



PILLAR III

# PUBLIC DISCLOSURES

FOR THE QUARTER ENDED 31 DECEMBER 2018

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Discovery Bank Limited and Discovery Bank Holdings Limited Group

# Discovery Bank Limited and Discovery Bank Holdings Limited Group Public Disclosures for the quarter ended 31 December 2018

The Bank for International Settlements (BIS), through the Pillar III disclosure requirements, encourages banks to promote market discipline by providing market participants with meaningful information relating to their common key risk metrics such as the capital position, an assessment of their risk outlook applicable to crucial activities, as well as the manner in which they manage such risks.

The Prudential Authority regulates, through the Banks Act, (Act No. 94 of 1990) and the Regulations, Directives and Guidance Notes issued in relation thereto, with particular reference to Regulation 43 – Public Disclosure. This is in addition to that received from the Pillar III disclosure requirements outlined by the Basel Committee on Banking Supervision's (BCBS) most recently revised disclosure requirements in Directive D1 – 2018.

When providing this information, disclosures are required to be clear, comprehensive, meaningful, consistent and comparable. This is designed to foster confidence in the manner in which banks manage their respective businesses and further provide comfort that risks are adequately catered for in terms of their available capital composition and liquidity position. When considering the principle relating to "Consistency" (enable interested parties to identify trends in the bank's risk profile), it must be highlighted, that interested parties should expect substantial changes between reporting periods, with particular reference to key metrics such as Net Stable Funding Ratio (NSFR) and Liquidity Coverage Ratio (LCR) as a result of increased migration of Discovery Card clients as well as organic growth in client accounts.

Discovery Bank Limited has adopted a very prudent stance to its evolution as a digital entrant into the banking sector. The Bank fully complies with its

regulatory obligations with respect to the various BA returns, AML and CFT reporting, in addition to complying with industry PASA/SAMOS/VISA standards amongst others. However, the Bank has curtailed its activities and offering to a very limited number of clients who are internal staff. As comfort is gained, the Bank's activities and offerings have broadened in order to fully test the workings of the Bank in preparation for a full market launch.

Significant effort has, and continues to be undertaken with respect to ensuring resilience of the technology systems, seamless integration thereof, testing operating systems, customer front-end processes and risk monitoring activities through stressing of the numerous delivery channels and systems.

The migration of the current Discovery Card (a Visa credit card that was launched by the Discovery Group in a joint venture with FirstRand Bank Limited in October 2004), from FirstRand Bank onto the Discovery Bank platforms, in addition to the market launch of Discovery Bank, both scheduled for March of 2019, will drive the evolution of the change to key metrics such as those referred to above. As such, subsequent Pillar III disclosures will continue to re-align as the card migration materializes and new product offerings are added onto the Discovery Bank platform. A more settled and comparable representation is expected in forthcoming years.

In this maiden submission, the report encompasses the Discovery Bank (and the Discovery Bank Holdings Limited Group) entity and complies with both the letter as well as the spirit of the law with respect to the relevant Pillar III disclosures.

Discovery Bank Limited applied for condonation from the Prudential Authority on 2 July 2018 as it had not launched to the public and with limited information could not produce meaningful information relating to its common key risk metrics as well as the manner in which it manages such risks. In a response letter from the Prudential Authority, dated 8 August 2018, an extension was granted for submission of the Pillar III reports, for the Annual Report dated 30 June 2018 as well as the Quarterly report dated 30 September 2018. This quarterly report will thus contain no comparative figures due to the extension granted by the Prudential Authority.



# Contents

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<b>01   Overview of Risk Management and Risk-Weighted Assets</b>	<b>02</b>
1.1   KMI: Key metrics (at Holdings Consolidated Group Level)	02
1.2   OV1: Overview of Risk-Weighted Assets	04
<b>02   Leverage ratio</b>	<b>06</b>
2.1   LR1: Summary comparison of Accounting assets vs Leverage ratio exposure measure (January 2014 standard)	06
2.2   LR2: Leverage ratio common disclosure template (January 2014 standard)	07
<b>03   Liquidity</b>	<b>09</b>
3.1   LIQ1: Liquidity Coverage Ratio	09
<b>04   Abbreviations</b>	<b>11</b>



# 01 | Overview of Risk Management and Risk-Weighted Assets

## 1.1 | KMI: Key metrics (at Holdings Consolidated Group Level)

The section provides information on Discovery's Prudential Regulatory Metrics. Metrics include Discovery Bank's available capital and ratios, Risk-Weighted Assets, Leverage ratios, Liquidity Coverage Ratios and Net Stable Funding Ratios.

