Credit and Country Risk Management

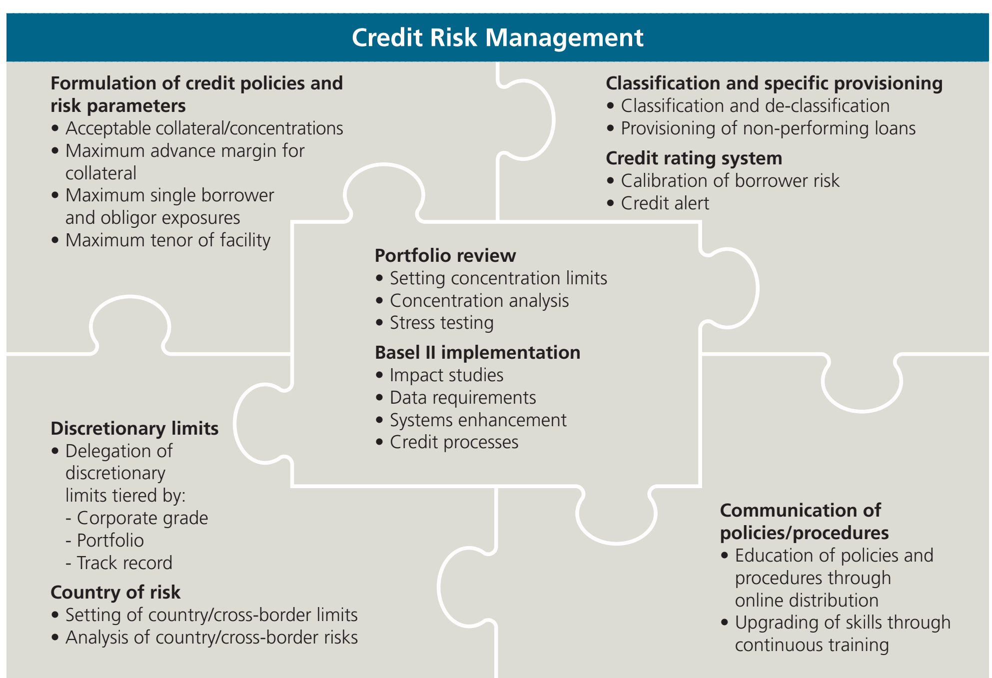
Credit risk

Counter-party and credit risk is defined as the potential loss arising from any failure by customers to fulfill their obligations, as and when they fall due. All credit exposures, whether on-balance sheet or off-balance sheet, are assessed. These obligations may arise from lending, trade finance, investment, receivables under derivative and foreign exchange contracts and other credit-related activities undertaken by the Group.

The Credit Committee, under delegated authority from the Board of Directors, approves credit policies, guidelines and procedures to control and monitor such risks. It has day-to-day responsibility for identifying and managing portfolio and risk concentration issues, including country exposure and industry sector exposure. The risk parameters for accepting credit risk are clearly defined and complemented by policies and processes to ensure that the Group maintains a well-diversified and high-quality credit portfolio. The decisions of the Credit Committee and its monthly risk management reports are reviewed by the Executive Committee of the Board.

Credit discretionary limits are delegated to officers of individual business units, depending on their levels of experience. Approval of all credits is granted in accordance with credit policies and guidelines. Defined credit risk parameters include single borrower, obligor, security concentrations, identified high-risk areas, maximum tenor, acceptable structure and collateral types.

Policies are also in place to govern the approval of 'Related Parties' credit facilities. 'Related Parties' refers to individuals or companies with whom the authorised credit approving authority and/or his/her immediate family members have a relationship, whether as director, partner, shareholder or any other relationship which would give rise to a potential conflict of interest.



Credit relationships with 'Related Parties' must be established on a strictly arm's length commercial basis. An approving authority shall abstain and absent himself/herself from the deliberation and approval of credit cases where the borrower is a 'Related Party' except when the 'Related Party' is a:

- company within the UOB Group;
- publicly listed company or company related to a publicly listed company;
- company formed by professional bodies, trade or clan associations, or societies.

The Board of Directors must be informed immediately in the event that any 'Related Party' borrower is in default of payment and/or in breach of any material term of the credit facility and such default or breach is not rectified within seven days of notice from the Group.

A comprehensive set of limits (country, regional, industry and counter-party) is in place to address concentration issues in the Group's portfolio. A rigorous process is established to regularly review and report asset concentrations and portfolio quality so that risks are accurately assessed, properly approved and monitored. These cover large credit exposures by obligor group, collateral type, industry, product, country, level of non-performing loans and adequacy of provisioning requirements.

In particular, the trends and composition of exposures to property-related loans are closely monitored, analysed and reported on an on-going basis to ensure that exposures are kept within regulatory limits and internal guidelines. The exposure concentrations and non-performing loans by industry type are reported to the Credit Committee and the Executive Committee of the Board on a monthly basis and to the Board of Directors on a quarterly basis.

Credit audits and reviews are regularly carried out to proactively identify and address potential weakness in the credit process and to pre-empt any unexpected deterioration in the credit quality.

The Group has made significant progress in its preparations for the New Basel Capital Accord (Basel II) and is already well in advance in developing, configuring and operationalising many of its systems and processes to prepare for the adoption of Basel II. The Group remains committed and will continue to invest in and strengthen its risk management systems, processes and practices to reach Internal Rating Based (IRB) compliance at the earliest date. To this end, the Group has engaged consultants in the relevant subject matters to provide advice on their fields of expertise.

Customer loans

Loans and advances are made to customers in various industry segments and business lines. The top 20 obligor group borrowers and top 100 group borrowers made up 14.4% and 23.7% of total loans and advances respectively.

Obligor groups are defined in accordance with Notice to Banks, MAS 623, to comply with Section 29(1)(a) of the Banking Act. Where the parent company is a borrower, exposures to the parent company and companies that it has 20% or more shareholding or power to control are aggregated into a single obligor group.

As at 31 December 2004, 38.3% of the Group's exposure was in its personal financial services portfolio, comprising mainly housing loans, other mortgage loans, credit cards and vehicle financing. The balance of the exposure was spread among various industry segments.

The composition of loans and advances and contingent liabilities to customers as at 31 December was as follows:

	Loans & advances			Contingent liabilities		
By industry type (%)	2004	2003	2002	2004	2003	2002
Transport, storage and communication	**3.1**	3.4	3.3	**2.2**	1.9	2.8
Building and construction	**11.0**	11.7	14.7	**16.4**	17.2	17.4
Manufacturing	**11.5**	9.4	8.6	**9.6**	8.4	10.3
Non-bank financial institutions	**15.0**	16.6	17.3	**42.2**	46.3	45.5
General commerce	**16.0**	14.8	15.0	**19.4**	17.2	13.7
Professionals and private individuals	**14.9**	15.4	15.0	**1.8**	2.6	2.7
Housing loans	**23.4**	23.6	22.2	**–**	–	–
Other	**5.1**	5.1	3.9	**8.4**	6.4	7.6
Total (%)	**100.0**	100.0	100.0	**100.0**	100.0	100.0
Total ($ million)	**67,977**	62,581	62,339	**9,818**	8,544	8,682

Classification and provision of loans

The Group classifies its loan portfolios according to the borrower's ability to repay the loan from its normal source of income. All loans and advances to customers are classified into the categories of 'Pass', 'Special Mention' or 'Non-Performing'. Non-Performing Loans are further classified as 'Substandard', 'Doubtful' or 'Loss' in accordance with Notice to Banks, MAS 612. The Group also practises split classifications of 'Substandard – Doubtful' and 'Substandard – Loss', whereby 'Substandard' is the secured portion. Interest income on all Non-Performing Loans is suspended and ceases to accrue. Such loans will remain classified until servicing of the account becomes satisfactory. Where appropriate, classified loans are transferred to in-house recovery specialists to maximise recovery prospects.

Loan classification	Description
Pass	All payments are current and full repayment of interest and principal from normal sources is not in doubt.
Special Mention	There is some potential weakness in the borrower's creditworthiness, but the extent of any credit deterioration does not warrant its classification as a Non-Performing Loan.
Non-Performing: Substandard	There is weakness in the borrower's creditworthiness that jeopardises normal repayment. Default has occurred or is likely to occur. The loan is more than 90 days past due, or the repayment schedule has been restructured.
Non-Performing: Substandard – Doubtful	The loan is partially secured by tangible collateral and the recovery rate on the unsecured portion is expected to be more than 50%.
Non-Performing: Substandard – Loss	The loan is partially secured by tangible collateral and the recovery rate on the unsecured portion is expected to be less than 50%.
Non-Performing: Doubtful	There is severe weakness in the borrower's creditworthiness, full repayment is highly questionable and no collateral is available.
Non-Performing: Loss	The chance of recovery from the loan is insignificant and no collateral is available.

The Group's provisions for credit losses are intended to cover probable credit losses through charges against profit. The provisions consist of an element that is specific to the individual loan and also a general element that has not been specifically identified to individual loans. The Group constantly reviews the quality of its loan portfolio based on its knowledge of the borrowers and, where applicable, of the relevant industry and country of operation.

