OUR OPERATING CONTEXT

We operate in a constantly changing environment where a complex and inter-related spectrum of existing and emerging threats and opportunities influence our business activities and shape our future sustainability.

Our approach

We identify our emerging threats and opportunities based on an ongoing assessment of global trends that are likely to have a material bearing on the group's operating environments and business models. Early identification enables us to leverage related opportunities and proactively mitigate negative impacts.

EMERGING THREATS AND OPPORTUNITIES

Issues on the horizon that represent external influences, which could impact the group in a multitude of ways but may not have materialised as yet.

In considering the group's operating environment and changes in the financial services industry, the following emerging threats and opportunities face the world, the continent, our clients and our operations. Technological advancement in particular is shaping how we operate.

1. Economic pressures
2. Political and geopolitical shifts
3. Social threats
4. Technological advancement
5. Environmental threats
6. Competitive landscape
7. Regulatory oversight

EMERGING THREATS AND OPPORTUNITIES

1 Economic pressures

Client impact: adverse impact on revenue, constrained ability to access finance, unemployment and higher levels of debt

Related risks for the group: financial crime risk, conduct risk, credit risk, market risk, liquidity and funding risk

Global

- The global growth path for 2019 was largely shaped by the **adverse effects of trade tensions** between the United States (US) and China. Germany, the primary growth driver of the European Union (EU), experienced recession in the manufacturing sector.
- China is Africa's single largest trading partner for exports of oil, gas and minerals. Initiatives in China to stabilise the financial sector, particularly shadow banking, and the impact of the trade tensions, together resulted in a **slowdown in Chinese economic growth**, injecting volatility into commodity prices and significantly impacting African markets. For some African countries, as much as 79% of their total foreign exchange earnings are from commodity exports.
- The Organisation for Economic Cooperation and Development (OECD) expects **global trade to slow** and the International Monetary Fund (IMF) expects an increase in global growth of only 3.3% in 2020. However, as relations between the US and China thaw meaningfully, aiding China, and central banks in developed world markets implement monetary policy easing, this will support global growth to some degree. Better liquidity flows into emerging markets will buoy their financial markets, potentially strengthening currencies and dousing inflation, allowing central banks to also ease monetary policy. Together these forces could create an environment of accelerated growth for emerging markets and sub-Saharan Africa.

Africa

- The World Bank expects a **slower recovery in sub-Saharan African economic growth**, lowering their 2019 GDP forecast to 2.4% from 3.3%, largely due to faltering growth in Nigeria, Angola and South Africa, which together contribute about 60% of the region's annual economic output. The dominant economic risks for the region include rising public debt, economic fragility, insufficient job creation, lack of infrastructure, low labour productivity and widespread poverty.
- The full impact of the COVID-19 outbreak on global growth remains unknown, however a further slowdown in China's growth and a disruption of Africa-China trade is likely to negatively impact the trade balances of sub-Saharan African commodity exporters and be inflationary for importers.
- The doubling of oil prices from very low prices in 2015/16 has meant that Angola and Nigeria have emerged from recession.
- Africa's low-resource eastern economies are not subject to volatility in commodity prices, and are likely to remain resilient with **economic growth for Kenya, Tanzania and Uganda projected at around 6% by the IMF**. Mozambique will add gas to their GDP from 2022/23. In time, the discovery of oil in the Great Lakes region will put Kenya, Tanzania and Uganda on course to become hydro-carbon extracting and exporting economies.
- **South Africa's structural reform programme**, aimed at reviving the country's struggling economy, is seeing incremental gains at a slow pace. Record unemployment, particularly among the youth (53% of people under the age of 35 are unemployed), poses serious risks to economic recovery and social cohesion. The financial health of SOEs, especially Eskom, is likely to put additional pressure on public finances and ongoing power outages are curbing economic growth and placing the sustainability of smaller businesses at risk. The government's reform programme requires the rebuilding of state institutions, pragmatic public finance management, policymaking that supports investment and aims to make doing business easier and less costly.

