16 May 2018

The Audit Committee
**Capitec Bank**
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Dear Audit Committee,

## OPEN LETTER

It is our belief that Capitec management have continued to mislead investors since our previous correspondence with the company. End-of-financial-year announcements in 2018 are reflective deteriorating business conditions and corroborate the continuity of several intentionally misleading accounting practices we have reported in the past.

We will again entertain Capitec's invitation to field questions regarding its business. We believe these questions are quite straightforward, as per our last correspondence on February 20, 2018, and we would appreciate straightforward answers.

In this instance, we are addressing the audit committee with our concerns, as they relate to broader financial reporting transparency and flawed management analysis, corroborating our previous analysis of unsustainable business practices. Our continued review of Capitec's practices and financial results leads us to believe management's delivery of analysis to stakeholders is extremely misleading, and not at all reflective of declining business fundamentals.

This report will follow issues we have raised in previous reports and correspondence with management. You can find all of these reports on our website:

https://viceroyresearch.org/category/capitec-jsecpi/

**We advise that this letter and accompanying documents will be uploaded in full to Viceroy's website on Monday 21 May 2018.**

We look forward a response from the audit committee.

**Yours faithfully**

**Viceroy Research Group**

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## 1. Can the audit committee justify management's analysis that Capitec loans are trending towards the long-term?

Capitec management have emphasized their goal in targeting longer-term (over 6-month) loans as more sustainable and higher-quality assets.

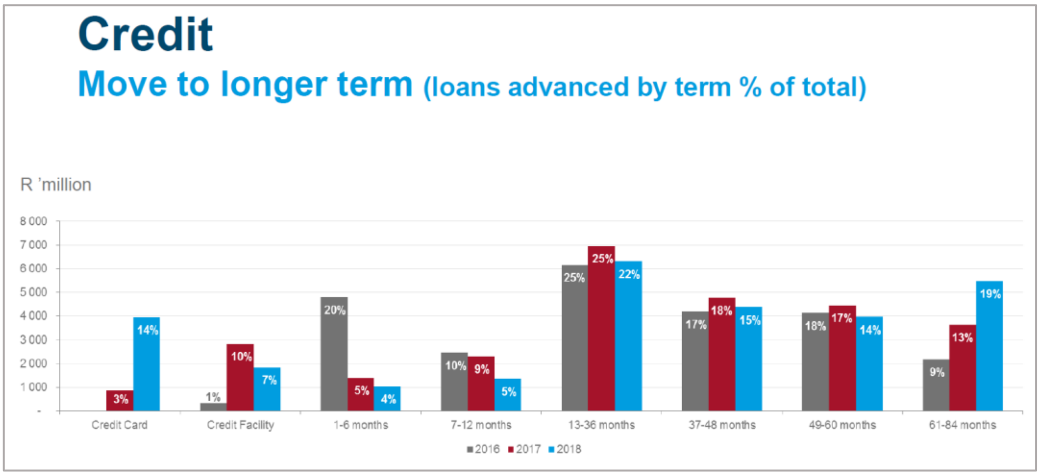


*Figure 1 2018 Capitec Earnings Presentation*

An analysis of Capitec's loan book over the past 3 years does not corroborate this narrative.

