

Management Discussion and Analysis

OVERVIEW

	2004 S\$m	2003 S\$m	+ / (-) %
Selected profit and loss data:			
Net interest income	1,518	1,435	6
Fees and commissions	464	373	24
Dividends	87	75	16
Rental income	72	64	14
Income from insurance ⁽¹⁾	243	–	n.m.
Other income	260	247	5
Total income	2,643	2,193	21
Less : Operating expenses	974	855	14
Operating profit	1,669	1,338	25
Less : Amortisation of goodwill and intangibles	158	127	25
Less : Total provisions	77	225	(66)
Add : Share of associated companies' results	121	235	(49)
Profit before tax	1,555	1,222	27
Net profit attributable to shareholders	1,162	954	22
Cash basis net profit attributable to shareholders ⁽²⁾	1,321	1,081	22
Selected balance sheet data:			
Total assets	119,882	84,497	42
Assets excluding life fund net assets	90,986	84,497	8
Loans to customers (net of provisions)	52,963	50,155	6
Deposits of non-bank customers	57,287	53,460	7
Ordinary shareholders' funds	10,346	9,163	13
Total (ordinary and preference) shareholders' funds	11,242	10,059	12
Key Indicators:			
Return on ordinary shareholders' funds (% p.a.) ⁽³⁾	11.4	10.0	
Return on ordinary shareholders' funds (% p.a.) – Cash basis ⁽³⁾	13.0	11.4	
Return on total shareholders' funds (% p.a.)	10.8	9.8	
Return on total shareholders' funds (% p.a.) – Cash basis	12.3	11.1	
Return on assets (% p.a.) ⁽⁴⁾	1.30	1.13	
Return on assets (% p.a.) – Cash basis ⁽⁴⁾	1.48	1.28	
Basic earnings per ordinary share (S\$) ⁽⁵⁾	0.86	0.72	20
Cash earnings per ordinary share (S\$) ⁽⁵⁾	0.98	0.82	20
Net asset value per ordinary share (S\$)			
– Before valuation surplus	7.86	7.16	10
– After valuation surplus	11.14	9.95	12

⁽¹⁾ Comprise profit from life assurance and net earned premiums from general insurance.

⁽²⁾ Excluding goodwill and intangibles amortisation charge.

⁽³⁾ Calculated after deducting preference shares dividends paid and estimated to be due as at end of period from net profit attributable to shareholders.

⁽⁴⁾ Return on assets is calculated based on assets excluding life fund net assets attributable to policyholders.

⁽⁵⁾ Calculated after deducting declared and/or paid preference shares dividends from net profit attributable to shareholders.

⁽⁶⁾ Some of the figures may not add up to the relevant totals due to rounding.

⁽⁷⁾ n.m. – Not meaningful.

⁽⁸⁾ Certain comparative figures have been restated to conform with current year's presentation.

Management Discussion and Analysis

Group net profit for the financial year ended 31 December 2004 rose 22% to S\$1,162 million, from S\$954 million in 2003. The improved performance was largely driven by strong growth in fee income, higher net interest income, lower provisions and higher contribution from Great Eastern Holdings ("GEH"). Return on ordinary shareholders' funds ("ROE") improved from 10.0% in 2003 to 11.4% in 2004, while cash ROE increased from 11.4% to 13.0%.

The divestment of non-core assets contributed S\$97 million to net profit in 2004, as compared to S\$126 million in 2003. Excluding these gains, the Group's core net profit grew by 29%, from S\$828 million in 2003 to S\$1,065 million in 2004.

Operating profit before provisions and goodwill amortisation rose 25% to S\$1,669 million, as revenue grew 21% to S\$2,643 million, outpacing the 14% increase in expenses to S\$974 million. Net interest income rose 6% to S\$1,518 million, as loans grew by 5% and net interest margin remained stable. Non-interest income increased by 48% to S\$1,126 million, with fee and commission income registering a broad-based expansion of 24% to S\$464 million, boosted in particular by strong wealth management sales.

