

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

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**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

REPORT OF THE DIRECTORS

The directors of DBS Bank (Hong Kong) Limited (the “Bank”) submit their report together with the audited accounts of the Bank and its subsidiaries (the “Group”) for the year ended 31st December 2003.

Legal Merger

Pursuant to the Dao Heng Bank Limited (Merger) Ordinance (Chapter 1172), all the undertakings of DBS Overseas Limited (formerly known as Overseas Trust Bank, Limited), a wholly owned subsidiary of the Bank, and DBS Kwong On Limited (formerly known as DBS Kwong On Bank Limited), a fellow subsidiary of the Bank, were transferred to and vested in the Bank with effect from 21st July 2003.

Principal activities

The principal activity of the Bank is the provision of banking and related financial services. The principal activities of the subsidiaries are shown in Note 23 to the accounts.

Change of name

By a special resolution passed by all members of the Bank on 30th June 2003, the name of the Bank was changed from Dao Heng Bank Limited to DBS Bank (Hong Kong) Limited with effect from 21st July 2003.

Results and appropriations

The results of the Group for the year ended 31st December 2003 are set out in the consolidated profit and loss account on page 5.

For the year ended 31st December 2003, a special dividend of approximately HK\$0.653846 per share totalling HK\$3,400,000,000 was paid on 25th April 2003 (year ended 31st December 2002: nil) and no interim dividend was paid (year ended 31st December 2002: HK\$0.04504 per share totalling HK\$234,204,572).

The directors do not recommend the payment of a final dividend for the year ended 31st December 2003 (year ended 31st December 2002: HK\$0.039139 per share totalling HK\$203,523,061).

Reserves

Details of the movements in the reserves of the Bank and the Group during the year are set out in Note 32 to the accounts.

Fixed assets

Details of the movements in fixed assets during the year are set out in Note 24 to the accounts.

Donations

Donations made by the Group during the year amounted to HK\$827,000 (year ended 31st December 2002: HK\$178,000).

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

REPORT OF THE DIRECTORS (CONTINUED)

Directors

The directors during the year and up to the date of this report are:-

Wong Kwong Shing, Frank - Chairman
Randolph Gordon Sullivan - Chief Executive and Managing Director
Jackson Peter Tai
Fock Siew Wah
Leung Chun Ying
Cheng Wai Chee, Christopher
Chan Tak Kin
Leung Ting Mow, Kenneth (appointed on 24th November 2003)
Fung Kwok King, Victor (resigned on 21st July 2003)

In accordance with Article 98 of the Bank's Articles of Association, Messrs. Wong Kwong Shing, Frank, Jackson Peter Tai, Fock Siew Wah, Leung Chun Ying, Cheng Wai Chee, Christopher and Chan Tak Kin retire from office at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

In accordance with Article 90 of the Bank's Articles of Association, Mr. Leung Ting Mow, Kenneth retires from office at the forthcoming Annual General Meeting and, being eligible, offers himself for re-election.

Interests in contracts

No contract of significance, to which the Bank or any of its subsidiaries or its holding companies or any subsidiary of its holding companies was a party and in which a director of the Bank had a material interest, subsisted at the end of the year or at any time during the year.

Arrangements to acquire shares

The following were arrangements which subsisted at the end of the year or at any time during the year which enabled the directors of the Bank to acquire benefits by means of the acquisition of shares of DBS Group Holdings Ltd. ("DBSH"), the ultimate holding company of the Bank, or to be awarded shares of DBSH.

(a) Share Option Scheme/Plan

The DBSH Share Option Scheme (the "Option Scheme") was adopted by the shareholders of DBSH at an Extraordinary General Meeting held on 18th September 1999, to replace the DBS Bank Share Option Scheme (the "DBS Bank Option Scheme") implemented by DBS Bank Ltd. (formerly known as The Development Bank of Singapore Ltd.) ("DBS Bank") following the restructuring of DBS Bank as a wholly-owned subsidiary of DBSH. The Option Scheme was terminated on 18th October 1999 and the outstanding existing DBSH options will continue to remain valid until the date of expiration of the relevant DBS Bank options which they respectively replaced.

The DBS Bank Share Option Plan (the "DBS Bank Option Plan") was adopted by the shareholders of DBS Bank at an Extraordinary General Meeting of DBS Bank held on 19th June 1999 to replace the DBS Bank Option Scheme. The DBSH Share Option Plan (the "Option Plan") was adopted by the shareholders of DBSH at an Extraordinary General Meeting held on 18th September 1999 to replace the DBS Bank Option Plan implemented by DBS Bank.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

REPORT OF THE DIRECTORS (CONTINUED)

(a) Share Option Scheme/Plan (continued)

During the year, options to subscribe for a total of 259,300 shares in DBSH were granted to Messrs. Wong Kwong Shing, Frank, Jackson Peter Tai, Randolph Gordon Sullivan and Chan Tak Kin pursuant to the above DBSH option arrangements. None of the directors acquired shares in DBSH by exercising options granted pursuant to the DBSH option arrangements during the year under review.

(b) Performance Share Plan

The DBSH Performance Share Plan (“PSP”) is a stock-based plan where DBSH ordinary shares are given free of charge to eligible employees. During the year, Messrs. Wong Kwong Shing, Frank, Jackson Peter Tai, Randolph Gordon Sullivan and Chan Tak Kin were eligible to receive performance shares under the PSP.

(c) Vesting of Shares

During the year, a total of 74,480 DBSH shares were vested in Messrs. Wong Kwong Shing, Frank, Jackson Peter Tai, Randolph Gordon Sullivan and Chan Tak Kin under the PSP or as part of the retention packages to the relevant director(s).

Apart from the above, at no time during the year was the Bank or any of its subsidiaries or its holding companies or any subsidiary of its holding companies a party to any arrangement to enable the directors of the Bank to acquire benefits by means of the acquisition of shares in or debentures of the Bank or any other body corporate.

Management contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Bank were entered into or existed during the year.

Compliance with the guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions”

The Group has fully complied with the requirements set out in the guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions” issued by the Hong Kong Monetary Authority.

Auditors

The accounts have been audited by Ernst & Young who retire at the forthcoming annual general meeting and offer themselves for re-appointment.

On behalf of the Board

Wong Kwong Shing, Frank
Chairman

Hong Kong, 9th February 2004

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

REPORT OF THE AUDITORS

TO THE MEMBERS

DBS BANK (HONG KONG) LIMITED
(Formerly known as Dao Heng Bank Limited)
(Incorporated in Hong Kong with limited liability)

We have audited the financial statements on pages 5 to 56 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective responsibilities of directors and auditors

The Companies Ordinance requires the directors to prepare financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, in accordance with Section 141 of the Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes an examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Bank's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31st December 2003 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the Companies Ordinance.

Ernst & Young
Certified Public Accountants

Hong Kong, 9th February 2004

DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)

CONSOLIDATED PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31ST DECEMBER 2003

	Note	2003 HK\$'000	Restated 2002 HK\$'000
Interest income	4	5,331,490	4,856,198
Interest expense	5	(1,681,330)	(2,144,036)
Net interest income		3,650,160	2,712,162
Other operating income	6	1,755,111	961,735
Operating income		5,405,271	3,673,897
Operating expenses	7	(2,171,454)	(1,648,498)
Impairment of fixed assets	8	(25,236)	(241,136)
Operating profit before provisions		3,208,581	1,784,263
Charge for bad and doubtful debts	9	(821,003)	(509,665)
Operating profit		2,387,578	1,274,598
Net (loss) / gain on disposal of fixed assets		(21,374)	19,433
Net gain on disposal of non-trading securities and held-to-maturity securities	10	10,338	19,064
Impairment loss on non-trading securities		–	(13,998)
Share of profit of a jointly controlled entity		2,376,542	1,299,097
		10,022	3,509
Profit before taxation		2,386,564	1,302,606
Taxation	12	(379,154)	(179,892)
Profit attributable to shareholders	13	2,007,410	1,122,714
Dividends	14	3,603,523	474,816

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

**CONSOLIDATED BALANCE SHEET
AS AT 31ST DECEMBER 2003**

	Note	2003 HK\$'000	Restated 2002 HK\$'000
Assets			
Cash and short-term funds	15	23,274,188	19,112,211
Placements with banks and other financial institutions maturing between one and twelve months		4,794,928	8,523,654
Certificates of deposit held	16	1,216,013	837,797
Trading securities	17	1,147,080	2,078,229
Held-to-maturity securities	18	24,719,284	18,298,518
Advances less provisions	19	92,722,726	69,742,660
Non-trading securities	21	5,789,244	2,190,166
Interest in a jointly controlled entity	22	80,481	72,471
Fixed assets	24	4,734,347	4,184,842
Other assets	25	4,226,391	3,693,970
Total assets		<u>162,704,682</u>	<u>128,734,518</u>
Liabilities			
Deposits and balances of banks and other financial institutions		1,070,642	1,387,039
Deposits from customers	26	121,604,354	92,242,833
Certificates of deposit issued		7,865,776	5,718,942
Other liabilities	29	13,020,057	12,234,315
Amount due to a jointly controlled entity	22	1,122,438	1,103,780
7.75% fixed rate subordinated notes	27	2,030,956	2,040,278
Deferred tax liabilities	30	134,243	17,383
Total liabilities		<u>146,848,466</u>	<u>114,744,570</u>
Shareholders' funds			
Share capital	31	5,200,000	5,200,000
Reserves	32	10,656,216	8,789,948
		<u>15,856,216</u>	<u>13,989,948</u>
Total liabilities and shareholders' funds		<u>162,704,682</u>	<u>128,734,518</u>

Wong Kwong Shing, Frank
Director

Randolph Gordon Sullivan
Director

Chan Tak Kin
Director

Wong Wai Nar, Doris
Secretary

DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)

BALANCE SHEET

AS AT 31ST DECEMBER 2003

	Note	2003 HK\$'000	Restated 2002 HK\$'000
Assets			
Cash and short-term funds	15	23,272,681	18,365,029
Placements with banks and other financial institutions maturing between one and twelve months		4,794,928	8,523,654
Certificates of deposit held	16	1,216,013	837,797
Trading securities	17	1,147,080	2,078,229
Held-to-maturity securities	18	24,719,284	18,296,518
Advances less provisions	19	92,722,726	51,424,674
Non-trading securities	21	5,789,244	2,190,066
Interest in a jointly controlled entity	22	500	500
Investments in subsidiaries	23	171,179	4,002,411
Amount due from subsidiaries		615,946	270,650
Fixed assets	24	4,721,596	3,267,783
Other assets	25	4,225,408	2,992,453
Total assets		<u>163,396,585</u>	<u>112,249,764</u>
Liabilities			
Deposits and balances of banks and other financial institutions		1,070,642	1,302,210
Deposits from customers	26	121,604,354	72,516,328
Certificates of deposit issued		7,865,776	5,718,942
Other liabilities	29	12,972,678	12,078,077
Amount due to subsidiaries		897,644	5,489,308
Amount due to a jointly controlled entity	22	1,122,438	1,103,701
7.75% fixed rate subordinated notes	27	2,030,956	2,040,278
Deferred tax liabilities	30	134,074	39,228
Total liabilities		<u>147,698,562</u>	<u>100,288,072</u>
Shareholders' funds			
Share capital	31	5,200,000	5,200,000
Reserves	32	10,498,023	6,761,692
		<u>15,698,023</u>	<u>11,961,692</u>
Total liabilities and shareholders' funds		<u>163,396,585</u>	<u>112,249,764</u>

Wong Kwong Shing, Frank
Director

Randolph Gordon Sullivan
Director

Chan Tak Kin
Director

Wong Wai Nar, Doris
Secretary

**DBS BANK (HONG KONG) LIMITED
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**CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31ST DECEMBER 2003**

	Note	2003 HK\$'000	2002 HK\$'000
Net cash outflow from operating activities before taxation	37(a)	(4,709,766)	(719,617)
Hong Kong profits tax paid		(222,934)	(128,472)
Overseas tax paid		(5,141)	(3,896)
Net cash outflow from operating activities		(4,937,841)	(851,985)
Investing activities			
Placements from a jointly controlled entity		18,659	317,034
Purchase of fixed assets		(74,273)	(157,493)
Proceeds from disposal of fixed assets		160,980	161,124
Net cash inflow from investing activities		105,366	320,665
Financing activities			
Dividends paid		(3,603,523)	(474,816)
Interest paid for certificates of deposit issued		(158,525)	(216,379)
Interest paid for 7.75% fixed rate subordinated notes		(159,705)	(159,670)
Issue of certificates of deposit		5,247,185	3,892,628
Redemption of certificates of deposit		(3,411,710)	(1,853,399)
Net cash (outflow)/inflow from financing activities		(2,086,278)	1,188,364
(Decrease)/increase in cash and cash equivalents		(6,918,753)	657,044
Cash and cash equivalents at 1st January		18,046,457	17,391,700
Additions through merger	38(b)	7,162,456	–
Effect of foreign exchange movements		(538)	(2,287)
Cash and cash equivalents at 31st December	37(c)	18,289,622	18,046,457

**DBS BANK (HONG KONG) LIMITED
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**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31ST DECEMBER 2003**

	Note	2003 HK\$'000	Restated 2002 HK\$'000
Total equity as at 1st January		14,007,331	13,433,526
Effect of changes in accounting policies	32(c),(e) & (g)	(17,383)	(16,762)
Total equity as at 1st January as restated		13,989,948	13,416,764
Impairment of fixed assets	32 (c) & (d)	(84,753)	(59,537)
Change in fair value of non-trading securities	32(e)	77,844	(7,560)
Exchange differences arising on translation of net investments in overseas branches and subsidiary companies	32(g)	(538)	(2,287)
Net losses not recognised in the profit and loss account		(7,447)	(69,384)
Additions through merger			
Share premium	38(a)	564,152	–
Premises revaluation reserve	38(a)	715,926	–
Investment properties revaluation reserve	38(a)	81,752	–
Investments revaluation reserve	38(a)	6,550	–
General reserve	38(a)	1,715,543	–
Retained earnings	38(a)	403,719	–
		3,487,642	–
Profit attributable to shareholders	32(g)	2,007,410	1,122,714
Reserves transferred to profit and loss account upon disposal of non-trading securities	32(e)	(8,794)	(15,950)
Dividends	32(g)	(3,603,523)	(474,816)
Release (to)/from deferred taxation	32(c) & (e)	(9,020)	10,620
Total equity as at 31st December		15,856,216	13,989,948

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS

1 Legal Merger

With effect from 21st July 2003, Dao Heng Bank Limited (“DHB”) has been merged with Overseas Trust Bank Limited (“OTB”) and DBS Kwong On Bank Limited (“DKOB”) through the Dao Heng Bank Limited (Merger) Ordinance (“Merger Ordinance”). Under the Merger Ordinance, all assets, liabilities and every existing reserve relating to the property and liabilities of OTB and DKOB have been transferred to DHB. By virtue of the Merger Ordinance, the accounts of DHB for the year ended 31st December 2003 were prepared as if the undertakings of OTB and DKOB had vested in DHB on 1st January 2003.

