

1998/99

A n n u a l R e p o r t

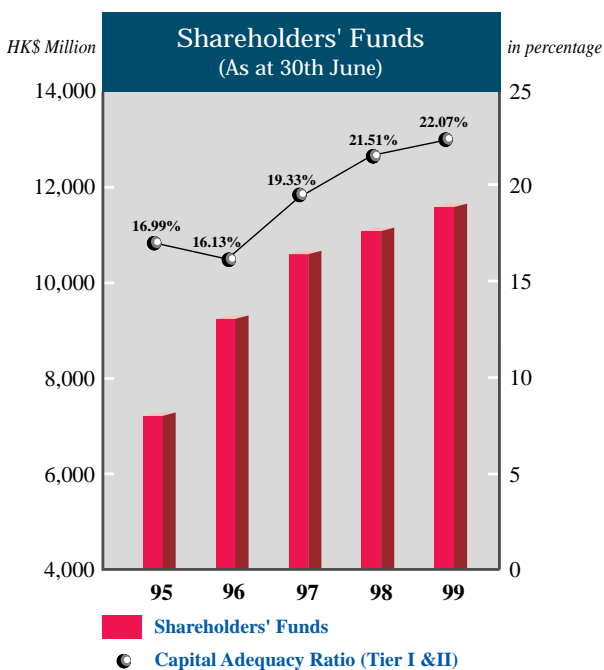


道亨銀行集團有限公司

Dao Heng Bank Group Limited

Financial Highlights

| | 1999 HK\$'M | 1998 HK\$'M | % Change |
|------------------------------------|----------------|----------------|-------------|
| Total Assets | 131,876 | 122,934 | +7.3 |
| Total Deposits | 104,978 | 99,725 | +5.3 |
| Total Advances (net of provisions) | 64,941 | 64,738 | +0.3 |
| Shareholders' Funds | 11,657 | 11,074 | +5.3 |
| Consolidated Net Profit | 1,203 | 1,255 | -4.1 |
| Loan/Deposit Ratio | 61.86% | 64.92% | |
| Return on Average Equity | 10.59% | 11.58% | |
| Return on Average Assets | 0.94% | 1.01% | |



A nighttime photograph of a city skyline, featuring a prominent skyscraper with a spire, illuminated against a dark sky. The city lights and water are visible in the background.

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Corporate Information

BOARD OF DIRECTORS

Quek Leng Chan — Chairman
 Kwek Leng Hai — Managing Director
 Randolph Gordon Sullivan
 Sat Pal Khattar
 Kwek Leng San
 Tung Hsi Hui, Frank
 Mishal Abdulah Abdulaziz Al Masad
 Sir Jack Cater
 Harry Richard Wilkinson
 Jamal Al-Babtain

COMPANY SECRETARY

Doris W.N. Wong
 (E-mail address: doriswong@guoco.com)

AUDITORS

KPMG
 Certified Public Accountants

BRANCH SHARE REGISTRARS

Central Registration Hong Kong Limited
 Shops 1712-6,
 17th Floor, Hopewell Centre,
 183 Queen's Road East, Hong Kong

REGISTERED ADDRESS

Cedar House, 41 Cedar Avenue,
 Hamilton, HM12, Bermuda

PRINCIPAL OFFICE

11th Floor, The Center,
 99 Queen's Road Central,
 Hong Kong
 Telephone: (852) 2218 8899
 Fax: (852) 2285 3899
 Internet address: <http://www.daoheng.com>
 Telex: HX73345

FINANCIAL CALENDAR

| | |
|---|---|
| Interim results announcement | 18th March, 1999 |
| Closure of Register of Members | 7th April, 1999 to 15th April, 1999 |
| Interim dividend of HK\$0.25 per share paid on | 16th April, 1999 |
| Annual results announcement | 6th October, 1999 |
| Closure of Register of Members | 8th November, 1999 to 12th November, 1999 |
| Annual General Meeting | 12th November, 1999 |
| Final dividend of HK\$0.65 per share payable on | 15th November, 1999 |



Biographical Details of Directors and Senior Management

BOARD OF DIRECTORS

Quek Leng Chan, aged 56, is the Executive Chairman of Dao Heng Bank Group Limited (“the Company”). He is the Chairman of Guoco Group Limited (“Guoco”- the Company’s holding company), Guoco Land Limited (“Guoco Land”), Dao Heng Bank Limited (“DHB”) and Overseas Trust Bank, Limited (“OTB”). He is also the Executive Chairman of the Hong Leong Group Malaysia. Mr. Quek has a law degree and has extensive business experience in various business sectors, including financial services, manufacturing and real estate. He has been the Chairman of the Guoco Group and DHB since 1982. Mr. Quek is a Director of Guoline Overseas Limited (“GOL”), a substantial shareholder of Guoco. He is a brother of Mr. Kwek Leng Hai and Mr. Kwek Leng San.

Kwek Leng Hai, aged 46, is the Managing Director of the Company and the President and Chief Executive of Guoco. He is also the Chief Executive of DHB and OTB. Mr. Kwek is a qualified chartered accountant. Prior to joining DHB in 1985, he was the Managing Director of Hong Leong Industries Berhad. Mr. Kwek has extensive experience in financial services, manufacturing and property investment. Mr. Kwek is a Director of GOL, a substantial shareholder of Guoco. He is a brother of Mr. Quek Leng Chan and Mr. Kwek Leng San.

Randolph Gordon Sullivan, aged 51, is a Director of the Company and Guoco. He is also the Managing Director and Alternate Chief Executive of DHB and OTB. Mr. Sullivan holds a bachelor of science degree in foreign service from Georgetown University and has done post-graduate work at the Insead executive programme in Fontainebleau, France. He has over 27 years of banking experience. Prior to joining DHB in 1987, he had worked in a major international bank for 16 years and held various positions in North America, Europe and the Middle East. He has been appointed as a member of the Deposit-Taking Companies Advisory Committee since June 1997.

Sat Pal Khattar*, aged 56, is a Director of the Company, Guoco, Guoco Land, DHB and OTB. Mr. Khattar obtained a LLM degree and a LLB(Hons) degree from the University of Singapore. He is a senior partner of Khattar Wong & Partners in Singapore. He is also the Chairman of First Capital Corporation Ltd (“FCC”), a subsidiary of Guoco, in Singapore and other public and private companies in Singapore and elsewhere.

Kwek Leng San*, aged 44, is a Director of the Company, Guoco, DHB and OTB. He is the President and Chief Executive Officer of Hong Leong Industries Berhad, a member of the Hong Leong Group Malaysia. He holds a bachelor of science degree in engineering and a master of science degree in finance. Mr. Kwek is a Director of GOL, a substantial shareholder of Guoco. He is a brother of Mr. Quek Leng Chan and Mr. Kwek Leng Hai.

Tung Hsi Hui, Frank*, aged 78, is a Director of the Company, DHB and OTB. Mr. Tung obtained a bachelor of arts degree from St. John’s University in Shanghai, China in 1945. He has 52 years of banking experience in Hong Kong and is presently the business adviser to DHB.

Biographical Details of Directors and Senior Management

BOARD OF DIRECTORS (CONT'D)

Mishal Abdulah Abdulaziz Al Masad*, aged 41, is a Director of the Company, Guoco, DHB and OTB. He is a Senior Investment Manager of Kuwait Investment Office, London. He holds an associate student certificate in business studies and a bachelor of arts degree in economics. He has been a Director of Guoco since 1986.

Sir Jack Cater*, aged 77, is a Director of the Company and DHB. He held various senior positions with the Hong Kong Government and was the first Commissioner of the Independent Commission Against Corruption and the Chief Secretary of Hong Kong during the 1970's. He was the Acting Governor and Deputy Governor on several occasions and was also a member of the Legislative Council and the Executive Council. Sir Jack Cater is also a director of ABN AMRO Asia Limited and Television Broadcast Limited.

Harry Richard Wilkinson*, aged 56, is a Director of the Company, Guoco and DHB. He is also a Director and Chief Financial Officer of Orient Overseas (International) Limited. Mr. Wilkinson was previously Managing Director and Regional Manager of Chemical Bank for Hong Kong, China and Taiwan and has considerable experience in shipping and banking. His career began at Manufacturers Hanover Trust Company in New York in 1975, where he held various positions. Manufacturers Hanover Trust Company was the predecessor of Chemical Bank, which was absorbed by merger in 1992. Mr. Wilkinson was a US Navy Officer for five years and was awarded three Military awards. He holds three master degrees from Horace H Rackham School of Graduate Studies, The University of Michigan at Ann Arbor. He was previously on the Banking Advisory Committee to the Government and is currently on the Visiting Committee of the University of Michigan Business School.

Jamal Al-Babtain*, aged 37, is a Director of the Company, Guoco, FCC, Overseas Union Bank Ltd and Grupo Torras SA, Madrid. He is a Vice President of Kuwait Investment Office, London. He holds a bachelor of arts degree in business administration. He has been a Director of Guoco since 1998.

* *Non-executive Director*

Biographical Details of Directors and Senior Management

SENIOR MANAGEMENT

Leung Kin Hee, aged 51, is an Executive Director of DHB and is responsible for Dao Heng Bank Group's Credit and Risk Management activities. He has a BBA degree and a MBA degree from the Chinese University of Hong Kong and joined DHB in 1973.

Wilson C. Wong, aged 50, is the General Manager of the Commercial and Corporate Banking Division of DHB. He has a bachelor degree in business administration with over 31 years of banking experience. Prior to joining DHB in 1990, he had worked with three international banks in Hong Kong for over 22 years.

Tam Ping Shing, aged 43, is the General Manager of the Dao Heng Markets Division of DHB. He obtained a B.Soc.Sc.(Hons) degree from the University of Hong Kong in 1979 and has over 20 years of experience in global treasury business with major international banks. He was the president of the HK Forex Association from 1992-1996.

Loretta Liu Lee Kai Fong, aged 53, is the General Manager of the Personal Banking Division of DHB. She holds a bachelor of arts degree. She has 26 years of banking experience and joined DHB in 1991.

Paul Wong Hok Leung, aged 46, is the General Manager of the Mortgage Banking Division of DHB. He holds a bachelor of science degree and is a fellow member of the Association of Chartered Certified Accountants. He has over 22 years of experience in banking, accounting, finance and information technology.

Lincoln Lee Yuk Ling, aged 49, is the General Manager of Dao Heng Card Centre. He holds a master degree in business administration and is a fellow member of the Chartered Institute of Management Accountants and the Hong Kong Institute of Company Secretaries, and an associate member of the Hong Kong Society of Accountants. He has over 22 years of experience in banking and has 11 years of service with DHB. Prior to joining DHB, he had worked with a major international bank for 11 years.

Frederick Ho Fat Chuen, aged 48, is the General Manager of Dao Heng Finance Limited. He has a diploma in management studies and has over 21 years of experience in management of project investment and finance. He joined DHB in 1989.

Steve Wong Ho Sing, aged 46, is the Controller, Finance and Operations Division of DHB. He is a fellow member of the Association of Chartered Certified Accountants and the Hong Kong Society of Accountants. He is also an associate member of the Hong Kong Institute of Company Secretaries. He has over 22 years of experience in banking.



Chairman's Statement

On behalf of the Board of Directors, I am pleased to present the Annual Report and Accounts of Dao Heng Bank Group Limited ("the Group") for the year ended 30th June, 1999.

Hong Kong's recession intensified during 1998, registering negative 5.1% growth for the full year. During the first half of 1999 the trend began to improve, with a 3.1% decline in real GDP for the first quarter and a small 0.7% increase during the second quarter. Unemployment has levelled at 6.1% and deflation is currently running at minus 4.0% year-on-year, resulting in a real interest rate of 12% versus 5% one year ago. Consumer confidence and retail spending, while above their lows, continue to be depressed.

The banking industry is experiencing rising levels of problem loans with the consequent need to make additional loan loss provisions. While it is possible that loan provisioning will peak by year end 1999, reinvigorated loan demand will probably not be seen until well into the year 2000. Hence growth in the banking sector is anticipated to continue to be constrained for another six to twelve months.

On a more positive note, nominal interest rates have been quite stable since late 1998, and the HK Dollar/US Dollar exchange rate has likewise been well managed by the Hong Kong Monetary Authority ("HKMA") in its gradual climb to 7.80. There has also been a remarkable recovery of Hong Kong's stock market, which recovered from a low of 6,660 in the Hang Seng Index in August 1998 to 13,534 as of 30th June, 1999.

The Group continued to maintain its defensive posture in terms of liquidity and credit exposure, which has been the case since the outbreak of the Asian financial turmoil more than two years ago. In view of declining asset quality, the Group's loan portfolio was maintained at last year's level, although there was a meaningful shift in the loan mix as consumer loans grew 25.5% while commercial and corporate lending declined by 18.8%. Customer deposits, moreover, showed a healthy growth of 8.9% as interest rates stabilized at sustainable levels following the HKMA's actions to enhance liquidity and restore order in the domestic financial markets in the latter part of 1998.

The Group reported consolidated profit attributable to shareholders of HK\$1,203.3 million, a 4.1% decrease from the previous year. Earnings per share declined 3.3% to HK\$1.74 per share. Total assets increased 7.3% to HK\$131.9 billion and shareholders' funds continued to expand to HK\$11.7 billion, a 5.3% increase. As a consequence, the bank's capital adequacy ratio has strengthened further to 22.1%.

The Directors will recommend at the forthcoming Annual General Meeting for approval by shareholders the payment of a final dividend of HK\$0.65 per share, which is the same as last year. Together with the interim dividend of HK\$0.25 paid during the year, the aggregate dividend will be HK\$0.90 per share totalling HK\$624 million, which is approximately the same as last year's level.

The small drop in net profit was due entirely to higher loan loss provisions, reflecting widespread deterioration in the Hong Kong and regional economies. Most of the other key operating indicators of the Group reflected modest improvement over the prior fiscal year. Net interest income grew 4% and other operating income expanded by an impressive 18% which, when contrasted to a slight decline in operating expenses, combined to register a healthy 13.6% growth in operating profit.

Chairman's Statement

Active management of the Group's credit portfolio continues to be a critical success factor in the present weak phase of the credit cycle. Non-performing and past due loans have increased to 4.06% and 3.81% respectively of total loans, and restructured loans now account for 1.60% of our loan portfolio. Provisions made during the year for bad and doubtful loans and advances grew 60.17% to HK\$857 million, all of which was applied to specific provisions and loan write-offs. In addition, HK\$59 million in general provisions were transferred to specific provisions. As at 30th June, 1999, the Group's unallocated general loan loss provisions stood at HK\$816 million or 1.23% of total gross loans, well above the Group's target level of 1%.

The Group continues to carefully control its cross-border exposure to other Asian countries, in particular to those countries located in Southeast Asia. Approximately 96% of the Group's consolidated total loans were extended to customers in Hong Kong. The quality of PRC related credits continues to deteriorate, though it is believed the majority of Mainland China borrowers now experiencing difficulties will be able to work with their creditors to safeguard their financial viability. While we expect that additional provisions may be necessary for this sector, the Group's relatively small scale of exposure at less than 1% of total assets limits our vulnerability.

The Group continues to reshape its domestic branch operations to better serve its customers through a wide range of delivery channels. Presently we operate three consumer relationship segments, namely Personal Banking, Premier Banking and Global Private Banking, which are complemented by two consumer product segments, namely Mortgage Banking and Credit Card. Personal Banking Division manages our extensive domestic branch network, as well as numerous offsite ATMs and several high tech automated banking centres. The Premier Banking and Global Private Banking Divisions further differentiate our product and service offerings to meet diverse client needs and preferences.

A new Mortgage Banking Division has recently been established to enable the Group to excel in the delivery of our most important consumer loan product. The industry leading telemarketing capabilities of our Mortgage Direct call centre are also now being applied to other important consumer products such as insurance and share trading. Dao Heng Card was launched in January 1999 as the successor to our OTB Card product and is rapidly gaining prominence as one of the market's most successful brands.

In order to provide our business banking customers with a seamless transition in meeting their changing financial service needs as they grow and evolve, our Commercial and Corporate Banking Divisions are now being merged into two centralized units, one on Hong Kong Island and the other in Kowloon. In addition a new Trade Finance and Corporate Services Division is being established to reinvigorate these important products and services for our commercial and corporate clients.

The Group's treasury related activities under the leadership of its Dao Heng Markets Division achieved outstanding results, with major contributions coming from trading and investment income as Dao Heng Markets capitalized on wider business aspects than the normal interest rate movements in the Hong Kong Dollar market. Dao Heng Markets' role as one of the most active market makers in Hong Kong Dollar instruments was affirmed with the successful launch of a new "Dao Heng Government Bonds Master Index", which has rapidly become the benchmark for measuring performance in Hong Kong Government fixed income securities.

Chairman's Statement

The Group continues to maintain five offices in Mainland China, and one office each in Macau and Taipei. New business activity however continues to be subdued as a cautious approach to new lending mitigates against rapid asset growth in the present economic environment. In London we have recently relocated our West End Branch to a more prominent site in Chinatown to better serve our customers there. In order to focus more closely its resources on core markets, the sale of Colombo Branch to a group of prominent Sri Lankan and international investors took place in June 1999. The 60% owned subsidiary in the Philippines, Dao Heng Bank, Inc. ("DHBI"), completed its third year of operations in January 1999. DHBI presently operates 15 branches in the country and is focusing on a consumer banking strategy closely aligned with that of its parent bank in Hong Kong.

Hong Kong and its banking industry continue to experience difficult operating conditions with muted demand for banking services, rising individual and corporate delinquencies, weak external trade, and high real interest rates. Recent economic indicators, however, are beginning to signal that Hong Kong may have started to emerge from the recessionary cycle.

I believe Dao Heng Bank Group has a sound corporate strategy and its investment in new technologies is enhancing Group competitiveness. Despite higher charges for loan loss provisions, the underlying core operating profitability of the Group is improving, and the capital base remains solid. While a rapid recovery in Hong Kong's economy is not expected, the signs are increasingly positive that the worst period of the recession is behind us. As such the Group is cautiously optimistic that the current fiscal year will see a modest improvement in business conditions.

In closing, I would like to thank our customers for their loyalty, our shareholders for their support, and the Board of Directors for its wise counsel. Finally, I thank the Group's management and staff for their dedication and commitment to the Group during this challenging operating environment.