| | 2017 | | 2018 | |
|---|---|---|---|---|
| **Credit Sales Analysis** | **H1** | **H2** | **H1** | **H2** |
| $ of loans advanced (ZAR m) | 12,810 | 14,416 | 14,139 | 14,153 |
| *yoy %* | *16%* | *10%* | *10%* | *-2%* |
| # of loans advanced (000's) | 1711 | 1797 | 1871 | 2076 |
| *yoy %* | *-5%* | *-5%* | *9%* | *16%* |
| Average loan size advanced (ZAR) | 7,487 | 8,022 | 7,557 | 6,817 |
| *yoy %* | *22%* | *15%* | *1%* | *-15%* |
| Average loan size advanced <6 months (ZAR) | 1,751 | 1,905 | 2,128 | 2,078 |
| *yoy %* | | | *22%* | *9%* |
| Average loan size advanced >6 months (ZAR) | 25,794 | 26,605 | 29,990 | 32,133 |
| *yoy %* | | | *16%* | *21%* |
| | | | | |
| % of loans advanced <6 months | 76% | 75% | 81% | 84% |
| % of loans advanced >6 months | 24% | 25% | 19% | 16% |
| | | | | |
| Number of loans advanced <6 months (000's) | 1,303 | 1,352 | 1,506 | 1,749 |
| *yoy %* | | | *16%* | *29%* |
| Number of loans advanced >6 months (000's) | 408 | 445 | 365 | 327 |
| *yoy %* | | | *-11%* | *-26%* |
| | | | | |
| value advanced <6 months (ZAR m) | 2,281 | 2,575 | 3,206 | 3,634 |
| *yoy %* | | | *41%* | *41%* |
| value advanced >6 months (ZAR m) | 10,529 | 11,841 | 10,933 | 10,519 |
| *yoy %* | | | *4%* | *-11%* |

*Figure 2 Viceroy Analysis*

The above analysis utilizes figures from Capitec's releases over the past 2 years and shows that – contrary to management's assertions – the number of long-term loans issued over the past 12 months has substantially declined while the number of short-term loans issued has substantially increased.

Figure 2 above clearly shows that value and number of loans greater than 6 months has decreased in 2018. At the same time the value advanced into <6-month loans is up 41% year-on-year in the last 12 months.

Note that these loan sales figures **explicitly** do not include consolidations and rescheduled loans as per the company's statements.

> We report the net amount of credit issued and we exclude the consolidation loans from loan sales.

> Loan sales do not include any rescheduled loans. Rescheduling is an amendment to an existing loan contract with no new credit granted. No initiation fees are charged on rescheduled loans.

*Figures 3 & 4 2018 Capitec CFO Report*

What is the company's honest interpretation of this trend?

When comparing loan sales during a certain period to the company's total credit book at the end of that period, it is apparent that the average value of a long-term loan existing in the company's credit book is significantly larger than the average value of long-term loans issued over that reporting period.

| | 2016 | | 2017 | | 2018 | |
|---|---|---|---|---|---|---|
| **Credit book** | **H1** | **H2** | **H1** | **H2** | **H1** | **H2** |
| Total gross loans | | 40,891 | | 45,135 | | 47,642 |
| Balance sheet provisions | | - 5,131 | | - 5,930 | | - 5,828 |
| Net loans | | 35,760 | | 39,205 | | 41,814 |
| | | | | 10% | | 7% |
| Average loan size <6 months - Beginning of period | | 2,636 | | 2,736 | | 2,621 |
| *yoy %* | | | | *4%* | | *-4%* |
| Average loan size advanced <6 months (ZAR) - During period | | 1,749 | 1,751 | 1,905 | 2,128 | 2,078 |
| *yoy %* | | | | | *22%* | *9%* |
| Average loan size >6 months - Beginning of period | | 30,901 | | 31,123 | | 36,302 |
| *yoy %* | | | | *1%* | | *17%* |
| Average loan size advanced >6 months (ZAR) - During period | | 25,229 | 25,794 | 26,605 | 29,990 | 32,133 |
| *yoy %* | | | | *5%* | *16%* | *21%* |

*Figure 5 Viceroy Analysis*

Viceroy believes this is inconsistent with Figure 1 wherein the company implies it is moving to longer term loans.

Capitec claims that this difference is due to lower value loans being paid down, and uses the example below to illustrate:

> The average loan size at year end greater than 6 months was R36 302, whereas the average loan amount sold (new credit granted) greater than 6 months was R32 133 for the current year. The difference is best explained by the way of an example:
>
> Assume 4 loans of R12 500 each and 1 loan of R50 000 were granted during the year. This results in an average loan amount sold of R20 000 per loan for the period. If 1 of the 4 R12 500 loans is fully repaid, the average loan size at year end would be R21 875.