At the same time, DHB changed its name to DBS Bank (Hong Kong) Limited (the “Bank”) and continues to operate the integrated banking businesses. OTB changed its name to “DBS Overseas Limited” and DKOB changed its name to “DBS Kwong On Limited”.

2 Principal activities

The principal activities of the Bank and its subsidiary companies (the “Group”) are the provision of banking and related financial services.

3 Summary of significant accounting policies

The following is a summary of the significant accounting policies applied by the Group and, except where noted, are consistent with those applied in the previous financial year. The principal accounting policies adopted in the preparation of the accounts are set out below:

(a) Basis of presentation

The accounts are prepared in accordance with the historical cost convention, modified by the revaluation of certain fixed assets and investments in securities to market value. They are prepared in accordance with the requirements of the Companies Ordinance and the accounting principles generally accepted in Hong Kong and complied with Statements of Standard Accounting Practice (“SSAPs”) issued by the Hong Kong Society of Accountants (“HKSA”).

In 2003, the Group has adopted the new SSAP 12 - Income Taxes issued by the HKSA which is effective for accounting periods commencing on or after 1st January 2003. The effect of adopting the new standard is included in the respective policy note. As a result of this adoption, certain comparative amounts in the accounts have been restated.

Before the legal merger as mentioned in Note 1, there were several accounting policies adopted by DKOB that were different from those adopted by the Group. However, starting from the date of the legal merger, all accounting policies are now consistent to what the Group had already been adopting previously. As the impacts to the accounts are considered immaterial, no prior year adjustments have been made.

(b) Basis of consolidation

The consolidated accounts incorporate the accounts of the Bank and all its subsidiary companies. These subsidiary companies are companies in which the Bank has an interest of more than 50% in the issued share capital at balance sheet date.

The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity.

The results of subsidiary companies acquired or disposed of during the year are included from the date of acquisition or up to the date of disposal.

Intercompany balances and transactions and resulting unrealised profits or losses are eliminated on consolidation.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(c) *Subsidiary companies*

Investments in subsidiaries (as defined in Note 3(b)) are stated in the accounts of the Bank at cost less provision for impairment losses. The results of subsidiary companies are accounted for by the Bank on the basis of dividends received or receivable.

(d) *Investment in jointly controlled entities*

A joint venture is a contractual agreement whereby the Group or Bank and its joint venture partners undertake an economic activity, which is subject to joint control, and none of the parties involved unilaterally have control over the economic activity.

Investments in jointly controlled entities are accounted for under the equity method of accounting. The Group's share of the results of its jointly controlled entities are included in the consolidated profit and loss account. The Group's share of the post acquisition reserves of its jointly controlled entities is included in the carrying value of its investments in jointly controlled entities in the consolidated balance sheet.

In the Bank's balance sheet, the investments in jointly controlled entities are stated at cost less provision for impairment losses. The results of jointly controlled entities are accounted for by the Bank on the basis of dividends received and receivable.

(e) *Advances to customers, banks and other financial institutions*

Advances to customers, banks and other financial institutions are reported on the balance sheet at the principal amount outstanding net of provisions for bad and doubtful debts. Advances to banks and other financial institutions include placements with banks and other financial institutions of more than one year.

All advances are recognised when cash is advanced to borrowers.

(f) *Provisions for bad and doubtful debts*

Provisions for bad and doubtful debts comprises specific provisions against certain loans and advances and a general provision on total loans and advances.

A specific provision is made when the Group has doubt on the ultimate recoverability of principal or interest in full. Specific provision is made to reduce the carrying value of loan or advance, taking into account available collateral, to the expected net realisable value based on the Group's assessment of the potential losses on those identified loans and advances on a case-by-case basis. Where it is not possible to estimate the loss realistically, the Group applies pre-determined provisioning levels to the unsecured portion of loans and advances based on the classification of the respective loans and advances.

The Group internally classifies loans and advances into pass, special mention, substandard, doubtful and loss. The classification of loans and advances is largely based on the assessment of the borrower's capacity to repay and on the degree of doubt about the collectibility of interest and/or principal. The periods that payments of interest and/or principal have been overdue are also taken into account when classifying the loans and advances. A specific provision is made against loans and advances where there is doubt about the collectibility of interest and/or principal.

In addition, amounts have been set aside as a general provision for bad and doubtful debts. Both specific and general provisions are deducted from "Advances to customers" in the balance sheet.

Bad debts are written off against provisions when recovery action has been instituted and the losses can be determined with reasonable certainty. The Group continues to make every effort to recover amounts owing, even after write-offs have been recorded.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(g) *Repossessed assets*

Assets acquired by repossession of collateral for realisation continue to be reported as advances. Provision is made on the shortfall between the expected sales proceeds from realisation of the repossessed assets and the outstanding advances.

(h) *Hire purchase contracts and finance leases*

Where the Group is a lessor under finance leases and hire purchase transactions, the amounts due under the leases, net of unearned finance income, are recognised as a receivable and are included in “Advances to customers”. Finance income implicit in rentals receivable is credited to the profit and loss account over the lease period so as to produce an approximately constant periodic rate of return on the net investment outstanding for each accounting period. Dealer commissions paid for hire purchase contracts or lease financing loans are included in “Other assets” and are amortised against interest income over the life of the contract or lease term on an effective yield basis.

(i) *Operating leases*

Leases where substantially all the risks and rewards of ownership of assets remain with the lessor are accounted for as operating leases. Rentals applicable to such operating leases net of any incentives received from the lessor are charged to the profit and loss account on a straight line basis over the lease term.

Where the Group is a lessor under operating leases, rentals receivable under operating leases are credited to the profit and loss account on a straight line basis over the lease term.

(j) *Investments in securities*

(i) Held-to-maturity securities

Held-to-maturity securities are dated debt securities which the Group has the expressed intention and ability to hold to maturity. These securities are stated at cost adjusted for the amortisation of premiums or discounts arising on acquisition over the periods to maturity, less provision for diminution in their value which is other than temporary. Provisions are made for the amount of the carrying value which the Group does not expect to recover and are recognised as an expense in the profit and loss account as they arise.

In addition, amounts have been set aside as a general provision for certain held-to-maturity debt securities. General provisions are deducted from “Held-to-maturity securities” in the balance sheet.

The amortisation of premiums and discounts arising on acquisition of dated debt securities is included as part of interest income. Profits or losses on realisation of held-to-maturity securities are accounted for in the profit and loss account as they arise.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(j) Investments in securities (continued)

(ii) Trading and non-trading securities

Securities which are not held-to-maturity are classified as being either trading securities or non-trading securities. Trading securities are stated at fair value. Changes in fair value of trading securities are recognised in the profit and loss account as they arise. Fair value represents the quoted market price for securities that are actively traded in a liquid market. For securities which are not actively traded, fair value is estimated by way of various pricing techniques including discounted cash flow analyses. Profits or losses on disposal of trading securities, representing the difference between the net sales proceeds and the carrying amounts, are recognised in the profit and loss account as they arise.

Non-trading securities include debt and equity securities which are not held for trading purposes and are stated at fair value on the balance sheet. Changes in fair value of non-trading securities are recognised in the investments revaluation reserve until the security is sold or determined to be impaired, at which time the cumulative gain or loss representing the difference between the net sales proceeds and the carrying amount of the relevant security, together with any surplus/deficit transferred from the investments revaluation reserve, is included in the profit and loss account.

(k) Sale and Repurchase agreements

Securities sold under sale and repurchase agreements are considered to be, in substance, secured loans. Therefore the securities are maintained on the balance sheet at amortised cost or fair value depending on their classification as held to maturity securities, non-trading securities or trading securities and the proceeds of the sale are included in “Deposits from customers” or “Deposits and balance of banks and other financial institutions” depending on the identity of the counterparty. The difference between the sale price and the repurchase price is amortised to interest expense on an effective yield basis over the period from the date of sale to the date of repurchase.

Conversely, securities purchased under agreements to resell are not recognised on the balance sheet and the purchase cost is recorded as “Advances to customers” or “Placements with banks and other financial institutions” depending on the identity of the counterparty. The difference between the purchase price and resale price is amortised to interest income on an effective yield basis over the period from the date of purchase to the date of resale.

(l) Fixed assets and depreciation

(i) Premises

Premises are stated at cost or valuation, less accumulated impairment losses and depreciation calculated to write off the assets over their estimated useful lives on a straight line basis as follows:

Freehold land	Not depreciated
Leasehold land	Over the remaining terms of leases
Buildings	Over the remaining lease period of the land on which it is situated or 50 years, whichever is shorter
Leasehold improvements	Over the lease term of leased premises or 8 years, whichever is shorter

Some of the Group’s premises are included at directors’ valuation made having regard to independent professional valuations carried out in 1993. The surplus arising on revaluation is credited to the revaluation reserve. Additions to revalued premises made subsequent to the revaluation are included at cost. Premises which have not been the subject of a revaluation are included at cost. The Group places reliance on paragraph 80 of SSAP 17 which provides exemption from the need to make regular revaluations of premises.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(l) Fixed assets and depreciation (continued)

(ii) Investment properties

Investment properties are interests in land and buildings in respect of which construction work and development have been completed and which are held for their investment potential, any rental income being negotiated at arm's length.

Investment properties are stated at cost or estimated open market value as determined by the directors less accumulated impairment losses. Investment properties are not depreciated except where the unexpired term of the lease is 20 years or less in which case depreciation is provided on the carrying amount over the remaining term of the lease.

(iii) Furniture, fixtures and equipment

Furniture, fixtures and equipment are stated at cost less accumulated impairment losses and accumulated depreciation. Depreciation on furniture, fixtures and equipment is calculated to write off the assets on a straight line basis over their estimated useful lives of between 3 and 8 years.

(iv) Impairment

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that premises, investment properties, furniture, fixtures and equipment are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease.

(v) Gain or loss on disposal

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account. Upon the disposal of an investment property, the relevant portion of the revaluation reserve realised in respect of any previous valuation is released from the investment properties revaluation reserve to the profit and loss account. For premises, any premises revaluation reserve balance remaining attributable to the relevant asset is transferred to retained earnings on disposal and shown as a movement in reserves.

(m) Provisions and other liabilities

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount can be made.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(n) Treasury related off-balance sheet financial instruments

The accounting treatment applied to treasury related off-balance sheet financial instruments, including forward, swap, futures and options, is based upon the intention for entering into the transactions as elaborated below.

(i) Non-trading transactions

Derivatives may be designated as a hedge of interest rate, exchange rate or price exposures that are inherent in the assets and liabilities of the Group.

The criteria required for a derivative to be classified as a designated hedge are:

- a) the derivative instrument must be reasonably expected to match or eliminate a significant proportion of the risk inherent in the assets, liabilities, other positions or cashflows being hedged; and
- b) there is adequate evidence of the intention to hedge. Linkage with the underlying risk inherent in the assets, liabilities, other positions or cashflows being hedged, must be established at the outset of the transaction.

Profits and losses on derivatives entered into for specifically designated hedging purposes against assets, liabilities, other positions or cashflows measured on an accrual accounting basis are included in the related category of income or expense in the profit and loss account on the same basis as that arising from the underlying hedging transactions.

Hedging transactions, which have been superseded, cease to be effective or are terminated prior to the end of the life of the assets, liabilities, other positions or cashflows being hedged, are measured at fair value. Any profit or loss arising from the fair value measurement is deferred and amortised as interest income or expense in the profit and loss account over the remaining life of the items previously being hedged.

When the underlying assets, liabilities, other positions or cashflows are terminated prior to the hedging transactions, or anticipated transactions are no longer likely to occur, the hedging transactions are measured on a fair value accounting basis prior to being transferred to the trading portfolio. The profit or loss arising from the fair value measurement prior to the transfer to the trading portfolio is included in the category of income and expense in the profit and loss account relating to the previously hedged transactions.

(ii) Trading transactions

Derivative transactions which do not meet the criteria to be designed as hedges are deemed to be trading transactions. Derivatives entered into for trading purpose include swaps, forward rate agreements, futures, options and combinations of these instruments.

Derivatives entered into as trading transactions are measured at fair value and the resultant profits and losses are taken up in the profit and loss account as "Other operating income". Unrealised valuation gains or losses are included in "Other assets" and "Other liabilities" respectively.

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(n) Treasury related off-balance sheet financial instruments (continued)

(iii) Valuation adjustments for trading instruments

All financial and derivative instruments entered into for trading purposes are stated at fair value. Quoted market prices, when available, are used to determine the fair values of derivatives held for trading. Where mid prices are used, a bid-offer spread adjustment will be made to ensure that all long positions are marked to bid prices and short positions to offer prices. In addition, where appropriate, adjustments are made for illiquid positions. The reserves are recognised as a charge to the profit and loss account as they arise. The resultant profits and losses are taken up in as part of “Other operating income” and the reserves are included in “Other liabilities” in the balance sheet.

(o) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(p) Interest income

Interest income is recognised on an accrual basis.

In the case of doubtful debts, interest is credited to a suspense account which is netted off against accrued interest receivable except for credit card advances and overdrafts, where interest is accrued and the related specific provision on the interest receivable is included in the charge for bad and doubtful debts.

(q) Fees and commission income

Fees and commission income are recognised in the profit and loss account as and when service is performed and when considered recoverable except where the fees are charged to cover the costs of a continuing service to, or risk borne for, the customer, or are interest in nature. In these cases, the fees are recognised on an appropriate basis over the relevant period.