Quek Leng Chan

Chairman

Hong Kong, 6th October, 1999



Operational Review

I. FINANCIAL HIGHLIGHTS

Results

The consolidated net profit of the Group for the 1998/99 fiscal year ended 30th June, 1999, after minority interests, provisions for doubtful loans, depreciation and taxation amounted to HK\$1,203.3 million, a decline of 4.1% from the previous fiscal year. Earnings per share were HK\$1.74.

The consolidated financial highlights of the Dao Heng Bank Group are shown below:

| | As at 30.6.99 (HK\$ million) | As at 30.6.98 | Percentage Change |
|------------------------------------|------------------------------------|------------------|----------------------|
| Total Assets | 131,876 | 122,934 | +7.3 |
| Total Deposits | 104,978 | 99,725 | +5.3 |
| Total Advances (net of provisions) | 64,941 | 64,738 | +0.3 |
| Shareholders' Funds | 11,657 | 11,074 | +5.3 |
| Consolidated Net Profit | 1,203 | 1,255 | -4.1 |
| Loan/Deposit Ratio | 61.86% | 64.92% | |
| Return on Average Equity | 10.59% | 11.58% | |
| Return on Average Assets | 0.94% | 1.01% | |

II. REVIEW OF ACTIVITIES

1999 began with a continuation of the recessionary economic environment in the first quarter of the year, although the rate of negative growth was lower at -3.1% compared to -5.1% for all of 1998. However the second quarter of 1999 managed to record a small positive increase in GDP of 0.7%. Unemployment has levelled off at 6.1% and deflation is currently running at -4.0% year-on-year, resulting in a real interest rate of 12% versus 5% one year ago. Consumer confidence and consumer spending, while above their lows, continue to be depressed.

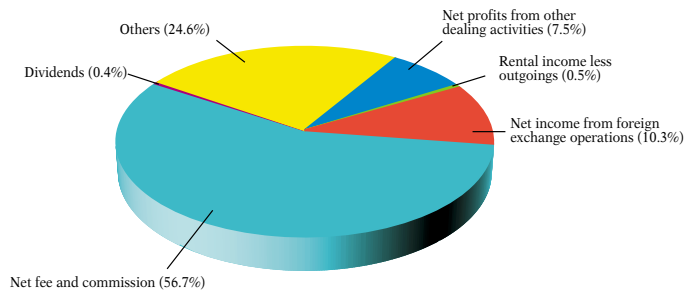
Operational Review

The banking industry is experiencing rising levels of problem loans with the consequent need to make additional loan loss provisions. While it is possible that loan provisioning will peak by year end 1999, reinvigorated loan demand will probably not be seen until well into the year 2000. Hence, growth in the banking sector is anticipated to continue to be constrained for another six to twelve months.

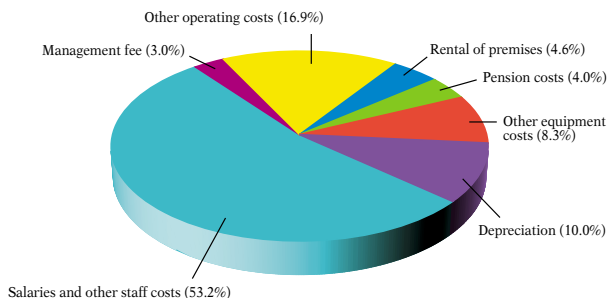
On a more positive note, nominal interest rates have been quite stable since late 1998, and the HK Dollar/US Dollar exchange rate has likewise been well managed by the Hong Kong Monetary Authority in its gradual climb to 7.80. There has also been a remarkable recovery of Hong Kong's stock market, which recovered from a low of 6,660 in the Hang Seng Index in August 1998 to 13,534 as of 30th June, 1999.

III. FINANCIAL REVIEW

Other operating income (HK\$ 1,020 million)
For the year ended 30th June, 1999



Operating expenses (HK\$ 1,472 million)
For the year ended 30th June, 1999



Operating Results

Net interest income increased by 4.0%, primarily due to a more favourable HK Dollar Prime-Hibor spread during the second half of the fiscal year. As a result, the net interest margin improved 10 basis points to 2.38%. Moreover, a strong performance in other operating income, which grew 17.9% to HK\$1,020 million, was recorded.

The growth in non-interest income was due to the one time gain of HK\$181 million reported in our first half results combined with a large contribution of HK\$77 million from trading income compared to HK\$30 million in the prior year. With total operating expenses at a slightly lower level than

Operational Review

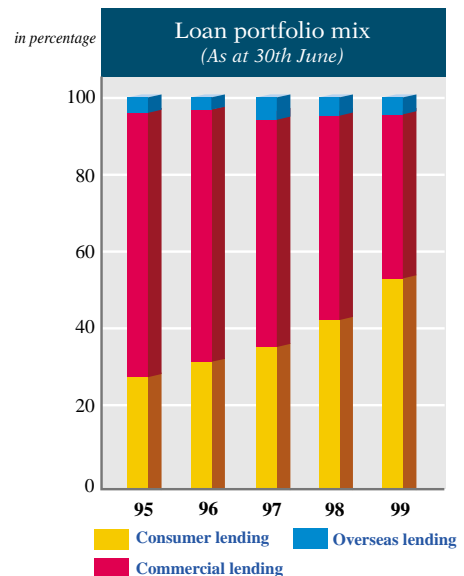
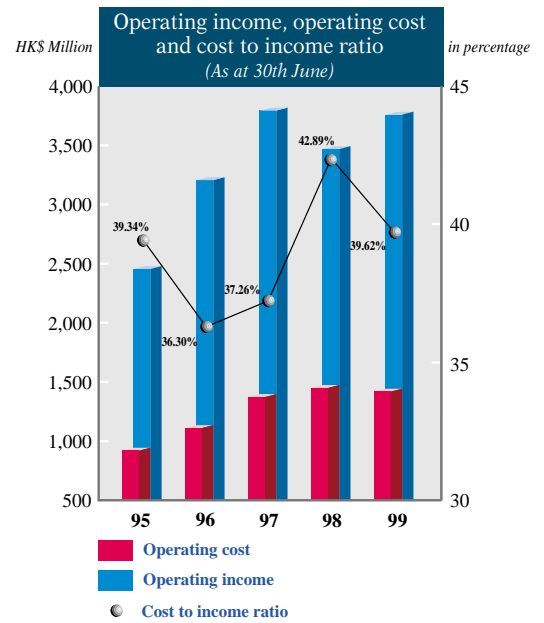
last year, operating profit before provisions registered a healthy increase of 13.6%. The cost to income ratio improved to 39.6% from 42.9% in the previous fiscal year.

The Group has adopted the new Statement of Standard Accounting Practice 24 “Accounting for Investments in Securities” issued by the Hong Kong Society of Accountants with effect from 1st July, 1998 which resulted in a change of accounting policy in respect of treasury bills, certificates of deposit, and securities held for dealing and investment purposes. Debt securities which are intended to be held to maturity are accounted for as held to maturity securities. Other securities are accounted for using the benchmark treatment.

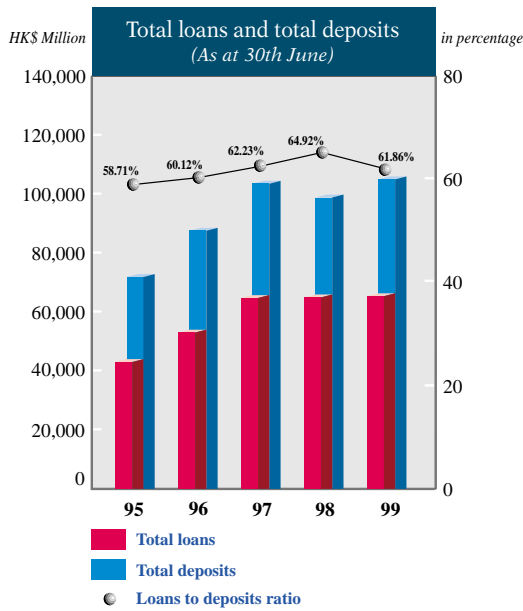
This change in accounting policy was applied retrospectively in the financial year 1997/98. As the amount of resulting adjustments relating to periods prior to 1st July, 1997 is immaterial, the opening retained earnings for 1997/98 were not restated. The effect of the change of the accounting policy was to decrease net profit by HK\$20.5 million for the year ended 30th June, 1998. The opening retained earnings for 1998/99 were restated by the same amount accordingly. The net profit for the year ended 30th June, 1999 was increased by HK\$14.5 million. Comparative figures for the year ended 30th June, 1998 were restated to reflect the change in accounting policy.

Balance Sheet Structure

As at 30th June, 1999, total deposits were HK\$105 billion, reflecting a growth rate of 5.3% from the previous year. Total loans grew 0.3% to HK\$64.9 billion, resulting from slack demand for new credit and our more judicious risk appetite. Although there was minimal overall loan growth, a meaningful shift in the loan mix was evident as consumer loans grew 25.5% while commercial and corporate lending declined by 18.8%. The Group’s loans to deposits ratio of 61.9% and loans to assets ratio of 49.2% were deliberately managed at such conservative levels to ensure that the



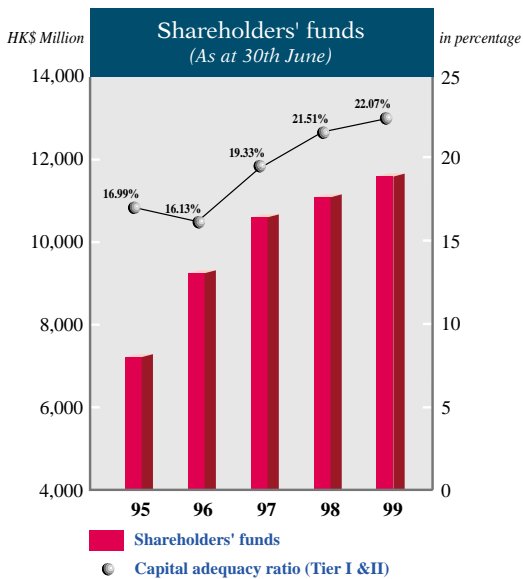
Operational Review



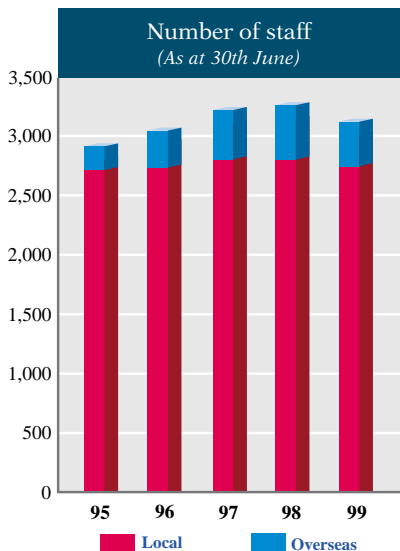
Group would not be overly exposed to declining loan quality at the current stage of the credit cycle.

Shareholders' funds increased 5.3% to HK\$11.7 billion, with Dao Heng Bank Limited's consolidated capital adequacy ratio at a solid 22.07% (of which the Tier I ratio was 16.99%). The Group continued to exhibit a highly liquid balance sheet, with 44.7% of total assets held in the form of government securities, interbank placements, and negotiable securities.

Asset Quality



The Group experienced increased problem loans in its trade finance, corporate, taxi, PRC and credit card portfolios. Non-accrual loans and loans overdue for more than 90 days increased to 4.06% and 3.81% of total loans respectively due to the impact of a weak Hong Kong economy on a broad cross-section of our customer base. Our residential mortgage portfolio continues to perform acceptably, with overdues greater than 90 days representing 0.95% of the portfolio as of the reporting date.



Rescheduled loans accounted for 1.60% of total loans, which reflects our efforts to work with customers whose business remains viable to help them overcome the negative impact of the recession. Provisions made during the year for bad and doubtful loans and advances grew 60.17% to HK\$857 million, all of which was applied to specific provisions and loan write-offs. In addition, HK\$59 million in general provisions were transferred to specific provisions. As at 30th June, 1999, the Group's unallocated general loan loss provisions stood at HK\$816 million or 1.23% of total gross loans, well above the Group's target level of 1%.

Operational Review

The quality of PRC related credits continues to deteriorate, though it is believed the majority of PRC borrowers now experiencing difficulties will be able to work with their creditors to safeguard their financial viability. While we expect that additional provisions may be necessary for this sector, our Group's relatively small scale of exposure at less than 1% of total assets limits our vulnerability.

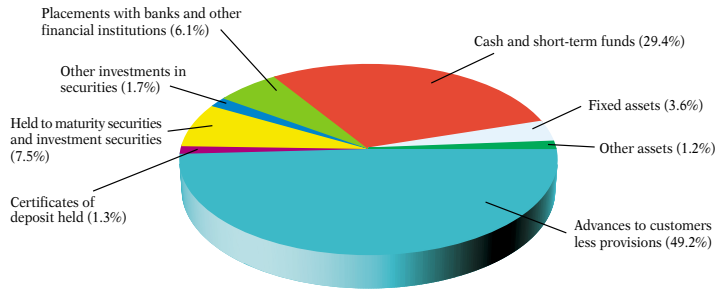
IV. BUSINESS REVIEW

Consumer Banking

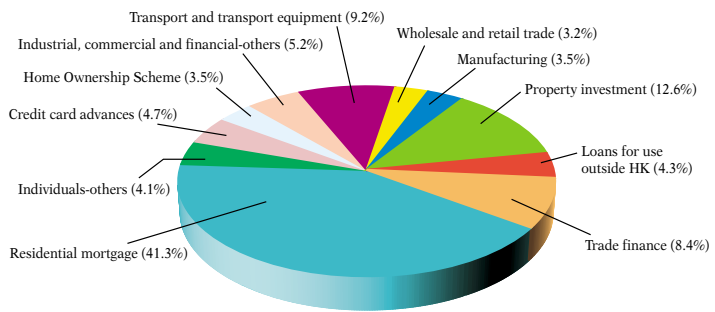
To better serve our customers and position our Group for the rapidly evolving financial services industry, we continue to develop our organizational structure to reflect global best practice. Presently we operate three consumer relationship segments, namely Personal Banking, Premier Banking and Global Private Banking, which are complemented by two consumer product segments, namely Mortgage Banking and Credit Card.

Personal Banking Division manages our extensive domestic branch network, as well as a range of offsite ATMs and several high tech automated banking centres. Personal Banking initiatives now underway include implementing

Analysis of total assets
As at 30th June, 1999 (HK\$131,876 million)



Analysis of advances to customers by industry sectors
As at 30th June, 1999 (HK\$66,423 million)



"The New Generation Easy Saver Plan" helps customers attain their goals.

Operational Review

a more customer friendly and sales oriented branch layout, which encourages cross-selling a wide variety of consumer banking products.

Dao Heng Bank Group is committed to providing our customers with a full range of delivery channel alternatives to facilitate convenient access “anytime, anywhere”. Our latest new service, the first of its kind by a bank in Hong Kong, is mobile phone banking and share trading. Using new SIM card mobile phone technology, our customers can



Special counters are set to promote the Bank's mortgage business.



The telemarketing capabilities are applied to important customer products such as insurance and share trading.



The new Total Payroll service provides SMEs with a comprehensive salary management service and MPF opportunities for the Bank.



The Dao Heng Direct Club offers customers quality financial and insurance services.

Operational Review



The Global Private Banking team is committed to meet the personal needs of customers.



The Premier Banking Center team and the new Dao Heng Premier Card.

now perform a wide variety of menu-driven financial transactions on their mobile phone screen including a sophisticated price-alert capability for monitoring their stock market transactions.

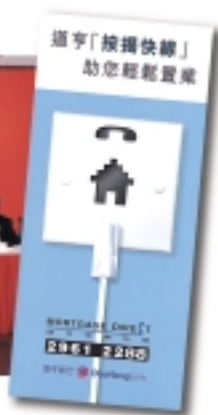
The Premier Banking and Global Private Banking Divisions further differentiate our product and service offerings to meet diverse client needs and preferences. The customized service that these divisions offer enable our Group to better satisfy the increasing demand for personalized financial service products among Hong Kong's more affluent customer segments.

A new Mortgage Banking Division has recently been established to enable our Group to excel in the delivery of our most important consumer loan product. Based on state of the art call centre

technology, and an advanced product development and loan fulfilment capability, the Mortgage Banking Division will enable us to be the low cost provider in our marketplace. The industry leading telemarketing capabilities of our Mortgage Direct call centre are also now being applied to other important consumer products such as insurance and share trading.



Dao Heng Bank Group participated in the Mortgage Insurance Programme introduced by the Hong Kong Mortgage Corporation Limited.



Operational Review



Dao Heng Card was launched as the successor to our OTB Card products.



Dao Heng Card was launched in January 1999 as the successor to our OTB Card product and is rapidly gaining acceptance as one of the market's most successful brands. During the past year several I.T. based systems have been introduced or upgraded to position our Credit Card Division for an anticipated surge in growth once consumer confidence in Hong Kong improves. Among our new product capabilities is the introduction of S.E.T. technology to assure the security of our customer's internet based transactions.

Commercial and Corporate Banking

Demand for commercial loans was weak during the past year as Hong Kong's economy was in the midst of a deflationary environment exacerbated by high real interest rates. Most of our Group's problem loans emanated from this sector, with particularly challenging operating conditions in the taxi lending business of Dao Heng Finance.

The Group is taking advantage of the present slow market to accelerate the restructuring of its Commercial Banking Division to enable us to offer a wide range of business banking products in a more professional, productive and profitable manner. In order to provide our business banking customers with a seamless transition in meeting their changing financial



Dao Heng's Commercial and Corporate Banking Division provides a wide range of banking services to institutional customers.

Operational Review

service needs as they grow and evolve, our Commercial and Corporate Banking Divisions are now being merged into two centralized units, one on Hong Kong Island and the other in Kowloon. In addition, a new Trade Finance and Corporate Services Division is being established to reinvigorate these important products and services for our commercial and corporate clients.

Dao Heng Markets

The Group's treasury related activities under the leadership of its Dao Heng Markets Division achieved outstanding results, particularly during the first half of the fiscal year. The largest contributions came from trading and investment income as Dao Heng Markets capitalized on interest rate volatility in the Hong Kong Dollar market. Dao Heng Markets' role as one



Dao Heng Markets was appointed by the Hong Kong Mortgage Corporation Limited as one of five Primary Dealers for its HK\$20 billion Debt Issuance Programme.



The Dao Heng Markets dealing centre was honored with a visit by the senior executives of the Hong Kong Monetary Authority.

Operational Review



The Foreign Exchange "Flexi-Point" promotion programme was well received.