A specific provision is made when the Group believes that the creditworthiness of a borrower has deteriorated to such an extent that the recovery of the entire outstanding loan is in doubt. The amount of specific provision to be made is based on the difference between the collateral value or discounted cash flows of an impaired loan and the carrying value of that loan.

A general provision is made to cover possible losses and could be used to cushion any losses known from experience to exist in the loan portfolio. In relation to the loan portfolios of its overseas operations, the Group's policy is to make provisions based on local (ie, the country of domicile of the overseas operation) regulatory requirements for local reporting purposes and then, where necessary, to make additional provisions to comply with the Group's provisioning policy and the Monetary Authority of Singapore (MAS) regulations.

Specific provision is made for each loan grade in the following manner:

Loan classification	Recovery expectation	Provision
Substandard	> 90% to 100%	10% to 50% of any unsecured loan outstanding
Doubtful	50% to 90%	50% to 100% of any unsecured loan outstanding
Loss	< 50%	100% of any unsecured loan outstanding

Loan interest

The classification of a loan as non-performing does not disqualify the Group of its entitlement to interest income. It merely registers the uncertainty faced by the Group in the collection of such interest income. The Group has adopted the approach that once a loan is classified as non-performing, interest will be suspended and will cease to accrue, irrespective of whether any collateral would be adequate to cover such payments.

Write-off

A classified account is written off where there is no realisable tangible collateral securing the account and all feasible avenues of recovery have been exhausted or where the borrower and guarantors have been bankrupted, wound up, and/or proof of debt filed. Approval from MAS must be obtained before director-related loans and other loans, as required under Notice to Banks, MAS 606, can be written off.

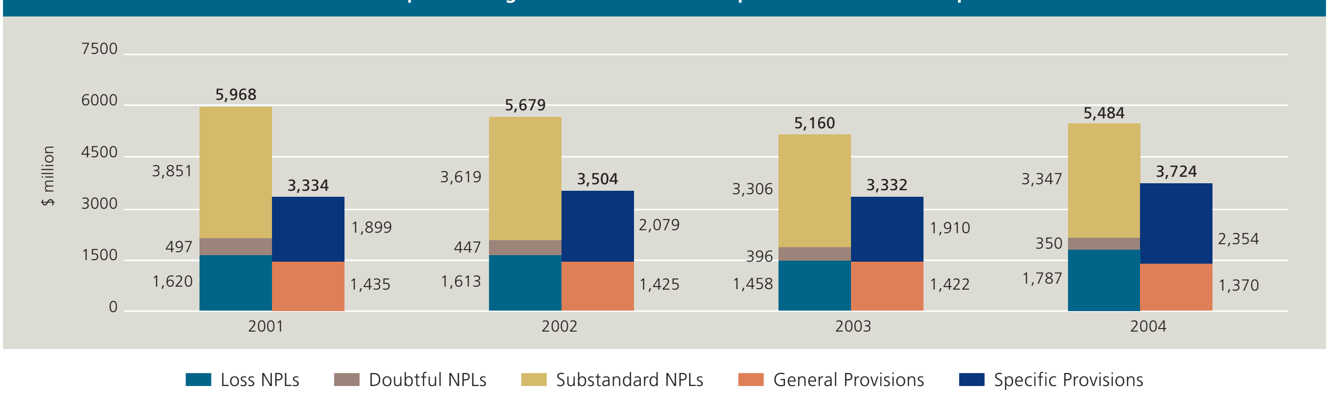
Non-performing loans (NPLs) and cumulative provisions of the Group

NPLs rose by $324 million or 6.3% to $5,484 million as at 31 December 2004, compared to $5,160 million as at 31 December 2003 due to the acquisition of Bank of Asia (BOA). NPL ratio was 8.0% as at 31 December 2004. Excluding BOA's NPLs of $1,030 million, Group's NPLs would have edged down by 13.7% to $4,454 million over 31 December 2003 and the NPL ratio would have improved to 6.9%. Of the total NPLs, $3,347 million or 61.0% was in the Substandard category and $2,797 million or 51.0% were secured by collateral.

Total cumulative provisions of $3,724 million as at 31 December 2004 increased 11.8%, compared to $3,332 million as at 31 December 2003. Excluding BOA's provision of $589 million, the Group's total cumulative provisions would have reduced by 5.9% to $3,136 million which was in line with lower NPLs. The total cumulative provisions provided 67.9% cover against total NPLs, compared to 64.6% as at 31 December 2003. Unsecured NPLs as at 31 December 2004 were 138.6% covered by total cumulative provisions, compared to 141.4% as at 31 December 2003.

NPLs by loan classification and cumulative provisions as at 31 December were as follows:

Non-performing loans and cumulative provisions of the Group



Ratios (%)	2004	2003	2002	2001
NPLs*/Gross customer loans	**8.0**	8.1	9.0	9.3
NPLs+/Gross customer loans and debt securities	**7.2**	7.7	8.7	9.0
NPLs/Total assets	**4.1**	4.5	5.3	5.2
Cumulative provisions/NPLs	**67.9**	64.6	61.7	55.9
Cumulative provisions/Doubtful & Loss NPLs	**174.3**	179.7	170.1	157.5
Cumulative provisions/Unsecured NPLs	**138.6**	141.4	138.3	136.6
Cumulative provisions*/Gross customer loans	**5.4**	5.2	5.5	5.2
General provisions/Gross customer loans (net of specific provisions* for loans)	**2.1**	2.3	2.4	2.3

* Excluding debt securities.

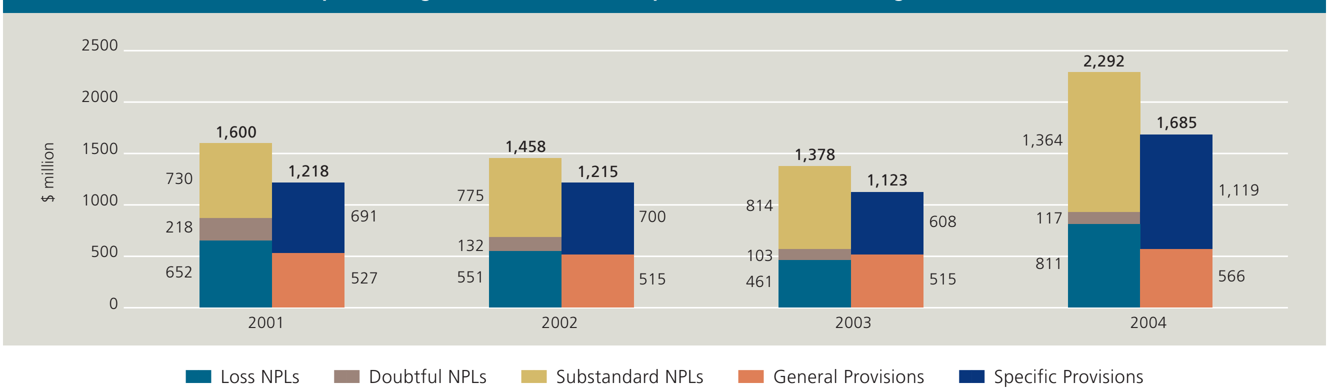
\+ Including debt securities.

NPLs and cumulative provisions of the Five Regional Countries

NPLs of the Five Regional Countries increased by 66.3% to $2,292 million as at 31 December 2004 from $1,378 million as at 31 December 2003. Excluding BOA's NPLs of $1,030 million, regional NPLs would have registered a decline of 8.4% to $1,262 million over 31 December 2003 and NPL ratio would have dropped to 12.4% as at 31 December 2004.

Total cumulative provisions for the Five Regional Countries were $1,685 million as at 31 December 2004. This was 50.0% or $562 million higher than the provisions of $1,123 million as at 31 December 2003. The cumulative provisions represented 73.5% of total NPLs and 181.6% of Doubtful and Loss NPLs in the Five Regional Countries.

Non-performing loans and cumulative provisions of the Five Regional Countries



Ratios (%)	2004	2003	2002	2001
NPLs*/Gross customer loans	**15.2**	14.1	17.0	19.2
NPLs+/Gross customer loans and debt securities	**13.9**	13.4	16.6	18.0
Cumulative provisions/NPLs	**73.5**	81.5	83.3	76.1
Cumulative provisions/Doubtful & Loss NPLs	**181.6**	199.1	177.9	140.0
Cumulative provisions*/Gross customer loans	**11.1**	11.5	14.1	14.7
General provisions/Gross customer loans (net of specific provisions* for loans)	**4.1**	5.7	6.6	7.0
NPLs/Gross exposure to the Five Regional Countries	**7.5**	6.7	8.9	8.9

* Excluding debt securities.

