans to mitigate operational risks, and as a commitment to continue business to our shareholders, customers and employees. The BCM framework has been implemented to provide for a Disaster Recovery site with data being updated as per preset recovery time objectives. This minimizes operational, financial, legal, reputational and other material consequences arising from any disruption to the primary IT infrastructure.

The BCM Framework in place has the following in-built principles:

- responsibility rests on the Bank's Board of Directors and Senior Management;
- explicitly consider and plan for major operational disruptions;
- recovery objectives are in line with the criticality of the operation of the banking system;
- in the "worst case scenario", the recovery time objective (RTO) is set as 4 hours for the core banking application with a Recovery Point Objective (RPO) of 15 minutes;
- certain non-critical functions may be recovered within a maximum threshold of 24 hours (RTO) after declaring the crisis. The RPO for these systems is set to the state of business as of previous end of day;
- preparation for clear and regular communication during a major operational disruption;
- highlights on cross-border communications during a major operational disruption, as the Bank has global reach;
- ensuring that business continuity plans are effective and identify necessary modifications through periodic testing; and
- ensuring that appropriate procedures for business continuity management reflecting that recovery objectives are adopted and reviewed periodically.

The Bank has put in place a BCM Steering Committee to review the processes after each testing exercise and to review the policy every year with a view to continuously improving resilience. The ultimate objective is to cater for any eventual disruption of operations to be restored within a minimum lapse of time such that the Bank resumes to normal operations within a reasonable time frame.

RISK MANAGEMENT REPORT (CONTINUED)

The Bank has moved its data centre to Ebène and set up the Disaster Recovery (DR) site in its premises at Port Louis.

The network of the Bank has been upgraded this year to mitigate the risk of failure from a single provider. There are redundant links between the Bank sites in Port Louis and Ebène and also for internet connectivity.

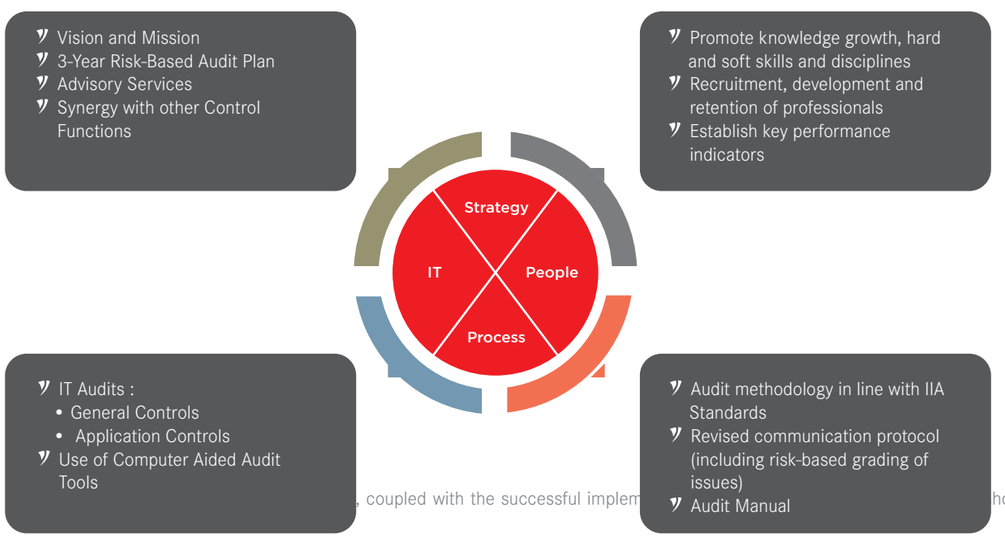
A BCM test is performed annually for all critical infrastructure involving all functions and user groups of the Bank to ensure the effectiveness of the processes and the readiness of the infrastructure and people.

INTERNAL AUDIT

During the year under review, the Internal Audit Department has conducted 29 operational audits and ad hoc assignments covering several business operations of the Bank. As at this date, a significant number of recommendations has been satisfactorily addressed by Management. In addition, an independent service provider performed an IT Security Assessment, whereby - after necessary corrective actions - it was concluded that AfrAsia Bank Limited's network, operating and database systems (including Internet Banking) were adequately secured.