Reflecting the Group's improved asset quality and the economic recovery, total provision charges declined from S\$225 million in 2003 to S\$77 million in 2004. The Group's non-performing loans ("NPLs") ratio improved significantly from 6.9% to 4.9%.

GEH, previously equity accounted as an associate, was consolidated as a subsidiary from June 2004. Its total net profit contribution to the Group, after taking into account goodwill and minorities, was S\$189 million in 2004, up from S\$163 million in 2003.

A final dividend of 19 cents per share for ordinary shareholders has been proposed, bringing the total dividends for 2004 to 38 cents, an increase of 65% over the 23 cents paid for 2003 (excluding the special dividend paid in July 2003). The estimated total net dividends of S\$403 million for 2004 represent 38% of the Group's core net profit of S\$1,065 million, which is consistent with the Group's dividend policy which targets a minimum payout of 35% of core earnings.

CONSOLIDATION OF GREAT EASTERN HOLDINGS

The Group's shareholding in GEH increased from 48.9% to 81.1% following a voluntary unconditional offer launched in May 2004. The offer was made on the basis of 976 new OCBC shares in exchange for every 1,000 GEH shares. In total, 136.2 million new OCBC shares were issued arising from the offer. The Group's 2004 results included seven months' full consolidation of GEH's results as a subsidiary from June 2004. Prior to June 2004, the Group's 48.9% share of GEH's profit was reflected under the associates' contribution line.

GEH's results are prepared based on Financial Reporting Standard ("FRS") 39 on the Recognition and Measurement of Financial Instruments, but were consolidated on a "non-FRS 39" basis as OCBC Group will only be adopting FRS 39 with effect from 1 January 2005.

The consolidation of GEH contributed S\$304 million to the Group's total income in 2004 (of which S\$243 million was classified under insurance income) and S\$51 million to operating expenses. The full year net profit contribution from GEH was S\$189 million, comprising S\$121 million as a subsidiary (after taking into account goodwill amortisation and minority interests) and S\$68 million as an associate. In 2003, GEH's net profit contribution as an associate was S\$163 million. GEH's consolidation was the main reason for the 42% increase in the Group's total assets from S\$84 billion in December 2003 to S\$120 billion in December 2004.

Total goodwill and intangible assets arising from the acquisition of the additional stake in GEH was S\$1,085 million, comprising S\$295 million of goodwill and S\$790 million of intangible asset pertaining to the value of in-force business. This was computed based on the difference between the acquisition cost of S\$1,811 million and the Bank's additional share in the estimated fair value of GEH's net tangible assets of S\$726 million. Of the total goodwill and intangible assets, S\$32 million was amortised in June-December 2004. With the adoption of Financial Reporting Standard (FRS) 103 on Business Combinations in January 2005, the goodwill portion will no longer be amortised but will be subject to impairment testing. The intangible asset component will continue to be amortised over 20 years, translating to an estimated S\$40 million per annum.

Management Discussion and Analysis

NET INTEREST INCOME

Net interest income increased by 6% to S\$1,518 million in 2004, driven by growth in interest earning assets, primarily customer loans and fixed income securities. Net interest margin improved slightly from 1.90% in 2003 to 1.91% in 2004, as higher average yields on interest earning assets offset the increase in cost of funds in a rising interest rate environment.

Average Balance Sheet ⁽¹⁾

	Average Balance ⁽¹⁾ S\$m	2004 Interest S\$m	Average Rate %	Average Balance ⁽¹⁾ S\$m	2003 Interest S\$m	Average Rate %
Assets						
Loans and advances to non-bank customers	51,823	1,923	3.71	48,309	1,791	3.71
Placements with and loans to banks	13,305	296	2.22	14,526	267	1.84
Other interest earning assets ⁽²⁾	14,336	341	2.38	12,610	322	2.55
Total interest earning assets	79,464	2,560	3.22	75,445	2,381	3.16
Non-interest earning assets	24,950	–	–	8,873	–	–
Total assets	104,414	–	–	84,317	–	–
Liabilities						
Deposits of non-bank customers	56,625	717	1.27	55,452	681	1.23
Deposits and balances of banks	13,698	211	1.54	12,135	158	1.30
Other borrowings ⁽³⁾	4,758	114	2.40	4,175	106	2.54
Total interest bearing liabilities	75,081	1,043	1.39	71,763	946	1.32
Non-interest bearing liabilities	18,312	–	–	2,780	–	–
Total liabilities	93,392	–	–	74,543	–	–
Net interest income/margin		1,518	1.91		1,435	1.90

⁽¹⁾ Average balances are based on monthly averages.