Opportunities

The African Continental Free Trade Agreement – effective 30 May 2019 – has created a free trade area covering 52 of Africa's 54 countries, with a total gross domestic product (GDP) of USD2 trillion. The removal of non-trade barriers currently inhibiting the cross-border movement of goods will be a critical driver of long-term growth.

Economic growth prospects for the continent will be supported by one billion people with rising purchasing power. African consumers are projected to spend USD2 trillion by 2025.

Africa has vast sources of power and access to renewable energy – hydro, thermal and solar. 30% of the globe's reserves of mineral resources are found on the continent.

As economic reform in South Africa gains momentum, sentiment, investment and economic growth should improve.

Strong growth prospects

References:

- Standard Bank internal research and analysis.
- OECD – Economic outlook, Interim report March 2020.
- IMF – World Economic Outlook, update January 2020.
- World Bank – Global Economic Prospects: Slow growth, policy challenges.
- Statistics South Africa – Quarterly labour force survey, Q1 2019.
- World Economic Forum (WEF) on Africa 2019 – various articles.

2 Political and geopolitical shifts

Client impact: adverse impact on revenue, disruption, constrained ability to access finance and unemployment

Related risks for the group: regulatory impact risk

- Political dissatisfaction and associated civil unrest in many countries, as well as **rising populism and nationalism** leading to protectionist policies and heightened geopolitical tension, are affecting trade, technology, migration and availability of skills.
- 20 African nations held elections in 2019, with some countries experiencing discontent over the results. **Election-based civil unrest** may indicate dwindling trust in free and fair elections, increasing the risk of conflict and instability.
- Political discontent raises the risk of **reactionary policymaking** and inconsistent implementation, leading to deteriorating sovereign credit ratings and foreign direct investment required to stimulate economic growth. In addition, persistent uncertainty undermines business confidence.
- Africa continues to face the challenges of **poor governance, weak institutions and corruption**.
- There is **increased social pressure** on corporations to speak out on political issues.

Opportunities

The group interacts with governments directly and through various associations, advocating for enabling policy environments that promote national and regional objectives, and beneficial socioeconomic outcomes.

Purpose-driven organisation

3 Social threats

Client impact: unemployment created by digitisation, a need to update skill sets and adapt business practices

Related risks for the group: technology risk, regulatory impact risk, conduct risk, credit risk, people risk

- There is a need for **higher public and private investment in people capabilities,** as well as labour-intensive economic sectors to improve productivity, promote lifelong learning and generate wider benefits for society. Fair remuneration, gender equality and transparency in remuneration, fair working hours and health and safety protection will be required.
- Violations of **human rights and sexual and gender-based violence** fuel conflict and instability.
- ESG considerations are increasingly being integrated into investment processes and there is **growing pressure from stakeholders** for lenders and investors to restrict the financing of unsustainable business practices and to hold corporates, particularly financial services organisations, accountable for the impacts of their business activities.
- There is demand for **better transparency** in ESG indicators. Additionally, regulators are looking to **prescribe how key ESG issues are managed** by business.
- Millennials, now the largest generation in the workforce, along with Generation Z, will form the largest voting bloc in 2020. These generations want to do business with and work for institutions that operate transparently and with **socially conscious business practices**.
- **'Triple Balance Sheet' institutions** – those that focus on people, planet, and profits – are on the rise.

Opportunities

It is estimated that meeting the UN's SDGs could generate USD12 trillion in market opportunities in the areas of food and agriculture, energy and materials, cities, health and wellbeing, and could create up to 380 million jobs globally by 2030.

Innovations in several industries, including healthcare and food production, as well as the advancement of smart cities, will open up new markets with Africa representing an untapped market for these solutions.

Protecting the health and rights of women and young people strengthens the rule of law and drives equity, equality and inclusive growth.

Developing strong relationships with our clients, as well as a holistic understanding of their businesses and our broader impact, will allow the group to embed the SEE framework throughout our business as a viable and significant commercial opportunity.