Dao Heng Markets launched a series of new products to penetrate the retail banking sector.



Executives of the Bank were invited to attend the opening ceremony of the London office of the Hong Kong Monetary Authority on 28th September, 1999.

of the most active market makers in Hong Kong Dollar instruments was affirmed with the successful launch of a new "Dao Heng Government Bonds Master Index", which has rapidly become the benchmark for measuring performance in Hong Kong Government fixed income securities. Another major initiative was the promotion of Dao Heng's new concept to retailize selected institutional instruments in both US and HK Dollars to our premier and private banking customer base. Dao Heng Markets also continues to be one of the largest arrangers and issuers of Hong Kong Dollar denominated instruments.



Dao Heng Markets retailizes Dao Heng Bank's Yankee Bonds.

International Banking

Our Group continues to maintain five offices in Mainland China, and one office each in Macau and Taipei. New business activity however continues to be subdued as a cautious approach to new lending



The new branch in the heart of London's Chinatown delivers quality products and services to our customers whilst raising the Group's profile in the U.K.

Operational Review

mitigates against rapid asset growth in the present economic environment. In London we have recently relocated our West End Branch to a more prominent site in Chinatown to better serve our customers there. In order to focus more closely its resources on core markets, the sale of our Colombo Branch to a group of prominent Sri Lankan and international investors took place in June 1999.

Our 60% owned subsidiary in the Philippines, Dao Heng Bank, Inc. (“DHBI”), completed its third year of operations in January 1999. Although new business activities have been constrained due to the continuing impact of the Asian financial turmoil, DHBI continues to invest in the necessary infrastructure to ensure our ability to take advantage of opportunities that are expected to present themselves once the Philippine economy emerges from the current sluggish business conditions. DHBI presently operates 15 branches in the country and is focusing on a consumer banking strategy closely aligned with that of its parent bank in Hong Kong.



Dao Heng Bank, Inc. launched an inspiring multi-media advertising campaign in the Philippines during the year.

Information Technology and Operations Support

Dao Heng Bank Group’s policy is to benchmark itself against global best practice in the financial services industry to ensure the Group’s long term competitiveness. To this end, Dao Heng has stepped up its investment in information technology in spite of the relatively weak economic environment during the past year. This increased I.T. investment is supporting both the development of new delivery channels as well as providing enhanced new product capabilities for our customers.

In parallel with the introduction of new automated systems, the Group continues to centralize numerous operational activities that were formerly handled in our personal banking branches, thereby offering enhanced efficiency for our customers while providing them with more value-added and personalized services at the branch level.

Year 2000 Project

Many computer systems and other electronic devices (with embedded chips) use two digits rather than four to represent specific years. Unless corrected, this problem could cause system failure

Operational Review

or malfunction, resulting in possible disruption to business operations on or beyond the first day of the year 2000.

Through a designated team, the Group has completed the validation and implementation of its mission critical systems (including hardware and software) for Year 2000

compliance, meaning that these systems should perform, function and manage data involving dates without being abnormally affected by dates spanning the period prior to, during and after the year 2000. Progress of such activities has been regularly reported to Senior Management and the Board of Directors.

While its internal systems have been addressed, the Group's business operations may also be disrupted by the non-compliance of other entities such as suppliers, business partners, creditors, borrowers and customers.

Therefore, the Group has now obtained compliant certification from its major counterparties. In addition, it has performed testing and validation of all significant external interfaces with relevant counterparties and participated (more than once in some cases) in industry-wide testing activities applicable to its business. However, there is no way to prevent a failure of the systems of other companies, on which the Group's business transactions rely, from having an adverse effect on the Group. A comprehensive Year 2000 contingency plan has also been established which calls for various action teams to be mobilized, either on-site or standby on a 24 hour non-stop basis, prior to and during any critical dates to:

1. Print all ledger/customer account balances prior to any critical date.
2. Arrange for extra cash and liquid funding, for the period prior to, during and after the turn of the Century, to satisfy a likely increase in customer demand.
3. Verify the functioning of our computer systems (including data communication networks), building facilities, and office equipment as soon as possible on the critical date.



Specially designed pamphlets on the Year 2000 issue are sent to customers.



Operational Review

4. Activate an Event Management (Command) Centre to coordinate, manage and monitor activities being carried out by various action teams.
5. Manage institutional, public and customer relationships in respect of Year 2000 issues.

The contingency plan also includes resumption procedures to recapture manual transactions upon successful repairing of any failed system. In addition, all essential staff will be required to be on duty or standby during any public holidays and certain other times within these critical periods. Testing of this plan had been completed as of 30th June, 1999 and further refinement in accordance with the Hong Kong Monetary Authority's guidelines has been completed as of 30th September, 1999.

The Group has achieved 100% completion on the modification, upgrading and user acceptance testing of its internal computer systems and remaining activities will be the preparation for successful rolling over and contingency planning in respect of major critical dates that may have Year 2000 issues.

The Group has also considered purchasing additional Year 2000 insurance. However, after careful assessment of the scope of insurance cover available, insurance cover already held and its Year 2000 program progress, it has decided not to purchase any such separate insurance protection.

The total Year 2000 project cost for the Group is estimated at approximately HK\$26.1 million, a decrease of HK\$1.2 million from previous estimates. The variance is due to the decision to invest in new replacement systems with expanded functionality, best attributable to business expansion rather than for the sole purpose of Year 2000 compliance. As is usual, the capital expenditure of acquiring improved hardware and software systems will be capitalized as fixed assets while other project costs will be expensed as incurred. Up to the period ended 30th June, 1999, the Group has incurred approximately HK\$20.8 million in capital expenditure and HK\$3.3 million in expenses. As at 30th June, 1999, HK\$0.2 million has been contracted but not provided for in the accounts. The Group expects a further amount of HK\$1.8 million will be spent to complete its Year 2000 project.

Operational Review

Community Services

As part of our commitment to the community, for many years the Group has always strongly supported the fund-raising campaigns organized by various charitable organizations, such as Oxfam, The Community Chest, Tung Wah Group of Hospitals and Pok Oi Hospital. In addition, the Group's Sport and Social Club regularly organises visits to the elderly and the needy.



The Group is committed to caring for the community and will continue its efforts to support charity events in Hong Kong.

Human Resources

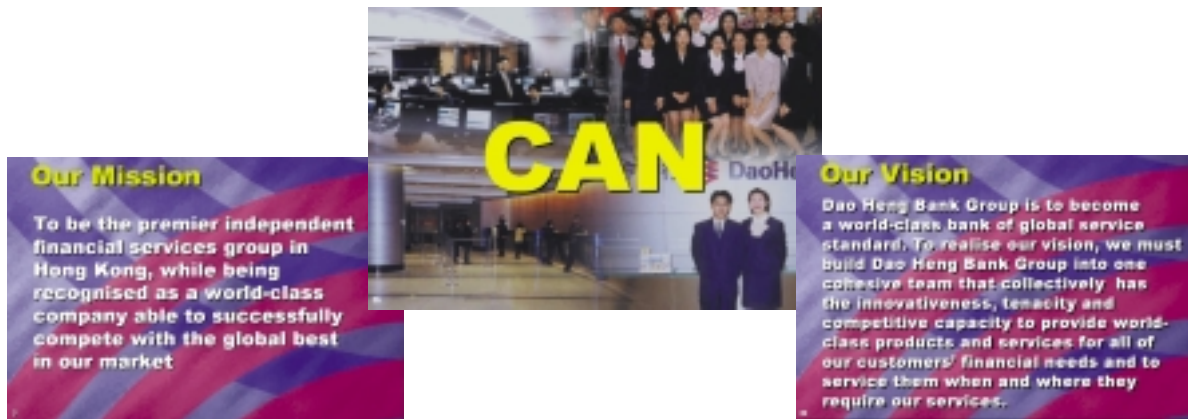
The Group offers in-house and external training courses to its staff members. Training programmes are tailor made to align with the business activities and strategic direction of the Group. Intensive training has been given to over 400 staff members to prepare them for the examination regarding the Mandatory Provident Fund Scheme which will be launched next year.

The Group held a Sales Conference in August. The Group's vision and mission together with a revamped corporate structure were cascaded to the senior executives. In parallel with the introduction of new automated systems, the Group continues to centralize numerous operational



Over 300 senior executives participated in the Annual Sales Conference.

Operational Review



The Group's vision and mission were shared with the participants at the Annual Sales Conference.


activities that were formerly handled in our personal banking branches, thereby offering enhanced efficiency for our customers while providing them with more value-added and personalized services at the branch level.

V. OUTLOOK


Hong Kong and its banking industry continue to experience difficult operating conditions with muted demand for banking services, rising individual and corporate delinquencies, weak external trade, and high real interest rates. Recent economic indicators, however, are beginning to signal that Hong Kong may have started to emerge from the recessionary cycle. Most crucial was positive real GDP growth of 0.7% during the second quarter of 1999. Other signs are a stable unemployment rate, rising equity prices, and a modest rebound in retail sales.

We believe the Dao Heng Bank Group will emerge from the current difficulties as a more productive and stronger organization. Our corporate strategy is sound and our investment in new technologies is enhancing our Group's competitiveness. Despite significantly higher charges for loan loss provisions, the underlying core operating profitability of our Group is improving, and our capital base remains solid. While a rapid recovery in Hong Kong's economy is not expected, the signs are increasingly positive that the worst period of the recession is behind us. As such our Group is cautiously optimistic that the current fiscal year will see a modest improvement in business conditions.

Dao Heng Bank Group is entering into a new era

•  We have enhanced our presence in the community by moving into our new home at The Center.




•  We have created a new model for our branch network with the opening of our Main Branch at The Center.

"A Symbol for a New Era"




Our new corporate logo embodies the traditional character and culture of our Group while at the same time its contemporary and dynamic design projects the modern image of the Group as it moves into the 21st Century with new technology and revitalised programmes. The bold and elegant graphics of the logo represents the coming together of the Group's various business divisions moving forward to serve our customers more effectively and simultaneously symbolises the Group's corporate motto of "Reaching Out To You" with our assurance of quality products and services as we advance on the "Road To Prosperity".

•  We have designed and implemented a new logo. It symbolizes our preparedness for the next phase of our growth.



•  We have launched the new "Dao Heng Credit Card" which was positioned as the first "Dao Heng" brand name credit card.

-  We have achieved good growth in the mortgage sector.


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- 15分鐘批核貸款
- 24小時法律顧問服務
- \$4,800律師費優惠

MORTGAGE DIRECT
2961 2288

EST. 1982 DIRECT A Division Of Dao Heng Bank




-  We have renamed the Treasury Division as Dao Heng Markets to reflect its increasing role in Hong Kong's capital markets. Dao Heng Markets pioneered the "Hong Kong Government Bonds Master Index", and the retailization of capital instruments.




| DH GOVT BONDS MASTER INDEX | TOTAL RETURN INDEX | DAY-5 CHANGE % | AVG CPU % | AVG YIELD % | AVG BAT-YR | AVG SUP-YR |
|----------------------------|--------------------|----------------|-----------|-------------|------------|------------|
| DH GOVT BONDS MASTER INDEX | 187.42 | 8.84 | 7.53 | 6.88 | 3.58 | 2.93 |
| HKER NOTE 2-5 YR INDEX | 183.94 | 0.85 | 7.08 | 6.33 | 2.65 | 2.31 |
| HKER NOTE 1-5 YR INDEX | 186.51 | 0.88 | 7.58 | 7.29 | 6.88 | 5.82 |
| HKRC NOTE INDEX | 185.41 | -8.92 | 7.89 | 6.86 | 3.77 | 1.60 |
| HKTC NOTE INDEX | 185.85 | -8.41 | 8.38 | 6.93 | 2.95 | 1.79 |
| HKR NOTE INDEX | 185.85 | -8.84 | 8.19 | 7.29 | 2.86 | 2.43 |

BASE DATE : 21 DEC 98 BASE VALUE : 100



-  We achieved another first by being the first bank in Hong Kong to launch fully automated Mobile Phone Banking.

-  Dao Heng Bank ("DHB") was the first local bank invited by the World Bank to participate in its supranational issues. In August 1998, DHB was invited to act as senior co-lead manager and market-maker for the World Bank's HK\$1 billion 2-year floating-rate note and HK\$1 billion 2-year fixed-rate note syndication.





Ten Year Summary

HK\$'000

| Years | Total loans | Total deposits and other accounts (Note 4) | Total assets | Shareholders' funds | Net profit after tax (Note 5) |
|-------|-------------|--|--------------|---------------------|-------------------------------|
| 1990 | 7,198,905 | 15,449,001 | 16,295,022 | 789,741 | 151,016 |
| 1991 | 9,416,232 | 17,919,575 | 19,641,593 | 1,648,018 | 232,014 |
| 1992 | 11,667,852 | 23,509,139 | 25,419,953 | 1,808,814 | 320,451 |
| 1993 | 15,722,483 | 29,724,608 | 31,854,378 | 1,949,970 | 400,857 |
| 1994 | 36,137,714 | 59,882,012 | 66,889,359 | 6,016,680 | 1,133,977 |
| 1995 | 42,736,049 | 73,965,778 | 82,213,503 | 7,223,192 | 1,203,113 |
| 1996 | 52,795,266 | 93,628,836 | 103,480,286 | 9,234,417 | 1,505,811 |
| 1997 | 64,546,650 | 111,085,903 | 125,485,256 | 10,600,880 | 2,119,708 |
| 1998 | 64,738,305 | 108,053,498 | 122,934,242 | 11,073,988 | 1,255,314 |
| 1999 | 64,941,463 | 117,015,748 | 131,876,313 | 11,656,833 | 1,203,301 |

Notes:

1. The 1990 figures relate to the Dao Heng Bank Limited group ("DHB group") only, as Dao Heng Bank Group Limited was incorporated on 21st September, 1990 and became the holding company of DHB group pursuant to a Scheme of Arrangement which became effective on 21st January, 1991.
2. The 1991 to 1993 figures relate to the Dao Heng Bank Group Limited group.
3. The 1994 to 1999 figures include Overseas Trust Bank, Limited group.
4. The figures for 1990 to 1994 include the former inner reserves which are restated to general reserve and included under shareholders' funds since 1995.
5. The figures for 1994 to 1999 were before transfer to general reserve while those for 1990 to 1993 were after such transfers.

Financial Section

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Report of the Directors

The directors have pleasure in presenting their report together with the audited statement of accounts for the year ended 30th June, 1999.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. The principal activities of the subsidiaries which materially affected the results or assets of the Group are the provision of commercial and retail banking, deposit-taking, bullion, trustee and nominee services to individuals, commerce, industry and institutions.

Over 90% of the Group's turnover and trading results for the year were attributable to the Group's operations in Hong Kong.

ACCOUNTS

The consolidated profit of the Group for the year ended 30th June, 1999 and the state of affairs of the Company and the Group at that date are set out in the accounts on pages 36 to 72.

MAJOR CUSTOMERS

During the year, the five largest customers of the Group accounted for less than 30% of the total interest income and other operating income of the Group.

CHARITABLE DONATIONS

Donations made by the Group during the year amounted to HK\$714,000 (1998 : HK\$1,345,000).

DIVIDENDS

An interim dividend of HK\$0.25 (1998 : HK\$0.25) per share totalling HK\$173,155,000 (1998 : HK\$174,154,250) was paid on 16th April, 1999. The directors are recommending the payment of a final dividend in respect of the year ended 30th June, 1999 of HK\$0.65 (1998 : HK\$0.65) per share totalling approximately HK\$451,120,000 (1998 : HK\$450,201,700).

CLOSURE OF REGISTER OF MEMBERS

The Register of Members of the Company will be closed from 8th November, 1999 to 12th November, 1999, both days inclusive, during which period no share transfers will be registered.

To qualify for the final dividend, all transfers accompanied by the relevant share certificates must be lodged with the Company's Branch Share Registrars in Hong Kong not later than 4:00 p.m. on 5th November, 1999.

FIXED ASSETS

Movements in fixed assets during the year are set out in Note 21 on the accounts.

SHARE OPTION SCHEME

A Share Option Scheme is maintained by the Company, under which eligible employees (including directors) of the Group are entitled to the grant of share options for subscription of shares in the Company. Details regarding share options granted are set out in Note 26 on the accounts.

Report of the Directors

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SHARES

During the year, the Company purchased a total of 2,394,500 shares out of its issued share capital at an aggregate consideration of HK\$17,091,000 on The Stock Exchange of Hong Kong Limited. The directors considered that the repurchases were beneficial to the Company and its shareholders. Particulars of the aforesaid repurchase are set out in Note 26 on the accounts.

RESERVES

Movements in the reserves of the Company and the Group during the year are set out in Note 27 on the accounts.

SUBSIDIARIES

Particulars of the principal subsidiaries of the Company are set out in Note 18 on the accounts.

DIRECTORS

The directors during the financial year were:-

- Quek Leng Chan - Chairman
- Kwek Leng Hai - Managing Director
- Randolph Gordon Sullivan
- ** Sat Pal Khattar
- * Kwek Leng San
- ** Tung Hsi Hui, Frank
- * Mishal Abdulah Abdulaziz Al Masad
- ** Sir Jack Cater
- ** Harry Richard Wilkinson
- * Jamal Al-Babtain (appointed on 7th April, 1999)
- * *Non-executive director*
- ** *Independent non-executive director*

In accordance with Clause 102(B) of the Company's Bye-Laws, Mr. Jamal Al-Babtain retires from office by rotation at the forthcoming annual general meeting and, being eligible, offers himself for re-election.

In accordance with Clause 99 of the Company's Bye-Laws, Mr. Randolph Gordon Sullivan and Sir Jack Cater retire by rotation at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

None of the directors has a service contract with the Company or any of its subsidiaries which is not determinable by the Company within one year without payment of compensation, other than normal statutory obligations.

The non-executive directors of the Company were not appointed for a specific term but are subject to retirement by rotation at annual general meetings in accordance with the Bye-Laws of the Company.