⁽²⁾ Comprise debt securities, government securities and treasury bills.

⁽³⁾ Comprise debt securities issued (including Upper Tier 2 subordinated debt, Floating Rate Notes and Euro Commercial Papers) and bills payable.

The table below analyses the changes in net interest income due to changes in volume and changes in rate for 2004 compared to 2003.

Volume and Rate Analysis

	2004 over 2003 Incr/(Decr) due to change in		Net Change S\$m
	Volume S\$m	Rate S\$m	
Interest Income			
Loans and advances to non-bank customers	131	2	132
Placements with and loans to banks	(27)	56	29
Other interest earning assets	41	(22)	19
Total	144	35	180
Interest Expense			
Deposits of non-bank customers	15	21	36
Deposits and balances of banks	24	29	53
Other borrowings	14	(6)	8
Total	53	44	97
Net Interest Income	91	(9)	83

Management Discussion and Analysis

NON-INTEREST INCOME

	2004 S\$m	2003 S\$m	+ / (-) %
Fee and commission income			
Brokerage	53	62	(15)
Wealth management ⁽¹⁾	129	78	65
Fund management	42	19	119
Credit card	35	30	19
Loan-related	66	74	(10)
Trade and remittances ⁽²⁾	57	45	26
Guarantees	18	18	4
Investment banking	19	12	63
Service charges ⁽²⁾	36	31	16
Others	7	4	68
	464	373	24
Dividends	87	75	16
Rental income	72	64	14
Income from insurance ⁽³⁾	243	–	n.m.
Other income			
Dealing in foreign exchange	87	61	44
Dealing in securities and derivatives	(51)	(19)	n.m.
Disposal of investment securities	23	92	(76)
Disposal of associated companies	54	–	n.m.
Disposal of properties	79	47	67
Others	68	66	4
	260	247	5
Total non-interest income	1,126	758	48
Fees and Commissions/Total Income	17.5%	17.0%	
Non-Interest Income/Total Income	42.6%	34.6%	

⁽¹⁾ From sale of unit trusts, bancassurance products and structured deposits and notes.

⁽²⁾ 2003 figures have been restated to reflect the reclassification of remittance fee income from "service charges" to "trade and remittances".

⁽³⁾ Comprise profit from life assurance and net earned premiums from general insurance.

Total non-interest income jumped 48% to S\$1,126 million in 2004, boosted by stronger fee and commission income, and by the consolidation of GEH which contributed S\$285 million in non-interest income. Fees and commissions registered a broad-based expansion of 24% to S\$464 million, led by wealth management income which grew 65% to S\$129 million and fund management income which rose 119% to S\$42 million. Income from investment banking, trade and remittances, and credit cards also performed better, offsetting the decline in stockbroking income.

Foreign exchange dealing income registered strong growth of 44% to S\$87 million. Dealing in securities and derivatives recorded a net loss of S\$51 million in 2004, compared to S\$19 million loss in 2003, mainly due to losses on interest rate swaps sustained under difficult market conditions.

The divestment of non-core assets contributed S\$132 million to non-interest income in 2004, compared to S\$128 million in 2003. The gains in 2004 comprised S\$55 million from the sale of former associate Raffles Investments, and S\$77 million (S\$43 million after minority interests of 45%) from the sale of Whitesands Shopping Mall by a 55%-owned subsidiary.