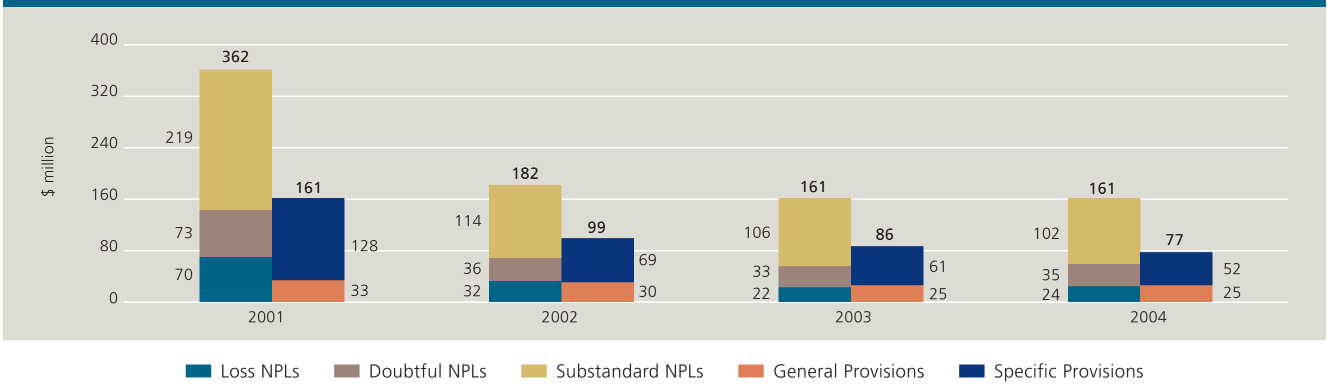
\+ Including debt securities.

NPLs and cumulative provisions of Greater China

NPLs of Greater China of $161 million as at 31 December 2004 remained the same as that as at 31 December 2003. However, the NPL ratio for Greater China improved by 0.2% point to 8.0% as at 31 December 2004 from 8.2% as at 31 December 2003.

Total cumulative provisions for Greater China of $77 million as at 31 December 2004 were $9 million or 10.5% lower compared to $86 million as at 31 December 2003. The cumulative provisions provided coverage of 47.8% for the total NPLs and 130.5% for the Doubtful and Loss NPLs.

Non-performing loans and cumulative provisions of Greater China



Ratios (%)	2004	2003	2002	2001
NPLs*/Gross customer loans	**8.0**	8.2	7.3	12.4
NPLs+/Gross customer loans and debt securities	**7.0**	7.4	6.1	10.7
Cumulative provisions/NPLs	**47.8**	53.4	54.4	44.5
Cumulative provisions/Doubtful & Loss NPLs	**130.5**	156.4	145.6	112.6
Cumulative provisions*/Gross customer loans	**3.8**	4.4	4.0	5.5
General provisions/Gross customer loans (net of specific provisions* for loans)	**1.3**	1.3	1.2	1.2
NPLs/Gross exposure to Greater China	**1.5**	1.7	2.4	5.7

* Excluding debt securities.
\+ Including debt securities

NPLs by region

By geographical region, Singapore accounted for $2,949 million or 53.8% of the total NPLs as at 31 December 2004. NPLs of Singapore decreased $581 million or 16.5% compared to the $3,530 million as at 31 December 2003.

As at 31 December 2004, NPLs of the Five Regional Countries were $2,292 million and constituted 41.8% of the total NPLs as at 31 December 2004. The increase was from Thailand, mainly due to the NPLs of $1,030 million from BOA. Excluding the NPLs from BOA, NPLs for the Five Regional Countries would have fallen to $1,262 million, representing 28.3% of the total NPLs as at 31 December 2004.

As at 31 December 2004, the NPLs of Greater China of $161 million was the same as that as at 31 December 2003.

$ million	2004	2003	2002	2001
Singapore	**2,949**	3,530	3,935	3,819
Malaysia	**873**	930	943	1,028
Indonesia	**88**	119	156	169
Philippines	**160**	184	208	242
Thailand	**1,170**	140	144	151
South Korea	**1**	5	7	10
Five Regional Countries	**2,292**	1,378	1,458	1,600
Greater China	**161**	161	182	362
Other	**82**	91	104	187
Group total	**5,484**	5,160	5,679	5,968

NPLs by industry

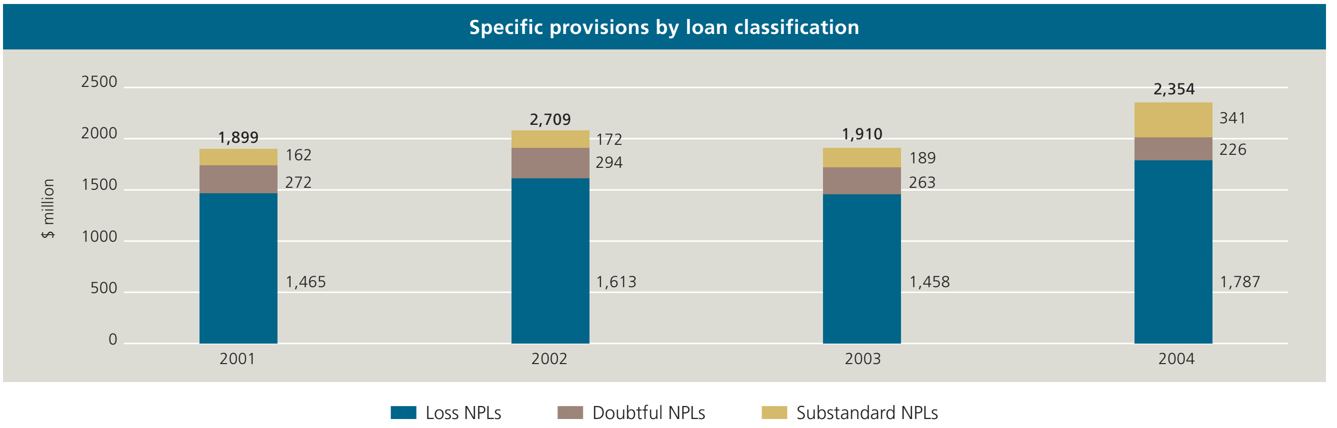
The increase in NPLs as at 31 December 2004 over that as at 31 December 2003 were mainly from the manufacturing (51.7%) and general commerce (34.0%) sectors while NPLs for consumer loans reduced (10.0%).

NPLs by industry as at 31 December were as follows:

	2004		2003		2002		2001	
Industry type	Amount ($ million)	As % of gross customer loan	Amount ($ million)	As % of gross customer loan	Amount ($ million)	As % of gross customer loan	Amount ($ million)	As % of gross customer loan
Transport, storage and communication	**119**	**5.7**	105	5.0	124	6.0	99	4.3
Building and construction	**844**	**11.3**	756	10.3	843	9.2	1,163	12.0
Manufacturing	**1,130**	**14.5**	745	12.7	874	16.2	895	16.8
Non-bank financial institutions	**660**	**6.5**	984	9.5	1,029	9.5	1,022	9.5
General commerce	**1,006**	**9.2**	751	8.1	769	12.4	825	13.1
Professionals and private individuals	**897**	**8.8**	926	9.6	1,014	10.9	939	9.9
Housing loans	**505**	**3.2**	632	4.3	668	4.8	556	4.2
Other	**244**	**7.1**	182	5.7	294	5.3	445	6.4
Sub-Total	**5,405**	**8.0**	5,081	8.1	5,615	9.0	5,944	9.3
Debt securities	**79**		79		64		24	
Total	**5,484**		5,160		5,679		5,968	

Specific provisions by loan classification

Of the total specific provisions of $2,354 million as at 31 December 2004, 75.9% was for 'Loss' accounts compared to 76.3% as at 31 December 2003. The specific provisions for each classified loan grade as at 31 December are shown in the following chart:



Specific provisions by region

As at 31 December 2004, Singapore and the Five Regional Countries accounted for 49.2% and 47.5% respectively of the Group's total specific provisions of $2,354 million, compared to 62.8% for Singapore and 31.8% for the Five Regional Countries as at 31 December 2003.

$ million	2004	2003	2002	2001
Singapore	**1,157**	1,200	1,271	1,037
Malaysia	**331**	383	428	439
Indonesia	**68**	78	111	88
Philippines	**80**	76	72	72
Thailand	**640**	69	87	88
South Korea	**–**	2	2	4
Five Regional Countries	**1,119**	608	700	691
Greater China	**52**	61	69	128
Other	**26**	41	39	43
Specific provisions for the Group	**2,354**	1,910	2,079	1,899
General provisions for the Group	**1,370**	1,422	1,425	1,435
Total	**3,724**	3,332	3,504	3,334

Specific provisions by industry

Specific provisions as at 31 December 2004 were mainly for manufacturing and general commerce. Specific provisions for manufacturing accounted for 26.1% of the total specific provisions for loans as at 31 December 2004, representing an increase of 7.2% points over the 18.9% as at 31 December 2003.

$ million	2004	2003	2002	2001
Transport, storage and communication	**56**	44	35	28
Building and construction	**337**	275	369	336
Manufacturing	**602**	352	398	370
Non-bank financial institutions	**190**	319	309	308
General commerce	**503**	316	309	305
Professionals and private individuals	**386**	360	329	296
Housing loans	**93**	98	143	80
Other	**139**	98	138	161
Sub-total	**2,306**	1,862	2,030	1,884
Debt securities	**48**	48	49	15
Total	**2,354**	1,910	2,079	1,899

Rescheduled and restructured accounts

A rescheduled account is one where repayment terms have been modified, but the principal terms and conditions of the original contract have not changed significantly. This is done to alleviate a temporary cash flow difficulty experienced by a borrower. It is expected that the problem is short-term and not likely to recur. The full amount of the debt is still repayable and no loss of principal or interest is expected.