The Bank has appointed a new Head of Internal Audit, effective 1 July 2015, following the retirement of the former Head. As was previously the case, reporting lines will remain to the Audit Committee for direction and accountability and to the Executive Directors for administrative interface and support in line with good governance practices.

A more robust framework, through the elaboration of a 3-year strategic plan amongst others, is being implemented to enable the Internal Audit Function to progressively position itself as a strategically focused unit as defined by the Institute of Internal Auditors (IIA)*. Four pillars, namely (i) Strategy, (ii) People (iii) Process and (iv) Information Technology, have been identified as primary basis to help accomplishing the set objective, as illustrated below:



, coupled with the successful implem hould in the near future be in a position to provide relevant stakeholders of the Bank with more value added solutions, insight and innovative approach to help the organisation accomplish its objectives.

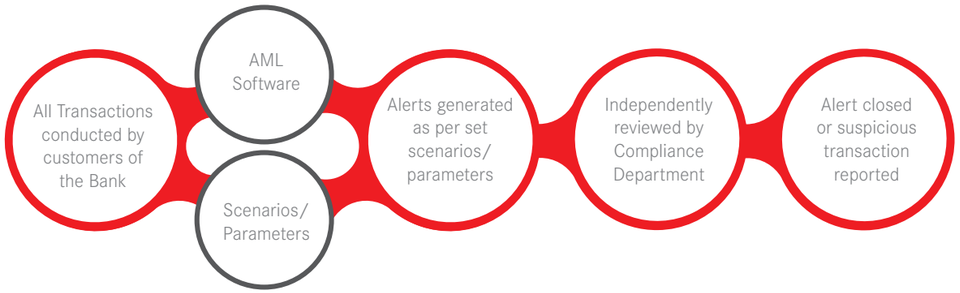
*Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

COMPLIANCE

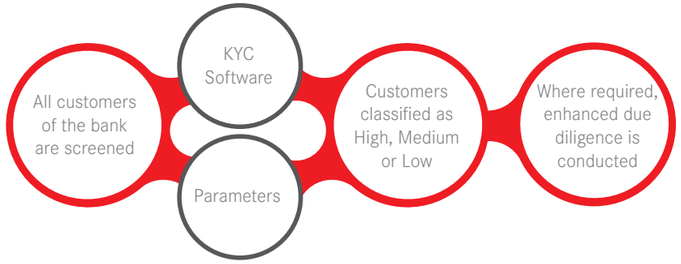
The Bank's Compliance Function is responsible for the identification and management of Compliance and Money Laundering Risk. Internal control and risk mitigation measures are put in place and implemented to ensure compliance with the relevant laws, regulations and internal policies and procedures.

As per the approved Compliance Plan, Compliance reviews of departments are conducted and reports are duly submitted to Senior Management, the Compliance Committee, Audit Committee of the Board and the Board of Directors.

With the implementation of a fully automated Anti-Money Laundering Software, the Compliance Department independently reviews transactions and the Anti-Money Laundering alerts generated based on agreed parameters, transaction amounts and frequency. The transaction monitoring system in place also assists in the independent investigations of suspicious cases. Consequently, appropriate decisions and actions are taken by the Money Laundering Reporting Officer.



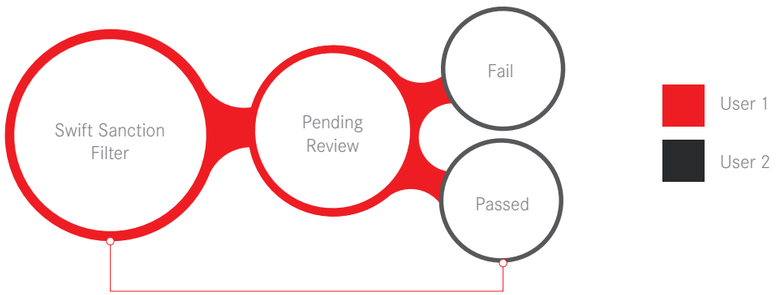
Furthermore the Know Your Customer software in place allows KYC profiling, which is improved through enhanced due diligence, customer identification, screening and customer risk scoring.



RISK MANAGEMENT REPORT (CONTINUED)

The SWIFT Sanction Screening system of the Bank, which screens all details contained in incoming and outgoing Swift messages, ensures that the Bank is not facilitating payments for individuals and organisations blacklisted under the US, EU, OFAC and UN Sanction lists.