Management Discussion and Analysis

OPERATING EXPENSES

	2004 S\$m	2003 S\$m	+ / (-) %
Staff costs	531	478	11
Premises and equipment			
Depreciation of fixed assets	62	81	(24)
Amortisation of computer software costs	24	20	19
Maintenance and hire of fixed assets	33	36	(9)
Rental expenses	18	18	1
Others	79	69	15
	216	225	(4)
Other operating expenses	227	152	49
Total operating expenses	974	855	14
Group staff strength – period end	10,582	7,424	43
Group staff strength – average	9,089	7,350	24
Cost-to-income ratio	36.8%	39.0%	

Total operating expenses in 2004 were S\$974 million, an increase of 14% over 2003 partly due to the consolidation of GEH expenses from June 2004, which amounted to S\$51 million. Excluding GEH expenses, operating expenses rose by 8%, mainly attributable to higher staff costs and business promotion expenses. Staff expenses increased due to higher headcount and sales commissions, while business promotion and professional expenses rose in tandem with new business initiatives launched during the year.

With stronger growth in revenue compared to expenses, the cost-to-income ratio in 2004 improved to 36.8% from 39% in 2003.

The Group's headcount was 10,582 at end December 2004, including 2,315 headcount from GEH. Excluding GEH, headcount increased by 11% since December 2003.

Management Discussion and Analysis

PROVISION CHARGES

	2004 S\$m	2003 S\$m	+ / (-) %
Specific provision for loan losses			
– Singapore	114	191	(40)
– Malaysia	40	55	(27)
– Other regional countries	(16)	(27)	41
– Others	5	(25)	n.m.
	143	194	(26)
General provision for loan losses			
– Five regional countries ⁽¹⁾	(32)	(31)	n.m.
– Singapore & others	#	5	n.m.
	(32)	(26)	(27)
Specific provision for diminution in value of investment securities and other assets	(34)	57	n.m.
Total provision charge	77	225	(66)

⁽¹⁾ Five regional countries comprise Malaysia, Indonesia, Thailand, South Korea and the Philippines.

Amount under S\$500,000.

Total provisions in 2004 were S\$77 million, down 66% from S\$225 million in 2003. The decline was contributed by lower specific provisions for loans, and net reversals in general provisions and provisions for diminution in value of investment securities and other assets.

Specific provisions for loans fell from S\$194 million in 2003 to S\$143 million in 2004, reflecting the improvement in the Group's credit processes and stable economic conditions in Singapore and Malaysia.

The Group also reversed a net S\$32 million from its surplus general provisions in 2004, compared to S\$26 million reversed in 2003. The reversal in general provisions was used to offset a provision charge taken to write down the collateral values for long outstanding NPLs in Malaysia, following a special review of the Malaysia NPL portfolio in the fourth quarter.

A sustained improvement in the value of certain investment securities and properties held by the Group during the year resulted in a net reversal of S\$34 million in provisions for such assets, compared to a charge of S\$57 million in 2003.

LOANS AND ADVANCES

Gross loans to customers grew by 5% year-on-year to S\$55.22 billion as at 31 December 2004. Growth was led by housing loans which expanded by 12% to S\$17.29 billion, accounting for 31% of total loans. Loans to general commerce, manufacturing and professionals and individuals registered growth of 20%, 7% and 5% respectively.

	31 Dec 2004		31 Dec 2003	
	S\$m	%	S\$m	%
Loans By Industry				
Agriculture, mining & quarrying	718	1	519	1
Transport, storage and communication	1,568	3	1,525	3
Building and construction	7,123	13	7,302	14
Manufacturing	3,484	6	3,265	6
Financial institutions, investment and holding companies	8,478	15	8,924	17
General commerce	4,652	9	3,871	7
Professionals and individuals	8,575	16	8,129	15
Housing loans	17,287	31	15,382	29
Others	3,339	6	3,672	8
	55,224	100	52,589	100