(r) Dividend income

Dividend income from equities are recognised when declared payable.

(s) Cash rebates

Cash rebates granted in relation to residential mortgage loans are capitalised and amortised on a straight line basis over the prepayment penalty period not exceeding three years.

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(t) Employee benefits

(i) Profit sharing and bonus plans

Liabilities for profit sharing and bonus plans due wholly within twelve months after the balance sheet date are recognised when the Group has a present or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

(ii) Pension obligations

The Group offers a mandatory provident fund scheme and participates in a defined contribution plan operated by a subsidiary of the Group's ultimate holding company, the assets of which are generally held in separate trustee-administered funds. These pension plans are generally funded by payments from employees and by the Group.

The Group's contributions to the mandatory provident fund scheme and defined contribution plan are expensed as incurred and are reduced by contributions forfeited by those employees who leave the scheme or the plan prior to vesting fully in the contributions.

(iii) Equity compensation benefits

There is a Share Option Scheme and a Share Option Plan run by DBS Group Holdings Ltd ("DBSH"), the ultimate holding company of the Bank. Under the Scheme and the Plan, share options are granted to eligible staff. There is also a Performance Share Plan run by DBSH. Under this plan, ordinary shares in DBSH are given free of charge to eligible employees based on the performance of the DBS Group and of the individual.

Equity compensation benefits resulting from the issue of shares and share options to the Group's employees are not recognised in the Group's accounts.

The Bank has taken advantage of the provisions of paragraph 4(c) of SSAP 20 "Related party disclosures", which exempt the Bank from disclosing details of the equity compensation benefits as a related party transaction. The Bank is a wholly-owned subsidiary of DBSH and DBSH has issued consolidated financial statements that include the Bank and include the disclosures of the relevant Scheme and Plans as required by the SSAP.

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(u) Taxation

The current taxation charged to the profit and loss account represents tax at the current rate based on taxable profits earned during the financial year. Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. Taxation rates enacted or substantively enacted by the balance sheet date are used in the determination of deferred income tax.

Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred tax liabilities are provided on temporary differences arising on investments in subsidiary companies and joint venture company, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets and liabilities are credited or charged in the profit and loss account, except when they relate to items credited or charged directly to reserves, in which case the deferred tax assets and liabilities are also dealt with in reserves.

In the prior year, deferred taxation was accounted for at the then current taxation rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or an asset was expected to be payable or recoverable in the foreseeable future. The adoption of the new SSAP 12 represents a change in accounting policy, which has been applied retrospectively so that the comparatives presented have been restated to conform to the changed policy (Note 12, 30 and 32).

(v) Foreign currencies

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Assets and liabilities in foreign currencies are translated into Hong Kong dollars at the exchange rates prevailing at balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

The balance sheet of subsidiaries and overseas branches in foreign currencies are translated at exchange rate prevailing at balance sheet date. Exchange differences are dealt with as a movement in reserves.

(w) Cash and cash equivalents

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months maturity from the date of acquisition including cash, balance with banks and other financial institutions, treasury bills, other eligible bills and certificates of deposit.

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

3 Summary of significant accounting policies (continued)

(x) Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

The Group conducts business of acceptances that comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursement from the customers. Acceptances are accounted for as off-balance sheet transactions and are disclosed as contingent liabilities.

(y) Related party transactions

For the purposes of these accounts, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or entities.

(z) Fiduciary activities

Assets and income arising thereon together with related undertakings to return such assets to customers are excluded from the accounts where the Group acts in a fiduciary capacity such as nominee, trustee or agent.

4 Interest income

	2003	2002
	HK\$'000	HK\$'000
Interest income on listed investments	393,474	410,755
Interest income on unlisted investments	407,014	723,909
Other interest income	4,531,002	3,721,534
	<u>5,331,490</u>	<u>4,856,198</u>

5 Interest expense

Interest expense includes interest on the 7.75% fixed rate subordinated notes amounting to HK\$159,390,000 (2002: HK\$159,679,000).

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

6 Other operating income

	2003	2002
	HK\$'000	HK\$'000
Fees and commission income	987,558	840,663
Less: fees and commission expenses	(128,039)	(130,148)
Net fees and commission income	859,519	710,515
Net income from foreign exchange operations (Note)	201,086	132,275
Dividend income from listed investments	13,792	10,237
Dividend income from unlisted investments	6,793	8,729
Gross rental income from investment properties	4,151	3,134
Net profits from other dealing activities		
- Net gain from trading securities	36,195	37,437
- Net gain / (loss) from other dealing activities (Note)	596,707	(2,197)
Others	36,868	61,605
	<u>1,755,111</u>	<u>961,735</u>

Note: Net income from foreign exchange operations and net gain/(loss) from other dealing activities include gain from sales of treasury and treasury investment products.

7 Operating expenses

	2003	2002
	HK\$'000	HK\$'000
Staff costs		
- Salaries and other costs	1,100,081	839,057
- Pension costs	62,214	53,453
Premises and equipment expenses excluding depreciation		
- Rental of premises	62,791	41,107
- Others	162,204	155,738
Depreciation	244,884	187,571
Auditors' remuneration	7,327	5,866
Other operating expenses	531,953	365,706
	<u>2,171,454</u>	<u>1,648,498</u>

For the year ended 31st December 2002, the costs above include staff costs and other operating expenses of HK\$18,100,000 relating to retention packages for certain key staff of the Group and other costs incurred as a result of the reorganisation of the Group.

8 Impairment of fixed assets

An impairment loss of HK\$25,236,000 (2002: HK\$241,136,000) was recognised during the year as a result of the impairment of certain premises within fixed assets. The impairment loss was primarily a result of a reduction in property values and partly due to a reduction in the expected future cash inflows generated by those premises, including those branches scheduled for closure.

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

9 Charge for bad and doubtful debts

	2003	2002
	HK\$'000	HK\$'000
Specific provisions		
- New provisions	1,193,252	1,056,901
- Releases	(315,157)	(452,001)
- Recoveries	(84,223)	(43,561)
	<u>793,872</u>	<u>561,339</u>
General provisions		
- Advances to customers	11,253	(53,860)
- Held-to-maturity securities	15,878	2,186
	<u>27,131</u>	<u>(51,674)</u>
Charge for bad and doubtful debts	<u>821,003</u>	<u>509,665</u>

10 Net gain on disposal of non-trading securities and held-to-maturity securities

	2003	2002
	HK\$'000	HK\$'000
Net gain on disposal of non-trading securities	8,794	18,175
Net gain on disposal of held-to-maturity securities	1,544	889
	<u>10,338</u>	<u>19,064</u>

11 Directors' emoluments

The aggregate amounts of emoluments payable to directors of the Bank during the year are as follows:

	2003	2002
	HK\$'000	HK\$'000
Fees	520	–
Salaries, housing and other allowances and benefits in kind	13,026	17,293
Pension	401	292
	<u>13,947</u>	<u>17,585</u>

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

12 Taxation

(a) Taxation in the consolidated profit and loss account represents:

	2003	2002
	HK\$'000	HK\$'000
<u>Current taxation:</u>		
Hong Kong profits tax	391,028	163,159
Overseas taxation	3,719	5,473
	<u>394,747</u>	<u>168,632</u>
<u>Deferred taxation:</u>		
Deferred taxation relating to the origination and reversal of temporary differences	(9,288)	11,241
Deferred taxation resulting from an increase in tax rate	(8,316)	–
	<u>(17,604)</u>	<u>11,241</u>
Share of a jointly controlled entity's taxation	2,011	19
	<u>379,154</u>	<u>179,892</u>

The provision for Hong Kong profits tax is calculated at 17.5% (2002: 16%) of the estimated assessable profits for the year. Taxation for overseas subsidiaries and branches is charged at the appropriate current rates of taxation ruling in the countries in which they operate.

(b) The deferred taxation (credit)/charge in the profit and loss account comprises the following temporary differences:

	2003	2002
	HK\$'000	HK\$'000
Accelerated depreciation allowances	(1,693)	9,591
General provisions for bad and doubtful debts	(15,911)	1,650
	<u>(17,604)</u>	<u>11,241</u>

As detailed in Note 3(u), the adoption of the new SSAP 12 represents a change in accounting policy, opening retained earnings at 1st January 2002 and 2003 have been reduced by HK\$76,070,000 and HK\$64,829,000, respectively for the Group and HK\$37,598,000 and HK\$40,325,000, respectively for the Bank, which represent the unprovided net deferred tax liabilities. The profit for the year ended 31st December 2002 has been reduced by HK\$11,241,000 and the amount released to reserves for the year ended 31st December 2002 increased by HK\$10,620,000.

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

12 Taxation (continued)

(c) *The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the taxation rate of the Hong Kong basic tax rate as follows:*

	2003	2002
	HK\$'000	HK\$'000
Profit before taxation	2,386,564	1,302,606
Calculated at a taxation rate of 17.5% (2002: 16%)	417,649	208,417
Attributable share of estimated Hong Kong profits tax losses arising from investments in partnerships (Note)	(130,015)	(14,928)
Investments in limited partnerships written off (Note)	98,139	11,880
Effect of different tax rates in other countries	(824)	(1,148)
Income not subject to tax	(37,783)	(43,927)
Increase in opening net deferred tax assets resulting from an increase in tax rates	(8,316)	–
Expenses not deductible for taxation purposes	39,696	37,654
Release of provision from prior period	–	(27,000)
Others	608	8,944
	379,154	179,892

Note:

The Group has entered into a number of transactions involving special purpose partnerships in which the Group is the only general partner. As at 31st December 2003, the Group's investment in such partnerships, which is included in "Other assets" in the balance sheet amounted to HK\$168,885,000 (2002: HK\$237,070,000). The Group's investments in limited partnerships are amortised over the life of the partnership in proportion to the taxation benefits resulting from those investments. The total assets and liabilities of such partnerships at 31st December 2003 are HK\$752,307,000 and HK\$487,655,000, respectively (2002: HK\$822,000,000 and HK\$581,000,000, respectively).

13 Profit attributable to shareholders

The profit attributable to shareholders is dealt with in the accounts of the Bank to the extent of HK\$3,108,060,000 (2002: HK\$1,002,599,000).

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

14 Dividends

	2003	2002
	HK\$'000	HK\$'000
Final dividend proposed and paid for 2002 after the balance sheet date of HK\$0.039139 (2002: HK\$0.04627 per share)	203,523	240,611
1st interim dividend paid of HK\$Nil (2002: HK\$0.04504 per share)	–	234,205
Special dividend paid of HK\$0.653846 per share (2002: HK\$Nil)	3,400,000	–
	<u>3,603,523</u>	<u>474,816</u>

15 Cash and short-term funds

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cash and balances with banks and other financial institutions	1,354,415	987,085	1,354,415	817,778
Money at call and short notice	18,315,557	12,853,685	18,314,050	12,853,685
Treasury bills (including Exchange Fund Bills)	3,604,216	5,271,441	3,604,216	4,693,566
	<u>23,274,188</u>	<u>19,112,211</u>	<u>23,272,681</u>	<u>18,365,029</u>

The analysis of treasury bills (including Exchange Fund Bills) is as follows:

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Held-to-maturity securities, unlisted at amortised cost	242,404	1,387,224	242,404	1,208,689
Trading securities, unlisted at fair value	2,761,886	2,386,256	2,761,886	2,386,256
Non-trading securities, unlisted at fair value	599,926	1,497,961	599,926	1,098,621
	<u>3,604,216</u>	<u>5,271,441</u>	<u>3,604,216</u>	<u>4,693,566</u>

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

16 Certificates of deposit held

	Group and Bank	
	2003	2002
	HK\$'000	HK\$'000
Held-to-maturity securities, unlisted at amortised cost	–	460,000
Non-trading securities, unlisted at fair value	1,216,013	377,797
	<u>1,216,013</u>	<u>837,797</u>

17 Trading securities

	Group and Bank	
	2003	2002
	HK\$'000	HK\$'000
Debt securities, at fair value		
- Listed in Hong Kong	1,089,769	2,067,187
- Listed outside Hong Kong	39,258	–
	1,129,027	2,067,187
- Unlisted	18,053	11,042
	<u>1,147,080</u>	<u>2,078,229</u>

Trading securities are analysed by issuer as follows:

- Central governments and central banks	1,087,757	2,039,209
- Public sector entities	21,664	38,580
- Banks and other financial institutions	16,459	440
- Corporate entities	21,200	–
	<u>1,147,080</u>	<u>2,078,229</u>

DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

18 Held-to-maturity securities

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Balance as at 1st January 2003	18,298,518	16,757,853	18,296,518	16,755,849
Additions through merger	469,779	–	469,779	–
Amortisation of premium	(82,423)	(3,585)	(82,423)	(3,581)
Additions	12,921,480	15,884,786	12,923,480	15,884,786
Amortised cost of securities redeemed	(7,460,763)	(9,920,610)	(7,460,763)	(9,920,610)
Amortised cost of securities sold during the year	–	(4,586,632)	–	(4,586,632)
General provision charged	(15,878)	(2,186)	(15,878)	(2,186)
Exchange differences	588,571	168,892	588,571	168,892
	24,719,284	18,298,518	24,719,284	18,296,518
	<u>24,719,284</u>	<u>18,298,518</u>	<u>24,719,284</u>	<u>18,296,518</u>
Listed securities, at amortised cost less provision				
- Listed in Hong Kong	4,680,551	3,726,793	4,680,551	3,726,793
- Listed outside Hong Kong	7,840,330	5,387,709	7,840,330	5,387,709
	12,520,881	9,114,502	12,520,881	9,114,502
Unlisted	12,198,403	9,184,016	12,198,403	9,182,016
	24,719,284	18,298,518	24,719,284	18,296,518
	<u>24,719,284</u>	<u>18,298,518</u>	<u>24,719,284</u>	<u>18,296,518</u>
Market value of listed securities	24,889,424	9,226,706	24,889,424	9,226,706
	<u>24,889,424</u>	<u>9,226,706</u>	<u>24,889,424</u>	<u>9,226,706</u>
Held-to-maturity securities are analysed by issuer as follows:				
- Central governments and central banks	4,094,176	2,976,503	4,094,176	2,976,503
- Public sector entities	1,263,720	3,539,524	1,263,720	3,539,524
- Banks and other financial institutions	18,168,417	11,238,736	18,168,417	11,238,736
- Corporate entities	1,192,971	543,755	1,192,971	541,755
	24,719,284	18,298,518	24,719,284	18,296,518
	<u>24,719,284</u>	<u>18,298,518</u>	<u>24,719,284</u>	<u>18,296,518</u>

For the year ended 31st December 2002, securities classified as held-to-maturity amounting to HK\$4,586,632,000 were sold to reduce exposures in accordance with DBS Group credit limits.