Report of the Directors

DIRECTORS' INTERESTS IN SECURITIES

As at 30th June, 1999, the interests of the directors in the securities of the Company and its associated corporations (within the meaning of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance")) as recorded in the register maintained under Section 29 of SDI Ordinance or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited pursuant to the Model Code for Securities Transactions by Directors of Listed Companies or as otherwise known to the directors were as follows:

Interests in the shares of the Company

| Director | Personal Interests | Family Interests | Number of shares | | | Total Interests |
|--------------------------|--------------------|------------------|---------------------|-----------------|-------------|-----------------|
| | | | Corporate Interests | Other Interests | | |
| Quek Leng Chan | 11,000 | – | 496,854,664 * | – | 496,865,664 | |
| Kwek Leng Hai | 66,000 | – | – | – | 66,000 | |
| Randolph Gordon Sullivan | 180,000 | – | – | – | 180,000 | |
| Sat Pal Khattar | 11,000 | – | – | – | 11,000 | |
| Kwek Leng San | 7,000 | – | – | – | 7,000 | |
| Tung Hsi Hui, Frank | 5,010 | – | – | – | 5,010 | |

* These shares represented the interest of Guoco Group Limited with respect to which Mr. Quek Leng Chan had a corporate interest pursuant to the SDI Ordinance.

Interests in share options in the Company

| Director | Number of share options |
|--------------------------|-------------------------|
| Quek Leng Chan | 2,000,000 |
| Kwek Leng Hai | 4,000,000 |
| Randolph Gordon Sullivan | 2,000,000 |
| Sat Pal Khattar | 2,000,000 |
| Kwek Leng San | 300,000 |
| Tung Hsi Hui, Frank | 300,000 |
| Harry Richard Wilkinson | 300,000 |

On 29th April, 1998, the directors were granted share options pursuant to the Share Option Scheme adopted on 22nd November, 1993. Such share options are exercisable at the subscription price of HK\$21.82 during the period from 15th April, 1998 to 15th July, 2002. During the year ended 30th June, 1999, none of the directors exercised any share options in the Company.

Report of the Directors

Interests in the securities of associated corporations

| Director | Name of Company | Personal Interests | Family Interests | Number of shares | | Total Interests |
|--------------------------|---|--------------------|------------------|----------------------|----------------|-----------------|
| | | | | Corporate Interests | Other Interest | |
| Quek Leng Chan | Guoco Group Limited | 220,000 | - | 135,005,740 (Note 1) | - | 135,225,740 |
| | First Capital Corporation Ltd | 662,261 | - | 181,128,299 (Note 2) | - | 181,790,560 |
| | Guoco Land Limited | - | - | 184,983,706 (Note 2) | - | 184,983,706 |
| | Guoco Land Limited (Warrants) | - | - | 22,793,281 (Note 2) | - | 22,793,281 |
| | First Capital Corporation Ltd (NCCPS**) | 53,833 | - | 39,483,489 (Note 2) | - | 39,537,322 |
| Kwek Leng Hai | Guoco Group Limited | 1,320,000 | - | - | - | 1,320,000 |
| | First Capital Corporation Ltd | 1,180,261 | - | - | - | 1,180,261 |
| | First Capital Corporation Ltd (NCCPS**) | 53,833 | - | - | - | 53,833 |
| Randolph Gordon Sullivan | Guoco Group Limited | 11,000 | 2,000 | - | - | 13,000 |
| Sat Pal Khattar | Guoco Group Limited | 582,330 | - | - | - | 582,330 |
| | First Capital Corporation Ltd | - | - | 100,000 | - | 100,000 |
| | First Capital Corporation Ltd (NCCPS**) | - | - | 4,494,908 | - | 4,494,908 |
| Kwek Leng San | Guoco Group Limited | 143,200 | - | - | - | 143,200 |
| Tung Hsi Hui, Frank | Guoco Group Limited | 28,200 | - | - | - | 28,200 |

Notes : -

1. These shares represented the interest of Guoline Overseas Limited (133,817,740 shares) and another company (1,188,000 shares) with respect to which Mr. Quek Leng Chan had a corporate interest pursuant to the SDI Ordinance.
2. These shares represented the interest of Guoco Group Limited with respect to which Mr. Quek Leng Chan had a corporate interest pursuant to the SDI Ordinance.

** NCCPS - Non-redeemable convertible cumulative preference shares.

Certain directors held qualifying shares in a subsidiary in trust for another subsidiary of the Company.

Apart from the above, as at 30th June, 1999, there was no other interests or rights recorded in the register required to be kept under Section 29 of the SDI Ordinance.

SUBSTANTIAL SHAREHOLDERS

As at 30th June, 1999, those persons (other than the directors of the Company) having an interest of 10% or more in the Company's issued share capital as recorded in the register of substantial shareholders maintained under Section 16(1) of the SDI Ordinance, were as follows :

| Name | Number of shares held in the Company | Shareholding |
|---------------------|--------------------------------------|--------------|
| Guoco Group Limited | 496,854,664 | 71.67% |

Report of the Directors

BOARD AUDIT COMMITTEE

The Company established an Audit Committee of the Board of Directors with written terms of reference on 9th October, 1998. The Audit Committee comprises Messrs. Harry Richard Wilkinson, Sir Jack Cater and Tung Hsi Hui, Frank.

The Audit Committee meets regularly to consider the nature and scope of audit reviews and the effectiveness of the systems of internal control and compliance.

COMPLIANCE WITH THE CODE OF BEST PRACTICE

The Company has complied throughout the year with the Code of Best Practice adopted by the Company based on the guidelines set out in the Rules Governing the Listing of Securities of The Stock Exchange of Hong Kong Limited.

INTERESTS IN CONTRACTS AND CONNECTED TRANSACTIONS

Tenancy agreements

On 1st February, 1997, Wanchai Property Investment Limited (“WPIL”), a fellow subsidiary of the Company, entered into tenancy agreements with OTB Card Company Limited (“OTBC”), a wholly-owned subsidiary of the Company, in respect of the letting of Portion B on the 18th Floor and 19th Floor of the O.T.B. Building, 160 Gloucester Road, Hong Kong (“OTB Building”) with a total gross floor area of approximately 8,666 sq.ft. to OTBC at a monthly rental of HK\$225,316 for two years. Both leases expired during the year.

On 15th January, 1999, a tenancy agreement was entered into between W.C.H. Limited (“WCH”), a fellow subsidiary of the Company, and Dao Heng Bank Limited (“DHB”), a wholly-owned subsidiary of the Company, in respect of the letting of the premises at 33rd, 34th and 35th Floors of Wu Chung House, No. 213 Queen’s Road East, Hong Kong with a gross floor area of approximately 73,674 sq.ft. to DHB for two years commencing from 15th January, 1999 at a monthly rental of HK\$1,105,110. There was an option to renew for two further years at the then market rental to be agreed between the parties. The aforesaid lease was a renewal of a tenancy agreement which expired on 14th January, 1999.

On 1st February, 1999, WPIL entered into a tenancy agreement with DHB in respect of the letting of the 19th Floor of the OTB Building with a gross floor area of approximately 7,344 sq.ft. to DHB for 2 years commencing from 1st February, 1999 at a monthly rental of HK\$110,160. There was an option to renew for two further years at the then market rental to be agreed between the parties.

Purchase of properties

On 25th August, 1998, a conditional sub-sub-sale and sub-sub-purchase agreement (“Agreement”) was entered into between Supreme Goal Investments Limited (“SGIL”), a fellow subsidiary of the Company, and DHB in respect of the sale of the 11th Floor, The Center, 99 Queen’s Road Central, Hong Kong (“The Center”) from SGIL to DHB for a cash consideration of HK\$185,000,000. The consideration was determined with reference to the valuation of an independent valuer as at 25th August, 1998. The Agreement was conditional upon the written approval of the Land Development Corporation and The Director of Lands Department to the sale of property and the approval by the independent shareholders of Guoco Land Limited (“GLL”), the holding company of SGIL. The Agreement became unconditional in September 1998 and sale of the property was completed on 12th October, 1998.

Report of the Directors

On 26th February, 1999, a Pre-Sale Contract for Foreign Sales Property and a Supplemental Agreement thereto were entered into between Beijing Minghua Property Development Co., Ltd. ("Beijing Minghua") and DHB whereby DHB agreed to purchase Rooms 821 and 822, 8th Floor, Block B, Corporate Square, No. 35 Finance Street, Xi Cheng District, Beijing, the People's Republic of China, with a total gross floor area of approximately 309 square metres for a cash consideration of US\$648,900. The consideration was determined after arm's length negotiations with reference to the valuation of the Corporate Square by an independent property valuer as at 31st July, 1998 and the transacted price of units or floors in Corporate Square between Beijing Minghua and the independent third parties. Beijing Minghua is a 75% subsidiary of Guoco Properties Limited ("GPL"), a subsidiary which is owned as to 55% by Guoco Group Limited ("Guoco") and 45% by First Capital Corporation Ltd.

On 27th September, 1999, a conditional sale and purchase agreement was entered into between SGIL and DHB whereby SGIL agreed to sell and DHB agreed to purchase the 16th, 17th and 18th Floors of The Center for a cash consideration of HK\$481,030,000. The consideration was determined with reference to the valuation of an independent valuer as at 30th June, 1999. It was conditional upon the approval by the independent shareholders of the Company and GLL. HK\$48,103,000 being 10% of the total consideration was paid by DHB to SGIL as deposit upon signing of the agreement. The balance of the consideration of HK\$432,927,000 shall be payable by DHB upon completion of the agreement. Completion of agreement is expected to take place on or before 20th November, 1999 but in any event not later than 30th December, 1999.

Reimbursement of renovation costs

On 25th August, 1998, DHB entered into a reimbursement agreement with SGIL, Dao Heng Securities Limited and Dao Heng Fund Management Limited, fellow subsidiaries of the Company, whereby all parties agreed to reimburse the actual costs for the renovation of the 12th Floor of The Center incurred by DHB. The actual costs were assessed by the relevant contractor as to the actual costs incurred in each of the three office areas and in the shared areas. The apportioned amount was reimbursed by the relevant companies to DHB during the year.

Services agreements and banking services arrangements

Under a services agreement entered into in 1982 with Hong Leong Overseas (H.K.) Limited ("HLO"), DHB pays to HLO an annual fee equal to three per cent of the consolidated profit before tax of DHB for the provision of certain senior executives and other management services by HLO to DHB. Either party may terminate the agreement by giving not less than six months' notice in writing. Messrs. Quek Leng Chan, Kwek Leng Hai and Kwek Leng San are directors of HLO and are interested in this agreement as shareholders of Hong Leong Company (Malaysia) Berhad ("HLCM"), the indirect holding company of HLO. Mr. Kwek Leng Hai, the chief executive of DHB, is also entitled to receive a salary together with benefits as an executive director.

DHB entered into a services agreement in 1993 with Guoco Management Company Limited ("GMCL"), a wholly-owned subsidiary of Guoco, for the provision by GMCL of various management, administrative, financial and legal services to companies in the Guoco group on a cost reimbursement basis. Either party may terminate the agreement by giving not less than three months' notice in writing.

The Group provides a number of services to Guoco and its connected persons as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and subsidiaries of, and companies related to, HLCM in the ordinary course of its banking business including, inter alia, loan advances, deposits, cheque clearing, remittances, the provision of account services in a variety of currencies, nominee and custodian services and occasionally short term credit accommodation. All services provided by the Group are in the ordinary course of business and on normal commercial terms.

Certain companies in the Guoco group regularly conduct banking, investment, insurance, stockbroking and other activities in the ordinary course of business and on normal commercial terms with subsidiaries of, and companies related to, HLCM. Messrs. Quek Leng Chan, Kwek Leng Hai and Kwek Leng San are directors of Guoco and are interested in such transactions as shareholders of HLCM.

Report of the Directors

Apart from the above, no contract of significance, to which the Company or any of its subsidiaries or its holding company or any subsidiary of its holding company was a party and in which a director of the Company had a material interest, subsisted at the end of the year or at any time during the year.

Guoco operates an Executive Share Option Scheme (“Scheme”) enabling eligible employees, including directors of the Company, to acquire shares in Guoco. Messrs. Kwek Leng Hai and Tung Hsi Hui, Frank held shares in Guoco, which were acquired under the terms of the Scheme.

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

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company’s Bye-Laws or the laws of Bermuda.

BEST PRACTICE GUIDE ON FINANCIAL DISCLOSURE BY AUTHORISED INSTITUTIONS

The accounts of the Group for the year ended 30th June, 1999 has fully complied with the recommendations in the Best Practice Guide on Financial Disclosure by Authorised Institutions issued by the Hong Kong Monetary Authority.

AUDITORS

On 19th November, 1998, our auditors changed the name under which they practise to KPMG and, accordingly, have signed their report in their new name.

A resolution for the re-appointment of KPMG as auditors of the Company is to be proposed at the forthcoming annual general meeting.

By Order of the Board

Kwek Leng Hai
Managing Director

Hong Kong, 6th October, 1999

Auditors' Report



TO THE SHAREHOLDERS OF DAO HENG BANK GROUP LIMITED

(Incorporated in Bermuda with limited liability)

We have audited the accounts on pages 36 to 72 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of accounts which give a true and fair view. In preparing accounts which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgements and estimates are made which are prudent and reasonable and that the reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion to you.

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 examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the circumstances of the Company and of the Group, 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 accounts are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion, the accounts give a true and fair view, in all material respects, of the state of affairs of the Company and of the Group as at 30th June, 1999 and of the Group's profit and cash flows for the year then ended, and have been properly prepared in accordance with accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

Hong Kong, 6th October, 1999

Consolidated Profit and Loss Account

For the year ended 30th June, 1999

| | Note | 1999 HK\$'000 | 1998 HK\$'000 |
|---|-------|------------------|------------------|
| Interest income | | 9,432,886 | 9,951,162 |
| Interest expense | | (6,738,605) | (7,360,410) |
| Net interest income | 3 | 2,694,281 | 2,590,752 |
| Other operating income | 4 | 1,020,482 | 865,743 |
| Operating income | | 3,714,763 | 3,456,495 |
| Operating expenses | 5 | (1,471,748) | (1,482,613) |
| Operating profit before provisions | | 2,243,015 | 1,973,882 |
| Provisions for bad and doubtful loans and advances | 15(b) | (856,761) | (534,895) |
| Operating profit | | 1,386,254 | 1,438,987 |
| Share of profit of a jointly controlled entity | | 8,362 | 7,021 |
| Share of profit/(loss) of an associated company | | 45 | (540) |
| Profit before taxation | | 1,394,661 | 1,445,468 |
| Taxation | 6(a) | (209,073) | (191,877) |
| Profit after taxation | | 1,185,588 | 1,253,591 |
| Minority interests | | 17,713 | 1,723 |
| Profit attributable to shareholders | 9 | 1,203,301 | 1,255,314 |
| Dividends | 10 | (624,275) | (624,356) |
| Retained profit for the year | 27 | 579,026 | 630,958 |
| Profit retained in: | | | |
| Company and subsidiaries | | 570,811 | 624,535 |
| Jointly controlled entity | | 8,170 | 7,021 |
| Associated company | | 45 | (598) |
| | | 579,026 | 630,958 |
| Earnings per share | | | |
| Basic | 11 | HK\$1.74 | HK\$1.80 |
| Diluted | 11 | N/A | HK\$1.80 |

The notes on pages 40 to 72 form part of these accounts.

Consolidated Balance Sheet

As at 30th June, 1999

| | Note | 1999 HK\$'000 | 1998 HK\$'000 |
|---|------|--------------------|--------------------|
| ASSETS | | | |
| Cash and short-term funds | 12 | 38,766,614 | 41,783,210 |
| Placements with banks and other financial institutions maturing between one and twelve months | | 8,098,000 | 2,199,670 |
| Certificates of deposit held | 13 | 1,722,860 | 1,691,301 |
| Other investments in securities | 14 | 2,257,110 | 723,180 |
| Advances to customers less provisions | 15 | 64,941,463 | 64,738,305 |
| Other assets | 16 | 1,541,991 | 1,369,070 |
| Held to maturity securities and investment securities | 17 | 9,830,332 | 7,330,089 |
| Interest in an associated company | 19 | – | 2,458 |
| Interest in a jointly controlled entity | 20 | 10,035 | 1,866 |
| Fixed assets | 21 | 4,707,908 | 3,095,093 |
| | | <u>131,876,313</u> | <u>122,934,242</u> |
| LIABILITIES | | | |
| Deposits and balances of banks and other financial institutions | | 4,437,648 | 6,536,994 |
| Current, fixed, savings and other deposits of customers | | 93,071,462 | 85,454,416 |
| Certificates of deposit issued | | 7,469,173 | 7,733,274 |
| Other accounts and provisions | | 12,037,465 | 8,328,814 |
| Proposed dividend | 10 | 451,120 | 450,202 |
| Amount due to a jointly controlled entity | 20 | 501,836 | 514,003 |
| 7.75% Fixed rate subordinated notes | 23 | 2,083,820 | 2,711,975 |
| | | <u>120,052,524</u> | <u>111,729,678</u> |
| SHAREHOLDERS' FUNDS | | | |
| Share capital | 26 | 2,678,346 | 2,685,007 |
| Reserves | 27 | 8,978,487 | 8,388,981 |
| Shareholders' funds | | <u>11,656,833</u> | <u>11,073,988</u> |
| MINORITY INTERESTS | | | |
| | | <u>166,956</u> | <u>130,576</u> |
| | | <u>11,823,789</u> | <u>11,204,564</u> |
| | | <u>131,876,313</u> | <u>122,934,242</u> |

Approved by the Board of Directors on 6th October, 1999

Kwek Leng Hai
Randolph Gordon Sullivan
Directors

The notes on pages 40 to 72 form part of these accounts.

Balance Sheet

As at 30th June, 1999

| | Note | 1999 HK\$'000 | 1998 HK\$'000 |
|---------------------------------|------|------------------|------------------|
| ASSETS | | | |
| Cash and short-term funds | | | |
| - deposits with subsidiary bank | 12 | 78,791 | 77,068 |
| Investments in subsidiaries | 18 | 80,885 | 80,885 |
| Amounts due from subsidiaries | | 5,583,351 | 5,584,433 |
| Other assets | 16 | 700 | 832 |
| | | <u>5,743,727</u> | <u>5,743,218</u> |
| LIABILITIES | | | |
| Other accounts and provisions | | 859 | 727 |
| Proposed dividend | 10 | 451,120 | 450,202 |
| | | <u>451,979</u> | <u>450,929</u> |
| SHAREHOLDERS' FUNDS | | | |
| Share capital | 26 | 2,678,346 | 2,685,007 |
| Reserves | 27 | 2,613,402 | 2,607,282 |
| | | <u>5,291,748</u> | <u>5,292,289</u> |
| | | <u>5,743,727</u> | <u>5,743,218</u> |

Approved by the Board of Directors on 6th October, 1999

Kwek Leng Hai
 Randolph Gordon Sullivan
Directors

The notes on pages 40 to 72 form part of these accounts.