When an account has been rescheduled three months before it meets the criteria for auto-classification, the account can be graded as 'Performing'. However, if the rescheduling takes place after the account has been graded as 'Non-Performing', it remains as such and is upgraded to 'Pass' after six months and provided there are no excesses and past dues.

A restructured account is one where the original terms and conditions of the facilities have been modified significantly to assist the borrower to overcome financial difficulties where the longer-term prospect of the business or project is still deemed to be viable. A restructuring exercise could encompass a change in the credit facility type, or in the repayment schedule including moratorium, or extension of interest and/or principal payments and reduction of accrued interest, including forgiveness of interest and/or reduction in interest rate charged.

When an account has been restructured based on financial consideration, the account will be graded as 'Non-Performing'. It can only be upgraded to 'Pass' after six months when all payments are current in terms of the restructured terms and conditions and there is no reasonable doubt as to the ultimate collectability of principal and interest.

Loans that were classified and restructured during the financial year were as follows:

$ million	2004		2003		2002		2001	
	Amount	Specific provisions	Amount	Specific provisions	Amount	Specific provisions	Amount	Specific provisions
Substandard	**223**	**22**	196	31	292	9	176	8
Doubtful	**49**	**37**	–	–	29	13	115	42
Loss	**30**	**30**	35	35	37	36	65	57
Total	**302**	**89**	231	66	358	58	356	107

Ageing of NPLs

The full outstanding balance of an account is deemed non-current and aged when there are arrears in interest servicing or principal repayment. The ageing of NPLs as at 31 December was as follows:

Ageing (Days)	2004		2003		2002		2001	
	Amount ($ million)	% of total NPLs	Amount ($ million)	% of total NPLs	Amount ($ million)	% of total NPLs	Amount ($ million)	% of total NPLs
Current	**548**	**10.0**	670	13.0	774	13.6	925	15.5
≤ 90	**357**	**6.5**	378	7.3	473	8.3	874	14.6
91 to 180	**596**	**10.9**	464	9.0	789	13.9	547	9.2
≥ 181	**3,983**	**72.6**	3,648	70.7	3,643	64.2	3,622	60.7
Total	**5,484**	**100.0**	5,160	100.0	5,679	100.0	5,968	100.0

Accounts that have payment records that are current or ≤ 90 days past due and/or in excess may be classified as 'Non-Performing' if the borrowers are deemed to be financially weak.

Collateral types

The majority of the classified loans are secured by properties in Singapore. Properties are valued at forced sale value and such valuations are updated semi-annually. NPLs are also secured by other types of collateral such as marketable securities that include listed stocks and shares, cash and deposits, and bankers' standby letters of credit/guarantees.

As at 31 December 2004, 51.0% of total Group NPLs was secured by collateral, compared to 54.3% as at 31 December 2003.

Secured/unsecured NPLs

	2004		2003		2002		2001	
	Amount ($ million)	% of total NPLs	Amount ($ million)	% of total NPLs	Amount ($ million)	% of total NPLs	Amount ($ million)	% of total NPLs
Group NPLs								
Secured	**2,797**	**51.0**	2,804	54.3	3,146	55.4	3,528	59.1
Unsecured	**2,687**	**49.0**	2,356	45.7	2,533	44.6	2,440	40.9
Total	**5,484**	**100.0**	5,160	100.0	5,679	100.0	5,968	100.0

The secured NPLs of the Group by collateral type and based on country of risk as at 31 December were as follows:

$ million	Properties	Marketable securities	Cash and deposits	Other	Total
2004					
Singapore	**1,442**	**21**	**19**	**36**	**1,518**
Five Regional Countries	**1,008**	**85**	**15**	**42**	**1,150**
Greater China	**84**	**–**	**–**	**–**	**84**
Other	**45**	**–**	**–**	**–**	**45**
Total	**2,579**	**106**	**34**	**78**	**2,797**
2003					
Singapore	1,883	51	16	78	2,028
Five Regional Countries	579	69	9	41	698
Greater China	44	1	2	–	47
Other	30	–	–	1	31
Total	**2,536**	**121**	**27**	**120**	**2,804**
2002					
Singapore	2,067	86	36	135	2,324
Five Regional Countries	569	102	2	43	716
Greater China	61	2	–	–	63
Other	43	–	–	–	43
Total	**2,740**	**190**	**38**	**178**	**3,146**
2001					
Singapore	2,282	136	14	64	2,496
Five Regional Countries	643	97	3	45	788
Greater China	109	11	–	11	131
Other	111	–	2	–	113
Total	**3,145**	**244**	**19**	**120**	**3,528**

Country risk

International lending involves additional risks compared to domestic lending in that there may be impediments arising from events in a foreign country that prevent repayment of the foreign borrowers' obligations to the Group. Such events may affect all borrowers of the same country. As such, it is important to set limits to safeguard various facets of the Group's exposures to any single country.

A system of country and cross-border limits are in place for monitoring country exposures and avoiding concentration of transfer, economic or political risks. Cross-border exposure is the summation of all country exposures including intra-group exposures, but excludes locally funded facilities provided by the Group's branches/subsidiaries to local borrowers/counter-parties or where the residual risks remain within a country.

The limit setting process is based on ratings by external agencies and internal country gradings. The latter is based on updates by country managers and/or business development managers who may be familiar with the country to quantify the risks of countries monitored, together with an assessment of current events and developments for each country. This process enables us to incorporate various quantitative key indicators as well as qualitative factors relating to each country's economic, social and political situation. A composite score is then derived and applied to a standard in-house scale to obtain a numeric rating for the country. This numeric rating is used to determine the appropriate country and cross-border limits based on a risk scale that curtails limits to countries where the Group does not have a presence. The limit setting process also takes into account the size of the Bank's capital funds, Group assets, the perceived economic strength and stability of the country of exposure and the assessment of the Group's portfolio spread and risk appetite.

These limits are reviewed regularly and reports on country and cross-border exposure are presented to the Credit Committee at least four times a year. At shorter intervals, based on updates by country and/or business development managers and other external sources, current events and developments, limits may be reviewed and business strategies revised as and when deemed necessary.

Country and cross-border limits approved by the Credit Committee are the primary limits for all transactions across all counter-parties. Extension of credit may thus be denied where a country/cross-border risk ceiling is reached although sufficient counter-party limits are available.

Exposure by country of operations

The Group's total direct net exposure to the countries (outside Singapore) in which it has a presence amounted to $49.1 billion or 36.4% of Group assets as at 31 December 2004, compared to $37.1 billion or 32.7% of Group assets as at 31 December 2003. Exposure reported below (excluding contingent liabilities) is categorised into loans to non-banks, banks, balances due from government and investments.

Exposure to countries outside Singapore (where UOB Group has a presence)