R'000	31 December 2018
<b>Available capital (amounts)</b>	
1 Common Equity Tier 1 (CET1)	2 943 843
1a Fully loaded ECL accounting model	
2 Tier 1	2 943 843
2a Fully loaded ECL accounting model Tier 1	
3 Total capital	2 943 927
3a Fully loaded ECL accounting model total capital	
<b>Risk-Weighted Assets (amounts)</b>	
4 Total Risk-Weighted Assets (RWA)	4 005 965
<b>Risk-based capital ratios as a percentage of RWA</b>	
5 Common Equity Tier 1 ratio (%)	73.480%
5a Fully loaded ECL accounting model Common Equity Tier 1 (%)	
6 Tier 1 ratio (%)	73.480%
6a Fully loaded ECL accounting model Tier 1 ratio (%)	
7 Total capital ratio (%)	73.480%
7a Fully loaded ECL accounting model total capital ratio (%)	
<b>Additional CET1 buffer requirements as a percentage of RWA</b>	
8 Capital conservation buffer requirement (2.5% from 2019) (%)	1.875%
9 Countercyclical buffer requirement (%)	0
10 Bank G-SIB and/or D-SIB additional requirements (%)	0
11 Total of Bank CET1 specific buffer requirements (%) (row 8 + row 9 + row 10)	1.875%
12 CET1 available after meeting the Bank's minimum capital requirements (%)	64.860%



R'000	31 December 2018
<b>Basel III leverage ratio</b>	
13 Total Basel III leverage ratio exposure measure	3 200 725
14 Basel III leverage ratio (%) (row 2; row 13)	92.970%
14a Fully loaded ECL accounting model Basel III leverage ratio (%) (row 2a; row 13)	
<b>Liquidity Coverage Ratio</b>	
15 Total HQLA	120 957
16 Total net cash outflow	30
17 LCR (%)	402 786.510%
<b>Net Stable Funding Ratio</b>	
18 Total available stable funding	4 030 866
19 Total required stable funding	3 918 827
20 NSFR	103

Discovery Bank adopted IFRS 9 on 1 July 2017. Therefore, the figures presented include the effects of IFRS 9.



## 1.2 | OV1: Overview of Risk-Weighted Assets (RWA)

The section provides an overview of the Risk-Weighted Assets of Discovery Bank Limited and the Discovery Bank Holdings Limited Group.

R'000	Discovery Bank Limited		Discovery Bank Holdings Limited Group		
	RWA	Minimum capital requirement	RWA	Minimum capital requirement	
	31 December 2018	31 December 2018	31 December 2018	31 December 2018	
<b>1</b>	<b>Credit risk (excluding counterparty credit risk) (CCR)</b>	<b>2 847 965</b>	<b>227 837</b>	<b>48 671</b>	<b>3 894</b>
2	Of which: standardised approach (SA)	2 847 965	227 837	2 847 965	3 894
3	Of which: foundation internal ratings-based (F-IRB) approach	0	0	0	0
4	Of which: supervisory slotting approach	0	0	0	0
5	Of which: advanced internal ratings-based (A-IRB) approach	0	0	0	0
<b>6</b>	<b>Counterparty credit risk (CCR)</b>	<b>25 537</b>	<b>2 043</b>	<b>25 537</b>	<b>2 043</b>
7	Of which: standardised approach for counterparty credit risk (SA-CCR)	25 537	2 043	25 537	2 043
8	Of which: internal model method (IMM)	0	0	0	0
9	Of which: other CCR	0	0	0	0
<b>10</b>	<b>Credit valuation adjustment (CVA)</b>	<b>20 025</b>	<b>1 602</b>	<b>20 025</b>	<b>1 602</b>
11	Equity positions under the simple risk weight approach	0	0	0	0
12	Equity investments in funds: look-through approach	0	0	0	0
13	Equity investments in funds: mandate-based approach	0	0	0	0
14	Equity investments in funds: fall-back approach	0	0	0	0
15	Settlement risk	0	0	0	0
16	Securitisation exposures in banking book	0	0	0	0
17	Of which: securitisation internal ratings-based approach (SEC-IRBA)	0	0	0	0
18	Of which: securitisation external ratings-based approach (SEC-ERBA), including internal assessment approach (IAA)	0	0	0	0
19	Of which: securitisation standardised approach (SEC-SA)	0	0	0	0