Consolidated Cash Flow Statement

For the year ended 30th June, 1999

| | Note | 1999 HK\$'000 | 1998 HK\$'000 |
|--|-------|--------------------------|--------------------------|
| NET CASH INFLOW FROM OPERATING ACTIVITIES | 29(a) | <u>7,135,073</u> | <u>897,789</u> |
| RETURNS ON INVESTMENTS AND SERVICING OF FINANCE | | | |
| Dividends paid | | (623,357) | (769,154) |
| Interest paid for certificates of deposit issued | | (584,029) | (561,717) |
| Interest paid for 7.75% fixed rate subordinated notes | | (195,206) | (210,021) |
| Dividends received on equity investments | | <u>3,811</u> | <u>3,579</u> |
| NET CASH OUTFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE | | <u>(1,398,781)</u> | <u>(1,537,313)</u> |
| TAXATION | | | |
| Hong Kong profits tax paid | | (36,582) | (198,513) |
| Overseas tax paid | | <u>(14,736)</u> | <u>(10,581)</u> |
| TAX PAID | | <u>(51,318)</u> | <u>(209,094)</u> |
| INVESTING ACTIVITIES | | | |
| Purchase of held to maturity securities | | (9,771,007) | (5,518,993) |
| Purchase of debt securities-investment securities | | (35,349) | (86,573) |
| Purchase of equity investment-investment securities | | (3) | - |
| Proceeds from disposal of held to maturity securities | | 1,037,147 | 3,213,688 |
| Proceeds from disposal of debt securities-investment securities | | - | 93,956 |
| Proceeds from redemption of held to maturity securities | | 1,629,017 | 7,912,650 |
| Proceeds from redemption of debt securities- investment securities | | 76,648 | 18,916 |
| Proceeds from sale of equity investments-investment securities | | - | 2,033 |
| Amount due (from)/to a jointly controlled entity | | (11,974) | 188,373 |
| Purchase of fixed assets | | (1,785,158) | (139,696) |
| Proceeds from disposal of fixed assets | | 18,186 | 1,808 |
| Proceeds from liquidation of an associated company | | <u>2,503</u> | <u>-</u> |
| NET CASH (OUTFLOW)/INFLOW FROM INVESTING ACTIVITIES | | <u>(8,839,990)</u> | <u>5,686,162</u> |
| NET CASH (OUTFLOW)/INFLOW BEFORE FINANCING | | <u>(3,155,016)</u> | <u>4,837,544</u> |
| FINANCING | | | |
| Issue of certificates of deposit | 29(b) | 5,692,713 | 3,256,506 |
| Issue of share capital | 29(b) | 14,616 | - |
| Redemption of issued share capital | 29(b) | (17,091) | (57,731) |
| Redemption of certificates of deposit | 29(b) | (5,956,915) | (2,966,670) |
| Redemption of subordinated notes | 29(b) | (449,425) | - |
| Investment by minority shareholders | 29(b) | <u>40,590</u> | <u>29,537</u> |
| NET CASH (OUTFLOW)/INFLOW FROM FINANCING | | <u>(675,512)</u> | <u>261,642</u> |
| (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS | | <u>(3,830,528)</u> | <u>5,099,186</u> |
| CASH AND CASH EQUIVALENTS AT 1ST JULY | 29(c) | <u>41,529,308</u> | <u>36,468,276</u> |
| EFFECT OF FOREIGN EXCHANGE MOVEMENTS | | <u>22,744</u> | <u>(38,154)</u> |
| CASH AND CASH EQUIVALENTS AT 30TH JUNE | 29(c) | <u><u>37,721,524</u></u> | <u><u>41,529,308</u></u> |

The notes on pages 40 to 72 form part of these accounts.

Notes on the Accounts

1. BASIS OF PREPARATION

The consolidated accounts incorporate the accounts of the Company and all its subsidiaries made up to 30th June each year. All material intra-group accounts and transactions are eliminated upon consolidation. The Group's results include, in respect of any subsidiaries acquired during the year, their results attributable to the periods since the dates of acquisition and, in the case of subsidiaries disposed of during the year, their results attributable to the periods up to the dates of disposal.

Goodwill arising on consolidation represents the excess of the cost of investment over the fair value of the Group's share of the net assets of the subsidiaries, jointly controlled entities and associated companies acquired. The treatment of goodwill arising on each acquisition is determined by the directors according to the particular circumstances of that transaction. However, the usual practice of the Group is to eliminate goodwill arising on acquisition of subsidiaries, jointly controlled entities and associated companies against reserves in the year of acquisition.

Although not required to do so under the Bye-Laws of the Company, the accounts of the Company and the Group are prepared so as to comply with the disclosure requirements of the Hong Kong Companies Ordinance, the Statements of Standard Accounting Practice issued by the Hong Kong Society of Accountants and the recommendations in the Best Practice Guide on Financial Disclosure by Authorised Institutions issued by the Hong Kong Monetary Authority. The accounts also comply with the disclosure provisions of the Hong Kong Securities (Stock Exchange Listing) Rules.

2. PRINCIPAL ACCOUNTING POLICIES

(a) Revenue recognition

- (i) Interest income and expense are accrued on a time-apportioned basis on the principal outstanding and at the rate applicable. Fee income and expenses are recognised when earned or incurred.
- (ii) Dividend income is recognised as follows:
 - dividends from subsidiaries are recognised at the end of the subsidiaries' financial period to which such dividends relate ;
 - dividends from listed investments are recognised when the share price of such investments goes ex-dividend ; and
 - interim dividends from unlisted investments are recognised when the directors of such investments declare such dividends; final dividends from unlisted investments are recognised when the shareholders of such investments approve the dividends proposed by the directors at the general meeting.

(b) Investments

(i) Securities

The Group has adopted the new Statement of Standard Accounting Practice 2.124 "Accounting for Investments in Securities" issued by the Hong Kong Society of Accountants with effect from 1st July, 1998 which resulted in a change of accounting policy in respect of treasury bills, certificates of deposit, and securities held for dealing and investment purposes. Debt securities which are intended to be held to maturity are accounted for as held to maturity securities. Other securities are accounted for using the benchmark treatment.

Notes on the Accounts

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(b) Investments (Cont'd)

(i) Securities (Cont'd)

This change in accounting policy was applied retrospectively in the financial year 1997/98. As the amount of resulting adjustments relating to periods prior to 1st July, 1997 was immaterial, the opening retained earnings for 1997/98 were not restated. The effect of the change of the accounting policy was to decrease net profit by HK\$20,496,000 for the year ended 30th June, 1998. The opening retained earnings for 1998/99 were restated by the same amount accordingly. The net profit for the year ended 30th June, 1999 was increased by HK\$14,490,000. Comparative figures for the year ended 30th June, 1998 were restated to reflect the change in accounting policy.

Held to maturity securities

Investment in dated debt securities which are intended to be held to maturity are stated in the balance sheet at cost adjusted for the amortisation of premiums or discounts arising on acquisition, less any provisions for diminution in value.

The carrying amounts of held to maturity securities are reviewed as at the balance sheet date in order to assess the credit risk and whether the carrying amounts are expected to be recovered. Provisions are made when carrying amounts are not expected to be recovered and are recognised as an expense in the profit and loss account.

Investment securities

Equity and debt securities which are intended to be held on a continuing basis for an identified long term purpose are stated in the balance sheet at cost less any provisions for diminution in value.

The carrying amounts of investment securities are reviewed as at the balance sheet date in order to assess whether the fair values have declined below the carrying amounts. When such a decline has occurred, the carrying amount is reduced to the fair value unless there is evidence that the decline is temporary. The amount of the reduction is recognised as an expense in the profit and loss account.

Fair value is the amount for which an asset can be exchanged, or a liability settled, between knowledgeable willing parties in an arm's length transaction.

Other investments

Securities are stated in the balance sheet at fair value. Changes in fair value are recognised in the profit and loss account as they arise.

Provisions against the carrying value of held to maturity securities and investment securities are written back when the circumstances and events that led to the write-down or write-off cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

Profits or losses on disposal of investments in securities are accounted for in the profit and loss account as they arise.

Notes on the Accounts

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(b) Investments (Cont'd)

(ii) Investments in subsidiaries

A subsidiary is a company in which the Group, directly or indirectly, holds more than half of the issued share capital, or controls more than half of the voting power, or controls the composition of the board of directors.

Investments in subsidiaries are stated in the Company's balance sheet at cost less provision for permanent diminution in value as determined by the directors.

(iii) Investments in associated companies

An associated company is a company in which the Group has a long term equity interest and over which the Group is in a position to exercise significant influence, but not control or joint control, in its management, including participation in financial and operating policy decisions.

The consolidated profit and loss account includes the Group's share of the post acquisition results of its associated companies for the year. In the consolidated balance sheet, investments in associated companies are stated at the Group's share of their net assets.

(iv) Investments in jointly controlled entities

A joint venture is a contractual agreement whereby the Group or Company and at least one other party undertake an economic activity which is subject to control and none of the parties involved unilaterally has control over the economic activity.

The consolidated profit and loss account includes the Group's share of the post acquisition results of its jointly controlled entities for the year. In the consolidated balance sheet, investments in jointly controlled entities are stated at the Group's share of their net assets.

(c) Fixed assets and depreciation

- (i) In preparing these accounts, advantage has been taken of the transitional provisions set out in paragraph 72 of Statement of Standard Accounting Practice 2.117 "Property, plant and equipment" issued by the Hong Kong Society of Accountants, with the effect that premises have not been revalued to fair value at the balance sheet date.

The Group's premises are included at directors' valuation made having regard to independent professional valuations carried out in 1993. 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.

- (ii) The carrying amount of fixed assets is reviewed periodically in order to assess whether the recoverable amount has declined below the carrying amount. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recognised as an expense, unless it reverses a previous revaluation increase in which case it is charged directly against any related revaluation reserve to the extent that the reduction does not exceed the amount held in the revaluation reserve in respect of the same item. In determining the recoverable amount, expected future cash flows generated by the fixed assets are not discounted to their present values.

Notes on the Accounts

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(c) Fixed assets and depreciation (Cont'd)

A subsequent increase in the recoverable amount of an asset carried at depreciated cost is written back to the profit and loss account when the circumstances and events that led to the write-down or write-off cease to exist. Any subsequent increase in the recoverable amount of an asset carried at valuation is credited firstly to the profit and loss account to the extent of any deficit previously charged to the profit and loss account in respect of that same asset, and is thereafter taken to the revaluation reserve.

(iii) Premises are stated at cost or valuation less depreciation calculated to write off the assets over their estimated useful lives as follows:

- Freehold land is not depreciated.
- Land held on lease is depreciated over the unexpired terms of the leases on a straight line basis.
- Buildings and improvements thereto are depreciated at the higher of 2% per annum or over the unexpired terms of the leases on a straight line basis.
- Furniture, fixtures and equipment are stated at cost less depreciation calculated on a straight line basis to write off the assets over their estimated useful lives, taken as being between 3 to 15 years.

(iv) On disposal of premises, the profit or loss is determined as the difference between the net sale proceeds and the carrying amount. Any related revaluation surplus is transferred from the revaluation reserve to retained profits.

(d) Finance leases and hire purchase transactions

Amounts due from lessees in respect of finance leases and hire purchase transactions, net of unearned interest, are included in the balance sheet as advances to customers.

Net income on finance leases and hire purchase transactions is allocated to accounting periods over the lease terms in accordance with the investment period method so as to produce an approximately constant periodic rate of return on the net cash investment for each accounting period.

(e) Operating leases

Payments under operating leases are charged to the profit and loss account on a straight line basis over the periods of the respective leases.

(f) Provisions for bad and doubtful loans and advances

Specific provisions are made for bad and doubtful loans and advances as and when they are so considered by the directors. In addition, amounts have been set aside as general provisions for doubtful loans and advances. The specific element relates to individual accounts; the general element relates to other exposures not separately identified but known from experience to exist in any loan portfolio. These provisions are deducted from the relevant loans and advances. When there is no longer any realistic prospect of recovery, the outstanding loan is written off.

Interest on bad and doubtful loans and advances is credited to a suspense account which is netted off against the relevant balances.

Notes on the Accounts

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(g) Deferred taxation

Deferred taxation is provided using the liability method in respect of the taxation effect arising from all material timing differences between the accounting and tax treatment of income and expenditure, which are expected with reasonable probability to crystallise in the foreseeable future.

Future deferred tax benefits are not recognised unless their realisation is assured beyond reasonable doubt.

(h) Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the rates of exchange ruling at the transaction dates. Monetary assets and liabilities in foreign currencies and the accounts of overseas branches, subsidiaries and associated companies are translated into Hong Kong dollars at the rates of exchange ruling at the balance sheet date. Share capital is translated into Hong Kong dollars at the historical rates of exchange ruling at the respective transaction dates. Differences on foreign currency translation are dealt with in the profit and loss account with the exception of those arising on the translation of foreign currency accounts of overseas branches, subsidiaries and associated companies which are dealt with in reserves.

(i) 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 cost or market value depending on their classification as held to maturity securities, investment securities or other investments and the proceeds of the sale are included in "Current, fixed, savings and other deposits of customers", "Deposits and balance of banks and other financial institutions" or "Other accounts and provisions" depending on the identity of the counterparty. The difference between the sale price and the repurchase price is amortised 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 on an effective yield basis over the period from the date of purchase to the date of resale.

(j) Retirement costs

The Group operates a defined contribution scheme and the contributions thereto are charged to the profit and loss account for the year.

(k) Off-balance sheet financial instruments

Off-balance sheet financial instruments arise from future, forward, swap and option transactions undertaken by the Group in the foreign exchange, interest rate and equity markets. The accounting for these instruments is dependent upon whether the transactions are undertaken for dealing purposes, to hedge risk, or as part of the management of asset and liability portfolios.

Transactions undertaken for dealing purposes are marked to market and the net present value of the gain or loss arising is recognised in the profit and loss account as dealing profits/losses, after appropriate deferrals for unearned credit margin and future servicing costs.

Notes on the Accounts

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(k) Off-balance sheet financial instruments (Cont'd)

Transactions designated as hedges are valued on an equivalent basis to the assets, liabilities or net positions which they are hedging. Any profit or loss is recognised on the same basis as that arising from the related assets, liabilities or net positions.

Interest rate swap transactions undertaken as part of the management of asset and liability portfolios are separately identified and interest income or expense arising therefrom is netted off against the related interest income or expense on the on-balance sheet items these transactions are hedged against.

Unrealised gains on transactions which are marked to market are included in "Other assets" in the balance sheet. Unrealised losses on transactions which are marked to market are included in "Other accounts and provisions".

(l) 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.

In preparing these accounts, advantage has been taken of the transitional provisions in paragraph 28 of Statement of Standard Accounting Practice 2.120 "Related Party Disclosures" issued by the Hong Kong Society of Accountants with the effect that no comparative information has been provided in respect of income and expense and balance sheet from related party transactions as this information is not readily available.

3. NET INTEREST INCOME

(a) Interest income

| | The Group | |
|---|-----------|-----------|
| | 1999 | 1998 |
| | HK\$'000 | HK\$'000 |
| Interest income on listed investments | 346,968 | 282,573 |
| Interest income on unlisted investments | 983,392 | 976,886 |
| Other interest income | 8,102,526 | 8,691,703 |
| | 9,432,886 | 9,951,162 |
| | 9,432,886 | 9,951,162 |

(b) Interest expense

Interest expense included interest on 7.75% fixed rate subordinated notes amounted to HK\$174,559,000 (1998: HK\$208,865,000).

Notes on the Accounts

4. OTHER OPERATING INCOME

| | The Group | |
|--|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Net fee and commission income | 578,901 | 658,966 |
| Net income from foreign exchange operations | 104,648 | 123,855 |
| Dividend income from listed investments | 2 | – |
| Dividend income from unlisted investments | 3,809 | 3,579 |
| Rental income less outgoings | 5,386 | 8,507 |
| Net profits from other dealing activities | | |
| Realised and unrealised gain/(loss) on other investments | 83,771 | (44,664) |
| (Loss)/profit from other dealing activities | (7,042) | 74,734 |
| Others | 251,007 | 40,766 |
| | <u>1,020,482</u> | <u>865,743</u> |

An one time gain of HK\$181 million from the early redemption of US\$81 million face value of 7.75% fixed rate subordinated notes (Note 23) is included in "Others".

5. OPERATING EXPENSES

(a) Items making up the operating expenses are as follows:-

| | The Group | |
|--------------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Staff costs | | |
| Salaries and other costs | 782,179 | 792,674 |
| Pension costs (Note 31) | 58,545 | 56,637 |
| Premises and equipment | | |
| Rental of premises | 67,873 | 88,153 |
| Depreciation (Note 21) | 147,359 | 117,306 |
| Others | 122,402 | 106,604 |
| Management fee | 44,675 | 47,736 |
| Auditors' remuneration | 5,600 | 7,085 |
| Other operating expenses | 243,115 | 266,418 |
| | <u>1,471,748</u> | <u>1,482,613</u> |

For 1997/98, realised losses on disposal of investment securities and provisions on investment securities amounted to HK\$897,112 and HK\$3,678,184 respectively which are included in "Other operating expenses". No such losses or provisions are reported for 1998/99.

Notes on the Accounts

5. OPERATING EXPENSES (CONT'D)

(b) The emoluments of the five highest paid individuals :-

Among the five highest paid individuals of the Group, two (1998: two) are directors whose remuneration is disclosed in Note 7.

The remuneration of the other three (1998: three) is as follows :-

| | The Group | |
|---|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Salaries, allowances and benefits in kind | 5,478 | 5,171 |
| Pension contributions | 473 | 430 |
| Discretionary bonuses | 1,130 | 2,075 |
| | <u>7,081</u> | <u>7,676</u> |
| | | |
| | 1999 | 1998 |
| | Number of | Number of |
| | Individuals | Individuals |
| HK\$ | | |
| 2,000,001 – 2,500,000 | 3 | 1 |
| 2,500,001 – 3,000,000 | – | 2 |
| | <u>3</u> | <u>3</u> |

6. TAXATION

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

| | The Group | |
|---|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Hong Kong profits tax | 197,197 | 176,770 |
| Overseas taxation | 11,684 | 15,049 |
| | <u>208,881</u> | <u>191,819</u> |
| Share of a jointly controlled entity's taxation | 192 | – |
| Share of an associated company's taxation | – | 58 |
| | <u>209,073</u> | <u>191,877</u> |

The provision for Hong Kong profits tax is calculated at 16% (1998: 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.