*Figure 6 2018 Capitec CFO Statement*

Essentially the company is claiming that the discrepancy is due to lower-value loans being paid down. However the justification above only holds true if:

1. The loan book composition substantially changes to include higher-value through proportionately higher sales of said loans
2. The number of loans in the book holds steady once lower-value loan have been paid off (i.e. Capitec stops issuing new loans), and/or;
3. No principal repayments are made on the remaining four loans in the time one loan has been paid in entirety.

Neither of the above are the case, as proven above. Viceroy considers this a flimsy attempt to hide declining business fundamentals.

However, it is consistent with Viceroy's previously iterated belief that Capitec's longer term loan book increases are due to refinanced loans. Corroborating these views are Capitec claims that rescheduled loans are not included in loan sales. The consistency of this difference despite growth in the long-term book leads Viceroy to believe that these loans are accruing rather than being paid down.

> Loan sales do not include any rescheduled loans. Rescheduling is an amendment to an existing loan contract with no new credit granted. No initiation fees are charged on rescheduled loans.

*Figure 7 2018 Capitec CFO Report*

## 2. Can the audit committee elaborate on the nature of internal consolidation and provide analysis into the net loan sales executed to customers who have consolidated existing loans?

The below graph by Capitec shows what are referred to by the company as "internal consolidations". The company has never released this figure prior to this earnings presentation.

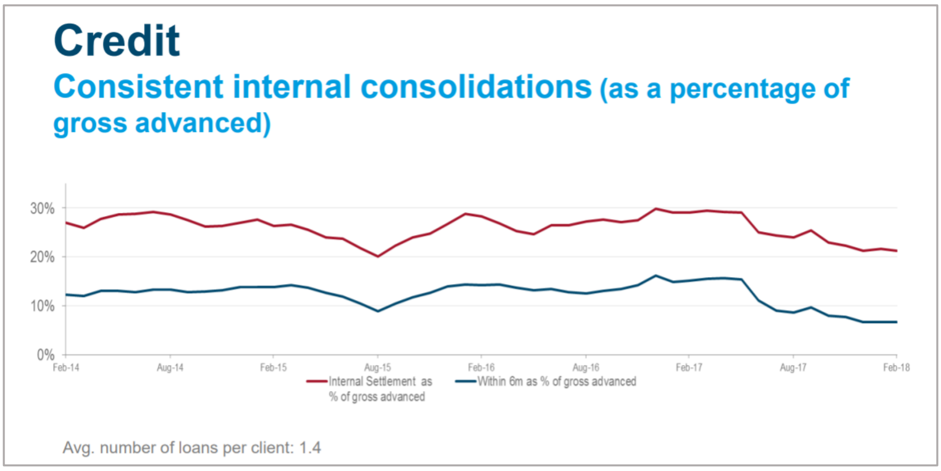


*Figure 8 2018 Capitec Earnings Presentation*

Capitec claims that as of February 2018, internal consolidations averaged 20% of settlements as a percentage of the gross loan sum advanced.

Firstly, we point out that a 20%-30% range of internal consolidations is huge, and comparable to African Bank's levels during their 2014 collapse.

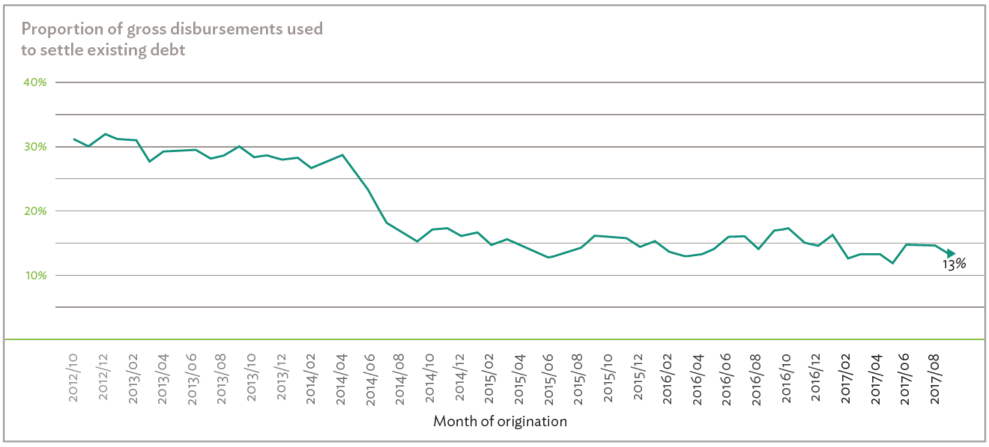


*Figure 9 2017 African Bank Integrated Annual Report*

This implies that a large number and value of new loans issued are being granted to repeat customers: repeat customers needing progressively larger drawdowns.