R'000	Discovery Bank Limited		Discovery Bank Holdings Limited Group		
	RWA	Minimum capital requirement	RWA	Minimum capital requirement	
	31 December 2018	31 December 2018	31 December 2018	31 December 2018	
20	<b>Market risk</b>	11 800	944	11 800	944
21	Of which: standardised approach (SA)	11 800	944	11 800	944
22	Of which: internal model approaches (IMA)	0	0	0	0
23	Capital charge for switch between trading book and banking book	0	0	0	0
24	<b>Operational risk</b>	967 952	77 436	997 790	79 823
25	Amounts below the thresholds for deduction (subject to 250% risk-weight)	102 848	11 519	102 848	11 519
26	Floor adjustment	0	0	0	0
27	<b>Total (1+6+10+11+12+13+14+15+16+20+23+24+25+26)</b>	<b>3 976 127</b>	<b>321 381</b>	<b>1 206 671</b>	<b>99 825</b>

Line 2 of the OV1 table includes other assets of R2.8bn (RWA R2.8bn). This includes R2.7bn of prepayments relating to the purchase of the Discovery Card business.



## 02 | Leverage ratio

### 2.1 | LR1: Summary comparison of Accounting assets vs Leverage ratio exposure measure (January 2014 standard)

This table reconciles to the total assets as published in the financial statements to the Leverage ratio exposure measure as reported at 31 December 2018.

R'000	31 December 2018
1 Total consolidated assets as per published financial statements	3 765 325
2 Adjustment for investments in banking, financial, insurance or commercial entities that are consolidated for accounting purposes but outside the scope of regulatory consolidation	0
3 Adjustment for fiduciary assets recognised on the balance sheet pursuant to the operative accounting framework but excluded from the Leverage ratio exposure measure	0
4 Adjustments for derivative financial instruments	7 615
5 Adjustment for securities financing transactions (i.e. repos and similar secured lending)	0
6 Adjustment for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	857
7 Other adjustments	(573 072)
<b>8 Leverage ratio exposure measure</b>	<b>3 200 725</b>

In the leverage calculation of the BA 700 table, credit impairment provisions are added back to the total assets line, and therefore the LR1 table aligns with this calculation methodology.





## 2.2 | LR2: Leverage ratio common disclosure template (January 2014 standard)

The purpose of the Leverage ratio disclosure is to provide a detailed breakdown of the components of the Leverage ratio denominator.

R'000	31 December 2018	
<b>On-balance sheet exposures</b>		
1	On-balance sheet exposures (excluding derivatives and securities financing transactions (SFTs))	3 747 403
2	(Asset amounts deducted in determining Basel III Tier 1 capital)	(573 072)
3	<b>Total on-balance sheet exposures (excluding derivatives and SFTs) (sum of row 1 and 2)</b>	<b>3 174 331</b>
<b>Derivative exposures</b>		
4	Replacement cost associated with all derivatives transactions (where applicable net of eligible cash variation margin and/or with bilateral netting)	17 922
5	Add-on amounts for PFE associated with all derivatives transactions	7 615
6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the operative accounting framework	0
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	0
8	(Exempted CCP leg of client-cleared trade exposures)	0
9	Adjusted effective notional amount of written credit derivatives	0
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)	0
11	<b>Total derivative exposures (sum of rows 4 to 10)</b>	<b>25 537</b>
<b>Securities financing transaction exposures</b>		
12	Gross SFT assets (with no recognition of netting), after adjusting for sale accounting transactions	0
13	(Netted amounts of cash payables and cash receivables of gross SFT assets)	0
14	CCR exposure for SFT assets	0
15	Agent transaction exposures	0
16	<b>Total securities financing transaction exposures (sum of rows 12 to 15)</b>	<b>0</b>
<b>Other off-balance sheet exposures</b>		
17	Off-balance sheet exposure at gross notional amount	4 285
18	(Adjustments for conversion to credit equivalent amounts)	(3 428)
19	<b>Off-balance sheet items (sum of row 17 and 18)</b>	<b>857</b>



R'000	31 December 2018
<b>Capital and total exposures</b>	
20 Tier 1 capital	2 939 936
21 Total exposures (sum of rows 3, 11, 16 and 19)	3 200 725
<b>Leverage ratio</b>	
22 Basel III Leverage ratio	92



## 03 | Liquidity

### 3.1 | LIQ1: Liquidity Coverage Ratio (LCR)

Table LIQ1 shows the breakdown of Discovery Bank's expected cash outflows and cash inflows, as well as its available High-Quality Liquid Assets (HQLA), as measured and defined according to the LCR standard.