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NOTES TO THE ACCOUNTS (CONTINUED)

19 Advances less provisions

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Advances to customers	94,126,595	70,931,406	94,126,595	52,257,312
Provisions for bad and doubtful debts (Note 20)				
- General	(919,072)	(694,040)	(919,072)	(503,987)
- Specific	(770,328)	(736,183)	(770,328)	(570,128)
	92,437,195	69,501,183	92,437,195	51,183,197
Advances to banks and other financial institutions	285,531	241,477	285,531	241,477
	92,722,726	69,742,660	92,722,726	51,424,674
Included in advances to customers are:				
Trade bills	1,255,317	602,986	1,255,317	458,978
General provisions	(9,211)	(6,030)	(9,211)	(4,590)
	1,246,106	596,956	1,246,106	454,388

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

19 Advances less provisions (continued)

(a) Non-performing advances and provisions

The gross amount of non-performing advances, net of suspended interest, which represent advances on which interest is being placed in suspense or on which interest accrual has ceased, and specific provisions attributable to such advances are as follows:

	Group			
	2003		2002	
	HK\$'000	% of total advances to customers	HK\$'000	% of total advances to customers
Gross non-performing advances	2,228,288	2.37	1,719,730	2.42
Specific provisions made in respect of such advances	(727,047)		(631,939)	
	<u>1,501,241</u>		<u>1,087,791</u>	
Suspended interest	<u>266,611</u>		<u>273,450</u>	
	Bank			
	2003		2002	
	HK\$'000	% of total advances to customers	HK\$'000	% of total advances to customers
Gross non-performing advances	2,228,288	2.37	1,259,931	2.41
Specific provisions made in respect of such advances	(727,047)		(477,324)	
	<u>1,501,241</u>		<u>782,607</u>	
Suspended interest	<u>266,611</u>		<u>174,463</u>	

The specific provisions were made after taking into account the value of collateral in respect of such advances.

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NOTES TO THE ACCOUNTS (CONTINUED)

19 Advances less provisions (continued)

(b) Advances to customers include finance lease receivables and hire purchase contracts and are analysed as follows:

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Gross investment in finance leases and hire purchase contracts receivable:				
Not later than one year	1,217,722	519,208	1,217,722	25,048
Later than one year and not later than five years	2,715,657	1,558,189	2,715,657	97,061
Later than five years	5,321,763	4,274,468	5,321,763	387,536
	<u>9,255,142</u>	<u>6,351,865</u>	<u>9,255,142</u>	<u>509,645</u>
Unearned future finance income	(72,738)	(74,759)	(72,738)	(1,630)
	<u>9,182,404</u>	<u>6,277,106</u>	<u>9,182,404</u>	<u>508,015</u>
Net investment in finance leases and hire purchase contracts	<u>9,182,404</u>	<u>6,277,106</u>	<u>9,182,404</u>	<u>508,015</u>
The net investment in finance leases and hire purchase contracts is analysed as follows:				
Not later than one year	1,189,658	491,881	1,189,658	24,326
Later than one year and not later than five years	2,677,195	1,518,745	2,677,195	96,165
Later than five years	5,315,551	4,266,480	5,315,551	387,524
	<u>9,182,404</u>	<u>6,277,106</u>	<u>9,182,404</u>	<u>508,015</u>

The unguaranteed residual values included in the gross investment in finance leases and hire purchase contracts as at 31st December 2003 and 31st December 2002 are not considered to be material.

The allowance for uncollectable finance lease receivables and hire purchase contracts included in the provision for bad and doubtful debts amounted to HK\$25,599,000 as at 31st December 2003 (2002: HK\$8,417,000).

DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

20 Provisions for bad and doubtful debts (continued)

2002	Group			Suspended interest HK\$'000
	Specific HK\$'000	General HK\$'000	Total HK\$'000	
At 1st January 2002	898,515	747,380	1,645,895	377,820
Amounts written off	(767,651)	–	(767,651)	(162,132)
Recoveries of advances written off in previous years	43,561	–	43,561	–
Net charge/(release) to profit and loss account	561,339	(53,860)	507,479	–
Interest suspended during the year	–	–	–	174,538
Suspended interest recovered	–	–	–	(117,099)
Exchange differences	419	520	939	323
At 31st December 2002	<u>736,183</u>	<u>694,040</u>	<u>1,430,223</u>	<u>273,450</u>
	Bank			Suspended interest HK\$'000
2002	Specific HK\$'000	General HK\$'000	Total HK\$'000	
At 1st January 2002	642,767	471,964	1,114,731	260,571
Amounts written off	(635,228)	–	(635,228)	(125,804)
Recoveries of advances written off in previous years	28,609	–	28,609	–
Net charge to profit and loss account	533,700	31,518	565,218	–
Interest suspended during the year	–	–	–	143,383
Suspended interest recovered	–	–	–	(103,892)
Exchange differences	280	505	785	205
At 31st December 2002	<u>570,128</u>	<u>503,987</u>	<u>1,074,115</u>	<u>174,463</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

21 Non-trading securities

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Debt securities, at fair value				
- Listed outside Hong Kong	1,114,002	20,819	1,114,002	20,819
- Unlisted	4,228,021	1,800,328	4,228,021	1,800,228
	5,342,023	1,821,147	5,342,023	1,821,047
Equity securities, at fair value				
- Listed in Hong Kong	230,354	133,335	230,354	133,335
- Listed outside Hong Kong	215,053	234,918	215,053	234,918
	445,407	368,253	445,407	368,253
- Unlisted	1,814	766	1,814	766
	447,221	369,019	447,221	369,019
	5,789,244	2,190,166	5,789,244	2,190,066

Non-trading securities are analysed by issuer as follows:

- Public sector entities	122,946	52,229	122,946	52,229
- Banks and other financial institutions	5,452,989	2,130,300	5,452,989	2,130,300
- Corporate entities	204,476	3,166	204,476	3,166
- Others	8,833	4,471	8,833	4,371
	5,789,244	2,190,166	5,789,244	2,190,066

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

22 Interest in a jointly controlled entity

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Share of net assets	80,481	72,471	500	500
Amount due to a jointly controlled entity	1,122,438	1,103,780	1,122,438	1,103,701

Details of the jointly controlled entity are as follows:

Name of company	Country of Incorporation	Principal place of operation	Particulars of issued shares held	Interest held	Principal activities
Hutchison DBS Card Limited	British Virgin Islands	Hong Kong	500,000 class A shares of HK\$1 each 500,000 class B shares of HK\$1 each	50%	Provision of credit card services

23 Investments in subsidiaries

	Bank	
	2003 HK\$'000	2002 HK\$'000
Unlisted shares, at cost after provisions	171,179	4,002,411

Details of the principal subsidiaries which are wholly and directly owned by the bank are as follows:

Name of company	Place of operation and incorporation	Particulars of issued share capital	Principal activities
Dao Heng Finance Limited	Hong Kong	250,000 shares of HK\$100 each	Money lending
Dao Heng Bank Trustee Limited	Hong Kong	30,000 shares of HK\$100 each	Trustee services
DBS Corporate Services (Hong Kong) Limited	Hong Kong	500,000 shares of HK\$1 each	Corporate services
Ting Hong Nominees Limited	Hong Kong	10,000 shares of HK\$1 each	Nominee services
Overseas Trust Bank Nominees Limited	Hong Kong	50,000 shares of HK\$1 each	Nominee services
DBS Trustee H.K. (Jersey) Limited	Jersey	100,000 shares of £1 each	Corporate services

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

24 Fixed assets

(a) Fixed assets

Group

	Premises HK\$'000	Investment properties HK\$'000	Furniture, fixtures and equipment HK\$'000	Total HK\$'000
Cost or valuation				
At 1st January 2003	4,640,312	93,147	787,369	5,520,828
Additions:				
- through merger	894,864	3,000	252,302	1,150,166
- others	22,242	–	52,031	74,273
Disposals	(242,111)	(15,750)	(96,508)	(354,369)
Transfers	–	–	(42,190)	(42,190)
Exchange adjustments	–	–	(33)	(33)
	<u>5,315,307</u>	<u>80,397</u>	<u>952,971</u>	<u>6,348,675</u>
At 31st December 2003				
Accumulated depreciation and impairment				
At 1st January 2003	776,183	–	559,803	1,335,986
Additions through merger	27,703	–	110,503	138,206
Charge for the year	129,568	–	115,316	244,884
Impairment loss recognised directly in equity (Note 32(c) & (d))	84,501	252	–	84,753
Impairment loss recognised in the profit and loss account (Note 8)	22,030	3,206	–	25,236
Disposals	(91,068)	(960)	(79,988)	(172,016)
Transfers	–	–	(42,190)	(42,190)
Exchange adjustments	(504)	–	(27)	(531)
	<u>948,413</u>	<u>2,498</u>	<u>663,417</u>	<u>1,614,328</u>
At 31st December 2003				
Net book value				
At 31st December 2003	<u>4,366,894</u>	<u>77,899</u>	<u>289,554</u>	<u>4,734,347</u>
At 31st December 2002	<u>3,864,129</u>	<u>93,147</u>	<u>227,566</u>	<u>4,184,842</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

24 Fixed assets (continued)

(a) Fixed assets (continued)

The net book values of premises and investment properties are analysed as follows:

Group

	2003		2002	
	Premises HK\$'000	Investment properties HK\$'000	Premises HK\$'000	Investment properties HK\$'000
In Hong Kong				
- Leasehold with over 50 years unexpired	1,645,234	71,302	1,121,032	73,800
- Leasehold with 10 to 50 years unexpired	2,700,282	6,597	2,670,620	19,347
- Leasehold with less than 10 years unexpired	–	–	42,085	–
Outside Hong Kong				
- Freehold	11,742	–	12,278	–
- Leasehold with 10 to 50 years unexpired	9,636	–	18,114	–
	4,366,894	77,899	3,864,129	93,147
The analysis of cost or valuation of premises and investment properties is as follows:				
At cost	2,547,954	80,397	2,662,475	93,147
At professional valuation in 2001	802,597	–	–	–
At directors' valuation in 1993	1,964,756	–	1,977,837	–
	5,315,307	80,397	4,640,312	93,147

All other fixed assets are stated at cost.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

24 Fixed assets (continued)

(a) Fixed assets (continued)

Bank

	Premises HK\$'000	Investment properties HK\$'000	Furniture, fixtures and equipment HK\$'000	Total HK\$'000
Cost or valuation				
At 1st January 2003	3,679,343	2,805	680,055	4,362,203
Additions:				
- through merger	1,803,947	91,433	317,321	2,212,701
- others	22,242	–	52,031	74,273
Disposals	(242,111)	(15,750)	(96,403)	(354,264)
Transfers	29,086	1,909	–	30,995
Exchange adjustments	–	–	(33)	(33)
	<hr/>	<hr/>	<hr/>	<hr/>
At 31st December 2003	5,292,507	80,397	952,971	6,325,875
Accumulated depreciation and impairment				
At 1st January 2003	619,363	–	475,057	1,094,420
Additions through merger	174,730	–	152,954	327,684
Charge for the year	129,047	–	115,316	244,363
Impairment loss recognised directly in equity (Note 32(c) & (d))	67,879	252	–	68,131
Impairment loss recognised in the profit and loss account (Note 8)	22,030	3,206	–	25,236
Disposals	(91,068)	(960)	(79,883)	(171,911)
Transfers	16,887	–	–	16,887
Exchange adjustments	(504)	–	(27)	(531)
	<hr/>	<hr/>	<hr/>	<hr/>
At 31st December 2003	938,364	2,498	663,417	1,604,279
Net book value				
At 31st December 2003	<u>4,354,143</u>	<u>77,899</u>	<u>289,554</u>	<u>4,721,596</u>
At 31st December 2002	<u>3,059,980</u>	<u>2,805</u>	<u>204,998</u>	<u>3,267,783</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

24 Fixed assets (continued)

(a) Fixed assets (continued)

The analysis of net book value of premises and investment properties is as follows:

Bank

	2003		2002	
	Premises HK\$'000	Investment properties HK\$'000	Premises HK\$'000	Investment properties HK\$'000
In Hong Kong				
- Leasehold with over 50 years unexpired	1,632,483	71,302	493,224	2,805
- Leasehold with 10 to 50 years unexpired	2,700,282	6,597	2,506,557	–
- Leasehold with less than 10 years unexpired	–	–	42,085	–
Outside Hong Kong				
- Freehold	11,742	–	–	–
- Leasehold with 10 to 50 years unexpired	9,636	–	18,114	–
	<u>4,354,143</u>	<u>77,899</u>	<u>3,059,980</u>	<u>2,805</u>

The analysis of cost or valuation of premises and investment properties is as follows:

At cost	2,514,423	80,397	2,651,744	2,805
Additions through merger	10,731	–	–	–
At professional valuation in 2001	802,597	–	–	–
At directors' valuation in 1993	1,964,756	–	1,027,599	–
	<u>5,292,507</u>	<u>80,397</u>	<u>3,679,343</u>	<u>2,805</u>

All other fixed assets are stated at cost.

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

24 Fixed assets (continued)

(b) Operating lease arrangements

The Group leases out investment properties under operating leases. The leases typically run for an initial period of one to five years, and may contain an option to renew the lease after that date at which time all terms are renegotiated. None of the leases include contingent rentals.

During the current year, HK\$4,151,000 (2002: HK\$3,134,000) was recognised as rental income in the profit and loss account in respect of operating leases.