Management Discussion and Analysis

NON-PERFORMING LOANS

By Grading, Security Coverage and Countries

	Total NPLs ⁽¹⁾ S\$m	Sub- Standard NPLs S\$m	Doubtful NPLs S\$m	Loss NPLs S\$m	Secured NPLs as % of total NPLs %	Non-bank NPLs as % of non-bank loans ⁽²⁾ %
Malaysia						
31 Dec 2004	902	580	230	93	64.8	9.0
31 Dec 2003	1,068	699	126	243	69.3	11.3
Other Four Regional Countries						
31 Dec 2004	98	3	76	19	15.5	13.0
31 Dec 2003	140	17	100	24	22.8	30.8
Total Regional Countries						
31 Dec 2004	1,001	582	307	112	59.9	9.3
31 Dec 2003	1,208	716	225	267	63.9	12.4
Singapore						
31 Dec 2004	1,735	1,082	436	217	60.7	4.4
31 Dec 2003	2,389	1,725	498	166	65.0	6.2
Others						
31 Dec 2004	131	54	75	2	43.2	2.0
31 Dec 2003	237	155	82	–	53.0	3.6
Group Total						
31 Dec 2004	2,866	1,718	817	331	59.6	4.9
31 Dec 2003	3,834	2,596	805	433	63.9	6.9

⁽¹⁾ Comprise non-bank loans, debt securities and contingent facilities.

⁽²⁾ Excluding debt securities.

Total NPLs declined by 25% from S\$3.83 billion at the end of 2003 to S\$2.87 billion as at the end of 2004. The decrease came mainly from Singapore NPLs, where the recoveries, upgrades and write-offs more than offset new NPLs classified during the year.

Singapore NPLs amounted to S\$1.74 billion and accounted for 61% of the Group's total NPLs, while Malaysia NPLs of S\$0.90 billion accounted for 31%. Of the total NPLs, 59.9% were in the substandard category while 59.6% were secured by collateral.

The Group's NPL ratio improved from 6.9% in December 2003 to 4.9% in December 2004. The Singapore NPL ratio improved from 6.2% to 4.4%, while the Malaysia NPL ratio improved from 11.3% to 9.0%.

Management Discussion and Analysis

	31 Dec 2004		31 Dec 2003	
	S\$m	%	S\$m	%
NPLs By Industry ⁽¹⁾				
Agriculture, mining & quarrying	42	5.9	33	6.2
Transport, storage and communication	25	1.6	131	8.6
Building and construction	579	8.1	753	10.3
Manufacturing	416	11.9	497	15.2
Financial institutions, investment and holding companies	360	4.2	523	5.9
General commerce	440	9.5	620	16.0
Professionals and individuals	466	5.4	600	7.4
Housing loans	256	1.5	223	1.4
Others	131	3.9	246	6.7
Sub-total	2,715	4.9	3,626	6.9
Debt securities	151		208	
Total	2,866		3,834	

⁽¹⁾ The percentages refer to the amount of NPLs over gross customer loans in each industry.

	31 Dec 2004		31 Dec 2003	
	S\$m	As % of Total NPLs	S\$m	As % of Total NPLs
NPLs By Period Overdue				
Over 180 days	1,668	58	2,223	58
Over 90 to 180 days	216	7	302	8
Over 30 to 90 days	187	7	242	6
Less than 30 days	106	4	136	4
No overdue	689	24	931	24
	2,866	100	3,834	100

Management Discussion and Analysis

CUMULATIVE PROVISIONS

	Total cumulative provisions ⁽¹⁾ S\$m	Specific provisions S\$m	General provisions S\$m	Specific provisions as % of total NPLs %	Cumulative provisions as % of total NPLs %	Cumulative provisions as % of unsecured NPLs %
Malaysia						
31 Dec 2004	721	362	359	40.2	79.9	226.9
31 Dec 2003	766	402	363	37.6	71.7	233.3
Other Four Regional Countries						
31 Dec 2004	319	106	213	107.6	324.4	384.0
31 Dec 2003	340	127	213	90.9	242.8	314.7
Total Regional Countries						
31 Dec 2004	1,040	468	572	46.8	103.9	259.4
31 Dec 2003	1,106	529	576	43.8	91.5	253.4
Singapore						
31 Dec 2004	1,152	680	472	39.2	66.4	168.9
31 Dec 2003	1,282	771	511	32.3	53.7	153.5
Others						
31 Dec 2004	183	82	102	62.5	140.1	246.6
31 Dec 2003	179	84	95	35.5	75.7	161.1
Group Total						
31 Dec 2004	2,375	1,230	1,145	42.9	82.9	205.2
31 Dec 2003	2,568	1,385	1,183	36.1	67.0	185.6

⁽¹⁾ Include provisions for classified debt securities.