Notes on the Accounts

6. TAXATION (CONT'D)

- (b) Taxation in the balance sheets which is included in "Other accounts and provisions" or "Other assets" represents :

| | The Group | | The Company | |
|--|------------------|------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Tax payable / (recoverable) for Hong Kong profits tax | 125,261 | (35,546) | - | - |
| Overseas taxation payable | 7,173 | 10,225 | - | - |
| | <u>132,434</u> | <u>(25,321)</u> | <u>-</u> | <u>-</u> |

- (c) No provision for deferred taxation is required as there are net deferred tax assets for the Group. At the balance sheet date, the major components of the unprovided deferred tax assets are as follows:

| | The Group | |
|--|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Depreciation allowances in excess of depreciation charges | (44,296) | (42,677) |
| General provisions for bad and doubtful loans and advances | 127,028 | 137,549 |
| Tax losses | 19,738 | 16,375 |
| | <u>102,470</u> | <u>111,247</u> |

The surplus arising on the revaluation of premises does not constitute a timing difference as the disposal of these assets at their carrying value would result in capital gains which are not subject to tax.

7. DIRECTORS' REMUNERATION

Directors' remuneration disclosed pursuant to Section 161 of the Hong Kong Companies Ordinance is as follows:

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|------------------|------------------|
| Fees | 685 | 636 |
| Salaries, allowances and benefits in kind | 9,963 | 10,102 |
| Pension contributions | 551 | 276 |
| Discretionary bonuses | 1,710 | 7,830 |
| | <u>12,909</u> | <u>18,844</u> |

Notes on the Accounts

7. DIRECTORS' REMUNERATION (CONT'D)

Included in the above are the following emoluments paid to independent non-executive directors :

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|------------------|------------------|
| Fees | 280 | 280 |
| Salaries, allowances and benefits in kind | 720 | 708 |
| Discretionary bonuses | 80 | 120 |
| | <u>1,080</u> | <u>1,108</u> |

The number of directors whose remuneration falls within the following bands is :

| HK\$ | 1999 Number of Directors | 1998 Number of Directors |
|------------------------|--------------------------------|--------------------------------|
| 0 – 1,000,000 | 8 | 7 |
| 5,000,001 – 5,500,000 | 1 | – |
| 6,000,001 – 6,500,000 | 1 | – |
| 7,500,001 – 8,000,000 | – | 1 |
| 9,500,001 – 10,000,000 | – | 1 |
| | <u>10</u> | <u>9</u> |

8. LOANS TO OFFICERS

Particulars of relevant loans disclosed pursuant to Section 161B of the Hong Kong Companies Ordinance:

| | Aggregate amount of relevant loans outstanding at 30th June | | Maximum aggregate amount of relevant loans outstanding during the year | |
|--|--|------------------|---|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Relevant loans made by subsidiary banks | <u>2,634</u> | <u>5,187</u> | <u>26,597</u> | <u>27,350</u> |

9. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The Group profit attributable to shareholders includes a profit after taxation of HK\$626,209,000 (1998: HK\$628,080,000) which has been dealt with in the accounts of the Company.

Notes on the Accounts

10. DIVIDENDS

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|-----------------------|-----------------------|
| Interim dividend paid of HK\$0.25 per share (1998: HK\$0.25 per share) | 173,155 | 174,154 |
| Final dividend proposed of HK\$0.65 per share (1998: HK\$0.65 per share) | <u>451,120</u> | <u>450,202</u> |
| | <u><u>624,275</u></u> | <u><u>624,356</u></u> |

11. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit attributable to shareholders of HK\$1,203,301,000 (1998: HK\$1,255,314,000) and on weighted average of 693,106,691 shares (1998: 698,444,754 shares) in issue during the year.

During the year ended 30th June, 1999, there were no dilutive potential shares. Fully diluted earnings per share are not disclosed.

The calculation of diluted earnings per share for 1998 is based on profit attributable to shareholders of HK\$1,255,314,000 and on weighted average number of 698,872,898 shares in issue during the year after adjusting for the effect of all dilutive potential shares.

12. CASH AND SHORT-TERM FUNDS

| | The Group | | The Company | |
|--|--------------------------|--------------------------|----------------------|----------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Cash and balances with banks and other financial institutions | 773,680 | 1,473,497 | 257 | 176 |
| Money at call and short notice | 20,846,394 | 17,690,160 | 78,534 | 76,892 |
| Treasury bills (including Exchange Fund Bills) | <u>17,146,540</u> | <u>22,619,553</u> | <u>-</u> | <u>-</u> |
| | <u><u>38,766,614</u></u> | <u><u>41,783,210</u></u> | <u><u>78,791</u></u> | <u><u>77,068</u></u> |

(a) Money at call and short notice represents deposits of up to a maximum of one month to maturity.

Notes on the Accounts

12. CASH AND SHORT-TERM FUNDS (CONT'D)

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

| | The Group | |
|------------------------------------|-------------------|-------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Held to maturity securities | | |
| Listed outside Hong Kong | 5,813,075 | 23,590 |
| Unlisted | 5,823,374 | 17,519,196 |
| | <u>11,636,449</u> | <u>17,542,786</u> |
| Other investments | | |
| Unlisted | 5,510,091 | 5,076,767 |
| | <u>17,146,540</u> | <u>22,619,553</u> |

Market value of listed treasury bills amounted to HK\$5,813,843,000 (1998 : HK\$23,590,000).

13. CERTIFICATES OF DEPOSIT HELD

| | The Group | |
|------------------------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Held to maturity securities | | |
| Unlisted | 130,986 | 130,850 |
| Other investments | | |
| Listed outside Hong Kong | 203,797 | 3,967 |
| Unlisted | 1,388,077 | 1,556,484 |
| | <u>1,591,874</u> | <u>1,560,451</u> |
| | <u>1,722,860</u> | <u>1,691,301</u> |

Market value of listed certificates of deposit amounted to HK\$203,797,000 (1998 : HK\$3,967,000).

Notes on the Accounts

15. ADVANCES TO CUSTOMERS LESS PROVISIONS

| | The Group | | The Company | |
|---|-------------------|-------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Advances to customers (Note a) | 66,422,639 | 65,871,710 | - | - |
| Provisions for bad and doubtful loans and advances (Note b) | | | | |
| General | (816,482) | (875,365) | - | - |
| Specific | (664,694) | (258,040) | - | - |
| | <u>64,941,463</u> | <u>64,738,305</u> | <u>-</u> | <u>-</u> |
| Included in advances to customers are : | | | | |
| Trade bills | 637,276 | 777,037 | - | - |
| General provisions for bad and doubtful loans and advances | (6,331) | (7,682) | - | - |
| | <u>630,945</u> | <u>769,355</u> | <u>-</u> | <u>-</u> |

- (a) Net cash investment in finance lease and hire purchase debtors included in advances to customers are as follows : -

| | The Group | | The Company | |
|-----------------------|------------------|------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Finance lease debtors | 50,186 | 83,778 | - | - |
| Hire purchase debtors | 5,546,368 | 5,798,479 | - | - |
| | <u>5,596,554</u> | <u>5,882,257</u> | <u>-</u> | <u>-</u> |

At 30th June, 1999, the cumulative cost of assets acquired by the Group for the purpose of letting under the above finance leases and hire purchase contracts amounted to approximately HK\$118 million (1998: HK\$164 million) and HK\$6,207 million (1998 : HK\$6,732 million) respectively.

The rentals receivable by the Group during the year in respect of finance leases and hire purchase contracts amounted to approximately HK\$77 million (1998 : HK\$81 million) and HK\$2,605 million (1998: HK\$2,669 million) respectively.

Notes on the Accounts

15. ADVANCES TO CUSTOMERS LESS PROVISIONS (CONT'D)

(b) Provisions for bad and doubtful loans and advances

| | The Group 1999 | | | |
|---|-------------------|----------------|------------------|-----------------------|
| | Specific | General | Total | Suspended interest |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| At 1st July | 258,040 | 875,365 | 1,133,405 | 80,585 |
| Amounts written off | (523,615) | - | (523,615) | (40,100) |
| Recoveries of advances written off in previous years | 19,166 | - | 19,166 | - |
| Charge/(release) to profit and loss account | 915,390 | (58,629) | 856,761 | - |
| Interest suspended during the year | - | - | - | 292,819 |
| Suspended interest recovered | - | - | - | (20,379) |
| Exchange and other adjustments | (4,287) | (254) | (4,541) | (11,582) |
| At 30th June | <u>664,694</u> | <u>816,482</u> | <u>1,481,176</u> | <u>301,343</u> |
| | The Group 1998 | | | |
| | Specific | General | Total | Suspended interest |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| At 1st July | 175,662 | 670,754 | 846,416 | 101,429 |
| Amounts written off | (262,026) | - | (262,026) | (82,025) |
| Recoveries of advances written off in previous years | 19,910 | - | 19,910 | - |
| Charge to profit and loss account | 327,586 | 207,309 | 534,895 | - |
| Interest suspended during the year | - | - | - | 79,798 |
| Suspended interest recovered | - | - | - | (15,912) |
| Exchange and other adjustments | (3,092) | (2,698) | (5,790) | (2,705) |
| At 30th June | <u>258,040</u> | <u>875,365</u> | <u>1,133,405</u> | <u>80,585</u> |

(c) The total advances, net of suspended interest, on which interest has been placed in suspense or has ceased to accrue are as follows:

| | The Group | | | |
|---------------------|------------------|------------------------|----------------|------------------------|
| | 1999 | | 1998 | |
| | HK\$'000 | % of Total Advances | HK\$'000 | % of Total Advances |
| Gross advances | 2,694,094 | 4.06 | 723,070 | 1.10 |
| Specific provisions | (580,164) | | (258,040) | |
| | <u>2,113,930</u> | | <u>465,030</u> | |

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

Notes on the Accounts

16. OTHER ASSETS

| | The Group | | The Company | |
|------------------|------------------|------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Accrued interest | 503,923 | 409,956 | 337 | 468 |
| Other accounts | 1,038,068 | 959,114 | 363 | 364 |
| | <u>1,541,991</u> | <u>1,369,070</u> | <u>700</u> | <u>832</u> |

17. HELD TO MATURITY SECURITIES AND INVESTMENT SECURITIES

| | The Group | |
|--|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Held to maturity securities - debt securities | | |
| Listed : | | |
| - in Hong Kong | 248,008 | - |
| - outside Hong Kong | 5,370,029 | 4,880,337 |
| | <u>5,618,037</u> | <u>4,880,337</u> |
| Unlisted | 4,069,585 | 2,316,281 |
| | <u>9,687,622</u> | <u>7,196,618</u> |
| Investment securities | | |
| Debt securities | | |
| Listed outside Hong Kong | 25,280 | - |
| Unlisted | 103,148 | 119,276 |
| | <u>128,428</u> | <u>119,276</u> |
| Equity securities | | |
| Listed outside Hong Kong | 133 | 133 |
| Unlisted | 14,149 | 14,062 |
| | <u>14,282</u> | <u>14,195</u> |
| | <u>142,710</u> | <u>133,471</u> |
| | <u>9,830,332</u> | <u>7,330,089</u> |
| Market value of listed securities : | | |
| Debt securities | 5,734,027 | 4,864,148 |
| Equity securities | 12,160 | 6,261 |
| | <u>5,746,187</u> | <u>4,870,409</u> |

Notes on the Accounts

17. HELD TO MATURITY SECURITIES AND INVESTMENT SECURITIES (CONT'D)

| Issued by : | The Group | |
|--|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| - Central governments and central banks | 788,803 | 416,328 |
| - Public sector entities | 1,618,090 | 827,930 |
| - Banks and other financial institutions | 6,864,422 | 5,767,009 |
| - Corporate entities | 554,555 | 313,423 |
| - Others | 4,462 | 5,399 |
| | <u>9,830,332</u> | <u>7,330,089</u> |

During the year, held to maturity securities shown in Notes 12(b), 13 and 17 with an amortised cost of HK\$990,222,000 were disposed of at a profit of HK\$46,925,000 being recognised in the profit and loss account. Management sold these held to maturity securities as a result of the disposal of the underlying liabilities being hedged.

18. INVESTMENTS IN SUBSIDIARIES

| Unlisted shares, at cost | The Company | |
|--------------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| | <u>80,885</u> | <u>80,885</u> |

(a) Details of the principal subsidiaries incorporated and operating in Hong Kong are as follows:

| Name of Company | Issued and paid up ordinary share capital | Percentage held by the | | Principal activities |
|--|--|---------------------------|-------|----------------------|
| | | Company | Group | |
| DHB Limited | 5,000,000 shares of HK\$100 each | 100 | | Investment holding |
| Dao Heng Bank Limited | 5,200,000,000 shares of HK\$1 each | | 100 | Banking |
| Dao Heng Finance Limited | 250,000 shares of HK\$100 each | | 100 | Finance |
| Dao Heng Bank Trustee Limited | 30,000 shares of HK\$100 each | | 100 | Trustee services |
| Dao Heng Corporate Services Limited (Formerly known as Dao Heng International Limited) | 500,000 shares of HK\$1 each | | 100 | Investment holding |
| Ting Hong Nominees Limited | 10,000 shares of HK\$1 each | | 100 | Nominee services |

Notes on the Accounts

18. INVESTMENTS IN SUBSIDIARIES (CONT'D)

| Name of Company | Issued and paid up ordinary share capital | Percentage held by the | | Principal activities |
|--------------------------------------|---|------------------------|-------|-------------------------------|
| | | Company | Group | |
| Dao Heng Bullion Limited | 5,000 shares of HK\$100 each | | 100 | Bullion broking |
| Hang Lung Bank (Nominee) Limited | 100 shares of HK\$100 each | | 100 | Nominee services |
| Hang Lung Godown Company, Limited | 3,500,000 shares of HK\$1 each | | 100 | Property holding |
| OTB Card Company Limited | 700,000 shares of HK\$100 each | | 100 | Property investment |
| Overseas Trust Bank, Limited | 2,000,000,000 shares of HK\$1 each | | 100 | Banking |
| EFI Nominees Limited | 2 shares of HK\$1 each | | 100 | Nominee services |
| Overseas Trust Bank Nominees Limited | 50,000 shares of HK\$1 each | | 100 | Nominee services |
| O.T.B. Investment Limited | 50,000 shares of HK\$1 each | | 100 | Share and property investment |
| OTB Property Management Limited | 10,000 shares of HK\$1 each | | 100 | Property management |

(b) Details of the principal subsidiaries incorporated and operating outside Hong Kong are as follows:

| Name of Company | Country of incorporation and operation | Issued and paid up ordinary share capital | Percentage held by the | | Principal activities |
|---------------------------------------|--|---|------------------------|-------|----------------------|
| | | | Company | Group | |
| Dao Heng Bank (London) Plc | United Kingdom | 20,000,000 shares of £1 each | | 100 | Banking |
| Benchmark Farm Finance (Four) Limited | United Kingdom | 20,000 shares of £1 each | | 100 | Finance |
| Dao Heng Nominees Limited | United Kingdom | 2 shares of £1 each | | 100 | Nominee services |
| Dao Heng Bank Trustee (BVI) Limited | British Virgin Islands | 250,000 shares of US\$1 each | | 100 | Trustee services |
| Dao Heng Bank, Inc. | Philippines | 22,500,000 shares of Peso 100 each | | 60 | Banking |

Notes on the Accounts

19. INTEREST IN AN ASSOCIATED COMPANY

| | The Group | |
|---------------------|-----------|----------|
| | 1999 | 1998 |
| | HK\$'000 | HK\$'000 |
| Share of net assets | - | 2,458 |

The associated company was liquidated during the year.

20. INTEREST IN A JOINTLY CONTROLLED ENTITY

| | The Group | |
|---|-----------|----------|
| | 1999 | 1998 |
| | HK\$'000 | HK\$'000 |
| Share of net assets | 10,035 | 1,866 |
| Amount due to a jointly controlled entity | 501,836 | 514,003 |

Details of the jointly controlled entity are as follows:

| Name of Company | Country of incorporation | Principal place of operation | Issued and paid up ordinary shares | Percentage of ordinary shares held by the Group | Principal activities |
|---|--------------------------|------------------------------|------------------------------------|---|---|
| Hutchison Dao Heng Card Limited (Formerly known as Hutchison OTB Card Limited) | British Virgin Islands | Hong Kong | 1,000,000 shares HK\$1 each | 50 | Provision of agency services for credit card business |

Notes on the Accounts

21. FIXED ASSETS

| | Premises | Furniture, fixtures & equipment | Total |
|---|-------------------------|---------------------------------------|-------------------------|
| | HK\$'000 | HK\$'000 | HK\$'000 |
| The Group | | | |
| Cost or valuation | | | |
| As at 1st July, 1998 | 2,944,265 | 616,780 | 3,561,045 |
| Additions | 1,688,871 | 96,287 | 1,785,158 |
| Disposals | (23,188) | (36,746) | (59,934) |
| Exchange and other adjustments | (1,145) | 686 | (459) |
| | <u>4,608,803</u> | <u>677,007</u> | <u>5,285,810</u> |
| As at 30th June, 1999 | | | |
| Accumulated depreciation | | | |
| As at 1st July, 1998 | 156,338 | 309,614 | 465,952 |
| Charge for the year | 69,728 | 77,631 | 147,359 |
| Written back on disposal | (6,151) | (28,906) | (35,057) |
| Exchange and other adjustments | (19) | (333) | (352) |
| | <u>219,896</u> | <u>358,006</u> | <u>577,902</u> |
| As at 30th June, 1999 | | | |
| Net book value as at 30th June, 1999 | <u>4,388,907</u> | <u>319,001</u> | <u>4,707,908</u> |
| Net book value as at 30th June, 1998 | <u>2,787,927</u> | <u>307,166</u> | <u>3,095,093</u> |

The analysis of net book value of premises is as follows:

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|------------------|------------------|
| In Hong Kong | | |
| - Leasehold with over 50 years unexpired | 1,619,202 | 1,631,611 |
| - Leasehold with 10 years to 50 years unexpired | 2,626,654 | 1,009,088 |
| Outside Hong Kong | | |
| - Freehold | 72,675 | 74,550 |
| - Leasehold with over 50 years unexpired | 2,658 | 11,935 |
| - Leasehold with 10 years to 50 years unexpired | 67,718 | 60,743 |
| | <u>4,388,907</u> | <u>2,787,927</u> |

The analysis of cost and valuation of premises is as follows:

| | | |
|---|------------------|------------------|
| At cost | 2,154,824 | 478,261 |
| At directors' valuation in October 1993 | 2,453,979 | 2,466,004 |
| | <u>4,608,803</u> | <u>2,944,265</u> |

All other fixed assets are stated at cost.