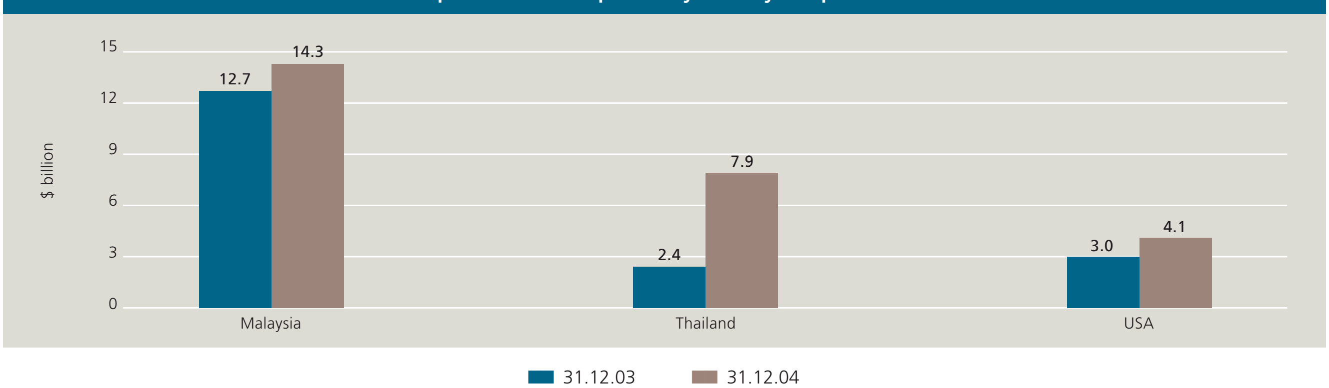
$ million	Loans to Non-bank	Loans to Bank	Government	Investments	Total	Less: Loans to/ investments in subsidiaries & branches	Net Exposure Total	Net Exposure % of Group assets	Contingent liabilities
Malaysia									
31-Dec-04	**7,051**	**5,014**	**3,377**	**1,009**	**16,451**	**2,137**	**14,314**	**10.6**	**1,066**
31-Dec-03	6,624	4,307	3,353	742	15,026	2,296	12,730	11.2	1,067
31-Dec-02	6,164	2,381	1,990	531	11,066	1,499	9,567	8.9	1,032
Indonesia									
31-Dec-04	**448**	**127**	**234**	**260**	**1,069**	**109**	**960**	**0.7**	**240**
31-Dec-03	491	48	165	79	783	50	733	0.7	132
31-Dec-02	444	106	127	67	744	50	694	0.6	67
Philippines									
31-Dec-04	**197**	**59**	**217**	**2**	**475**	**50**	**425**	**0.3**	**46**
31-Dec-03	241	53	221	12	527	41	486	0.4	60
31-Dec-02	254	44	225	9	532	31	501	0.5	56
Thailand									
31-Dec-04	**6,565**	**165**	**851**	**1,937**	**9,518**	**1,580**	**7,938**	**5.9**	**993**
31-Dec-03	1,642	112	523	244	2,521	156	2,365	2.1	332
31-Dec-02	1,178	112	814	203	2,307	185	2,122	2.0	285
South Korea									
31-Dec-04	**37**	**1,568**	**1,080**	**482**	**3,167**	**–**	**3,167**	**2.4**	**104**
31-Dec-03	41	825	596	209	1,671	–	1,671	1.5	173
31-Dec-02	45	1,354	298	98	1,795	12	1,783	1.7	253
Total Regional Countries									
31-Dec-04	**14,298**	**6,933**	**5,759**	**3,690**	**30,680**	**3,876**	**26,804**	**19.9**	**2,449**
31-Dec-03	9,039	5,345	4,858	1,286	20,528	2,543	17,985	15.9	1,764
31-Dec-02	8,085	3,997	3,454	908	16,444	1,777	14,667	13.7	1,693
Greater China									
31-Dec-04	**2,017**	**7,007**	**1,384**	**439**	**10,847**	**3,907**	**6,940**	**5.1**	**571**
31-Dec-03	1,968	5,943	1,038	352	9,301	3,340	5,961	5.2	639
31-Dec-02	2,482	4,311	233	648	7,674	2,536	5,138	4.8	504
Other OECD									
31-Dec-04	**4,878**	**7,012**	**1,937**	**2,215**	**16,042**	**943**	**15,099**	**11.2**	**911**
31-Dec-03	5,494	5,355	3,059	1,129	15,037	2,076	12,961	11.4	911
31-Dec-02	4,847	4,647	105	716	10,315	1,860	8,455	7.8	878
Other									
31-Dec-04	**195**	**121**	**19**	**5**	**340**	**68**	**272**	**0.2**	**74**
31-Dec-03	166	53	17	1	237	12	225	0.2	65
31-Dec-02	154	35	11	4	204	4	200	0.2	47
Grand Total									
31-Dec-04	**21,388**	**21,073**	**9,099**	**6,349**	**57,909**	**8,794**	**49,115**	**36.4**	**4,005**
31-Dec-03	16,667	16,696	8,972	2,768	45,103	7,971	37,132	32.7	3,379
31-Dec-02	15,568	12,990	3,803	2,276	34,637	6,177	28,460	26.5	3,122

Included in investments as at 31 December 2004 was an amount of $301 million, compared to $174 million as at 31 December 2003 that related to the dealing of debt and equity securities. Dealing and non-dealing securities as at 31 December were as follows:

$ million	2004			2003		
	Dealing	Non-dealing	Investments	Dealing	Non-dealing	Investments
Malaysia	**213**	**796**	**1,009**	14	728	742
Indonesia	**–**	**260**	**260**	4	75	79
Philippines	**1**	**1**	**2**	9	3	12
Thailand	**4**	**1,933**	**1,937**	32	212	244
South Korea	**26**	**456**	**482**	68	141	209
Five Regional Countries	**244**	**3,446**	**3,690**	127	1,159	1,286
Greater China	**27**	**412**	**439**	27	325	352
Other OECD	**26**	**2,189**	**2,215**	20	1,109	1,129
Other	**4**	**1**	**5**	–	1	1
Total	**301**	**6,048**	**6,349**	174	2,594	2,768

At the country level, the largest exposure was to Malaysia where the Group has a long-standing presence – $14.3 billion or 10.6% of Group assets as at 31 December 2004 against $12.7 billion or 11.2% of Group assets as at 31 December 2003. The second largest exposure was to Thailand, amounting to $7.9 billion or 5.9% of Group assets.

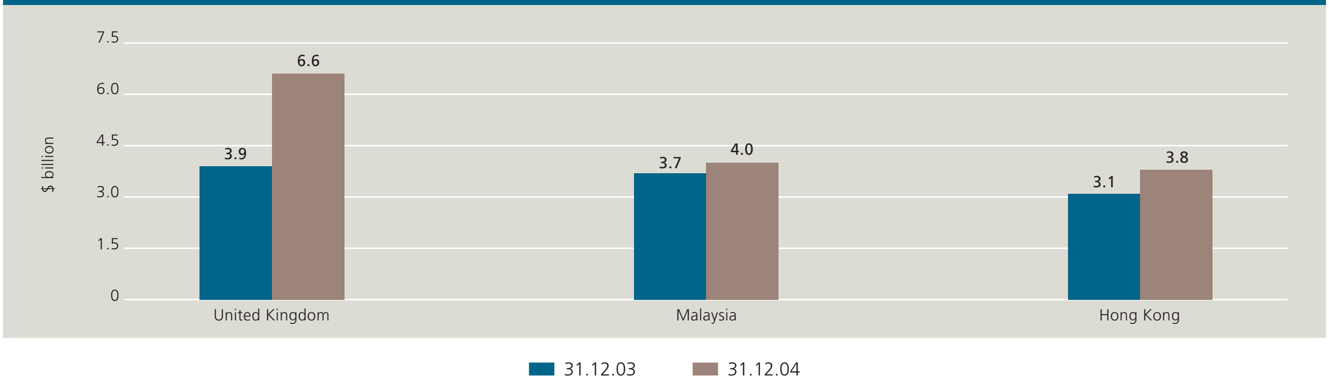
Top three direct exposure by country of operations



Cross-border exposure

As at 31 December 2004, total direct cross-border exposure to the countries where the Group has a presence amounted to $29.8 billion, compared to $22.7 billion as at 31 December 2003. The top three direct cross-border exposures were United Kingdom, Malaysia and Hong Kong.

Top three direct cross-border exposure by country



Cross-border exposure to countries outside Singapore (where UOB Group has a presence)

$ million	Loans to Non-bank	Loans to Bank	Government	Investments	Intra-Group	Total	% of Group assets
Malaysia							
31-Dec-04	**180**	**1,027**	**33**	**603**	**2,206**	**4,049**	**3.0**
31-Dec-03	192	826	34	465	2,230	3,747	3.3
31-Dec-02	130	471	35	342	1,393	2,371	2.2
Indonesia							
31-Dec-04	**199**	**63**	**5**	**260**	**139**	**666**	**0.5**
31-Dec-03	227	47	–	80	82	436	0.4
31-Dec-02	226	99	–	67	71	463	0.4
Philippines							
31-Dec-04	**–**	**4**	**–**	**2**	**52**	**58**	**–**
31-Dec-03	–	4	15	12	42	73	0.1
31-Dec-02	9	4	16	9	34	72	0.1
Thailand							
31-Dec-04	**95**	**104**	**–**	**1,451**	**76**	**1,726**	**1.3**
31-Dec-03	100	91	–	232	49	472	0.4
31-Dec-02	114	44	–	155	80	393	0.4
South Korea							
31-Dec-04	**32**	**1,517**	**–**	**482**	**31**	**2,062**	**1.5**
31-Dec-03	31	989	–	202	27	1,249	1.1
31-Dec-02	36	1,116	–	91	38	1,281	1.2
Total Regional Countries							
31-Dec-04	**506**	**2,715**	**38**	**2,798**	**2,504**	**8,561**	**6.3**
31-Dec-03	550	1,957	49	991	2,430	5,977	5.3
31-Dec-02	515	1,734	51	664	1,616	4,580	4.3
Greater China							
31-Dec-04	**656**	**3,482**	**–**	**195**	**4,015**	**8,348**	**6.2**
31-Dec-03	577	2,824	–	111	3,553	7,065	6.2
31-Dec-02	651	1,573	–	180	2,868	5,272	4.9
Other OECD							
31-Dec-04	**897**	**8,193**	**238**	**1,917**	**1,472**	**12,717**	**9.5**
31-Dec-03	841	5,310	7	861	2,517	9,536	8.4
31-Dec-02	420	5,901	7	371	2,238	8,937	8.3
Other							
31-Dec-04	**–**	**6**	**–**	**5**	**116**	**127**	**0.1**
31-Dec-03	–	10	–	1	110	121	0.1
31-Dec-02	–	4	–	4	101	109	0.1
Grand Total							
31-Dec-04	**2,059**	**14,396**	**276**	**4,915**	**8,107**	**29,753**	**22.1**
31-Dec-03	1,968	10,101	56	1,964	8,610	22,699	20.0
31-Dec-02	1,586	9,212	58	1,219	6,823	18,898	17.6

Balance Sheet Risk Management

Balance sheet risk is defined as the potential change in earnings arising from the effect of movements in interest rates and foreign exchange rates on the structural banking book of the Group that is not of a trading nature.