Total cumulative specific and general provisions amounted to S\$2.4 billion as at 31 December 2004, representing 82.9% of NPLs, a significant improvement from the coverage of 67.0% at 31 December 2003. Cumulative specific provisions covered 106.3% of unsecured NPLs (December 2003: 100.1%). Cumulative general provisions were 2.1% (December 2003: 2.3%) of total non-bank loans (net of specific provisions).

Management Discussion and Analysis

EXPOSURE TO THE FIVE REGIONAL COUNTRIES, HONG KONG AND CHINA

	Loans and debt securities			Investments S\$m	Gross Exposure S\$m	Less: Loans to and investments in subsidiaries /branches S\$m	Net Exposure	
	Bank S\$m	Central Bank and Government S\$m	Non-Bank S\$m				Total S\$m	% of Group assets %
Malaysia								
31 Dec 2004	3,048	3,040	9,034	683	15,804	2,734	13,071	14.4
31 Dec 2003	2,954	3,210	8,164	579	14,907	2,494	12,413	14.7
Indonesia								
31 Dec 2004	60	198	489	185	932	77	856	0.9
31 Dec 2003	91	121	285	68	566	68	498	0.6
Thailand								
31 Dec 2004	109	38	121	6	274	50	224	0.2
31 Dec 2003	70	46	87	–	203	55	148	0.2
Korea								
31 Dec 2004	529	50	288	12	879	30	848	0.9
31 Dec 2003	387	34	111	–	532	26	505	0.6
Philippines								
31 Dec 2004	22	17	65	4	107	0	107	0.1
31 Dec 2003	35	16	38	1	90	1	89	0.1
Total Regional Countries								
31 Dec 2004	3,767	3,343	9,997	890	17,997	2,891	15,106	16.6
31 Dec 2003	3,536	3,428	8,686	648	16,298	2,646	13,652	16.2
Hong Kong								
31 Dec 2004	249	11	1,159	146	1,564	144	1,420	1.6
31 Dec 2003	473	28	1,274	103	1,878	145	1,733	2.1
China								
31 Dec 2004	764	79	1,227	5	2,076	473	1,602	1.8
31 Dec 2003	592	7	891	3	1,493	370	1,123	1.3
Total								
31 Dec 2004	4,780	3,433	12,382	1,042	21,637	3,508	18,129	19.9
31 Dec 2003	4,601	3,463	10,851	754	19,669	3,160	16,508	19.5

Note: The exposure table above excludes GEH's life fund assets.

The Group's net exposure (excluding the exposure under GEH's life fund) to the five regional countries – Malaysia, Indonesia, Thailand, South Korea and Philippines – increased 11% during the year to S\$15.11 billion as at 31 December 2004, representing 16.6% of Group assets excluding the life fund. The increase was derived mainly from Malaysia, which accounted for 14.4% of Group assets.

Management Discussion and Analysis

DEPOSITS

	31 Dec 2004 S\$m	31 Dec 2003 S\$m	+ / (-) %
Deposits of non-bank customers	57,287	53,460	7
Deposits and balances of banks	12,455	12,480	-
	69,742	65,940	6
Loans-to-deposits ratio (net non-bank loans/non-bank deposits)	92.5%	93.8%	

Compared to 31 December 2003, total deposits increased by 6% to S\$69.74 billion. Non-bank customer deposits, which accounted for 82.1% of total deposits, rose by 7% to S\$57.29 billion, mainly due to higher fixed deposits and current account balances.

Arising from the launch of the Bank's 3-year US Dollar floating rate notes in June 2004 and the Euro Commercial Paper ("ECP") programme in August 2004, outstanding senior debt and short-term commercial papers amounted to S\$1.77 billion as at 31 December 2004. These debt issues are part of the Group's strategy to tap into the offshore capital markets and the short-dated ECP market for alternative cost-effective funding.