As previously alluded to by Viceroy: so long as a customer is current with their loan, they are theoretically able to gain an extension. As shown through numerous channel checks and evidenced through court documentation, these customers are not always in financial position to repay these loans.

We have shown this activity exists within Capitec, we believe it is systematic of the microlending environment in South Africa through poor controls established by the NCR. Refer to our previous reports for more information in this regard[1].

We remind stakeholders that these loans are marketed as affordable financing for incidental expenses. This is clearly not the case. Internal consolidations of 20%-30% show this is not the case. Given the nature of these transactions is to essentially draw a further loan amount, the average number of loans per client figure is significantly skewed to the point of irrelevance: it does not show how many customers have drawn down incremental instalments or how large those instalments have been.

This strengthens our belief that loan advancements have been over-represented. Concurrently, this may also explain the declining value of long-term loans issued: customers accruing debt are no longer able to draw down significant amounts. Note that while the consolidated loan amounts are not recorded as new debt, the net increases in loans issued are recorded as such, as are the number of loans.

Further, this amount does not include transactions where cash has been outlaid to customers by Capitec in the form of new loans which we have shown through court documents customers then use to repay existing loans. These types of transactions are not "internal" by nature and would not be represented in this analysis.

## 3. What is the rationale in decreasing bad debt provisions while bad debt is increasing exponentially?

Capitec has responded to an ***increase*** in bad debt by ***decreasing*** bad debt provisions in the 2018 financial year. This seems completely illogical to us, especially given that bad debt has been increasing exponentially since at least 2014 while the company's gross loan book has more-or-less plateaued.

> Our provision for doubtful debts as a percentage of gross loans and advances decreased from 13.1% to 12.2% and the provision coverage of arrears increased from 208% to 216%. The lower provision percentage and higher coverage ratio is a direct result of the better performing loan book.

*Figure 10 2018 Capitec Summarized audited results*

[1] https://viceroyresearch.org/category/capitec-jsecpi/

| | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|
| Bad debts written off | 6 662 | 5 447 | 3 981 | 4 396 |
| Movement in provision for doubtful debt | (102) | 799 | 1 274 | 220 |
| Gross provision for doubtful debt charge | 6 560 | 6 246 | 5 255 | 4 616 |
| Bad debts recovered | (1 280) | (1 125) | (854) | (602) |
| **Net provision for doubtful debt charge** | 5 280 | 5 121 | 4 401 | 4 014 |

*Figure 11 Viceroy analysis of 2018 Capitec summarized audited results*

Bad debt written off has increased 67% since 2016, vastly exceeding the 16.7% growth of Capitec's loan book over the same period. The table below summarizes this data.

| Provisioning Analysis | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|
| **Gross loans and advances** | **36,341** | **40,891** | **45,135** | **47,642** |
| *yoy %* | | *13%* | *10%* | *6%* |
| | | | | |
| **Bad debts written off** | **4,395** | **3,981** | **5,447** | **6,662** |
| *yoy %* | | *-9%* | *37%* | *22%* |
| *Bad debt as % of gross loans* | *12.1%* | *9.7%* | *12.1%* | *14.0%* |
| | | | | |
| **Gross provision for doubtful debt charge** | **4,742** | **5,255** | **6,246** | **6,560** |
| *yoy %* | | *11%* | *19%* | *5%* |
| | | | | |
| Movement in provision for doubtful debt | 347 | 1,274 | 799 | (102) |
| Bad debts recovered | 602 | 854 | 1,125 | 1,280 |
| *yoy %* | | *42%* | *32%* | *14%* |
| **Net provision for doubtful debt charge** | **4,140** | **4,401** | **5,121** | **5,280** |
| *yoy %* | | *6%* | *16%* | *3%* |

*Figure 12 Viceroy Analysis*

## 4. Why have Capitec changed their provisioning method?

It appears Capitec have introduced a vastly different arrears provisions categorization system based on **time in arrears** as opposed to **number of instalments missed**. We have not been able to locate a disclosure to stakeholders on this change of provisioning method.