Established franchise with a large, growing client base

4 Technological advancement

Client impact: individuals, enterprises and corporates expect embedded financial services, intuitive experiences, real-time individualised interactions and seamless service regardless of location

Related risks for the group: cyber risk, technology risk, information risk, business disruption risk, third-party risk

- Technology continues to redefine modern living. Consumers have **access to a multitude of digital tools to simplify decision-making**, shop online, pay bills and invoices, and transfer money. Technology is also being used to provide better estimates of business performance.
- **Smartphone penetration** is now at more than 51% of global consumers and is expected to reach at least 66% in sub-Saharan Africa by 2025.
- **Improving client experience** is becoming more challenging as businesses are increasingly expected to respond to clients with the same level of speed and consistency, irrespective of channel (email, SMS, Facebook Messenger etc).
- **Blockchain** has emerged as a payment mechanism and **AI and cloud** are transforming many aspects of banking. Algorithms have, however, been shown to perpetuate bias with demographic and gender targeting, and AI researchers are now pursuing technical fixes for machine learning bias.
- It is estimated that more than one billion people do not have official identity documents, **a barrier to financial inclusion** for low-income economies. This is further compounded by the increasing use of digital identities to deliver secure and seamless transactions. However, as the cashless future develops, it reduces the payment of smaller, more personal amounts (like charitable donations and cash tips), which further constrain financial inclusion.
- The rise of **cleverly designed misinformation** (fake news) distributed via social media has the potential to damage reputations, negatively impact financial decisions and have unknown consequences on politics.

Opportunities

Improvement to communication networks, the advent of 5G and the digitisation of many industries will give rise to substantially more opportunities for individuals and businesses. In addition, communication is becoming cheaper and providing greater access to rural areas and unbanked communities.

International trade is still driven by paperwork. Investment in digitisation is expected to reduce costs by up to USD6 billion within five years and boost trade revenues by 10%.

The future of urbanisation is smart cities, which combine infrastructure and technology to improve quality of life. These cities enhance citizen interaction with the environment and more accurately allocate resources using connected devices and the internet of things.

Using both non-traditional and traditional data points, new ways of creating reliable credit scores for previously unbanked individuals and businesses are being developed, enabling them to access finance. Similarly, the automation of identity verification will revolutionise the client experience, reduce friction and provide more people and informal businesses with better access to financial services.

Appetite to invest, deliver and partner

References:
- Standard Bank internal research and analysis.
- WEF – www.weforum.org/agenda/2019/06/3-ways-countries-can-boost-social-inclusion-and-economic-growth.
- GSMA Intelligence – The Mobile Economy 2019.
- Euromoney.com – Banks digital deficit, by Kanika Saigal (February 2019).
- MIT Technology Review – This is how AI bias really happens – and why its so hard to fix, by Karen Hao (February 2019).

5 Environmental threats

Client impact: traditional business practices and consumer behaviour will need to adapt to manage changing weather patterns and pollution, as well as to pressure from environmental activists

Related risks for the group: technology risk, regulatory impact risk, conduct risk, climate change risk, credit risk

- **Unpredictable weather patterns, dry conditions and drought** impact agriculture production, resulting in food scarcity, diminished spending on non-food items and inflation. In addition, more than half of sub-Saharan African power, excluding South Africa, is hydro-electric based, therefore lower rainfall affects power supply, impacting all industries.
- All fields of human activity, from agriculture to energy supply, are changing as awareness of the need to **transform the way business is conducted** to protect the environment grows. Corporates are responding by better-managing services and financial support to and from businesses that pollute the environment, have large carbon footprints and follow questionable practices. This could potentially lead to significant changes in loan portfolio mix and revenue outlook for financial services organisations.
- New research from MIT indicates that the **environmental cost of AI** is more substantial than anticipated, particularly as the use of AI models grows exponentially.
- **Ongoing degradation of natural capital** impacts the availability of resources, as well as livelihoods and human development. A reduction in the quality of soil, biodiversity and water impacts food security, the value of land and resettlement of people, and a degraded environment has further impact on health, nutrition and susceptibility to disease.
- Volumes of **oceanic plastic waste** are expected to more than double by 2030 and requires a global revolution in recycling and waste management. The EU will implement a wide-ranging ban on single use plastics from 2021. In Africa, bans on plastic bags have already been implemented in some countries. Activist investors may soon transition their focus to environmental pollutants in addition to the recent activism on coal-fired power funding.