The Group's loans-to-deposits ratio was 92.5% as at 31 December 2004, marginally lower than 93.8% as at end of 2003. Including the senior debt and commercial papers, the adjusted loans-to-deposits ratio was 89.7%.

	31 Dec 2004		31 Dec 2003	
	S\$m	%	S\$m	%
Non-Bank Deposits By Product				
Fixed deposits	36,270	63	34,273	64
Savings deposits	11,178	20	11,131	21
Current accounts	7,159	12	6,108	11
Others	2,680	5	1,948	4
	57,287	100	53,460	100

Management Discussion and Analysis

CAPITAL ADEQUACY RATIOS

	31 Dec 2004 S\$m	31 Dec 2003 S\$m
Tier 1 Capital		
Paid-up ordinary and preference shares	1,321	1,284
Disclosed reserves/others	10,409	8,791
Less: Goodwill/Others	3,088	2,089
	8,642	7,986
Tier 2 Capital		
Cumulative general provisions	859	777
Subordinated term notes	3,861	3,857
	4,720	4,634
Less: Capital investments in insurance subsidiary companies	1,042	–
Less: Others	179	1,167
Total Capital	12,141	11,453
Risk weighted assets including market risk	68,729	62,178
Tier 1 ratio	12.6%	12.8%
Total capital adequacy ratio	17.7%	18.4%

Note: Capital adequacy ratio is calculated in accordance with the MAS Notice 637 to Banks.

The total capital adequacy ratio of the Group, calculated in accordance with the revised capital framework as set out in the MAS Notice 637, remained strong at 17.7% as at 31 December 2004, while the Group's Tier 1 capital ratio was 12.6%.

A total of 136.2 million new OCBC ordinary shares were issued during the year in connection with the Bank's voluntary unconditional offer for GEH. This addition to share capital was partly offset by the cancellation of 80.2 million OCBC shares held by GEH, for a cash distribution of S\$991 million, under a selective capital reduction exercise.

The Group announced on 11 August 2004 that it would set aside S\$500 million for on-market buybacks of its ordinary shares. As at 31 December 2004, approximately 24.9 million ordinary shares have been purchased from the stock market for a total consideration of S\$337 million.

As part of on-going initiatives to enhance the efficiency of its capital structure, the Group launched its maiden offering of hybrid tier 1 preference shares in January 2005, raising S\$400 million of Tier 1 capital.

The Group's issued ordinary share capital as at the end of 2004 was 1,316.5 million shares, compared to 1,280.1 million shares as at end of 2003.

Management Discussion and Analysis

VALUATION SURPLUS

	31 Dec 2004			31 Dec 2003		
	Net book value S\$m	Market value S\$m	Surplus S\$m	Net book value S\$m	Market value S\$m	Surplus S\$m
Properties	1,169	2,552	1,382	1,274	2,664	1,390
Equity securities ⁽¹⁾	1,109	3,809	2,700	1,466	3,499	2,033
Debt securities ⁽²⁾	15,613	15,849	236	13,438	13,587	149
	17,891	22,210	4,318	16,178	19,750	3,572

⁽¹⁾ Includes investment in quoted subsidiary GEH.

⁽²⁾ Includes government treasury bills and securities.

The Group's unrealised valuation surplus amounted to S\$4.32 billion as at 31 December 2004, 21% higher when compared to 31 December 2003. The increase was attributable mainly to equity securities which accounted for S\$2.70 billion or 63% of the surplus, of which the surplus relating to GEH shares was S\$2.0 billion. The valuation surplus for properties was S\$1.38 billion, accounting for 32% of the total surplus.