Due to rescheduling, flexible repayment schedules and unrevised prior-year figures, a real year-on-year analysis of arrears provisioning between these systems is inaccurate. For example, a client who is two installments behind, but billed on a fortnightly basis, may still only be in the first tier of arrears provisioning from 2018, but on the second tier of arrears provisioning from previous years.

While the two are not comparable it should be noted that the highest-risk tiers incur a lower provision rate while low-risk clients incurred a much smaller provision rate reduction.

We provide 8% on current loans, 43% on loans one instalment behind, 81% for two instalments and 92% for three instalments, all statistically calculated. We provide on average 52% on clients that rescheduled any of their loans whilst in arrears within the last 6 months even though they are current in terms of their new agreement. For clients who rescheduled any of their loans whilst current we provide 15%. All provisions are based on the probability of default. All outstanding balances of clients who are 90 days in arrears on any loan are substantially provided for or written off.

At 28 February 2018, the model estimated average provision rates of 8% for clients in CD0, 42% for clients in CD1, 78% for clients in CD2 and 88% for clients in CD3. The model estimated provision rates of 17% for clients rescheduled out of arrears (not rehabilitated) and since rescheduling remained in CD0. This is more than double the provision rate for clients who have never rescheduled, but less than half the percentage relating to clients in CD1. Although the model predicts a default rate of 17% for rescheduled clients, the provision is maintained at 51%, as we do not release the arrears bucket provision when the client reschedules. Provisioning rates change monthly and are based on statistics.

*Figures 13 & 14 Extracts from Capitec 2017 annual report and Capitec 2018 CFO Report, respectively*

*Provisioning*

Capitec uses a provisioning model based on historic roll rates using the Markov chain method. At every month end, each loan is categorised with a specific status, for example:

- up-to-date with a contract delinquency of zero (CD0);
- clients who have missed an instalment and are 1 day up to 1 month in arrears (CD1);
- greater than 1 month up to 2 months in arrears (CD2);
- greater than 2 months up to 3 months in arrears (CD3); or
- clients that reschedule from either up-to-date or arrears statuses that are now up-to-date or in arrears.

*Figure 15 Capitec 2018 CFO Report*

If anything, the new provisioning method would materially decrease the provisioning amounts as clients less than one month in arrears can be over two installments late.

The implementation of this system appears to have moved loans of certain durations into a more favorable provision rate.

| Provision change analysis | Credit card | Credit facility | 1-6 months | 7-12 months | 13-36 months | 37-48 months | 49-60 months | 61-84 months |
|---|---|---|---|---|---|---|---|---|
| **2017** | | | | | | | | |
| Gross | 590 | 114 | 566 | 1,251 | 9,034 | 8,558 | 10,832 | 13,689 |
| Net | 528 | 104 | 498 | 666 | 7,621 | 7,352 | 9,551 | 12,511 |
| Impairment provisions | 62 | 10 | 68 | 585 | 1,413 | 1,206 | 1,281 | 1,178 |
| Provisions as % of gross | 10.51% | 8.77% | 12.01% | 46.76% | 15.64% | 14.09% | 11.83% | 8.61% |
| **2018** | | | | | | | | |
| Gross | 2,014 | 102 | 518 | 1,005 | 8,660 | 8,833 | 10,712 | 15,211 |
| Net | 1,845 | 95 | 469 | 596 | 7,431 | 7,586 | 9,438 | 13,925 |
| Impairment provisions | 169 | 7 | 49 | 409 | 1,229 | 1,247 | 1,274 | 1,286 |
| Provisions as % of gross | 8.39% | 6.86% | 9.46% | 40.70% | 14.19% | 14.12% | 11.89% | 8.45% |
| Change in provisions as % of growth yoy | -20.15% | -21.76% | -21.26% | -12.97% | -9.27% | 0.18% | 0.57% | -1.76% |