The decision workflow below is the internal process that the Bank applies for investigation and instruction on alerted messages. In the case of a false positive and no issue is found, User 1 takes the Pass decision and releases the message. In the case of a possible true hit, User 1 escalates the alert to User 2. This action moves the alert to a Pending Review state. User 2 then decides to Pass or Fail the message.



CAPITAL STRUCTURE AND ADEQUACY

RISK WEIGHTED ASSETS

AFRASIA BANK LIMITED BASEL	BASEL III	BASEL II	BASEL II
	2015	2014	2013
	MUR'000	MUR'000	MUR'000
Common Equity Tier 1 capital: instruments and reserves			
Share Capital	2,511,291	3,133,884	1,694,593
Share premium (from issue of ordinary shares included in CET1)	13,923	14,283	15,848
Statutory reserve	152,116	125,861	92,464
Accumulated other comprehensive income and other disclosed reserves	182,164	332,175	304,599
Common Equity Tier 1 capital before regulatory adjustments	2,859,494	3,606,203	2,107,504
Common Equity Tier 1 capital: regulatory adjustments			
Treasury (Own Shares)	-	(405,776)	-
Other intangible assets	(48,018)	(37,667)	(15,420)
Deferred Tax	(19,607)	(8,897)	(8,055)
Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	(94,781)	(356,045)	(191,557)
Total regulatory adjustments to Common Equity Tier 1 capital	(162,406)	(808,385)	(215,032)
Common Equity Tier 1 capital (CET1)	2,697,087	2,797,818	1,892,472

CAPITAL STRUCTURE AND ADEQUACY (CONTINUED)

AFRASIA BANK LIMITED BASEL	BASEL III	BASEL II	BASEL II
	2015	2014	2013
	MUR'000	MUR'000	MUR'000
Additional Tier 1 capital: instruments			
Instruments issued by the Bank that meet the criteria for inclusion in Additional Tier 1 capital (not included in CET1)	1,319,420	-	-
Additional Tier 1 capital before regulatory adjustments	1,319,420	-	-
Additional Tier 1 capital: regulatory adjustments			
Total regulatory adjustments to Additional Tier 1 capital	-	-	-
Additional Tier 1 capital (AT1)	1,319,420	-	-
Tier 1 capital (T1 = CET1 + AT1)	4,016,507	2,797,818	1,892,472
Tier 2 capital: instruments and provisions			
Instruments issued by the Bank that meet the criteria for inclusion in Tier 2 capital (and are not included in Tier 1 capital)	684,463	836,345	841,301
Provisions or loan-loss reserves (subject to a maximum of 1.25 percentage points of credit risk-weighted risk assets calculated under the standardised approach)	307,117	219,363	155,479
Tier 2 capital before regulatory adjustments	991,580	1,055,708	996,780
Tier 2 capital: regulatory adjustments			
Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	(94,781)	(356,045)	(191,557)
Other Adjustments to Tier 2 capital	-	-	-
Total regulatory adjustments to Tier 2 capital	(94,781)	(356,045)	(191,557)
Tier 2 capital (T2)	896,799	699,663	805,223
Total Capital (capital base) (TC = T1 + T2)	4,913,306	3,497,481	2,697,695
Risk weighted assets			
Credit Risk	33,646,596	25,170,144	20,215,748
Market Risk	491,320	418,328	681,890
Operational Risk	1,743,573	1,168,809	765,474
Total risk weighted assets	35,881,489	26,757,280	21,663,112

Capital ratios (as a percentage of risk weighted assets)	Regulatory Limits Under Basel III			
CET1 capital ratio	6.0%	7.5%	N/A	N/A
Tier 1 capital ratio	7.5%	11.2%	N/A	N/A
Total capital ratio	10.0%	13.7%	13.1%	12.5%

AfrAsia Bank Limited and its Group Entities
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RISK MANAGEMENT REPORT (CONTINUED)