The Asset Liability Committee (ALCO), under delegated authority from the Board of Directors, approves policies, strategies and limits in relation to the management of structural balance sheet risk exposures. This risk is monitored and managed within a framework of approved policies and advisory limits by Risk Management & Compliance sector – Asset Liability Management and is reported monthly to ALCO. The decisions of ALCO and its monthly risk management reports are reviewed by the Executive Committee of the Board and by the Board of Directors. On a tactical level, Global Treasury – Asset Liability Management is responsible for the effective management of the balance sheet risk in the banking book in accordance with the Group's approved balance sheet risk management policies.

In carrying out its business activities, the Group strives to meet customers' demands and preferences for products with various interest rate structures and maturities. Sensitivity to interest rate movements arises from mismatches in the repricing dates, cash flows and other characteristics of assets and liabilities. As interest rates and yield curves change over time, the size and nature of these mismatches may result in a gain or loss in earnings. In managing balance sheet risk, the primary objective, therefore, is to monitor and avert significant volatility in Net Interest Income (NII) and Economic Value of Equity (EVE). For instance, when there are significant changes in market interest rates, the Group will adjust its lending and deposit rates to the extent necessary to stabilise its NII.

The balance sheet interest rate risk exposure is quantified using a combination of dynamic simulation modelling techniques and static analysis tools, such as maturity/repricing schedules. The schedules provide a static indication of the potential impact on interest earnings through gap analysis of the mismatches of interest rate sensitive assets, liabilities and off-balance sheet items by time bands, according to their maturity (for fixed rate items) or the remaining period to their next repricing (for floating rate items).

In general, interest rate risk will arise when more assets/liabilities than liabilities/assets are repriced in a given time band of a repricing schedule. A positive interest rate sensitivity gap exists where more interest sensitive assets than interest sensitive liabilities reprice during a given time period. This tends to benefit NII when interest rates are rising. Conversely, a negative interest rate sensitivity gap exists where more interest sensitive liabilities than interest sensitive assets reprice during a given time period. This tends to benefit NII when interest rates are falling. Interest rate sensitivity may also vary during repricing periods and among the currencies in which the Group has positions. The table in Note 43(c) to the financial statements represents the Group's interest rate risk sensitivity based on repricing mismatches as at 31 December 2004. The Group had an overall positive banking book interest rate sensitivity gap of $8,873 million, which represents the net difference in the interest rate sensitive assets and liabilities across the time periods. The actual effect on NII will depend on a number of factors, including variations in interest rates within the repricing periods, variations among currencies, and the extent to which repayments are made earlier or later than the contracted dates. The interest rate repricing profile, which includes lending, funding and liquidity activities, typically leads to a negative interest rate sensitivity gap in the shorter term.

Complementing the static analysis is the dynamic simulation modelling process. In this process, the Group applies both the earnings and EVE approaches to measuring interest rate risk. The potential effects of changes in interest rates on NII are estimated by simulating the future course of interest rates, expected changes in the Group's business activities over time, as well as the effect of embedded options in the form of loans subject to prepayment and of deposits subject to preupliftment. The changes in interest rates are simulated using different interest rate scenarios depicting changes in the shape of the yield curve, including high and low rates, positive and negative tilt scenarios and implied forward interest rates.

EVE is simply the present value of the Group's assets less the present value of the Group's liabilities, currently held by the Group. In EVE sensitivity simulation modelling, the present values for all the Group's cash flows are computed, with the focus on changes in EVE under various interest rate environments. This economic perspective measures interest rate risk across the entire time spectrum of the balance sheet, including off-balance sheet items.

Stress testing is also performed regularly on balance sheet risk to determine the sensitivity of the Group's capital to the impact of more extreme interest rate movements. This stress testing is conducted to assess that even under more extreme market movements, for example, the Asian crisis, the Group's capital will not deteriorate beyond its approved risk tolerance. Such tests are also performed to provide early warning of potential worst-case losses so as to facilitate proactive management of these risks in the rapidly changing financial markets. The results of such stress testing are presented to ALCO, the Executive Committee of the Board and the Board of Directors.

The risks arising from the trading book, for example, interest rates, foreign exchange rates and equity prices, are managed and controlled under the market risk framework that is discussed under the section 'Market Risk Management' on pages 48 to 51.

Liquidity Risk Management

Liquidity risk is defined as the potential loss arising from the Group's inability to meet its contractual obligations when due. Liquidity risk arises in the general funding of the Group's activities and in the management of its assets and liabilities, including off-balance sheet items. The Group maintains sufficient liquidity to fund its day-to-day operations, meet customer deposit withdrawals either on demand or at contractual maturity, meet customers' demand for new loans, participate in new investments when opportunities arise, and repay borrowings as they mature. Hence, liquidity is managed to meet known as well as unanticipated cash funding needs.

Liquidity risk is managed within a framework of liquidity policies, controls and limits approved by ALCO. These policies, controls and limits ensure that the Group maintains well-diversified sources of funding, as well as sufficient liquidity to meet all its contractual obligations when due. The distribution of sources and maturities of deposits is managed actively in order to ensure cost-effective and continued access to funds and to avoid a concentration of funding needs from any one source. Important factors in assuring liquidity are competitive pricing in interest rates and the maintenance of customers' confidence. Such confidence is founded on the Group's good reputation, the strength of its earnings, and its strong financial position and credit rating.

The management of liquidity risk is carried out throughout the year by a combination of cash flow management, maintenance of high-quality marketable securities and other short-term investments that can be readily converted to cash, diversification of the funding base, and proactive management of the Group's 'core deposits'. 'Core deposits' is a major source of liquidity for the Group. These 'core deposits' are generally stable non-bank deposits, like current accounts, savings accounts and fixed deposits. The Group monitors the stability of its 'core deposits' by analysing their volatility over time.

In accordance with the regulatory liquidity risk management framework, liquidity risk is measured and managed on a projected cash flow basis. The Group is required to monitor liquidity under 'business as usual' and 'bank-specific crisis' scenarios. Liquidity cash flow mismatch limits have been established to limit the Group's liquidity exposure. The Group has also identified certain early warning indicators and established the trigger points for possible contingency situations. These early warning indicators are monitored closely so that immediate action can be taken. On a tactical daily liquidity management level, Global Treasury – Asset Liability Management is responsible for effectively managing the overall liquidity cash flows in accordance with the Group's approved liquidity risk management policies and limits.

Liquidity contingency funding plans have been drawn up to ensure that alternative funding strategies are in place and can be implemented on a timely basis to minimise the liquidity risks that may arise upon the occurrence of a dramatic change in market conditions. Under the plans, a team comprising senior management and representatives from all relevant units will direct the business units to take certain specified actions to create liquidity and continuous funding for the Group's operations.

Overseas banking branches and subsidiaries must comply with their local regulatory requirements with regard to liquidity and will operate on being self-sufficient in funding capabilities, whenever possible. However, the Group's Head Office in Singapore will provide funding to them on an exceptional basis, for instance, during a stressed liquidity crisis when they are unable to borrow sufficient funds for their operational needs or when it is cheaper to fund through Head Office.

The table in Note 43(d) to the financial statements shows the maturity mismatch analysis of the Group's nearer and longer-term time bands relating to the cash inflows and outflows based on contractual classifications arising from business activities. The projected net cash outflow in the 'Up to 7 days' time band comprises mainly customers' current accounts and savings accounts that are repayable on demand. However, when these customer deposits are adjusted for behavioural characteristics, the projected net cash outflow in the 'Up to 7 days' time band is very much reduced as they are adjusted out to the longer-term time bands due to the stable nature of these customer deposits.

Sources of Deposits

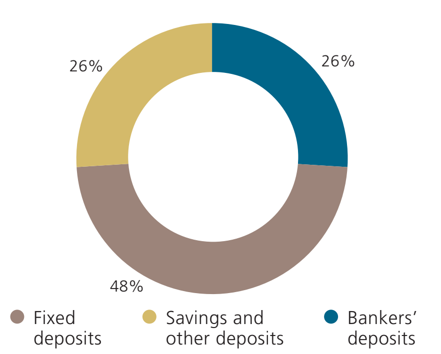
The Group has access to diverse funding sources. Liquidity is provided by a variety of both short-term and long-term instruments. The diversity of funding sources enhances funding flexibility, limits dependence on any one source of funds, and generally lowers the overall cost of funds. In making funding decisions, management considers market conditions, prevailing interest rates, liquidity needs, and the desired maturity profile of the Group's liabilities.

Non-bank customers' fixed deposits, savings and other deposits continued to form a significant part of the Group's overall funding base in the year under review. As at 31 December 2004, these customer deposits amounted to $79,019 million and accounted for 74% of total Group deposits. Bankers' deposits, on the other hand, amounted to $28,194 million and formed the remaining 26% of total Group deposits. In terms of deposit mix, fixed deposits comprised the majority of the funding base at 48%, followed by savings and other deposits at 26%. Bankers' deposits are also used by the Group to capitalise on money market opportunities and to maintain a presence in the inter-bank money markets.