*Figure 16 Viceroy Analysis*

As seen in the table above, even the most historically at-risk groups have seen drastic reductions in their provisioning. This makes sense: clients with shorter-term loans are more likely to have more than one payment a month, however those same loans are at the greatest risk. This would make sense, **if bad debt were not outpacing the growth of the loan book.**

Capitec's new provisioning system appears to reduce provisioning needs despite increases in clients under debt review. The obvious benefit of reducing provisions is a significant bump on earnings in the current period at the cost of future earnings.

We would like the audit committee to confirm whether or not the provisioning method has changed.

1. If so, what would be the real comparable impact year-on-year? Additionally, why were stakeholders not notified of this change?
2. If not, why have the depictions of the provisioning method changed so substantially in 2018? Were the prior year methods and descriptions accurate?

## 5. Deterioration in loan book quality

Viceroy's analysis of Capitec's financial results show deteriorating asset quality and supports our preliminary view that business practices are unsustainable. This is largely contradictory to management's analysis of the same figures. A summary of our analysis is below.

Can the audit committee elaborate on management's analysis of loan book quality?

### Bad debt review

Management attributes the large increase in bad debt to an increase in customers going into debt review and implies that this increase is diluted through improved debt collection.

> The increase in bad debt written off in the current year is mostly due to the increase in the number of clients in debt review.
> Bad debts recovered increased due to improved collection efficiencies and initiatives.

*Figure 17 2018 Capitec Summarized audited results*

Our analysis supports that both of these statements are misleading, bordering on false.

The value of Capitec loans in debt review has only increased on nominal terms. These figures has remained flat against bad debt per Figure 18 below. This suggests that a continued decline in loan book quality has led to increased bad debt and debt review clients, not vice-versa.

### Bad debt recovery

Bad debt recovery efficiency has decreased, contrary to management assertions in Figure 17. The nominal value of bad debt recovered has increased only due to exponentially larger increases in bad debt. The collection efficiency of bad debt has declined year-on-year in FY 2018.

| | 2015 | | | 2016 | | | 2017 | | | 2018 | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Debt Review Analysis (ZAR m)** | **H1** | **H2** | **FY** | **H1** | **H2** | **FY** | **H1** | **H2** | **FY** | **H1** | **H2** | **FY** |
| **Bad debts written off** | **2,129** | **2,266** | **4,395** | **2,118** | **1,863** | **3,981** | **2,394** | **3,053** | **5,447** | **3,400** | **3,262** | **6,662** |
| *yoy %* | | | | *-1%* | *-18%* | *-9%* | *13%* | *64%* | *37%* | *42%* | *7%* | *22%* |
| Bad debts recovered | 259 | 343 | 602 | 397 | 457 | 854 | 537 | 588 | 1,125 | 584 | 696 | 1,280 |
| *As % of prior year bad debt* | | | | | | *19%* | | | *28%* | | | *23%* |
| Gross loans and advances | 35,086 | 36,341 | 36,341 | 37,898 | 40,891 | 40,891 | 42,812 | 45,135 | 45,135 | 46,544 | 47,642 | 47,642 |
| *yoy %* | | | | *8%* | *13%* | *13%* | *13%* | *10%* | *10%* | *9%* | *6%* | *6%* |
| **Debt review** | | | | | | | | | | | | |
| Average balance under debt review (ZAR) | 12,500 | 12,500 | | 13,500 | 12,000 | | 18,000 | 19,500 | | 20,750 | 22,500 | |
| Number of clients under debt review (#) | 54,000 | 56,000 | | 55,000 | 52,000 | | 46,000 | 49,000 | | 62,000 | 50,500 | |
| Balance written off under debt review | 675 | 700 | 1,375 | 743 | 624 | 1,367 | 828 | 956 | 1,784 | 1,287 | 1,136 | 2,423 |
| yoy % | | | | 10.00% | -10.86% | -0.62% | 11.52% | 53.13% | 30.52% | 55.37% | 18.92% | 35.84% |
| **Debt review total balance as % of bad debt** | | | **31.3%** | | | **34.3%** | | | **32.7%** | | | **36.4%** |