At 31st December 2003, the Group and the Bank had future aggregate minimum lease receipts under non-cancellable operating leases as follows:

	2003	2002
	HK\$'000	HK\$'000
Not later than one year	3,638	3,835
Later than one year and not later than five years	5,810	8,920
	9,448	12,755

25 Other assets

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Accrued interest	427,671	308,806	427,671	298,967
Other accounts	3,798,720	3,385,164	3,797,737	2,693,486
	4,226,391	3,693,970	4,225,408	2,992,453

26 Deposits from customers

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Demand deposits and current accounts	8,484,415	3,796,130	8,484,415	2,501,265
Savings deposits	35,075,148	14,295,442	35,075,148	10,606,492
Time, call and notice deposits	78,044,791	74,151,261	78,044,791	59,408,571
	121,604,354	92,242,833	121,604,354	72,516,328

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

27 7.75% fixed rate subordinated notes

The 7.75% fixed rate subordinated notes (“Notes”) with an aggregate principal amount of US\$350,000,000 were issued by Dao Heng Bank Limited on 24th January 1997. The Notes will mature on 24th January 2007. Interest is payable semi-annually on 24th January and 24th July, commencing 24th July 1997. Subsequent to the issue, Dao Heng Bank Limited repurchased and cancelled part of the Notes. At 31st December 2003 and 2002, the outstanding principal amount of the Notes is US\$261,620,000.

28 Maturity profile

2003	Group						
	Repayable on demand HK\$'000	3 months or less HK\$'000	1 year or less but over 3 months HK\$'000	5 years or less but over 1 year HK\$'000	After 5 years HK\$'000	Undated HK\$'000	Total HK\$'000
Assets							
- Cash and short-term funds	1,365,680	20,769,832	1,138,676	-	-	-	23,274,188
- Placements with banks and other financial institutions maturing between one and twelve months	-	3,729,148	1,065,780	-	-	-	4,794,928
- Certificates of deposit held	-	178,108	598,003	439,902	-	-	1,216,013
- Trading debt securities	-	1,353	158,906	846,550	140,271	-	1,147,080
- Advances to customers (before provisions)	6,468,998	15,503,135	10,882,175	21,785,362	37,213,401	2,273,524	94,126,595
- Advances to banks and other financial institutions	-	-	-	-	285,531	-	285,531
- Held to maturity securities	-	1,099,015	4,129,090	18,466,988	1,024,191	-	24,719,284
- Non-trading debt securities	-	835,515	719,800	3,777,875	-	8,833	5,342,023
	<u>7,834,678</u>	<u>42,116,106</u>	<u>18,692,430</u>	<u>45,316,677</u>	<u>38,663,394</u>	<u>2,282,357</u>	<u>154,905,642</u>
Liabilities							
- Deposits and balances of banks and other financial institutions	111,021	934,297	25,324	-	-	-	1,070,642
- Deposits from customers	43,559,563	60,588,032	5,670,750	9,085,980	2,700,029	-	121,604,354
- Certificates of deposit issued	-	160,000	2,985,087	4,580,689	140,000	-	7,865,776
- 7.75% fixed rate subordinated notes	-	-	-	2,030,956	-	-	2,030,956
	<u>43,670,584</u>	<u>61,682,329</u>	<u>8,681,161</u>	<u>15,697,625</u>	<u>2,840,029</u>	<u>-</u>	<u>132,571,728</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

28 Maturity profile (continued)

2003	Bank						
	Repayable on demand HK\$'000	3 months or less HK\$'000	1 year or less but over 3 months HK\$'000	5 years or less but over 1 year HK\$'000	After 5 years HK\$'000	Undated HK\$'000	Total HK\$'000
Assets							
- Cash and short-term funds	1,364,173	20,769,832	1,138,676	-	-	-	23,272,681
- Placements with banks and other financial institutions maturing between one and twelve months	-	3,729,148	1,065,780	-	-	-	4,794,928
- Certificates of deposit held	-	178,108	598,003	439,902	-	-	1,216,013
- Trading debt securities	-	1,353	158,906	846,550	140,271	-	1,147,080
- Advances to customers (before provisions)	6,468,998	15,503,135	10,882,175	21,785,362	37,213,401	2,273,524	94,126,595
- Advances to banks and other financial institutions	-	-	-	-	285,531	-	285,531
- Held to maturity securities	-	1,099,015	4,129,090	18,466,988	1,024,191	-	24,719,284
- Non-trading debt securities	-	835,515	719,800	3,777,875	-	8,833	5,342,023
	<u>7,833,171</u>	<u>42,116,106</u>	<u>18,692,430</u>	<u>45,316,677</u>	<u>38,663,394</u>	<u>2,282,357</u>	<u>154,904,135</u>
Liabilities							
- Deposits and balances of banks and other financial institutions	111,021	934,297	25,324	-	-	-	1,070,642
- Deposits from customers	43,559,563	60,588,032	5,670,750	9,085,980	2,700,029	-	121,604,354
- Certificates of deposit issued - 7.75% fixed rate subordinated notes	-	160,000	2,985,087	4,580,689	140,000	-	7,865,776
	-	-	-	2,030,956	-	-	2,030,956
	<u>43,670,584</u>	<u>61,682,329</u>	<u>8,681,161</u>	<u>15,697,625</u>	<u>2,840,029</u>	<u>-</u>	<u>132,571,728</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

28 Maturity profile (continued)

2002	Group						
	Repayable on demand HK\$'000	3 months or less HK\$'000	1 year or less but over 3 months HK\$'000	5 years or less but over 1 year HK\$'000	After 5 years HK\$'000	Undated HK\$'000	Total HK\$'000
Assets							
- Cash and short-term funds	985,026	16,616,876	1,510,309	-	-	-	19,112,211
- Placements with banks and other financial institutions maturing between one and twelve months	-	6,156,770	2,366,884	-	-	-	8,523,654
- Certificates of deposit held	-	-	537,984	299,813	-	-	837,797
- Trading debt securities	-	331,424	101,434	1,510,077	135,294	-	2,078,229
- Advances to customers (before provisions)	4,278,425	10,553,306	6,519,931	16,124,977	31,183,204	2,271,563	70,931,406
- Advances to banks and other financial institutions	-	-	-	241,477	-	-	241,477
- Held to maturity securities	-	1,062,023	3,245,634	13,975,888	14,973	-	18,298,518
- Non-trading debt securities	-	820,818	280,344	663,285	52,229	4,471	1,821,147
	<u>5,263,451</u>	<u>35,541,217</u>	<u>14,562,520</u>	<u>32,815,517</u>	<u>31,385,700</u>	<u>2,276,034</u>	<u>121,844,439</u>
Liabilities							
- Deposits and balances of banks and other financial institutions	772,308	614,731	-	-	-	-	1,387,039
- Deposits from customers	18,091,572	69,677,920	4,057,212	416,129	-	-	92,242,833
- Certificates of deposit issued - 7.75% fixed rate subordinated notes	-	454,973	820,000	4,443,969	-	-	5,718,942
	-	-	-	2,040,278	-	-	2,040,278
	<u>18,863,880</u>	<u>70,747,624</u>	<u>4,877,212</u>	<u>6,900,376</u>	<u>-</u>	<u>-</u>	<u>101,389,092</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

28 Maturity profile (continued)

2002	Bank						
	Repayable on demand HK\$'000	3 months or less HK\$'000	1 year or less but over 3 months HK\$'000	5 years or less but over 1 year HK\$'000	After 5 years HK\$'000	Undated HK\$'000	Total HK\$'000
Assets							
- Cash and short-term funds	815,719	16,039,001	1,510,309	-	-	-	18,365,029
- Placements with banks and other financial institutions maturing between one and twelve months	-	6,156,770	2,366,884	-	-	-	8,523,654
- Certificates of deposit held	-	-	537,984	299,813	-	-	837,797
- Trading debt securities	-	331,424	101,434	1,510,077	135,294	-	2,078,229
- Advances to customers (before provisions)	3,206,455	8,853,027	5,224,963	11,335,135	21,897,837	1,739,895	52,257,312
- Advances to banks and other financial institutions	-	-	-	241,477	-	-	241,477
- Held to maturity securities	-	1,062,023	3,245,634	13,975,888	12,973	-	18,296,518
- Non-trading debt securities	-	820,818	280,344	663,285	52,229	4,371	1,821,047
	<u>4,022,174</u>	<u>33,263,063</u>	<u>13,267,552</u>	<u>28,025,675</u>	<u>22,098,333</u>	<u>1,744,266</u>	<u>102,421,063</u>
Liabilities							
- Deposits and balances of banks and other financial institutions	687,479	614,731	-	-	-	-	1,302,210
- Deposits from customers	13,107,757	55,690,639	3,394,533	323,399	-	-	72,516,328
- Certificates of deposit issued - 7.75% fixed rate subordinated notes	-	454,973	820,000	4,443,969	-	-	5,718,942
	-	-	-	2,040,278	-	-	2,040,278
	<u>13,795,236</u>	<u>56,760,343</u>	<u>4,214,533</u>	<u>6,807,646</u>	<u>-</u>	<u>-</u>	<u>81,577,758</u>

**DBS BANK (HONG KONG) LIMITED
(FORMERLY KNOWN AS DAO HENG BANK LIMITED)**

NOTES TO THE ACCOUNTS (CONTINUED)

29 Other liabilities

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Short positions in securities	7,700,545	8,967,137	7,700,545	8,967,137
Other liabilities and provisions	5,319,512	3,267,178	5,272,133	3,110,940
	13,020,057	12,234,315	12,972,678	12,078,077

30 Tax liabilities

(a) Current taxation

Taxation in the balance sheet which is included in "Other liabilities" represents:

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong profits tax payable	202,901	114,835	202,458	113,262
Overseas tax payable	2,186	3,035	2,186	468
	205,087	117,870	204,644	113,730

(b) Deferred taxation

Deferred taxation is calculated in full on temporary differences under the liability method using a principal taxation rate of 17.5% (2002: 16%).

The movement on the deferred tax liabilities/(assets) account is as follows:

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1st January				
- as previously reported	-	-	-	-
- effect of adopting SSAP 12	17,383	16,762	39,228	52,575
- as restated	17,383	16,762	39,228	52,575
Additions through merger	125,444	-	103,438	-
Deferred taxation (credited)/charged to profit and loss account (Note 12)	(17,604)	11,241	(17,612)	(2,727)
Deferred taxation charged/(released) to equity	9,020	(10,620)	9,020	(10,620)
At 31st December	134,243	17,383	134,074	39,228

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NOTES TO THE ACCOUNTS (CONTINUED)

30 Tax liabilities (continued)

(b) Deferred taxation (continued)

Deferred tax assets and liabilities are attributable to the following items:

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Deferred income tax liabilities				
Accelerated tax depreciation	53,696	44,470	53,527	39,098
Other temporary differences	240,552	83,306	240,552	80,647
	294,248	127,776	294,079	119,745
Deferred income tax assets				
Provision for loan losses	160,005	109,299	160,005	79,423
Other temporary differences	–	1,094	–	1,094
	160,005	110,393	160,005	80,517

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities when the deferred income taxes relate to the same fiscal authority. The following amounts, determined after appropriate offsetting, are shown in the balance sheets:

	Group		Bank	
	2003	2002	2003	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Deferred tax assets	160,005	110,393	160,005	80,517
Deferred tax liabilities	(294,248)	(127,776)	(294,079)	(119,745)
	(134,243)	(17,383)	(134,074)	(39,228)

Deferred income tax liabilities have not been established for the withholding tax and other taxes that would be payable on the unremitted earnings of certain subsidiaries and branches, as such amounts are permanently reinvested; such remitted earnings totalled HK\$142,890,000 at 31st December 2003 (2002: HK\$178,866,000).

31 Share capital

	Bank	
	2003	2002
	HK\$'000	HK\$'000
Authorised, issued and fully paid		
5,200,000,000 shares of HK\$1.00 each	5,200,000	5,200,000

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NOTES TO THE ACCOUNTS (CONTINUED)

32 Reserves

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
(a) Share premium				
At 1st January	31,351	31,351	31,351	31,351
Addition through merger	564,152	–	564,152	–
At 31st December	<u>595,503</u>	<u>31,351</u>	<u>595,503</u>	<u>31,351</u>
(b) Capital reserve				
At 1st January and 31st December	<u>11,636</u>	<u>11,636</u>	<u>–</u>	<u>–</u>
(c) Premises revaluation reserve				
At 1st January				
- as previously reported	520,664	580,201	504,042	563,579
- Effect of adopting SSAP 12	(83,306)	(92,832)	(80,647)	(90,173)
- as restated	437,358	487,369	423,395	473,406
Additions through merger	715,926	–	713,267	–
Transfer to retained earnings on disposal of premises	(96,837)	–	(96,837)	–
Impairment of fixed assets (Note 24)	(84,501)	(59,537)	(67,879)	(59,537)
Release from deferred taxation	7,563	9,526	7,563	9,526
At 31st December	<u>979,509</u>	<u>437,358</u>	<u>979,509</u>	<u>423,395</u>
(d) Investment properties revaluation reserve				
At 1st January	–	–	–	–
Additions through merger	81,752	–	81,752	–
Impairment of fixed assets (Note 24)	(252)	–	(252)	–
At 31st December	<u>81,500</u>	<u>–</u>	<u>81,500</u>	<u>–</u>
(e) Investments revaluation reserve				
At 1st January				
- as previously reported	(11,294)	12,216	(11,888)	–
- Effect of adopting SSAP 12	1,094	–	1,094	–
- as restated	(10,200)	12,216	(10,794)	–
Additions through merger	6,550	–	594	–
Change in fair value of non-trading securities	77,844	(7,560)	76,804	(8,154)
Disposal of non-trading securities	(8,794)	(15,950)	(1,204)	(3,734)
Release from/(to) deferred taxation	(16,583)	1,094	(16,583)	1,094
At 31st December	<u>48,817</u>	<u>(10,200)</u>	<u>48,817</u>	<u>(10,794)</u>

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NOTES TO THE ACCOUNTS (CONTINUED)

32 Reserves (continued)

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
(f) General reserve				
At 1st January	683,249	683,249	649,942	649,942
Additions through merger	1,715,543	–	1,633,986	–
At 31st December	<u>2,398,792</u>	<u>683,249</u>	<u>2,283,928</u>	<u>649,942</u>
(g) Retained earnings				
At 1st January				
- as previously reported	7,571,725	6,914,873	5,627,473	5,104,704
- Effect of adopting SSAP 12	64,829	76,070	40,325	37,598
- as restated	7,636,554	6,990,943	5,667,798	5,142,302
Additions through merger	403,719	–	1,239,415	–
Profit attributable to shareholders	2,007,410	1,122,714	3,108,060	1,002,599
Transfer from premises revaluation reserve on disposal of premises	96,837	–	96,837	–
Dividends (Note 14)	(3,603,523)	(474,816)	(3,603,523)	(474,816)
Translation of net investments in overseas branches and subsidiary companies	(538)	(2,287)	179	(2,287)
At 31st December	<u>6,540,459</u>	<u>7,636,554</u>	<u>6,508,766</u>	<u>5,667,798</u>
	<u>10,656,216</u>	<u>8,789,948</u>	<u>10,498,023</u>	<u>6,761,692</u>

Note:

The premises, investment properties and investments revaluation reserves do not represent realised profits and are not available for distribution.