	30 JUNE 2015			
Reconciliation with audited financial statements	Statement of Financial Position as in published financial statements	Statement of Financial Position as per Basel III	Differences	Remarks
	MUR	MUR	MUR	
Assets				
Cash and cash equivalent	2,512,469,499	2,512,469,499	-	
Trading assets	1,967,124,284	1,967,124,284	-	
Pledged assets	-	-	-	
Derivative assets held for risk management	-	-	-	
Loans and advances to banks	41,434,529,360	41,434,529,360	-	
Loans and advances to customers	21,707,867,640	21,838,898,874	(131,031,234)	Portfolio provision included as Tier 2 capital
Derivative financial instruments	68,527,133	68,527,133	-	
Financial investments - held for maturity	5,071,692,345	5,071,692,345	-	
Investment securities				
of which: Significant capital investments in financial sector entities exceeding 10% threshold	189,562,500	-	189,562,500	Included as a regulatory adjustment
Property, plant and equipment	98,955,009	98,955,009	-	
Intangible assets				
of which: Goodwill	-	-	-	
of which: Other intangible assets	48,018,166	-	48,018,166	Included as a regulatory adjustment
Deferred tax assets	19,607,046	-	19,607,046	Included as a regulatory adjustment
Other assets of which: Defined benefit pension fund assets	288,150,482	288,150,482	-	
Total assets	73,406,503,463	73,280,346,986	126,156,477	
Liabilities				
Deposits from banks	227,411,484	-	227,411,484	
Deposits from customers	66,928,650,521	-	66,928,650,521	
Derivative financial instruments	54,775,438	-	54,775,438	
Subordinated liabilities				
of which: Subordinated debt not eligible for inclusion in regulatory capital	409,811,103	-	409,811,103	
of which: Subordinated debt eligible for inclusion in regulatory capital	684,463,457	684,463,457	-	

	30 JUNE 2015			
Reconciliation with audited financial statements	Statement of Financial Position as in published financial statements	Statement of Financial Position as per Basel III	Differences	Remarks
	MUR	MUR	MUR	
Current tax liabilities	51,327,383	-	51,327,383	
Other liabilities	531,786,209	-	531,786,209	
Total liabilities	68,888,225,595	684,463,457	68,203,762,137	
Shareholders' Equity				
Share capital and share premium				
of which amount eligible for CET1	2,608,220,571	2,511,290,607	96,929,964	Not eligible for inclusion in CET1
of which amount eligible for AT1	1,385,768,119	1,319,419,547	66,348,572	Not eligible for inclusion in AT1
Retained earnings	107,087,117	107,087,117	-	
Other reserves	417,202,061	417,202,061	-	
Total shareholders' equity	4,518,277,868	4,354,999,332	163,278,536	

AfrAsia Bank Limited and its Group Entities
Annual Report 2015

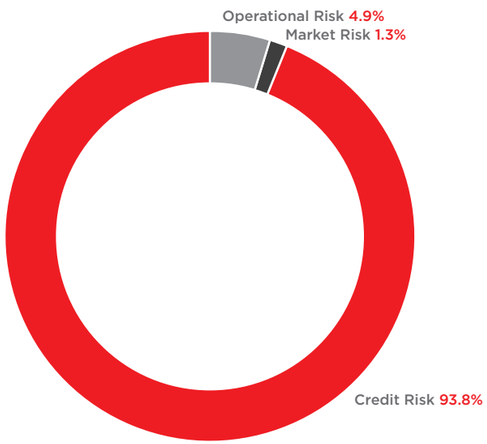
RISK MANAGEMENT REPORT (CONTINUED)

RISK WEIGHTED ASSETS

Total Risk Weighted Assets as at 30 June 2015 was at MUR 35,881,489,346 versus capital base of MUR 4,913,306,315.
Analysis by risk type:

- Credit Risk MUR 33,646,596,314
- Market Risk MUR 491,319,869
- Operational Risk MUR 1,743,573,163

RISK WEIGHTED ASSETS



SUPERVISORY REVIEW PROCESS AND STRESS TESTING

In line with the Bank of Mauritius Guideline on Supervisory Review Process, stress tests are performed on AfrAsia Bank's risk portfolio at least annually in order to assess the impact of possible adverse events on key profit and loss and statement of financial position ratios as well as on the Bank's ability to meet capital requirements at distinct stages of the economic cycle. The Supervisory Review Process recognises the responsibility of the Bank's management in developing a sound Internal Capital Adequacy Assessment Process (ICAAP) and setting up capital targets that are commensurate with the Bank's risk profile.