Opportunities

The emergence of new clean technologies and renewable energy programmes. The growth rate for renewable energy exceeds those for oil, gas and coal, and by 2050 is expected to be seven times higher than the average for other fuels.

Renewable energy is crucial to meeting global carbon reduction goals and is fast becoming the cheapest form of power generation in many markets as demand for renewables grows. Other elements include the re-engineering of infrastructure to create a smart grid, the electrification of entire industries, and the introduction of e-mobility across the transport sector. Digitisation, the emergence of smart devices, and the smart grid are opening up possibilities for consumers to gain direct access to the market and manage their consumption or feed any surplus electricity generated into the grid.

60% of the world's uncultivated land is in Africa, with between 480 million and 840 million hectares of unused agricultural land that could be used to increase production up to three times the current output if this is done using 'climate-smart' solutions for the sector.

Diversified revenue streams

References:
- Standard Bank internal research and analysis.
- McKinsey & Co – Fueling the energy transition: opportunities for financial institutions, and Winning in Africa's agricultural market.
- MIT Technology Review – Training a single AI model can emit as much carbon as five cars in their lifetime, by Karen Hao.
- The Banker – Pioneering an open future.
- African Development Bank – Economics Intelligence Unit.

6 Competitive landscape

Client impact: clients will move to competitors with lower-cost, more convenient offerings, and ecosystem players that are becoming intrinsic to their lives

Related risks for the group: cyber risk, technology risk, information risk, third-party risk, non-traditional risk models

- AI, automation, blockchain, cloud and the internet of things are **changing traditional banking operating models**, giving rise to three types of digital competition, namely FinTechs, digital only banks and BigTechs (technology giants with large asset pools, distribution capabilities and the ability to apply big data analytics). These entrants have cheaper startup costs and place pressure on traditional pricing models. To ensure their relevance, traditional banks must invest in replacing legacy systems and in new technology to update their offerings and service channels, driving up costs.
- Non-traditional financial services providers are focused on the unbanked market, **promoting financial inclusion**. Offerings include digitising cash, providing basic savings, accepting deposits, offering payments and remittance services, and issuing ATM cards.

Unrivalled African-focused capability

Opportunities

Partnerships with FinTechs improve the speed and execution of delivery, providing enhanced client experience. We will continue to build a digital portfolio with future ready low-cost models.

The integration of supply chains and client journeys to build ecosystems will help to protect our client base. The use of AI, automation and cloud to leverage vast pools of data will drive competitive differentiation.

By redesigning the work environment, companies can accelerate learning and build problem-solving skills using intuition, creativity, judgement, persuasion and empathy in a machine-dominated world.

Updated branch environments that appeal to the younger generation and small businesses and by offering these clients tailored advisory services.

7 Regulatory oversight

Client impact: onerous, costly and time-consuming processes to ensure regulatory compliance

Related risks for the group: information risk, regulatory impact risk, conduct risk

- The regulatory environment **continues to evolve** as regulators seek to address new and emerging threats in financial services, protect consumers' assets and ensure consumers are treated fairly. Changes in the already complex regulatory landscape, affect multiple parts of a business and implementing effective controls adds cost and is human resource intensive.
- Global financial institutions must diligently monitor and implement change in **three regulatory clusters:** financial stability, prudent operations and resolution. Across Africa, regulators have implemented more stringent capital requirements.
- Growing concerns regarding **information protection and privacy** are giving rise to open banking initiatives – being promoted in the EU – which put consumers in charge of their own data and could create new data sharing models.
- In Africa, most financial regulators are providing a view on **data residency**, including the movement of personal information in and out of their respective borders. This type of legislation will impact on digital and data strategies.

Opportunities

Leverage our knowledge of the different laws, regulations and legislation in the countries in which we operate to assist clients to manage their regulatory and compliance risk profiles.

Use AI, predictive analytics, machine learning and process automation to ensure compliance and provide clients with a simplified and personalised experience.

Apply specialist capability to monitor and assess the implications of regulatory developments and engage with relevant external stakeholders to understand and constructively influence regulation.

Robust capital and liquidity and strong ethical culture