Notes on the Accounts

22. AMOUNTS DUE FROM AND DUE TO THE ULTIMATE HOLDING COMPANY AND FELLOW SUBSIDIARIES

- (a) Included in the following balance sheet captions are balances due to the ultimate holding company detailed as follows:

| | The Group | | The Company | |
|---|------------------|------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Current, fixed, savings and other deposits of customers | 238,916 | 295,913 | - | - |
| Other accounts and provisions | 289 | 804 | - | - |
| | <u>239,205</u> | <u>296,717</u> | <u>-</u> | <u>-</u> |

- (b) Included in the following balance sheet captions are balances due from and due to fellow subsidiaries detailed as follows:

| | The Group | | The Company | |
|---|------------------|------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| Other assets | 10,087 | 9,152 | - | - |
| Held to maturity securities and investment securities | 9,000 | 9,000 | - | - |
| | <u>19,087</u> | <u>18,152</u> | <u>-</u> | <u>-</u> |
| Current, fixed, savings and other deposits of customers | 216,811 | 438,176 | - | - |
| Other accounts and provisions | 21,048 | 25,742 | - | - |
| | <u>237,859</u> | <u>463,918</u> | <u>-</u> | <u>-</u> |

23. 7.75% FIXED RATE SUBORDINATED NOTES

The 7.75% fixed rate subordinated notes ("Notes") with aggregate principal amount of US\$350 million were issued by a subsidiary, Dao Heng Bank Limited ("DHB") on 24th January, 1997. The Notes will mature on 24th January, 2007. Interest is payable on 24th January and 24th July of each year, commencing 24th July, 1997.

During the year, DHB repurchased US\$81,380,000 of the Notes which were subsequently cancelled. The profit on repurchase has been included in the profit and loss account as "Other operating income". As at 30th June, 1999, the outstanding amount of the Notes issued by DHB is US\$268,620,000 (1998 : US\$350,000,000).

Notes on the Accounts

24. MATURITY PROFILE

| | The Group 1999 | | | | | | |
|---|------------------------|---------------------|---|--|-------------------|------------------|--------------------|
| | Repayable on demand | 3 months or less | 1 year or less but over 3 months | 5 years or less but over 1 year | After 5 years | Undated | Total |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Assets | | | | | | | |
| - Cash and short-term funds | 773,680 | 33,347,815 | 4,645,119 | - | - | - | 38,766,614 |
| - Placements with banks and other financial institutions maturing between one and twelve months | - | 7,258,073 | 839,927 | - | - | - | 8,098,000 |
| - Certificates of deposit held | - | - | 113,989 | 1,608,871 | - | - | 1,722,860 |
| - Other investments in securities - debt securities | - | 310,286 | 443,902 | 1,427,072 | 38,344 | - | 2,219,604 |
| - Advances to customers | 4,923,877 | 6,991,568 | 4,455,523 | 14,859,065 | 33,601,483 | 1,591,123 | 66,422,639 |
| - Held to maturity securities - debt securities | - | 710,757 | 1,355,461 | 6,276,281 | 1,345,123 | - | 9,687,622 |
| - Investment securities - debt securities | - | 15,536 | - | 87,525 | 19,081 | 6,286 | 128,428 |
| | <u>5,697,557</u> | <u>48,634,035</u> | <u>11,853,921</u> | <u>24,258,814</u> | <u>35,004,031</u> | <u>1,597,409</u> | <u>127,045,767</u> |
| Liabilities | | | | | | | |
| - Deposits and balances of banks and other financial institutions | 222,093 | 4,099,564 | - | 115,991 | - | - | 4,437,648 |
| - Current, fixed, savings and other deposits of customers | 11,810,743 | 73,832,983 | 7,294,463 | 133,273 | - | - | 93,071,462 |
| - Certificates of deposit issued | - | 623,273 | 5,670,568 | 1,175,332 | - | - | 7,469,173 |
| - 7.75% Fixed rate subordinated notes | - | - | - | - | 2,083,820 | - | 2,083,820 |
| | <u>12,032,836</u> | <u>78,555,820</u> | <u>12,965,031</u> | <u>1,424,596</u> | <u>2,083,820</u> | <u>-</u> | <u>107,062,103</u> |

Notes on the Accounts

24. MATURITY PROFILE (CONT'D)

| | The Group 1998 | | | | | | |
|--|------------------------|---------------------|---|--|-------------------|----------------|--------------------|
| | Repayable on demand | 3 months or less | 1 year or less but over 3 months | 5 years or less but over 1 year | After 5 years | Undated | Total |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Assets | | | | | | | |
| - Cash and short-term funds | 1,473,497 | 39,485,616 | 824,097 | - | - | - | 41,783,210 |
| - Placements with banks and other financial institutions maturing between one and twelve months | - | 1,234,498 | 965,172 | - | - | - | 2,199,670 |
| - Certificates of deposit held | - | - | 234,159 | 1,457,142 | - | - | 1,691,301 |
| - Other investments in securities - debt securities | - | - | 133,004 | 551,343 | 17,370 | - | 701,717 |
| - Advances to customers | 6,810,839 | 9,102,270 | 4,583,310 | 14,232,386 | 30,175,722 | 967,183 | 65,871,710 |
| - Held to maturity securities - debt securities | - | 100,724 | 1,138,191 | 4,619,879 | 1,337,824 | - | 7,196,618 |
| - Investment securities - debt securities | - | - | 27,363 | 45,791 | 39,836 | 6,286 | 119,276 |
| | <u>8,284,336</u> | <u>49,923,108</u> | <u>7,905,296</u> | <u>20,906,541</u> | <u>31,570,752</u> | <u>973,469</u> | <u>119,563,502</u> |
| Liabilities | | | | | | | |
| - Deposits and balances of banks and other financial institutions | 453,286 | 6,083,708 | - | - | - | - | 6,536,994 |
| - Current, fixed, savings and other deposits of customers | 8,787,153 | 69,718,733 | 6,794,749 | 153,781 | - | - | 85,454,416 |
| - Certificates of deposit issued | - | 751,239 | 2,739,760 | 4,242,275 | - | - | 7,733,274 |
| - 7.75% Fixed rate subordinated notes | - | - | - | - | 2,711,975 | - | 2,711,975 |
| | <u>9,240,439</u> | <u>76,553,680</u> | <u>9,534,509</u> | <u>4,396,056</u> | <u>2,711,975</u> | <u>-</u> | <u>102,436,659</u> |

25. MATERIAL RELATED PARTY TRANSACTIONS

(a) Transactions with ultimate holding company and fellow subsidiaries

During the year, the Group entered into a number of transactions in the normal course of business with its ultimate holding company and fellow subsidiaries including deposit and correspondent banking transactions. The contracts were priced based on relevant market rates at the time of each transaction, and were under the same terms as those available to the independent counterparties and customers of the Group.

Notes on the Accounts

25. MATERIAL RELATED PARTY TRANSACTIONS (CONT'D)

(a) Transactions with ultimate holding company and fellow subsidiaries (Cont'd)

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

| (i) Income and expenses for the year ended 30th June, 1999 | The Group HK\$'000 |
|--|-----------------------|
| Interest income | 85 |
| Interest expense | 48,443 |
| Other income | 157 |
| Other expenses | 23,897 |

(ii) Balances as at 30th June, 1999

Details of balances due from and due to ultimate holding company and fellow subsidiaries are set out in Note 22 "Amounts due from and due to the ultimate holding company and fellow subsidiaries".

(iii) Staff retirement benefit scheme

The Group's ultimate holding company, Guoco Group Limited, maintains a staff retirement scheme in which the investment manager is a fellow subsidiary and the administrator is a subsidiary. During the year ended 30th June, 1999, the Group made a total contribution of HK\$57.5 million to the scheme.

(b) Transactions with companies in the Hong Leong Company (Malaysia) Berhad Group ("HLCM")

(i) Banking transactions

During the year, the Group entered into a number of transactions in the normal course of business with companies in the HLCM Group including deposit and correspondent banking transactions. The contracts were priced based on relevant market rates at the time of each transaction, and were under the same terms as those available to the independent counterparties and customers of the Group.

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

| Income and expenses for the year ended 30th June, 1999 | The Group HK\$'000 |
|--|-----------------------|
| Interest expense | 1,717 |
| Balance as at 30th June, 1999 | |
| | The Group HK\$'000 |
| Current, fixed, savings and other deposit of customers | 12,156 |

Notes on the Accounts

25. MATERIAL RELATED PARTY TRANSACTIONS (CONT'D)

(b) Transactions with companies in the Hong Leong Company (Malaysia) Berhad Group ("HLCM")
(Cont'd)

(ii) Management fee

Dao Heng Bank Limited has entered into management services agreements, which may be terminated by either party giving six months' notice in writing, with Hong Leong Overseas (H.K.) Limited ("HLO"), a subsidiary of HLCM, for the provision of certain senior executives and other management services to the Group by HLO. Total management fees (mainly an annual fee equal to three percent of the consolidated profit before tax of the Group) paid and payable to HLO for the year ended 30th June, 1999 amounted to HK\$42.3 million.

(c) Transactions with jointly controlled entity

The Group maintains an interest free shareholders' loan to the jointly controlled entity, Hutchision Dao Heng Card Limited ("HDHCL") (formerly known as Hutchision OTB Card Limited). The loan balance as at 30th June, 1999 amounted to HK\$15 million.

Deposit taken from the jointly controlled entity as at 30th June, 1999 amounted to HK\$440 million. Interest expense for the year ended 30th June, 1999 payable to HDHCL amounted to HK\$40 million. Gross management fee income from HDHCL to the Group for the year ended 30th June, 1999 amounted to HK\$112 million. The transactions were priced based on relevant market rates at the time of each transaction, and were under the normal commercial terms.

(d) Transactions with key management personnel

Transactions with key management personnel of the Group include their close family members and companies controlled or significantly influenced by them. However, an entity having one or more common directors with the Group would not be regarded as a related party of the Group unless these directors would at least be able to significantly influence the policies of the entity and the Group in their mutual dealings.

Loans and credit card advances balances as at 30th June, 1999 for key management personnel of the Group amounted to HK\$25,947,000, 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 30th June, 1999 amounted to HK\$1 million.

Notes on the Accounts

26. SHARE CAPITAL

| | The Company | |
|--|------------------|------------------|
| | 1999 | 1998 |
| | HK\$'000 | HK\$'000 |
| Authorised: | | |
| 2,000,000,000 shares of US\$0.50 each | <u>7,724,500</u> | <u>7,724,500</u> |
| Issued and fully paid: | | |
| 693,288,200 (1998 : 695,012,500) shares of US\$0.50 each | <u>2,678,346</u> | <u>2,685,007</u> |

During the year, the Company repurchased a total of 2,394,500 shares (1998 : 4,987,500 shares) of US\$0.50 each of the Company on The Stock Exchange of Hong Kong Limited.

The details of share repurchases are as follows:

| Month-Year | Number of shares repurchased | Highest price paid HK\$ | Lowest price paid HK\$ | Total paid HK\$'000 |
|-------------------------------------|------------------------------------|-------------------------------|------------------------------|------------------------|
| August 1998 | 996,000 | 8.00 | 6.70 | 7,209 |
| September 1998 | 1,398,500 | 7.45 | 6.80 | <u>9,792</u> |
| | | | | 17,001 |
| Total expenses on share repurchases | | | | <u>90</u> |
| | | | | <u>17,091</u> |

The repurchased shares were cancelled by the Company and accordingly the issued share capital of the Company was reduced by the nominal value of these shares.

An amount equivalent to the difference between consideration paid and nominal value of the cancelled shares was charged to share premium account.

Share Option Scheme :

A Share Option Scheme ("Scheme") was adopted by the Company on 22nd November, 1993 under which eligible employees (including directors) of the Group are entitled to the grant of share options for subscription of shares in the Company.

Options were granted in respect of a total of 20,135,000 ordinary shares under the Scheme to various directors and executives of the Company. Such options are exercisable at the subscription price of HK\$21.82 per share during the period from 15th April, 1998 to 15th July, 2002.

During the year, 670,200 share options were exercised to subscribe for 670,200 shares in the Company at a consideration (net of charges) of HK\$14,616,439, of which HK\$2,589,151 was credited to share capital and the balance of HK\$12,027,288 was credited to the share premium account. At 30th June, 1999, 19,464,800 share options were outstanding.

Notes on the Accounts

27. RESERVES

| | The Group | | The Company | |
|---|------------------|------------------|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 | 1999 HK\$'000 | 1998 HK\$'000 |
| (a) Share premium | | | | |
| As at 1st July | 2,382,871 | 2,421,333 | 2,385,871 | 2,424,333 |
| Repurchase of own shares | (7,841) | (38,462) | (7,841) | (38,462) |
| Exercise of share option scheme | 12,027 | – | 12,027 | – |
| As at 30th June | <u>2,387,057</u> | <u>2,382,871</u> | <u>2,390,057</u> | <u>2,385,871</u> |
| (b) Revaluation reserve | | | | |
| As at 1st July and 30th June | <u>633,660</u> | <u>633,660</u> | – | – |
| (c) General reserve | | | | |
| As at 1st July and 30th June | <u>828,039</u> | <u>828,039</u> | – | – |
| (d) Contributed surplus | | | | |
| As at 1st July and 30th June | <u>149,981</u> | <u>149,981</u> | <u>150,581</u> | <u>150,581</u> |
| (e) Retained earnings | | | | |
| As at 1st July (as previously reported) | 4,414,926 | 3,863,591 | 70,830 | 67,106 |
| Change in accounting policy with respect to investments in securities | (20,496) | – | – | – |
| As at 1st July (as restated) | <u>4,394,430</u> | <u>3,863,591</u> | <u>70,830</u> | <u>67,106</u> |
| Retained profit for the year | 579,026 | 630,958 | 1,934 | 3,724 |
| Exchange difference on translation of net investment in overseas branches, subsidiaries and associated companies | 6,294 | (100,119) | – | – |
| As at 30th June | <u>4,979,750</u> | <u>4,394,430</u> | <u>72,764</u> | <u>70,830</u> |
| | <u>8,978,487</u> | <u>8,388,981</u> | <u>2,613,402</u> | <u>2,607,282</u> |

Notes on the Accounts

28. OFF-BALANCE SHEET EXPOSURES

(a) Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liabilities and commitments :

| | The Group | |
|---|-------------------|-------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Direct credit substitutes | 510,484 | 814,919 |
| Transaction-related contingencies | 245,273 | 43,006 |
| Trade-related contingencies | 1,962,689 | 2,444,611 |
| Other commitments with an original maturity of under 1 year or which are unconditionally cancellable | 19,683,803 | 26,047,575 |
| Others | – | 947,072 |
| | <u>22,402,249</u> | <u>30,297,183</u> |

(b) Financial contracts

Financial contracts represent contracts whose value depends on the value of one or more underlying assets or indices.

The following is a summary of the notional amounts of each significant type of financial contracts entered into by the Group.

| | The Group | |
|-------------------------|-------------------|-------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Exchange rate contracts | | |
| Spot and forwards | 4,233,897 | 2,471,452 |
| Swaps | 24,489,981 | 15,573,042 |
| Options purchased | 29,703 | 8,920 |
| Options written | 29,703 | 8,920 |
| Interest rate contracts | | |
| Forwards and futures | 1,269,599 | – |
| Swaps | 10,961,582 | 2,424,707 |
| Options purchased | 7,830 | – |
| Options written | 67,334 | – |
| | <u>41,089,629</u> | <u>20,487,041</u> |

Exchange rate swap contracts and interest rate swap contracts with notional principal of HK\$19,572 million (1998: HK\$12,579 million) and HK\$2,680 million (1998: HK\$50 million) respectively were made for trading purposes. The above financial instruments include transactions that are initiated in response to customer demands. No other significant positions are maintained by the Group.

Notes on the Accounts

28. OFF-BALANCE SHEET EXPOSURES (CONT'D)

(b) Financial contracts (Cont'd)

The replacement costs and credit risk-weighted amounts of the above off-balance sheet exposures are as follows. These amounts do not take into account the effects of bilateral netting arrangements.

| | 1999 | | 1998 | |
|--|------------------------------|---|------------------------------|---|
| | Replacement cost HK\$'000 | Credit risk-weighted amount HK\$'000 | Replacement cost HK\$'000 | Credit risk-weighted amount HK\$'000 |
| Contingent liabilities and commitments | - | 912,877 | - | 2,102,299 |
| Exchange rate contracts | 63,687 | 81,376 | 74,077 | 57,353 |
| Interest rate contracts | 36,202 | 12,540 | 34,437 | 8,823 |
| | <u>99,889</u> | <u>1,006,793</u> | <u>108,514</u> | <u>2,168,475</u> |

The tables above give the contractual or notional amounts, replacement costs and credit risk-weighted amounts of off-balance sheet transactions. These are assessed in accordance with the Hong Kong Monetary Authority's guidelines which implement the Basle agreement on capital adequacy and depend on the status of the counterparty and the maturity characteristics.

The risk weights used range from 0% to 100% for contingent liabilities and commitments, and from 0% to 50% for exchange rate and interest rate contracts. Replacement cost represents the cost of replacing all contracts which have a positive value when marked to market. The credit risk-weighted amount refers to the amount as computed in accordance with the Third Schedule to the Hong Kong Banking Ordinance.

Contingent liabilities and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. Since a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

Off-balance sheet financial instruments arise from forward, future swap and option transactions undertaken by the Group in the foreign exchange, interest rate and equity markets.

The notional amounts of these instruments indicate the volume of transactions outstanding at the balance sheet date. They do not represent amounts at risk.