The general reserve is comprised of transfers from the previous years' retained earnings and is distributable.

The Bank operates under regulatory jurisdictions which require the maintenance of minimum capital adequacy ratios and which could therefore potentially restrict the amount of retained earnings which can be distributed to shareholders.

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NOTES TO THE ACCOUNTS (CONTINUED)

33 Balances with group companies

(a) *Included in the following balance sheet captions are balances with The DBS Bank Ltd, an intermediate holding company as at 31st December detailed as follows:*

	2003		2002	
	Group HK\$'000	Bank HK\$'000	Group HK\$'000	Bank HK\$'000
Cash and short-term funds	377,001	377,001	889,150	887,635
Advances less provisions	885,531	885,531	–	–
Other assets	32,080	32,080	160,872	160,872
	<u>1,294,612</u>	<u>1,294,612</u>	<u>1,050,022</u>	<u>1,048,507</u>
Deposits and balances of banks and other financial institutions	7,257	7,257	602,159	602,159
Other liabilities	186,075	186,075	218,715	218,715
	<u>193,332</u>	<u>193,332</u>	<u>820,874</u>	<u>820,874</u>

(b) *Included in the following balance sheet captions are balances due from and due to fellow subsidiaries as at 31st December detailed as follows:*

	2003		2002	
	Group HK\$'000	Bank HK\$'000	Group HK\$'000	Bank HK\$'000
Cash and short-term funds	465	465	7,090	7,090
Other assets	24,338	24,338	45,006	45,006
	<u>24,803</u>	<u>24,803</u>	<u>52,096</u>	<u>52,096</u>
Deposits and balances of banks and other financial institutions	845,232	845,232	23,000	23,000
Other liabilities	70	70	54,499	54,499
	<u>845,302</u>	<u>845,302</u>	<u>77,499</u>	<u>77,499</u>

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NOTES TO THE ACCOUNTS (CONTINUED)

34 Material related party transactions

(a) Transactions with an intermediate holding company and fellow subsidiaries

As part of the Bank and the Group's normal course of business, it entered into various transactions with its intermediate holding company and fellow subsidiaries on normal commercial terms. These transactions include interbank placements, taking of deposits and foreign exchange and derivatives.

Information relating to income and expenses from these transactions during the year and balances outstanding at the balance sheet date are set out below:

(i) Income and expenses with an intermediate holding company

	2003	2002
	HK\$'000	HK\$'000
Interest income	218,106	41,684
Interest expense	26,290	22,256
Other income	745,110	171,691
Other expenses	337,975	32,108

(ii) Balances as at 31st December 2002 and 2003

Details of balances due from and due to the intermediate holding company and fellow subsidiaries are set out in Note 33 "Balances with group companies".

(b) Transactions with a jointly controlled entity

Under the Joint Venture Agreement (the "Agreement") between the Bank, Whampoa Limited and Hutchison DBS Card Limited ("HDCL") (formerly known as Hutchison Dao Heng Card Limited), the Bank issues and services credit cards under the Compass brand. The Compass credit card receivable balances are included under "Advances to customers" in the Group's balance sheet. Under the Agreement, loan losses on the Compass cards are borne by HDCL and accordingly, no provisions have been made in the Group accounts for these balances. The revenues and expenses (including interest income and expense, fee income and loan losses) associated with the Compass cards are recognised by the Group through its 50% share of net profits of HDCL in the "Share of profit of a jointly controlled entity" line in the Group's consolidated accounts.

Deposits taken from the jointly controlled entity amounted to HK\$864,000,000 as at 31st December 2003 (2002: HK\$874,000,000). Interest expense for the year ended 31st December 2003 paid and payable to HDCL amounted to HK\$30,958,000 (2002: HK\$24,897,000). The transactions were priced based on relevant market rates at the time of each transaction and were under normal commercial terms. Gross service fee income from HDCL to the Group for the year ended 31st December 2003 amounted to HK\$91,447,000 (2002: HK\$117,542,000).

(c) Transactions with key management personnel

Loans and credit card advances as at 31st December 2003 for key management personnel of the Group amounted to HK\$14,799,000 (2002: HK\$15,389,000). All interest rates in connection with the credit facilities extended are under terms and conditions normally applicable to customers of comparable standing. The interest income from key management personnel receivable by the Group for the year ended 31st December 2003 amounted to HK\$381,000 (2002: HK\$413,000).

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NOTES TO THE ACCOUNTS (CONTINUED)

35 Off-balance sheet exposures

(a) Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment:

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Direct credit substitutes	899,191	596,809	899,191	490,744
Transaction-related contingencies	444,189	321,484	444,189	268,880
Trade-related contingencies	4,758,968	2,582,329	4,758,968	2,038,699
Other commitments with an original maturity of under 1 year or which are unconditionally cancellable	47,256,608	40,147,396	47,256,608	36,122,101
	<u>53,358,956</u>	<u>43,648,018</u>	<u>53,358,956</u>	<u>38,920,424</u>

(b) Derivatives

The following is an analysis of the aggregate notional amount of each significant type of derivative:

Group	2003			2002		
	Trading HK\$'000	Non-trading HK\$'000	Total HK\$'000	Trading HK\$'000	Non-trading HK\$'000	Total HK\$'000
Exchange rate contracts						
- Forwards	3,208,703	–	3,208,703	1,770,604	–	1,770,604
- Swaps	75,639,612	–	75,639,612	65,174,806	–	65,174,806
- Options purchased	1,886,608	–	1,886,608	639,824	–	639,824
- Options written	1,851,456	–	1,851,456	271,317	–	271,317
Interest rate contracts						
- Forwards and futures	18,239,962	–	18,239,962	9,764,075	–	9,764,075
- Swaps	117,042,845	23,659,036	140,701,881	140,356,210	14,045,777	154,401,987
- Options purchased	16,547,957	–	16,547,957	5,993,399	–	5,993,399
- Options written	16,535,149	–	16,535,149	5,993,399	–	5,993,399
Equity contracts						
- Options purchased	9,683,731	–	9,683,731	1,604,743	–	1,604,743
- Options written	9,683,731	–	9,683,731	1,604,743	–	1,604,743
	<u>270,319,754</u>	<u>23,659,036</u>	<u>293,978,790</u>	<u>233,173,120</u>	<u>14,045,777</u>	<u>247,218,897</u>

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NOTES TO THE ACCOUNTS (CONTINUED)

35 Off-balance sheet exposures (continued)

(b) Derivatives (continued)

Bank

	2003			2002		
	Trading HK\$'000	Non-trading HK\$'000	Total HK\$'000	Trading HK\$'000	Non-trading HK\$'000	Total HK\$'000
Exchange rate contracts						
- Forwards	3,208,703	–	3,208,703	1,914,093	–	1,914,093
- Swaps	75,639,612	–	75,639,612	65,251,194	–	65,251,194
- Options purchased	1,886,608	–	1,886,608	639,824	–	639,824
- Options written	1,851,456	–	1,851,456	271,317	–	271,317
Interest rate contracts						
- Forwards and futures	18,239,962	–	18,239,962	9,764,075	–	9,764,075
- Swaps	117,042,845	23,659,036	140,701,881	140,356,210	14,045,777	154,401,987
- Options purchased	16,547,957	–	16,547,957	5,993,399	–	5,993,399
- Options written	16,535,149	–	16,535,149	5,993,399	–	5,993,399
Equity contracts						
- Options purchased	9,683,731	–	9,683,731	1,604,743	–	1,604,743
- Options written	9,683,731	–	9,683,731	1,604,743	–	1,604,743
	<u>270,319,754</u>	<u>23,659,036</u>	<u>293,978,790</u>	<u>233,392,997</u>	<u>14,045,777</u>	<u>247,438,774</u>

Non-trading transactions as at 31st December 2003 include HK\$4,428,843,000 of interest rate swaps that were entered into to manage the interest rate positions of the Group

(c) Contract amounts, credit risk-weighted amounts and replacement costs

The contract amounts, credit risk-weighted amounts and replacement costs of the above off-balance sheet exposures are as follows:

Group

	2003			2002		
	Contract amount HK\$'000	Credit risk weighted amount HK\$'000	Replacement cost HK\$'000	Contract amount HK\$'000	Credit risk weighted amount HK\$'000	Replacement cost HK\$'000
Contingent liabilities and commitments	53,358,956	1,867,016	–	43,648,018	1,122,564	–
Derivatives						
- Exchange rate contracts	82,586,379	243,149	252,260	67,856,551	169,901	56,849
- Interest rate contracts	192,024,949	358,283	1,751,698	176,152,860	395,941	1,405,811
- Equity contracts	19,367,462	78,115	106,241	3,209,486	100,678	62,947
	<u>347,337,746</u>	<u>2,546,563</u>	<u>2,110,199</u>	<u>290,866,915</u>	<u>1,789,084</u>	<u>1,525,607</u>

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NOTES TO THE ACCOUNTS (CONTINUED)

35 Off-balance sheet exposures (continued)

(c) Contract amounts, credit risk-weighted amounts and replacement costs (continued)

Bank

	2003			2002		
	Contract amount HK\$'000	Credit risk weighted amount HK\$'000	Replacement cost HK\$'000	Contract amount HK\$'000	Credit risk weighted amount HK\$'000	Replacement cost HK\$'000
Contingent liabilities and commitments	53,358,956	1,867,016	–	38,920,424	933,122	–
Derivatives						
- Exchange rate contracts	82,586,379	243,149	252,260	68,076,428	168,538	57,305
- Interest rate contracts	192,024,949	358,283	1,751,698	176,076,428	395,941	1,405,811
- Equity contracts	19,367,462	78,115	106,241	3,209,486	91,924	62,947
	<u>347,337,746</u>	<u>2,546,563</u>	<u>2,110,199</u>	<u>286,282,766</u>	<u>1,589,525</u>	<u>1,526,063</u>

The above amounts are shown on a gross basis without taking into account the effect of bilateral netting arrangements.

The contract amounts of these instruments indicate the volume of transactions outstanding as at the balance sheet date; they do not represent amounts at risk.

The credit risk-weighted amounts are the amounts which have been calculated in accordance with the Third Schedule of the Banking Ordinance and guidelines issued by the Hong Kong Monetary Authority. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

Replacement cost is the cost of replacing all contracts which have a positive value when marked to market (should the counterparty default on its obligations) and is obtained by marking to market contracts with a positive value. Replacement cost is a close approximation of the credit risk for these contracts at the balance sheet date.

(d) Other contingent liabilities

In November 2002, the Group entered into a ten-year outsourcing agreement with IBM with respect to the provision of information technology and related support to the Group's operation in Hong Kong. As with all similar market standard arrangements, there are various termination clauses contained within the agreement that under certain circumstances could require the Group to pay a penalty on early termination of the contract. The exact amount of any penalty amount cannot be reliably determined as it is dependent upon business volumes over the period of the contract and on the timing of the termination itself.

In February 2002, the Group entered into a Life Insurance Bancassurance Distribution Agreement ("Agreement") with CGNU International Insurance PLC. Under the Agreement, the Group and a subsidiary of the Group's ultimate holding company, have a joint and several obligation, to pay a termination fee if the Group terminates the Agreement. The amount of termination fee payable is determined in accordance with the schedule of termination fees included in the Agreement, and ranges from HK\$145,000,000 to HK\$38,000,000, depending on when the Agreement is terminated.

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NOTES TO THE ACCOUNTS (CONTINUED)

36 Capital and lease commitments

(a) Capital commitments

Capital commitments for fixed assets outstanding at the balance sheet date not provided for in the accounts were as follows:

	Group		Bank	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Expenditure authorised and not provided for	21,584	30,018	21,584	28,213
Expenditure authorised but not contracted for	42,354	43,238	42,354	42,951
	63,938	73,256	63,938	71,164

The comparative figures for the above have been adjusted to conform with changes in the presentation for the current year.