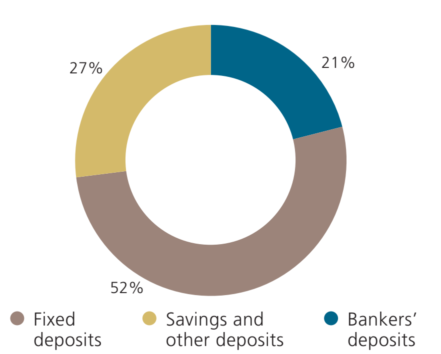
Sources of Deposits – 2004	$ million	%
Customer deposits		
Fixed deposits	**50,933**	**48**
Savings and other deposits	**28,086**	**26**
	79,019	**74**
Bankers' deposits	**28,194**	**26**
Total deposits	**107,213**	**100**

Sources of Deposits – 2003	$ million	%
Customer deposits		
Fixed deposits	**45,801**	**52**
Savings and other deposits	**24,062**	**27**
	69,863	**79**
Bankers' deposits	**18,839**	**21**
Total deposits	**88,702**	**100**

Sources of deposits – 2004



Sources of deposits – 2003



Market Risk Management

Market risk is defined as the potential loss in market value of a given portfolio that can be expected to be incurred arising from changes in market prices, namely, interest rates, foreign exchange rates, equity prices, credit spreads and option volatility relating to all the above rates or prices.

The Group is exposed to market risk in its trading portfolio because the values of its trading positions are sensitive to changes in market prices and rates.

Market risk is managed using a framework of market risk management policies and risk control procedures, as well as notional, greeks, risk and loss limits. These limits are proposed by every trading desk/division (including the Group's overseas operations), reviewed by Risk Management & Compliance sector – Market Risk Management and approved by ALCO annually. ALCO also reviews and approves new limits or changes to existing limits as and when these are proposed. The powers of ALCO are delegated by the Executive Committee of the Board whose powers are, in turn, delegated by the Board of Directors. The monitoring of market risk trading limits and the reporting of any limit excess and ratification are carried out independently by the Middle Office.

There is no single risk statistic that can reflect all aspects of market risk. The most common approaches are Value-at-Risk (VaR) and stress testing. These risk measures, taken together, provide a more comprehensive view of market risk exposure than any one of them individually. VaR is a measure of the dollar amount of potential loss from adverse market movements under a normal market environment. Statistical models of risk measurement, such as VaR, provide an objective and independent assessment of how much risk is being taken. They also allow consistent and comparable measurement of risks across financial products and portfolios.

Market risk is measured using VaR methodologies, namely, variance-covariance and historical simulation models based on historical market data changes for the past 260 days within a 95% confidence level and assuming a one-day trading horizon.

The variance-covariance methodology is a parametric approach that assumes returns are normally distributed. Under this methodology, a matrix of historical volatilities and correlations is computed from the past 260 days' market data changes. VaR is then computed by applying these volatilities and correlations to the current portfolio valued at current price levels.

The historical simulation methodology is a non-parametric approach that does not make any underlying assumption about the distribution of returns. The method assumes that actual observed historical changes in market rates, such as interest and foreign exchange rates, reflect future possible changes. It uses historical price changes for the past 260 days to compute the returns of the portfolio and a VaR figure is then obtained from the actual distribution of these returns of the portfolio based on a 95 percentile.

The VaR calculations are performed for all material trading portfolios.

However, there are certain limitations to the VaR methodologies. They do not reflect the extent of potential losses that may occur beyond the 95% confidence level or that may occur for positions that could not be liquidated within the one-day trading horizon. In addition, historical data may not accurately reflect price changes that are likely to occur in the future and all VaR methodologies are dependent on the quality of available market data. Hence, to evaluate the robustness of the VaR model, daily 'back testing' of VaR estimates are conducted against hypothetical losses. This is carried out in accordance with the Group's Back Testing Policy, as approved by ALCO.

To overcome the limitations of VaR as well as to complement VaR, stress and scenario tests are performed on the trading portfolios. These serve to provide early warning of potential worst-case losses so as to facilitate proactive management of these risks in the rapidly changing financial markets. While VaR estimates the Group's exposure to events in normal markets, stress testing discloses the risks under plausible events in abnormal markets. Portfolio stress testing is integral to the market risk management process and, together with VaR, are important components in risk measurement and control tools.

Stress tests are performed in accordance with the Group's Stress Testing Policy, as approved by ALCO. The Group's corporate stress tests are built around changes in market rates and prices that result from pre-specified economic scenarios, such as historical market events as well as hypothetical sensitivity analysis, and assume that no action is taken during the stress event to mitigate risks, reflecting the decreased liquidity that frequently accompanies market shocks.

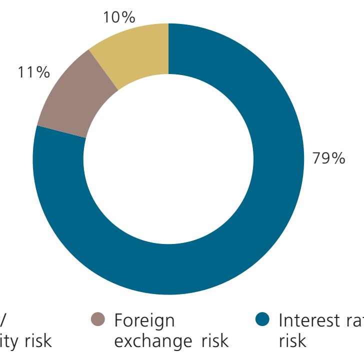
Some examples of stress tests that are performed include daily worst-case VaR based on the worst price changes experienced within the past 260 days and on historical events, for instance, the 1997/1998 Asian Financial Crisis, the 2000/2001 New Economy Crisis and the June – August 2002 Investor Confidence Crisis. Hypothetical sensitivity analysis includes parallel yield curve shifts, steepening and flattening of yield curves at different pivot tenor points for major trading currencies, equity price stress test, as well as FX stress test for pegged and Asian currencies.

As with VaR, stress test calculations are performed for all material trading portfolios.

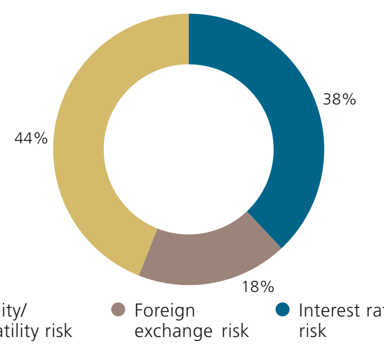
The VaR, stress and scenario testing results are reported to ALCO, the Executive Committee of the Board and the Board of Directors in accordance with the frequency that they meet.

The risks taken by the Group are measured against corresponding rewards to ensure that returns are commensurate with the risks taken. A risk-reward measure of Earnings-at-Risk (EaR) is used as a standard measurement of the risks against corresponding rewards across different products and business types. EaR is used as a benchmark in the setting of risk limits against prospective earnings.

Group Daily Diversified VaR – 2004



Group Daily Diversified VaR – 2003



Value-at-Risk (VaR)

The risks taken by the Group, as reflected by the level of VaR, are dependent on the level of exposure taken by the Group, and the level of market prices for the relevant period that is used in the computation of VaR.

The Group's Daily Diversified VaR, as at 31 December 2004, was $7.71 million and comprised mainly interest rate risk – including credit spread risk (79%), foreign exchange risk (11%) and equity/volatility risk (10%).

The Group's Daily Diversified VaR for 2004, averaging $4.39 million, ranged between a low of $2.07 million and a high of $10.02 million.

Group Daily Diversified VaR for 2004

$ million	31-Dec-04	High	Low	Average
Interest rate	7.97	9.55	0.39	3.48
Foreign exchange	1.09	3.34	0.52	1.38
Equity/volatility	1.00	4.16	0.41	1.58
Diversification effect	(2.39)	NM	NM	(2.03)
Total VaR	7.71*	10.02	2.07	4.39*

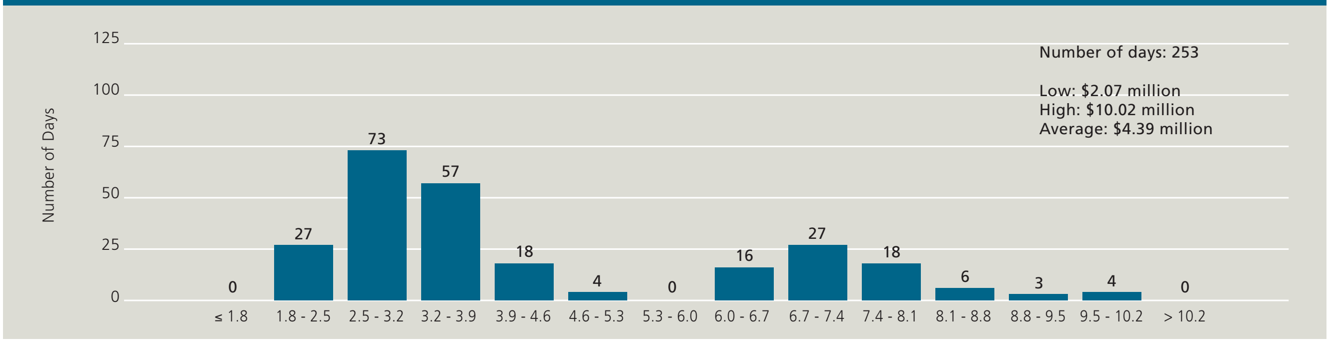
Group Daily Diversified VaR for 2003

$ million	31-Dec-03	High	Low	Average
Interest rate	2.30	2.82	1.17	1.82
Foreign exchange	1.05	5.81	0.60	1.43
Equity/volatility	2.62	3.76	0.64	1.75
Diversification effect	(1.94)	NM	NM	(1.90)
Total VaR	4.03*	6.81	1.95	3.11*

NM denotes 'Not Meaningful' to compute diversification effect because the high and low may occur on different days for different risk types.