Management Discussion and Analysis

FINANCIAL DERIVATIVES

In S\$'ooo	31 December 2004					
	Contractual or principal notional amount	Trading		Non-Trading		Fair value - liabilities
Fair value - assets		Fair value - liabilities	Contractual or principal notional amount	Fair value - assets		
Foreign exchange derivatives						
Forwards	885,331	8,819	9,793	4,878,988	38,829	36,036
Swaps	56,024,270	939,812	816,175	5,238,366	434,371	293,225
OTC options – bought and sold	747,398	3,247	4,035	765,544	6,038	2,242
Sub-total	57,656,999	951,878	830,003	10,882,898	479,238	331,503
Interest rate derivatives						
Forwards	27,313,673	5,969	6,372	–	–	–
Swaps	156,014,193	747,721	818,332	13,777,676	454,239	142,954
OTC options – bought and sold	2,196,028	3,557	8,315	669,055	3,698	1,851
Exchange traded futures – bought and sold	1,146,569	39	543	–	–	–
Sub-total	186,670,463	757,286	833,562	14,446,731	457,937	144,805
Equity derivatives						
Options written	–	–	–	6,000	–	–
Options bought	–	–	–	24,957	13	70
Sub-total	–	–	–	30,957	13	70
Credit derivatives						
Credit default swaps	–	–	–	8,170	–	740
Other derivatives						
Gold forwards – bought and sold	–	–	–	16,011	606	1
Total	244,327,462	1,709,164	1,663,565	25,384,767	937,794	477,119
Fair value of trading derivatives included in other assets and other liabilities		1,709,164	1,663,565			

The above table analyses the contractual or underlying principal amounts of derivative financial instruments entered with third parties for trading and non-trading purposes as at 31 December 2004. In addition, they also set out the corresponding gross positive and negative fair values by instrument type. In the financial statements, trading and non-trading (excluding those non-trading derivative financial instruments which are held for hedging and are accounted for on an accrual basis) derivative financial instruments are revalued on a gross position basis and the unrealised gains or losses are reflected in "Other assets" or "Other liabilities".

Management Discussion and Analysis

PERFORMANCE BY BUSINESS SEGMENT

For the purpose of financial reporting, OCBC Group's businesses are presented under the following main segments representing the key customer and product groups: Consumer Banking, Business Banking, Global Treasury and Insurance.

Net Profit by Business Segment

	2004 S\$m	2003 S\$m	+ / (-) %
Consumer Banking	309	220	41
Business Banking	472	392	20
Global Treasury	200	141	41
Insurance	189	–	n.m.
Others*	134	150	(11)
	1,304	903	44
Amortisation of goodwill and intangibles	(158)	(127)	25
Share of associates' profits	89	180	(50)
Minority interests	(73)	(2)	n.m.
Group	1,162	954	22

* Includes gains from divestment of non-core assets (2004: S\$132 million before minority interests; 2003: S\$112 million net of tax).

Consumer Banking

Consumer Banking comprises the full range of products and services offered to individuals, including deposit products (checking accounts, savings and fixed deposits), consumer loans (housing loans and other personal loans), credit cards, stock brokerage and wealth management products (unit trusts, bancassurance products and structured deposits).

Consumer Banking's net profit increased by 41% to S\$309 million in 2004 as a result of higher operating profit driven by loan growth and higher fee-based income.

Business Banking

Business Banking provides a full range of financial services to business customers, ranging from large corporates and the public sector to small and medium enterprises. The products and services offered include long-term loans such as project financing, short-term credit such as overdrafts and trade financing, deposit accounts and fee-based services such as cash management, trustee and custodian services.

Business Banking's net profit increased by 20% to S\$472 million, mainly as a result of lower provisions as asset quality improved.

Global Treasury

Global Treasury engages and assists customers in foreign exchange activities, financial futures trading and money market operations, as well as customer-driven derivatives business.

Global Treasury recorded profit growth of 41% to S\$200 million due to higher income from foreign exchange dealing and structured products as well as higher contributions from managing the Group's government securities portfolio.

Insurance

Insurance business is carried out by subsidiaries of the Bank's 81%-owned Great Eastern Holdings Limited, which provide both life and general insurance products to its customers in Singapore and Malaysia.

The profit of S\$189 million from the insurance business represents GEH's contribution as a subsidiary since June 2004, before amortisation of goodwill and intangibles and minority interests. Profit contribution from GEH as an associate prior to June 2004 is reflected under the associates' contribution line.

Others

The "Others" segment include investment banking, asset management, property development and investment holding, support units, other investments and unallocated items including one-time divestment gains and provisions for diminution in value of investments and other assets.