(b) Lease commitments

At the balance sheet date, the total future minimum lease payments under non-cancellable operating leases were payable as follows:

	Group			
	2003		2002	
	Properties HK\$'000	Others HK\$'000	Properties HK\$'000	Others HK\$'000
Within 1 year	63,328	22,531	32,606	16,735
After 1 year but within 5 years	88,751	26,962	15,645	20,215
Over 5 years	800	–	–	–
	152,879	49,493	48,251	36,950

	Bank			
	2003		2002	
	Properties HK\$'000	Others HK\$'000	Properties HK\$'000	Others HK\$'000
Within 1 year	63,328	22,531	30,454	16,735
After 1 year but within 5 years	88,751	26,962	15,224	20,215
Over 5 years	800	–	–	–
	152,879	49,493	45,678	36,950

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NOTES TO THE ACCOUNTS (CONTINUED)

37 Reconciliation for cash flow statement

(a) Reconciliation of operating profit to net cash outflow from operating activities

	2003	2002
	HK\$'000	HK\$'000
Operating profit	2,387,578	1,274,598
Net gain on disposal of non-trading securities and held-to-maturity securities	10,338	19,064
Impairment loss on non-trading securities	–	(13,998)
Charge for bad and doubtful debts	821,003	509,665
Impairment of fixed assets	25,236	241,136
Depreciation	244,884	187,571
Advances written off net of recoveries	(926,699)	(724,090)
Interest expense for certificates of deposit issued	154,515	207,380
Interest expense for the 7.75% fixed rate subordinated notes	159,390	159,679
	<hr/>	<hr/>
Net cash inflow from trading activities	2,876,245	1,861,005
Net increase in money at call and short notice maturing beyond three months	(4,573,733)	(429,582)
Net decrease in treasury bills maturing beyond three months	735,603	8,646,207
Net decrease in placements with banks and other financial institutions maturing beyond three months	4,324,597	1,039,594
Net decrease/(increase) in certificates of deposit	320,871	(130,712)
Net decrease/(increase) in trading securities	940,453	(87,458)
Net increase in held-to-maturity securities	(5,966,865)	(1,542,851)
Net (increase)/decrease in advances less provisions	(704,538)	2,295,333
Net decrease/(increase) in advances to banks and other financial institutions	2,293	(241,477)
Net increase in non-trading securities	(3,530,028)	(1,946,500)
Net decrease/(increase) in other assets	76,504	(772,893)
Net decrease in deposits and balances of banks and other financial institutions	(836,976)	(2,671,352)
Net increase/(decrease) in deposits from customers	1,871,454	(837,754)
Net decrease in other liabilities	(248,826)	(5,902,256)
Exchange differences and other adjustments	3,180	1,079
	<hr/>	<hr/>
Net cash outflow from operating activities	<u>(4,709,766)</u>	<u>(719,617)</u>

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NOTES TO THE ACCOUNTS (CONTINUED)

37 Reconciliation for cash flow statement (continued)

(b) Analysis of changes in financing during the period

	Share capital and share premium HK\$'000	Certificates of deposit issued HK\$'000	7.75% Fixed rate subordinated notes HK\$'000
Balance as at 31st December 2001	5,231,351	3,679,615	2,039,995
Cash inflow from financing	–	3,892,628	–
Cash outflow from financing	–	(1,853,399)	–
Effect of foreign exchange movements	–	98	283
	<hr/>	<hr/>	<hr/>
Balance as at 31st December 2002	5,231,351	5,718,942	2,040,278
Additions through merger	564,152	300,000	–
Cash inflow from financing	–	5,247,185	–
Cash outflow from financing	–	(3,411,710)	–
Effect of foreign exchange movements	–	11,359	(9,322)
	<hr/>	<hr/>	<hr/>
Balance as at 31st December 2003	<u>5,795,503</u>	<u>7,865,776</u>	<u>2,030,956</u>

(c) Analysis of the balances of cash and cash equivalents

	2003 HK\$'000	2002 HK\$'000
Cash and balances with banks and other financial institutions	1,354,415	987,085
Money at call and short notice repayable with original maturity within three months	11,333,555	11,121,968
Placements with banks and other financial institutions repayable with original maturity within three months	3,559,281	2,963,410
Treasury bills repayable with original maturity within three months	2,042,371	2,973,994
	<hr/>	<hr/>
	<u>18,289,622</u>	<u>18,046,457</u>

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NOTES TO THE ACCOUNTS (CONTINUED)

38 Additions through merger

(a) Net assets transferred:

	Group HK\$'000	Bank HK\$'000
Cash and short-term funds	7,839,008	14,473,360
Certificates of deposit held	699,087	699,087
Held-to-maturity securities	469,779	469,779
Advances less provisions	22,156,080	40,546,375
Non-trading securities	9,304	4,510
Fixed assets	1,011,960	1,885,017
Other assets	608,925	2,538,170
Investment in subsidiaries	–	(3,830,785)
Deposits and balances of banks and other financial institutions	(520,579)	(2,813,127)
Deposits from customers	(27,490,067)	(47,239,904)
Certificates of deposit issued	(300,000)	(300,000)
Other liabilities	(870,411)	(2,051,217)
Amount due to subsidiaries	–	(44,661)
Deferred tax liabilities	(125,444)	(103,438)
	<u>3,487,642</u>	<u>4,233,166</u>
Represented by:		
Additions to the following reserves:		
- Share premium	564,152	564,152
- General reserve	1,715,543	1,633,986
- Premises revaluation reserve	715,926	713,267
- Investment properties revaluation reserve	81,752	81,752
- Investment revaluation reserve	6,550	594
- Retained earnings	403,719	1,239,415
	<u>3,487,642</u>	<u>4,233,166</u>

For the Group, the net assets transferred represent the amount of net assets of the DBS Kwong On Bank Group as at 1st January 2003. For the Bank, the net assets transferred represent the amount of net assets of DBS Kwong On Bank Limited and Overseas Trust Bank Limited as at 1st January 2003.

The adoption of the SSAP 12 has resulted in an increase in deferred tax liabilities included in the net asset transferred as at 1st January 2003 by HK\$125,444,000 and HK\$103,438,000 for the Group and Bank, respectively. The additions to reserves as at 1st January 2003 have been reduced by the same amount accordingly.

(b) Analysis of net inflow of cash and cash equivalents through merger

	HK\$'000
Cash and short term funds with original maturity within three months	7,683,035
Deposits and balances of banks and other financial institutions with original maturity within three months	(520,579)
	<u>7,162,456</u>

**DBS BANK (HONG KONG) LIMITED
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NOTES TO THE ACCOUNTS (CONTINUED)

39 Loans to officers

Particulars of loans made to officers and disclosed pursuant to Section 161B(4B) of the Hong Kong Companies Ordinance:

	Balance outstanding as at 31st December		Maximum balance during the year	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Aggregate amount outstanding in respect of principal and interest	<u>1,080</u>	<u>–</u>	<u>1,437</u>	<u>–</u>

40 Assets pledged as security

The aggregate amount of secured liabilities and the nature and carrying values of the assets pledged as security are as follows:

	Group and Bank	
	2003 HK\$'000	2002 HK\$'000
Secured liabilities (Note 29)	<u>7,700,545</u>	<u>8,967,137</u>
Assets pledged as security		
- Treasury bills	3,556,654	4,693,566
- Other securities	<u>5,066,656</u>	<u>5,244,710</u>
	<u>8,623,310</u>	<u>9,938,276</u>

41 Ultimate holding company

The ultimate holding company is DBS Group Holdings Ltd, a listed company incorporated in Singapore.

42 Approval of accounts

The accounts were approved and authorized for issue by the board of directors on 9th February 2004.

**DBS BANK (HONG KONG) LIMITED
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UNAUDITED SUPPLEMENTARY INFORMATION

The following information is disclosed as part of the accompanying information to the accounts and does not form part of the audited accounts.

1 Capital adequacy and liquidity ratios

	2003	2002
Capital adequacy ratio	<u>19.47%</u>	<u>24.47%</u>
Adjusted capital adequacy ratio	<u>19.05%</u>	<u>23.42%</u>
Average liquidity ratio	<u>45.26%</u>	<u>38.41%</u>

The capital adequacy ratio represents the combined ratio of the Bank as required by the Hong Kong Monetary Authority for its regulatory purposes, and is computed in accordance with the Third Schedule of the Banking Ordinance.

The adjusted capital adequacy ratio represents the capital adequacy ratio adjusted to take into account market risk as at the balance sheet date computed in accordance with the guideline “Maintenance of Adequate Capital against Market Risks” issued by the Hong Kong Monetary Authority.

The average liquidity ratio is the simple average of each calendar month’s average liquidity ratio for the relevant period calculated for Hong Kong offices of the Bank, and is in accordance with the Fourth Schedule of the Banking Ordinance.

2 Components of capital base after deductions

The capital base after deductions used in the calculation of the above capital adequacy ratios as at 31st December and reported to the Hong Kong Monetary Authority is analysed as follows:

	2003	2002
	HK\$’000	HK\$’000
Core capital		
Paid up ordinary share capital	5,200,000	5,200,000
Share premium	595,503	31,351
Reserves (eligible for inclusion in core capital)	8,792,694	8,149,464
	<u>14,588,197</u>	<u>13,380,815</u>
Supplementary capital		
Reserve on revaluation of land and interests in land	742,706	358,301
Reserve on revaluation of holding of securities not held for trading purposes	34,172	(11,472)
General provisions for doubtful debts	937,135	696,227
Term subordinated debt	1,624,765	2,040,278
	<u>3,338,778</u>	<u>3,083,334</u>
Gross and eligible value of supplementary capital		
	<u>3,338,778</u>	<u>3,083,334</u>
Total capital base before deductions	17,926,975	16,464,149
Deductions from total capital base	(617,194)	(445,941)
	<u>17,309,781</u>	<u>16,018,208</u>
Total capital base after deductions		
	<u>17,309,781</u>	<u>16,018,208</u>

The capital base represents the capital base of the Bank as at 31st December computed in accordance with the Third Schedule of the Banking Ordinance.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

3 Currency concentrations

HK\$' million	Group		
	US\$	Others	Total
2003			
Hong Kong dollar equivalents			
Spot assets	36,449	14,886	51,335
Spot liabilities	(36,795)	(13,318)	(50,113)
Forward purchases	39,284	2,965	42,249
Forward sales	(38,482)	(4,458)	(42,940)
Net long non-structural position	456	75	531
Net structural position	–	215	215
2002			
Hong Kong dollar equivalents			
Spot assets	34,188	11,366	45,554
Spot liabilities	(33,727)	(11,186)	(44,913)
Forward purchases	33,608	2,626	36,234
Forward sales	(33,743)	(2,737)	(36,480)
Net long non-structural position	326	69	395
Net structural position	–	235	235

The net structural position represents the Group's investment in the Philippines.

**DBS BANK (HONG KONG) LIMITED
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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

4 Segmental information

(a) By geographical area

Over 90% of the Group's operating income, profit before taxation, total assets, total liabilities, contingent liabilities and commitments arise from or are booked in Hong Kong.

(b) By class of business

	Group			
	Commercial and retail banking HK\$'000	Treasury HK\$'000	Overseas branches and subsidiaries HK\$'000	Total HK\$'000
Year ended 31st December 2003				
Operating income	<u>4,111,788</u>	<u>1,253,857</u>	<u>39,626</u>	<u>5,405,271</u>
Operating profit/(loss) before provisions	<u>2,184,676</u>	<u>1,025,479</u>	<u>(1,574)</u>	<u>3,208,581</u>
Operating profit/(loss)	<u>1,429,028</u>	<u>1,009,577</u>	<u>(51,027)</u>	<u>2,387,578</u>
Profit/(loss) before taxation	<u>1,417,992</u>	<u>1,009,577</u>	<u>(41,005)</u>	<u>2,386,564</u>
Year ended 31st December 2002				
Operating income	<u>3,032,747</u>	<u>560,532</u>	<u>80,618</u>	<u>3,673,897</u>
Operating profit before provisions	<u>1,339,976</u>	<u>426,775</u>	<u>17,512</u>	<u>1,784,263</u>
Operating profit	<u>815,864</u>	<u>424,589</u>	<u>34,145</u>	<u>1,274,598</u>
Profit before taxation	<u>840,363</u>	<u>424,589</u>	<u>37,654</u>	<u>1,302,606</u>

Commercial and retail banking business mainly comprises deposit account services, residential mortgage and other consumer lending, credit card services, corporate lending, trade finance and international banking.

Treasury activities are mainly the provision of foreign exchange services and centralised cash management for deposit taking and lending, trading activities and management of investment securities and the overall funding of the Banking Group.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

4 Segmental information (continued)

(c) Advances to customers

(i) By industry sectors

The information concerning gross advances to customers by industry sectors has been classified according to the usage of the loan and is stated gross of any provisions.

	2003	2002
	HK\$'000	HK\$'000
Loans for use in Hong Kong		
Industrial, commercial and financial		
- Property development	162,640	34,124
- Property investment	10,766,258	6,324,483
- Financial concerns	1,039,712	1,023,613
- Stockbrokers	141,876	53,937
- Wholesale and retail trade	2,231,798	1,428,279
- Manufacturing	5,666,365	2,697,662
- Transport and transport equipment	7,864,913	6,396,372
- Others	3,330,415	2,631,777
Individuals		
- Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	3,470,608	3,776,764
- Loans for the purchase of other residential properties	36,143,250	30,802,745
- Credit card advances	5,185,788	4,804,480
- Others	4,046,157	3,020,767
	80,049,780	62,995,003
Trade finance	12,874,033	6,782,632
Loans for use outside Hong Kong	1,202,782	1,153,771
	<u>94,126,595</u>	<u>70,931,406</u>

(ii) By geographical areas

Over 90% of the gross advances to customers and the related non-performing loans and overdue advances were located in Hong Kong after taking into account the transfer of risks. In general, transfer of risk applies when an advance is guaranteed by a party in a country which is different from that of the counterparty.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

4 Segmental information (continued)

(d) Cross-border claims

HK\$' million	Group			
	Banks and other financial institutions	Public sector entities	Others	Total
2003				
Asia Pacific excluding Hong Kong	9,475	287	1,559	11,321
North and South America	5,208	392	110	5,710
Europe	30,682	4	93	30,779
Others	299	–	240	539
	<u>45,664</u>	<u>683</u>	<u>2,002</u>	<u>48,349</u>
2002				
Asia Pacific excluding Hong Kong	6,795	222	1,013	8,030
North and South America	2,883	213	2,346	5,442
Europe	24,938	6	136	25,080
Others	236	–	424	660
	<u>34,852</u>	<u>441</u>	<u>3,919</u>	<u>39,212</u>

5 Overdue and rescheduled advances to customers

(a) Overdue advances to customers

The gross amount of advances, net of accrued interest that has been capitalised but accrued to a suspense account, which have been overdue for:

	Group			
	2003		2002	
	HK\$'000	% of total advances to customers	HK\$'000	% of total advances to customers
Six months or less but over three months	385,890	0.41	518,957	0.73
One year or less but over six months	418,878	0.44	211,633	0.30
Over one year	561,400	0.60	551,442	0.78
	<u>1,366,168</u>	<u>1.45</u>	<u>1,282,032</u>	<u>1.81</u>

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

5 Overdue and rescheduled advances to customers (continued)

(b) Rescheduled advances

The rescheduled advances (net of those which have been overdue for over three months and reported in item (a) above):

	Group			
	2003		2002	
	HK\$'000	% of total advances to customers	HK\$'000	% of total advances to customers
Performing loans	57,889		154,449	
Non-performing loans	304,999		139,203	
Rescheduled advances	<u>362,888</u>	0.39	<u>293,652</u>	0.41

(c) Reconciliation of overdue advances to non-performing advances

	Group	
	2003	2002
	HK\$'000	HK\$'000
Overdue advances to customers as per (a) above	1,366,168	1,282,032
Less: Advances which are overdue for more than three months and on which interest is still being accrued	(61,651)	(94,153)
Add: Advances which are overdue for three months or less, or which are not yet overdue, and on which interest is being placed in suspense or on which interest accrual has ceased		
- included in rescheduled advances	304,999	139,203
- others	618,772	392,648
Non-performing loans	<u>2,228,288</u>	<u>1,719,730</u>

(d) Repossessed assets

At 31st December 2003, the repossessed assets of the Group amounted to HK\$217,751,000 (2002: HK\$214,626,000).