Stress testing is one of the main elements of the ICAAP and is performed on a monthly basis via ALCO to measure the impact of changes on interest rate (negative and positive interest rate shocks of 100bps across all maturity buckets), foreign currency (5% variance in exchange rates) and liquidity position. On at least an annual basis, stress tests are done on the Bank's portfolio to assess any impact on key performance indicators such as asset downgrade, decline in specific sectors, deposit withdrawal and defaulting counterparties as well as on the Bank's ability to meet capital requirements on the targeted plans. The ICAAP process is to ensure that the capital base reflects the risk and return profile of its business operations while adhering to all regulatory and statutory requirements and good corporate governance.

The ICAAP certificate for FY 2014 had been prepared in line with the guidelines and showed that the Bank has adequate capital to sustain targeted growth. This ICAAP exercise for FY 2014 had taken into account all unexpected scenarios to assess the impact of various operational risks on capital and potential risks associated with the Bank's strategy. This report also showed that the Bank's capital adequacy ratios compare well with those of domestic peers, and the highlighted growth in risk-weighted assets will support the Bank in complying with further regulatory requirements, as well as in maintaining investor confidence. It also demonstrates that chosen internal capital targets are well-founded and those targets are consistent with the Bank's overall risk profile and current operating environment.

BASEL III

BASEL III is a new global regulatory standard on bank capital adequacy and liquidity agreed by the members of the Basel Committee on Banking Supervision in December 2010. Basel III strengthens the Bank's capital requirements and introduces new regulatory requirements on the Bank's liquidity and leverage. It proposes many newer capital, leverage and liquidity standards to strengthen the regulation, supervision and risk management of the banking sector. The capital standards and new capital buffers will require the Bank to hold more capital and higher quality of capital than under current Basel III rules. The new leverage and liquidity ratios introduce a non-risk based measure to supplement the risk-based minimum capital requirements and measures to ensure that adequate funding is maintained in case of crisis. As per the recommendations, the Bank is expected to be compliant by 1st January 2018. Our local supervisor has issued guidelines and recommendations as to measures to be taken by the Bank in line with Basel III. The Bank is geared to implement the proposed Basel III requirements.

RELATED PARTY TRANSACTIONS, POLICIES AND PRACTICES

The Bank adheres to the Guideline on Related Party Transactions issued by the Bank of Mauritius in January 2009. In line with this Guideline, the Board of Directors appointed a Conduct Review Committee to review and approve all related party transactions. The Board has also adopted a policy which sets out the rules governing the identification of related parties, the terms and conditions applicable to transactions entered into with them, and reporting procedures to the Conduct Review Committee.

The Conduct Review Committee ("CRC") comprises three Independent Directors and one Independent Advisor who are not officers or employees of the Bank. This Committee is responsible for the approval of all Category 1 and Category 2 related party transactions, which are not exempted as per Bank of Mauritius guidelines (falling below 2% of Tier 1 capital).

All related party transactions are reviewed at the level of the Conduct Review Committee, which ensures that market terms and conditions are applied to such transactions. Those exceeding the 2% of Tier 1 capital, as and when request is sent for approval and for those exempted transactions i.e. below the 2% of Tier 1 capital; these are reviewed in the quarterly meetings. Furthermore all facilities granted to minority shareholders of the Bank and exceeding 2% of Tier 1 capital, even not classified as Related Party as per Bank of Mauritius guidelines, are reviewed by the CRC on a quarterly basis.

During the normal course of business in the year, the Bank entered into a number of banking transactions with its related parties. These include placements or loans to/from banks, deposits as well as other normal banking transactions. As at 30 June 2015, related party exposure was within regulatory guidelines at 37.6% (Cat 1 and Cat 2). However, the Bank has made a provision of MUR 100.2m on a facility granted to one of its subsidiaries, which has been considered as impaired.

The Bank has complied in all respects with the Bank of Mauritius Guideline on Related Party Transactions. Related party reporting to the Bank of Mauritius is made on a quarterly basis. Moreover, all related party transactions (including those transactions which are exempted as per the Guideline on Related Party Transactions) are monitored and reported to the Conduct Review Committee on a quarterly basis.

INSIGHT

We continue to leverage opportunities of 'The Hopeful Continent' while hiring people with varied expertise to gain insight into the dynamics of emerging African markets.