*Figure 18 Viceroy Analysis – Estimates used from Figure 6 below*

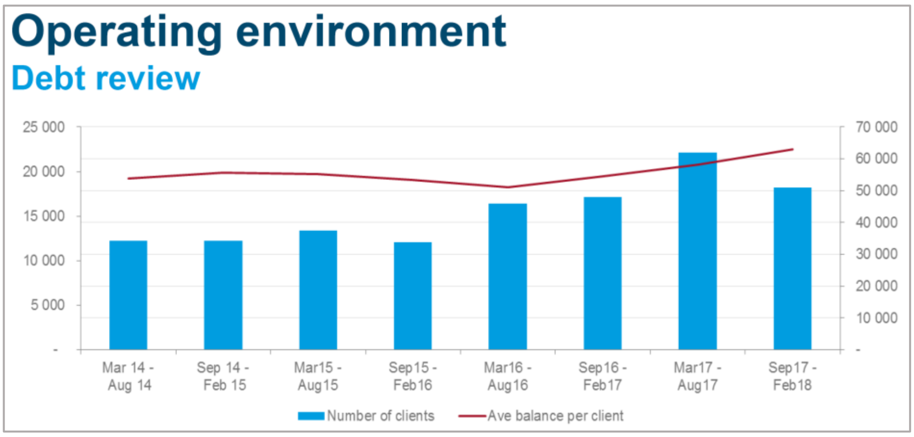


*Figure 19 2018 Capitec Earnings Presentation*

## Increase in loans falling into arrears

The below calculations are courtesy of management in response to a letter by Benguela Global Fund Managers ("Benguela") and related to Capitec's cure rate, a figure representative of the percentage of loans that go into and out of arrears.

| **(1) Estimate of cured arrears** | |
|---|---|
| Arrears balances | |
| Aug-16 | 2,561 |
| Feb-17 | 2,855 |
| Aug-17 | 2,498 |
| **Average arrears** | **2,638** |
| Cure rate (1-provision against arrears balances of 67.8%) | 32.8% |
| Time to cure (months) | 2 |
| Months in year | 12 |
| Estimated arrears cured during the year | 5,192 |

*Figure 20 Extract from Capitec's response to Benguela Global Fund Mangers*

| **Rm** | **Benguela Calculation** | **Capitec calculation** |
|---|---|---|
| **Loans resceduled from arrears:** | | |
| Six months to August 2017 | 1,396 | 1,396 |
| Six months to February 2017 | 1,583 | 1,583 |
| **Numerator: Balances rescheduled during the year** | **2,979** | **2,979** |
| | | |
| Loans in arrears August 2017 | 2,498 | 2,498 |
| **Loans resceduled from arrears:** | | |
| Six months to August 2017 | 1,396 | 1,396 |
| Six months to February 2017 | | 1,583 |
| Write-offs 12 months to August 2017 | | 6,453 |
| Estimated cured arrears 12 months to August 2017[1] | | 5,192 |
| **Denominator: Arrears during the year** | **3,894** | **17,122** |
| | | |
| **Estimated rescheduling % arrears** | 76.5% | 17.4% |

*Figure 21 Extract from Capitec's response to Benguela Global Fund Mangers*

Updated figures show no improvement whatsoever in Capitec's loan book quality. We continue to see anywhere between 30% - 45% of the value of the gross loan book falling into arrears EACH YEAR.