**DBS BANK (HONG KONG) LIMITED
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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

6 Corporate governance

The Board has delegated certain responsibilities to various committees while reserving certain key matters for its approval. The following specialized committees of the Bank were established:-

(a) Board Executive Committee and Sub-committee

The Board Executive Committee has all the powers of the Board except those powers that can only be exercised by the Board under the law and other matters specified under the terms of reference which require board approval. In practice, the Board Executive Committee functions as a discussion forum for all matters that would, in accordance with the Bank's practice, be approved by the Board. The Board Executive Committee comprises four executive directors appointed by the Board.

For operational efficiency, an Executive Sub-committee comprising two executive directors in Hong Kong has been established pursuant to the Articles of Association of the Bank. The Board Executive Sub-committee is authorized to do all things which are in the ordinary course of business of the Bank as stipulated under the terms of reference. The Board Executive Sub-committee shall report to the Board Executive Committee in respect of the matters which are not on normal commercial terms or which are outside the ordinary course of the business of the Bank, in such manner and at such time or occasion as the Board Executive Committee at its discretion may deem fit.

(b) Board Audit Committee

The Board Audit Committee is authorized by the Board to investigate any activity within its terms of reference. Its main duties include inter alia, the review of the Bank's financial statements before submission to the Board, the nomination and appointment of the external auditor, the audit fee and any questions of resignation or dismissal, to review the internal audit programme and consider the major findings of internal investigations and management's response. The Board Audit Committee comprises not less than three members of the independent non-executive directors of the Bank.

(c) Board Risk Management Committee

The Board Risk Management Committee provides comprehensive and Bank-wide oversight of all risks and their management. It represents the focus of enterprise-wide risk management policy and review and provides oversight, direction and counsel to other risk committees and risk management processes. Its critical responsibilities include the review of risk profiles in relation to returns, reviewing changes in risk limits, policies and practices and helping to identify opportunities to optimize risk-based return on capital. The Board Risk Management Committee comprises the Chairman of the Bank, the Chief Executive Officer and other directors nominated by the Chairman of the Bank.

(d) Management Committee

The Management Committee formulates a bank-wide strategy and is responsible for its implementation and results. It ensures the effective integration between the various business and support units, and it will prioritize and determine the allocation of resources and capital to those units that have growth potential. The Committee is responsible for the maintenance of high corporate governance, risk management and compliance standards in Hong Kong. The Committee will set policy and guideline on human resources, training and investments that will help the Bank to build and sustain for future. The Committee comprises the Chairman of the Bank, the Chief Executive Officer and other senior management in Hong Kong.

**DBS BANK (HONG KONG) LIMITED
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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

6 Corporate governance (continued)

(e) Credit Committee

The Credit Committee serves as an executive forum for discussion and decisions on all aspects of credit risk and its management. It defines the nature of credit risk and oversees the credit portfolio, limits and processes for influencing and managing credit risk of all kinds. Its major responsibilities include the discussion and approval of credit proposals, identification of the Bank's credit risk portfolio and assessment of credit risk taking and asset quality. The members of the Credit Committee are the Chief Country Credit Officer and other members appointed by the Chief Executive Officer.

(f) Asset and Liability Committee

The Asset and Liability Committee manages the Bank's income against changing interest and currency rate conditions and maturities/duration. It decides on appropriate liquidity adequacy and management and oversees the structure and effects of the entire balance sheet as well as significant off balance sheet assets and liabilities. Its key responsibilities include identifying, measuring and monitoring the liquidity profile, ensuring that current and future funding requirements are met and determining appropriate mismatching, liquidity and other asset/liability position targets and limits from regulatory, product/market and profitability perspectives. The members of the Asset and Liability Committee are the Chief Executive Officer and representatives from Central Treasury Unit, Finance, Risk Management, Treasury & Markets and others nominated by the Chief Executive Officer/Head of Central Treasury Unit.

(g) Human Resources Committee

The Human Resources Committee coordinates all policies, processes and activities across the Group pertaining to the recruitment, training, performance measurement, appraisal and development of staff of the Group. Its key responsibilities include the recruitment and training of staff and monitoring staff performance evaluation processes and coordination of compensation policies and practices. The members of the Human Resources Committee are Head of Human Resources and others nominated by the Chief Executive Officer.

(h) Project Council

The Project Council serves as the forum to provide perspective and oversight over the project portfolio of the Bank. It provides guidance and approval for a framework and a set of criteria to achieve a balanced portfolio of projects that are aligned to the core strategies of the DBS Group including the Bank. The Project Council comprises the Chief Executive Officer, representatives from the relevant business units and support units and others nominated by the Chief Executive Officer/Head of Information Technology.

(i) Service Quality Steering Committee

The Service Quality Steering Committee provides oversight, direction and counsel relating to the management of customer service quality. The overall vision is "to differentiate DBS through superior customer service, thereby maximizing customer satisfaction and loyalty". The Service Quality Steering Committee comprises the Chief Executive Officer, Chairman of the Service Quality Council, representatives from the relevant business units and support units and others nominated by the Chief Executive Officer/Chairman of the Service Quality Council.

(j) Outsourcing Supervisory Committee

The Outsourcing Supervisory Committee provides enterprise-wide oversight, direction and counsel relating to the management of outsourcing activities. It serves as the executive forum for review and discussion of matters concerning the outsourcing arrangements. The Outsourcing Supervisory Committee comprises the Managing Director of the Bank as Chairman, representatives from the relevant support units and others nominated by the Chief Executive Officer/Chairman of the Outsourcing Supervisory Committee.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

6 Corporate governance (continued)

(k) Market Risk Committee

The Market Risk Committee provides comprehensive and enterprise-wide oversight, direction and counsel relating to the management of market risk. It also serves as an executive forum for discussion and decisions on all aspects of market risk and its management. The Market Risk Committee comprises the Chief Executive Officer, representatives from relevant business units and support units and others nominated by the Chief Executive Officer/Chairman of the Market Risk Committee.

(l) Operational Risk Committee

The Operational Risk Committee provides comprehensive and enterprise-wide oversight, direction and counsel relating to the management of operational, reputation and legal risks. It serves as an executive forum for discussion and decisions on all aspects of these risks and their management. The Operational Risk Committee comprises the Head of Risk Management, representatives from the relevant support units and others nominated by the Chief Executive Officer/Chairman of the Operational Risk Committee.

7 Risk management

The Group has implemented policies and procedures to identify, mitigate and monitor risk across the firm. These policies and procedures rely on constant communication, judgement, and knowledge of products, markets and controls by business and support units. The Group believes that business and support units have the primary responsibility for managing risk. At the same time, we insist on independent risk management and oversight.

The Group considers having world-class skills in monitoring, interpreting and forecasting our risk profile to be a critical internal capability. Our approach to risk management has several components: comprehensive risk management processes, early identification systems, accurate risk measures, investments in people and technology to interpret and manage risk on a daily basis, stress tests and comprehensive process reviews in conjunction with internal auditors, external auditors and regulatory officials.

The primary role of internal audit is to provide an independent opinion to the Board and Executive Management on the adequacy and effectiveness of the risk management and control processes in operations throughout the Group. Internal audit also provides proactive support in the promotion of effective risk management and control.

(i) Capital Management

It is the Group's policy to maintain a strong capital base to support the development of the Group's business and to meet the statutory capital adequacy ratio. Capital is allocated to the various activities of the Group depending on the risk reward criteria and regulatory requirements.

(ii) Credit Risk Management

Credit risk is the risk of loss due to the inability or unwillingness of a customer or counterparty to meet its payment obligations.

The Group's Credit Policies and Procedures Manual defines the credit extension and measurement criteria, the credit review, approval and monitoring processes and the system of loan classification and provision. Credit applications are guided by a set of credit principles which all extensions of credit must adhere to and these applications are subject to regular independent review. Business units and credit approvers have the responsibility to ensure that credits are properly assessed and classified. Business units also assume the responsibility to ensure all crucial information is included in the application for the purpose of assessment and approval.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

7 Risk management (continued)

(ii) Credit Risk Management (continued)

The Group adopts a multi-level credit approval process requiring loan approval at successively higher levels and/or committees (as delegated) depending on, among other things, the size and nature of the proposed transactions.

Credit exposure is represented by the notional or principal value of on and off-balance sheet financial instruments. For derivatives, potential credit loss is measured by Pre-settlement Credit Exposure, which is in general only a fraction of the derivative contract or notional amount used to express the volume of instruments. Exposures are monitored against credit limits and other control limits (such as large exposures and concentration limits) by independent credit control units at both the transaction and portfolio levels.

These credit policies and limits are established taking into account factors such as prevailing business and economic conditions, the Group's risk appetite to a single customer, or particular industries or sectors and regulatory requirements.

(iii) Liquidity Risk Management

Liquidity obligations arise from withdrawals of deposits, repayments of purchased funds at maturity, extensions of credit and working capital needs. The Group seeks to manage its liquidity risk across all classes of assets and liabilities to ensure that even under adverse conditions, the Group has access to funds at a reasonable cost.

The primary tool for monitoring liquidity is the maturity mismatch analysis, which is monitored over successive time bands and across functional currencies. This analysis includes behavioral assumptions on, inter-alia, customer loans, customer deposits, and reserve assets. This is tested under normal and adverse market scenario conditions. Limits are established for the cumulative negative cash flow over successive time bands. Various liquidity ratios, concentration and stress limits are additional tools employed by the Bank to manage funding liquidity risk.

The Group maintains a diverse source of funding that includes liquid bonds and maturing assets.

(iv) Structural Market Risk Management

The Asset and Liability Committee oversees the structural interest rate risk, exchange rate risk and funding liquidity risk in the Bank. It sets overall limits on each of these risk types for the Bank.

Structural interest rate risk arises from mismatches in the interest rate profile of customer loans and deposits. The structural interest rate relates to basis risk arising from different interest rate benchmarks, interest rate repricing risk, yield curve movements and embedded optionality.

In managing structural interest rate risk, the Group tries to achieve a desired profile given the strategic considerations and market conditions of the various business segments. To monitor the structural interest rate risk, various tools are used including repricing gap reports, sensitivity analysis and income simulations under various scenarios. These measures take into account both economic value and earnings perspectives.

The Group attempts to limit the effect of exchange rate movements on its earnings where possible. Our policy is to fund foreign currency lending with the same foreign currencies. For foreign currency investments, the Bank's general policy is to borrow fundable currencies. Non-fundable or illiquid currencies may be hedged using other instruments. Where appropriate for currencies with high hedging costs or lack of liquidity, alternative hedging strategies may be used.

An Investment Framework governs the Bank's investment of funds arising from the banking business. The investment portfolio is subject to Board and senior management limits on the portfolio size, credit quality, product and sector concentrations and market risk sensitivities under the Framework.

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UNAUDITED SUPPLEMENTARY INFORMATION (CONTINUED)

7 Risk management (continued)

(v) Operational Risk Management

Operational risk is the risk of loss arising from inadequate or failed internal processes, people or systems, or from external events. An Operational Risk Management Framework has been developed to ensure that operational risks within the Group are properly identified, monitored, managed and reported. Key elements of the framework include operational risk policies, risk and control self assessment, risk event management, key risk indicators reporting, process risk mapping, risk analysis and reporting, Global Insurance Program and Business Continuity Planning Program.

Each new product introduced is subject to a risk review and sign-off process where all relevant risks are identified and assessed by departments independent of the risk-taking unit proposing the product. Variations of existing products, as well as outsourcing initiatives, are also subject to a similar process.

(vi) Trading Market Risk Management

Trading market risk arises from changes in market rates such as interest rates, foreign exchange rates and equity prices, as well as in their correlation and implied volatilities. The Group takes trading market risk in the course of making market to meet customer requirements as well as to benefit from market opportunities.

The trading market risk framework establishes limits to ensure that risk-takers do not exceed aggregate risk and concentration parameters set by senior management and the Board. The framework also requires independent validation of valuation and risk models and methodologies as well as independent mark-to-market valuation, reconciliation of positions and tracking of stop-loss for trading positions on a timely basis. Risk issues are identified for new products and services before launch.

The Group adopts a Daily Earnings at Risk (DEaR) methodology to estimate the Bank's trading market risk with a 99% level of confidence over a one-day horizon. DEaR is computed using a combination of parametric and historical simulation approaches. It takes into account all pertinent risk factors and covers all financial instruments which expose the Bank to market risk, across all geographies. On a daily basis, the Group estimates DEaR for each trading business unit, as well as for the Bank. These daily reports also provide DEaR for individual activity and risk type such as foreign exchange, interest rate or equity. To complement the DEaR framework, daily stress testing is carried out to monitor the Bank's vulnerability to unlikely but plausible events in extreme market conditions. The DEaR figures are backtested against profit or loss of the trading books to validate its effectiveness.

The average daily revenue arising from the Group's market risk related treasury activities for the period ended 31st December 2003 was HK\$1,951,000 (2002: HK\$489,000) and the standard deviation for such daily revenue was HK\$4,732,000 (2002: HK\$1,826,000). The average daily revenue/(loss) and its standard deviation are analysed by principal dealing activities as follows:

	Average daily revenue/(loss)		Standard deviation	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Interest rate dealing	926	(38)	4,488	2,108
Foreign exchange dealing	660	417	1,394	1,258