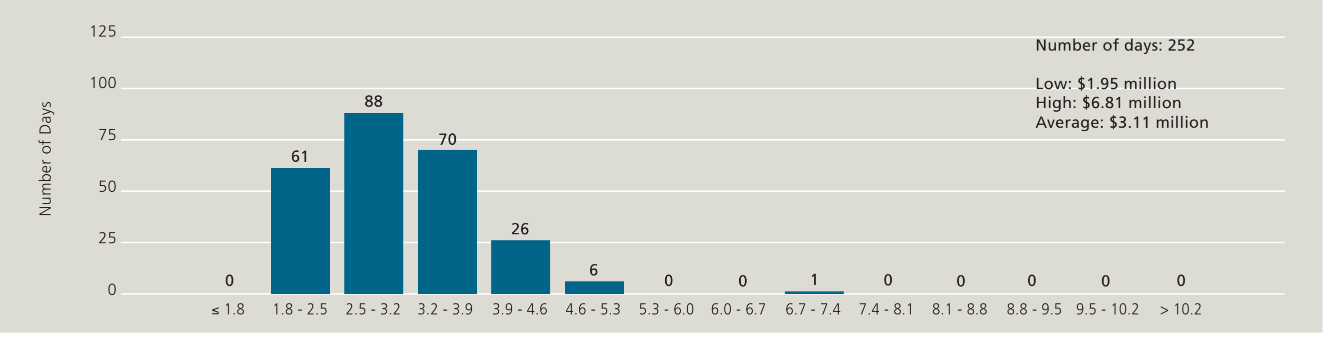
* Due to rounding

Group Daily Diversified VaR Distribution for 2004



Diversified VaR ($ million)

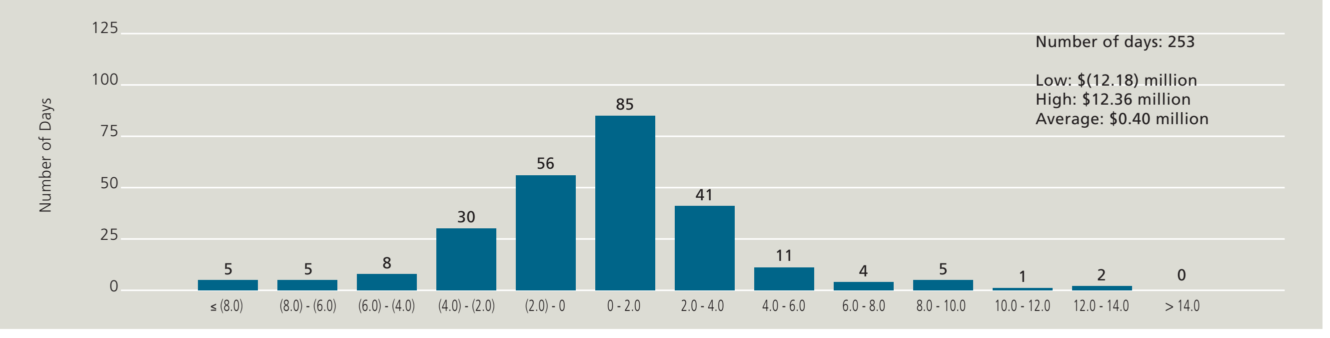
Group Daily Diversified VaR Distribution for 2003



Diversified VaR ($ million)

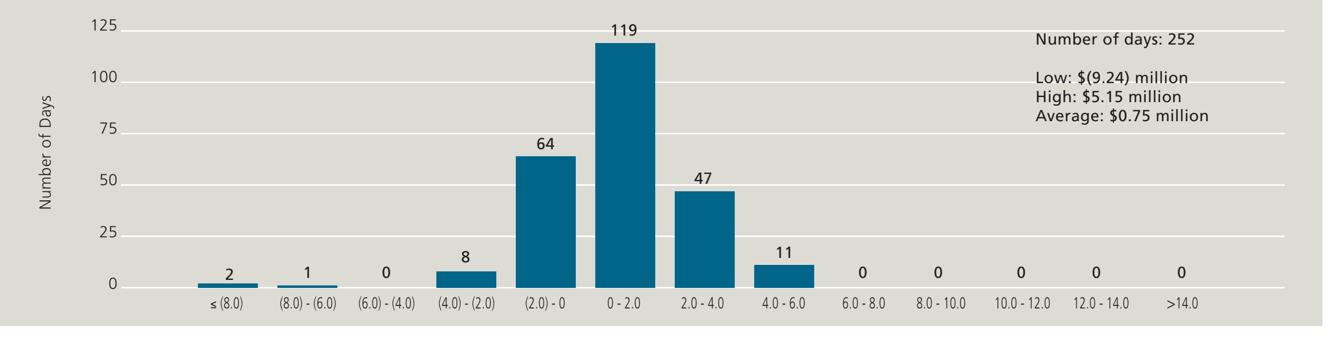
The Group's daily trading income for 2004, averaging $0.40 million, ranged between a low of $(12.18) million and a high of $12.36 million:

Group Daily Trading Income Distribution for 2004



Profit and Loss ($ million)

Group Daily Trading Income Distribution for 2003



Profit and Loss ($ million)

Operational Risk Management

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Potential loss may be in the form of financial loss or other damages, for example, loss of reputation and public confidence that will impact the Group's credibility and ability to transact, maintain liquidity and obtain new business.

Operational risk is managed through a framework of policies, techniques and procedures as approved by the Management Committee (MC) under its delegated authority from the Board of Directors. The decisions of the MC and its monthly risk management reports are reviewed by the Executive Committee of the Board.

This framework of techniques and procedures encompasses the following:
- building of Operational Risk Profiles (ORPs);
- conduct of Operational Risk Self Assessment (ORSA) based on the ORPs;
- development of an Operational Risk Action Plan (ORAP);
- monitoring of Key Operational Risk Indicators (KORIs);
- collection and analysis of operational risk events/loss data;
- monitoring and reporting of operational risk issues.

The building of ORPs involves risk identification, the assessment of inherent or absolute risks, as well as the identification and classification of management controls. The methodology provides the tool for the profiling of significant operational risks to which business and support units are exposed. These units then define the key management policies/procedures/controls that have been established to address the identified operational risks.

As part of the continual assessment, ORSA provides the business/support heads with an analytical tool to identify the wider operational risks, assess the adequacy of controls over these risks, and identify control deficiencies at an early stage so that timely action can be taken.

Where actions need to be taken, these are documented in the form of an ORAP for monitoring and reporting to top management.

KORIs are statistical data that are collected and monitored by business units on an on-going basis for the early detection of potential areas of operational control weakness. Trend analysis is carried out to determine whether there are systemic issues to be addressed.

A database for collection of operational risk events and losses has been established to enable the future use of advanced approaches for quantification of operational risks. Additionally, the analysis of operational risk events and sharing of lessons learnt help to further strengthen the operational risk management capability of the business units.

Included in the overall framework of operational risk is the disciplined product programme process. This process aims to ensure that the risks associated with each new product/service are identified, analysed and managed.

For the implementation of all online products and services, extra care and precautionary measures are taken to address and protect customers' confidentiality and interests. Clear instructions are also posted on the Group's website to advise and educate customers on the proper use and safekeeping of their access identification and passwords.

As part of the Group's comprehensive operational risk framework, an enhanced Group-wide Business Contingency Plan has been developed. In addition, in line with the increasing need to outsource internal operations in order to achieve cost efficiency, a Group policy has been established to regulate the outsourcing of services to third parties.

Risk transfer mechanisms, such as insurance, to mitigate the risk of high impact loss events also form part of this framework. Identified operational risks with relatively high residual risk assessment ratings and new risks that are beyond the control of the Group will be scrutinised for insurability.

Legal risk is part of operational risk. Legal risk arises from inadequate documentation, legal or regulatory incapacity or insufficient authority of customers and uncertainty in the enforcement of contracts. This is managed through consultation with the Group's legal counsel and external counsel to ensure that legal advice is appropriately taken where necessary.

As part of preparations to comply with Basel II, the Group has started mapping all its business activities to the eight Business Lines as defined by the Basel Committee on Banking Supervision.

Group Compliance

Group Compliance is an independent function that helps to identify, assess and monitor the Bank's compliance risk, that is, the risk of financial or reputational loss arising from failure to comply with all applicable laws, regulations, codes of conduct and standards of good practice relating to the business activities of the Bank. Group Compliance also advises and reports on the Bank's compliance risk.

To fulfill its role, Group Compliance has drawn up policies, guidelines and procedures in line with applicable laws, rules and standards to provide guidance to business units in their day-to-day activities. These include guidelines and procedures for the sale of investment products, opening of accounts and prevention of money laundering and terrorists financing activities. Additional guidelines and procedures are implemented in business units to avoid and mitigate conflicts of interests. Regular training sessions are held to create and heighten staff awareness of applicable laws, rules and standards.

Group Compliance achieves its objectives through a team of dedicated Compliance Officers in key business lines and support units, including the Group's overseas branches and subsidiaries. Overseas compliance officers carry out monitoring programmes in line with the relevant laws, regulations, policies and procedures in their respective countries, and report to the Head of Group Compliance who provides them with support and guidance to perform their tasks.

Group Compliance works closely with business units to manage the Bank's compliance risks.