| **Cure rate analysis** | **Average time to cure** | | | | **Average time to cure** | | |
|---|---|---|---|---|---|---|---|
| | **2 months** | **1.5 months** | **1 month** | | **2 months** | **1.5 months** | **1 month** |
| **2018** | | | | **2017** | | | |
| Arrears balances | | | | Arrears balances | | | |
| Feb-17 | 2,855 | 2,855 | 2,855 | Feb-16 | 2,297 | 2,297 | 2,297 |
| Aug-18 | 2,498 | 2,498 | 2,498 | Aug-16 | 2,561 | 2,561 | 2,561 |
| Feb-18 | 2,700 | 2,700 | 2,700 | Feb-17 | 2,855 | 2,855 | 2,855 |
| Average | 2,684 | 2,684 | 2,684 | Average | 2,571 | 2,571 | 2,571 |
| Cure rate (1 - 65%)* | 35% | 35% | 35% | Cure rate (1 - 67.2%)* | 32.8% | 32.8% | 32.8% |
| Time to cure | 2 | 1.5 | 1 | Time to cure | 2 | 1.5 | 1 |
| Months in year | 12 | 12 | 12 | Months in year | 12 | 12 | 12 |
| **Estimated arrears cured during the year** | **5,637** | **7,516** | **11,274** | **Estimated arrears cured during the year** | **5,060** | **6,746** | **10,119** |
| ***As percentage of gross advanced*** | ***11.83%*** | ***15.78%*** | ***23.66%*** | **As percentage of gross advanced** | **11.21%** | **14.49%** | **21.24%** |
| | | | | | | | |
| Loans rescheduled from arrears: | | | | Loans rescheduled from arrears: | | | |
| Six months to Feb 2018 | 1,227 | 1,227 | 1,227 | Six months to Feb 2017 | 1,227 | 1,227 | 1,227 |
| Six months to Aug 2017 | 1,396 | 1,396 | 1,396 | Six months to Aug 2016 | 1,396 | 1,396 | 1,396 |
| | | | | | | | |
| Write-offs 12 months to Feb 2018 | 6,662 | 6,662 | 6,662 | Write-offs 12 months to Feb 2018 | 6,662 | 6,662 | 6,662 |
| | | | | | | | |
| Loans in arrears Feb 2018 | 2,700 | 2,700 | 2,700 | Loans in arrears Feb 2017 | 2,855 | 2,855 | 2,855 |
| Loans in arrears Feb 2017 | 2,855 | 2,855 | 2,855 | Loans in arrears Feb 2016 | 2,297 | 2,297 | 2,297 |
| Change yoy | - 155 | - 155 | - 155 | Change yoy | 558 | 558 | 558 |
| | | | | | | | |
| **Total balance falling into arrears FY 2018** | **14,767** | **16,646** | **20,404** | **Total balance falling into arrears FY 2018** | **14,903** | **16,589** | **19,962** |
| ***As % of gross loan book*** | ***31.0%*** | ***34.9%*** | ***42.8%*** | ***As % of gross loan book*** | ***31.3%*** | ***34.8%*** | ***41.9%*** |

*Figure 22 Viceroy analysis*

We again note that Capitec's calculations utilize a 2-month average time to cure, however management's analysis claims that a 1-month time-to-cure is more realistic.

> model 32.8% of arrears balances cure. A rough estimate would be to take average arrears for the year, multiplied by the cure rate, multiplied by 12 and divided by the average period to cure (two months would be conservative, given that arrears are written off after month 3 and the highest cure rates are observed on clients that are one month in arrears). This would add a further R5.2 billion to the denominator for the period to

*Figure 23 Extract from Capitec's response to Benguela Global Fund Mangers*

As such we can assume that value equal to at least 31% of Capitec's gross loan book falls into arrears each year before being "cured" and made current, but that would be optimistic given highest cure rates are observed on clients that are on month in arrears.

## 6. Can the company elaborate on the effects of IFRS 9 implementation?

We note the following extract from Capitec's 2018 annual report regarding the incoming change to IFRS provisioning:

> Based on the IFRS 9 provisioning methodology, we expect our opening retained earnings on 1 March 2018 to be adjusted by an estimated range of between R850 million and R950 million (pre-tax). This is in line with what we disclosed in the prior year after taking the growth in the loans and advances book into consideration.

*Figure 24 Extract from Capitec's FY 2018 Annual report*

Can the audit committee state the direction of the financial impact?