At 31 December 2018		Current reporting period	
		Total unweighted (average)	Total weighted (average)
R'000			
<b>High-quality liquid assets</b>			
1	Total HQLA	0	120 957
<b>Cash outflows</b>			
2	Retail deposits and deposits from small business customers, of which:	776	78
3	Stable deposits	0	0
4	Less stable deposits	776	78
5	Unsecured wholesale funding, of which:	0	0
6	Operational deposits (all counterparties) and deposits in networks of cooperative banks	0	0
7	Non-operational deposits (all counterparties)	0	0
8	Unsecured debt	0	0
9	Secured wholesale funding	0	0
10	Additional requirements, of which:	0	0
11	Outflows related to derivative exposures and other collateral requirements	1	1
12	Outflows related to loss of funding on debt products	0	0
13	Credit and liquidity facilities	1 641	41
14	Other contractual funding obligations	0	0
15	Other contingent funding obligations	0	0
16	<b>TOTAL CASH OUTFLOWS</b>	<b>2 418</b>	<b>119</b>



At 31 December 2018		Current reporting period	
		Total unweighted (average)	Total weighted (average)
R'000			
<b>Cash inflows</b>			
17	Secured lending (e.g. reverse repos)	0	0
18	Inflows from fully performing exposures	283 876	282 796
19	Other cash inflows	2	2
20	<b>TOTAL CASH INFLOWS</b>	<b>283 878</b>	<b>282 798</b>
			<b>Total adjusted value</b>
21	<b>Total HQLA</b>	<b>0</b>	<b>120 957</b>
22	<b>Total net cash outflows</b>	<b>0</b>	<b>30</b>
23	<b>Liquidity Coverage Ratio (%)</b>	<b>0</b>	<b>662 461.410%</b>

The Liquidity Coverage Ratio (LCR) measures whether a bank has sufficient High-Quality Liquid Assets (HQLA) to survive a significant stress scenario lasting 30 calendar days.

The LIQ1 table complies with the Pillar III requirements as stipulated by BCBS d400 (March 2017) and Directive D1 – 2018.

The values in the table are calculated as the average of the 90-day calendar daily values over the period, October to December 2018, for Discovery Bank Limited. Discovery Bank's weighted values are based on weekdays (excluding public holidays and weekends).

Deposits within the 30-day window are the key drivers of LCR. The weighted outflow is determined by the liabilities falling into the 30-day contractual bucket. The required HQLA's to be held are based on the characteristics of the liabilities within the 30-day bucket to set-off modelled stressed outflows.

#### **The composition of the High-Quality Liquid Assets (HQLA):**

To date, the HQLA's held by Discovery Bank are treasury bills, spread across 91, 182, 274 and 364 days.

As per the reporting date, Discovery Bank has not launched to the public therefore the LCR values would not have a true reflection on the required ratio.



## 04 | Abbreviations

Abbreviation	Definition
A-IRB	Advanced Internal ratings-based approach
AML	Anti-Money Laundering
ASF	Available Stable Funding
BASA	Banking Association of South Africa
BCBS	Basel Committee on Banking Supervision
CCR	Counterparty Credit Risk
CET1	Common Equity Tier 1
CFT	Countering Financing of Terrorism
CRM	Credit Risk Mitigation
CVA	Credit Valuation adjustment
ECL	Expected Credit Loss
D-SIB	Domestic Systemically Important Banks
F-IRB	Foundation internal ratings-based approach
G-SIB	Global Systemically Important Banks
HQLA	High-Quality Liquid Assets
IAA	Internal Assessment Approach
IMA	Internal model approach
IMM	Internal model method
IRB	Internal Ratings-Based
LCR	Liquidity Coverage Ratio
MDB	Multilateral development banks
NSFR	Net stable funding ratio
PA	Prudential Authority of South Africa
PASA	Payments Association of South Africa
PSE	Public Sector entities
RSF	Required Stable Funding
RWA	Risk-Weighted Assets
SAMOS	South African Multiple Option Settlement
SA	Standardised Approach
SA-CCR	Standardised Approach for Counterparty Credit Risk
SEC-ERBA	Securitisation external ratings-based approach
SEC-IRBA	Securitisation internal ratings-based approach
TLAC	Total loss absorbing capacity
VISA	Visa International Service Association