Notes on the Accounts

28. OFF-BALANCE SHEET EXPOSURES (CONT'D)

(c) Capital commitments

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

| | The Group | |
|---|------------------|------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Expenditure authorised and contracted for | 75,500 | 100,467 |
| Expenditure authorised but not contracted for | 61,114 | 48,679 |
| | <u>136,614</u> | <u>149,146</u> |

(d) Lease commitments

Commitments under non-cancellable operating leases to make payments in the next year are as follows:

| | The Group | | | |
|---------------------------------|------------------------|--------------------|------------------------|--------------------|
| | 1999 | | 1998 | |
| | Properties HK\$'000 | Others HK\$'000 | Properties HK\$'000 | Others HK\$'000 |
| Leases expiring | | | | |
| Within 1 year | 11,559 | 8,469 | 23,575 | 3,157 |
| After 1 year but within 5 years | 36,591 | 4,116 | 23,434 | 1,952 |
| After 5 years | 1,806 | 39 | 677 | – |
| | <u>49,956</u> | <u>12,624</u> | <u>47,686</u> | <u>5,109</u> |

Notes on the Accounts

29. (a) Reconciliation of operating profit on ordinary activities to net cash inflow from operating activities

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|------------------|------------------|
| Operating profit on ordinary activities | 1,386,254 | 1,438,987 |
| Provisions for bad and doubtful loans and advances | 856,761 | 534,895 |
| Depreciation | 147,359 | 117,306 |
| (Write-back)/provision for diminution in value of investment securities | (323) | 3,678 |
| Advances written off net of recoveries | (504,449) | (242,116) |
| Loss on disposal of fixed assets | 6,691 | 2,021 |
| Profit on disposal of held to maturity securities | (46,925) | (4,328) |
| Loss on disposal of debt securities–investment securities | – | 45 |
| Amortisation of discount of held to maturity securities | (118,320) | (190,496) |
| Amortisation of premium of debt securities–investment securities | 368 | 268 |
| Loss on disposal of equity investments–investment securities | – | 897 |
| Profit on disposal of 7.75% fixed rate subordinated notes | (181,066) | – |
| Dividend income from equity investments–investment securities | (3,811) | (3,579) |
| Interest expense for certificates of deposit issued | 574,690 | 573,932 |
| Interest expense for 7.75% fixed rate subordinated notes | 174,559 | 208,865 |
| Net cash inflow from trading activities | 2,291,788 | 2,440,375 |
| Net decrease in money at call and short notice (repayable beyond three months) | 268,969 | 673,767 |
| Net (increase)/decrease in treasury bills (repayable beyond three months)–other investments | (187,474) | 1,021,411 |
| Net (increase)/decrease in placements with banks and other financial institutions (repayable beyond three months) | (2,136,625) | 1,473,249 |
| Net increase in certificates of deposit held–other investments | (31,423) | (1,018,613) |
| Net (increase)/decrease in other investments in securities | (1,533,930) | 236,514 |
| Net increase in advances to customers | (550,929) | (478,644) |
| Net increase in other assets | (172,921) | (72,530) |
| Net (decrease)/increase in deposits and balances of banks and other financial institutions | (2,099,346) | 1,536,839 |
| Net increase/(decrease) in current, fixed, savings and other deposits of customers | 7,617,046 | (5,820,129) |
| Net increase in other accounts and provisions | 3,580,882 | 975,161 |
| Exchange and other adjustments | 89,036 | (69,611) |
| Net cash inflow from operating activities | <u>7,135,073</u> | <u>897,789</u> |

Notes on the Accounts

29. (b) Analysis of changes in financing during the year

| | Share capital including share premium HK\$'000 | Certificates of deposit issued HK\$'000 | 7.75% Fixed rate subordinated notes HK\$'000 | Minority interest HK\$'000 |
|--|---|--|--|----------------------------------|
| Balance as at 1st July, 1998 | 5,067,878 | 7,733,274 | 2,711,975 | 130,576 |
| Cash inflow from financing | 14,616 | 5,692,713 | – | 40,590 |
| Cash outflow from financing | (17,091) | (5,956,915) | (449,425) | – |
| Minority interests' share of loss | – | – | – | (17,713) |
| Profit upon early redemption | – | – | (181,066) | – |
| Effect of foreign exchange movement | – | 101 | 2,336 | 13,503 |
| Balance as at 30th June, 1999 | 5,065,403 | 7,469,173 | 2,083,820 | 166,956 |

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

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|-------------------|-------------------|
| Cash and balances with banks and other financial institutions | 773,680 | 1,473,497 |
| Money at call and short notice repayable within three months | 20,819,631 | 17,394,428 |
| Placements with banks and other financial institutions repayable within three months | 4,751,461 | 989,756 |
| Treasury bills repayable within three months | 11,107,044 | 21,671,627 |
| Debt securities repayable within three months | 269,708 | – |
| | 37,721,524 | 41,529,308 |

30. ASSETS SUBJECT TO SALE AND REPURCHASE TRANSACTIONS

| | The Group | |
|--|-------------------|-------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Total assets subject to sale and repurchase transactions | 16,316,104 | 16,156,311 |

The above amount is mainly made up of items included in "Treasury Bills" totalling HK\$14,468 million (1998: HK\$15,773 million).

Notes on the Accounts

30. ASSETS SUBJECT TO SALE AND REPURCHASE TRANSACTIONS (CONT'D)

The Group has the following liabilities subject to sale and repurchase transactions:

| | The Group | |
|---|-------------------|-------------------|
| | 1999 | 1998 |
| | HK\$'000 | HK\$'000 |
| Deposits and balances of banks and other financial institutions | 1,278,219 | 3,282,193 |
| Current, fixed, savings and other deposits of customers | 4,648,682 | 7,573,657 |
| Other accounts and provisions | 10,224,047 | 6,530,029 |
| | <u>16,150,948</u> | <u>17,385,879</u> |

31. STAFF RETIREMENT SCHEME

The Group operates a non-contributory defined contribution provident fund scheme (the "Scheme") which benefits are paid on retirement or on leaving employment. Contributions to the defined contribution scheme are charged to the profit and loss account for the year. The assets of the Scheme are held separately from those of the Group in independently administered funds. The contributions are made by the Group based on 10% of employees' monthly salaries. The Group's contribution to the Scheme may be reduced by contributions forfeited by those employees who leave the Scheme prior to vesting fully in the contributions. The amount so utilised in the course of the year ended 30th June, 1999 was HK\$4 million (1998 : HK\$4 million) and the amount available for such use as at 30th June, 1999 was HK\$12 million (1998 : HK\$12 million).

32. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year's presentation.

33. POST BALANCE SHEET EVENT

A conditional sale and purchase agreement was entered into on 27th September, 1999 between Dao Heng Bank Limited ("DHB"), a wholly-owned subsidiary of the Company and Supreme Goal Investments Limited ("SGIL"), a fellow subsidiary company in respect of the purchase by DHB from SGIL of the property situated at 16th, 17th and 18th Floors, The Center, 99 Queen's Road Central, Hong Kong for a cash consideration of HK\$481 million.

34. ULTIMATE HOLDING COMPANY

The directors consider the ultimate holding company as at 30th June, 1999 to be Guoco Group Limited, incorporated in Bermuda.

Unaudited Supplementary Financial Information

(a) Capital adequacy and liquidity ratios

(i) Capital adequacy ratios

| | 1999 HK\$'000 | 1998 HK\$'000 |
|---|-------------------|-------------------|
| Total Tier I capital | 10,997,812 | 10,417,707 |
| Total Tier II capital | 3,330,334 | 3,983,958 |
| Total Tier I and Tier II capital before deductions | 14,328,146 | 14,401,665 |
| Deductions | (45,768) | (50,529) |
| Total Tier I and Tier II capital after deductions | <u>14,282,378</u> | <u>14,351,136</u> |
| Total risk-weighted assets | <u>64,721,912</u> | <u>66,726,073</u> |
| Total risk-weighted assets adjusted for market risk | <u>64,807,662</u> | <u>66,791,020</u> |
| Capital adequacy ratios as at 30th June | | |
| Before adjusting for market risk | | |
| Tier I (%) | <u>16.99</u> | <u>15.61</u> |
| Tier I and Tier II (after deductions) (%) | <u>22.07</u> | <u>21.51</u> |
| After adjusting for market risk | | |
| Tier I (%) | <u>16.97</u> | <u>15.60</u> |
| Tier I and Tier II (after deductions) (%) | <u>22.04</u> | <u>21.49</u> |

The unadjusted capital adequacy ratio is computed on the consolidated basis as required by the Hong Kong Monetary Authority for its regulatory purposes, and is in accordance with the Third Schedule to the Hong Kong Banking Ordinance.

The adjusted capital adequacy ratio which takes into account market risk as at the balance sheet date is computed in accordance with the Guideline "Maintenance of Adequate Capital against Market Risks" issued by the Hong Kong Monetary Authority and on the same consolidated basis as for unadjusted capital adequacy ratio.

(ii) Liquidity ratios

| | 1999 | 1998 |
|--|--------------|--------------|
| Average liquidity ratio for the year (%) | <u>51.51</u> | <u>44.93</u> |

The average liquidity ratio for the year is the simple average of each calendar month's average liquidity ratio, which is computed for Hong Kong offices of Dao Heng Bank Limited, and is in accordance with the Fourth Schedule to the Hong Kong Banking Ordinance.

Unaudited Supplementary Financial Information

(b) Segmental information

(i) By geographical area

The information concerning geographical analysis has been classified by the location of the principal operations of the subsidiaries, associated companies and jointly controlled entity, or in the case of the authorised institution itself, of the location of the branches responsible for reporting the results or booking the assets.

| | The Group | | | |
|----------------|--|--------------------|--|--------------------|
| | 1999 | Total | 1998 | Total |
| | Profit before taxation HK\$'000 | assets HK\$'000 | Profit before taxation HK\$'000 | assets HK\$'000 |
| Hong Kong | 1,381,048 | 126,999,478 | 1,319,504 | 117,654,209 |
| United Kingdom | 11,894 | 2,903,057 | 20,038 | 2,925,849 |
| Others | 1,719 | 1,973,778 | 105,926 | 2,354,184 |
| | <u>1,394,661</u> | <u>131,876,313</u> | <u>1,445,468</u> | <u>122,934,242</u> |

(ii) By class of business

| | The Group | | | |
|-------------------------------------|--|--------------------|--|--------------------|
| | 1999 | Total | 1998 | Total |
| | Profit before taxation HK\$'000 | assets HK\$'000 | Profit before taxation HK\$'000 | assets HK\$'000 |
| Commercial & retail banking | 1,024,148 | 80,805,278 | 1,118,004 | 86,073,609 |
| Treasury | 356,900 | 46,194,200 | 201,500 | 31,580,600 |
| Overseas branches & subsidiaries | 13,613 | 4,876,835 | 125,964 | 5,280,033 |
| | <u>1,394,661</u> | <u>131,876,313</u> | <u>1,445,468</u> | <u>122,934,242</u> |

Commercial & retail banking business mainly comprises deposit account services, residential mortgage and other consumer lending, 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, management of investment securities and trading activities and the overall funding of the Banking Group.

Unaudited Supplementary Financial Information

(c) Advances to customers - by industry sectors

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

| | The Group | |
|--|-------------------|-------------------|
| | 1999 HK\$'000 | 1998 HK\$'000 |
| Loans for use in Hong Kong | | |
| Industrial, commercial and financial | | |
| - Property development | 252,554 | 227,720 |
| - Property investment | 8,380,394 | 10,763,383 |
| - Financial concerns | 441,113 | 1,003,071 |
| - Stockbrokers | 30,699 | 56,188 |
| - Wholesale and retail trade | 2,154,102 | 2,669,365 |
| - Manufacturing | 2,336,640 | 2,754,179 |
| - Transport and transport equipment | 6,114,306 | 6,687,466 |
| - Others | 2,671,154 | 3,470,381 |
| Individuals | | |
| - Loans for the purchase of flats in the Home Ownership Scheme and Private Sector Participation Scheme | 2,307,003 | 2,050,113 |
| - Loans for the purchase of other residential properties | 27,450,357 | 19,957,107 |
| - Credit card advances | 3,145,170 | 3,245,509 |
| - Others | 2,707,144 | 3,110,383 |
| | 57,990,636 | 55,994,865 |
| Trade finance | 5,557,075 | 6,772,352 |
| Loans for use outside Hong Kong | 2,874,928 | 3,104,493 |
| | <u>66,422,639</u> | <u>65,871,710</u> |

(d) Overdue and rescheduled advances to customers

(i) Overdue advances to customers

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

| | The Group | | | |
|--|------------------|------------------------|------------------|------------------------|
| | 1999 HK\$'000 | % of Total Advances | 1998 HK\$'000 | % of Total Advances |
| Six months or less but over three months | 638,519 | 0.96 | 351,261 | 0.53 |
| One year or less but over six months | 1,103,992 | 1.66 | 193,853 | 0.29 |
| Over one year | 791,055 | 1.19 | 286,158 | 0.43 |
| | <u>2,533,566</u> | <u>3.81</u> | <u>831,272</u> | <u>1.25</u> |
| Market value of securities held against the secured advances | <u>2,281,959</u> | | <u>878,623</u> | |
| Secured overdue advances | 1,663,960 | | 502,608 | |
| Unsecured overdue advances | 869,606 | | 328,664 | |
| | <u>2,533,566</u> | | <u>831,272</u> | |
| Specific provisions made | <u>541,540</u> | | <u>258,040</u> | |

Unaudited Supplementary Financial Information

(ii) Rescheduled advances to customers

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

| | The Group | | | |
|----------------------|------------------|------------------------|------------------|------------------------|
| | 1999 HK\$'000 | % of Total Advances | 1998 HK\$'000 | % of Total Advances |
| Rescheduled advances | <u>1,060,955</u> | 1.60 | <u>251,130</u> | 0.38 |

(iii) Reconciliation of overdue advances to non-accrual advances :

| | 1999 HK\$'000 |
|--|------------------|
| Overdue advances to customers as per above (i) | 2,533,566 |
| Less: Advances which are overdue for more than Less: three months and on which interest is Less: still being accrued | (432,847) |
| Add: Advances which are overdue for three months or less and on which interest is being placed in suspense or on which interest accrual has ceased | 334,651 |
| Add: Advances which are not yet overdue and on which interest is being placed in suspense or on which interest accrual has ceased | <u>258,724</u> |
| Gross non-accrual advances | <u>2,694,094</u> |

(e) Risk management

Sound management of risk is fundamental to the business of banking and it is a high priority of the Group.

The Board and the Senior Management of the Group are responsible for establishing and maintaining a sound framework of policies and controls for identifying, evaluating, monitoring and controlling key risks pertaining to the Group's business. The key risks include credit risk, market risk, liquidity risk, capital management risk and operational risk. The management of business units and support functions are responsible for implementing the approved policies and procedures in achieving the Group's mission and objectives.

The risk related policies and controls are subject to regular review by the relevant business units, Risk Management Division and Senior Management based on changing customer needs and business conditions. Significant issues are reported to the Board and the Executive Committee. The internal and external auditors also conduct their independent reviews on the adequacy and effectiveness of these key policies and controls and report their opinions directly to the Senior Management and the Board as required.

(i) Credit risk management

Credit risk is the potential financial loss which can result from the failure of a counterparty to settle its financial and contractual obligations to the Group, as and when they are due.

The Group's Credit Policy Manual defines the credit extension criteria, the credit approval and monitoring processes, the loan classification system and provisioning policy. It also takes into account the regulatory requirements in countries in which the Group operates.

Unaudited Supplementary Financial Information

The Group manages its credit risk within a prudent framework of lending policy and controls. This includes:

- The staffing of key lending positions by experienced and skilled officers;
- The establishment of comprehensive lending policies and practices as approved by Senior Management;
- A thorough evaluation of the creditworthiness of the counterparties which generally covers the viability of the financing proposals, management, financial condition, quality of security, repayment capacity and industry outlook. Accounts are reviewed at least annually;
- The independent review and approval of credit applications by management, the Management Credit Committee, or the Board Credit Committee, are in accordance with the delegated authorities. The Credit Committees also review and, in some cases, approve important changes to the Group's lending policy, exposures, asset quality, problem loans and provisions on a regular basis;
- Daily independent monitoring and control of credit limit excesses by the centralized credit control which enables effective identification and management of existing and potential problem loans;
- Independent and central management of delinquent accounts and workouts by the Special Assets Management Unit;
- Maintenance of a diversified portfolio by industries and borrowers to minimize concentration risk;
- Independent review of credits and processes by specialized Credit Inspection Teams of the Group Internal Audit Division.

(ii) Liquidity management

Liquidity risk arises when the Group's cashflow is insufficient to meet the Group's obligations as they fall due. This shortfall may be due to a shortage of funding, inappropriate mismatching of cashflows, losses, even risk and other factors. The Group measures and monitors its liquidity through maintenance of prudent ratios and funding policies approved by Senior Management and the Asset & Liability Committee (ALCO). These include the quality of assets and liabilities, the statutory liquidity ratio, the loan-to-deposit ratio, interest rate gaps, maintenance of diversified deposit sources and management of maturity profiles.

The Hong Kong offices of Dao Heng Bank Limited had an average liquidity ratio of 51.51% for the year ended 30th June, 1999, which was more than double the statutory minimum ratio of 25%.

A prudent level of realizable liquid assets is also maintained by the Group to meet unexpected and material cash requirements.

(iii) 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 risk reward criteria and regulatory requirements.

Unaudited Supplementary Financial Information

Both the Group's adjusted consolidated capital adequacy ratio incorporating market risk of 22.04% and the unadjusted ratio of 22.07% as at 30th June, 1999 were well above the statutory minimum ratio of 8%.

(iv) Market risk management

Market risk arises from the net effect of changes in interest rates, foreign exchange rates, securities, equities and commodity prices in the markets in which the Group operates.

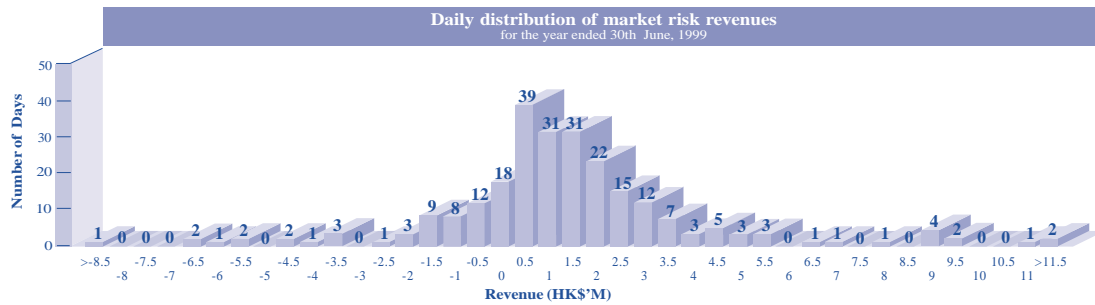
The Group's market risks originate from its holdings in the trading book of foreign exchange contracts, debt securities, equities and financial contracts. The Group's trading activities on financial contracts mainly arise from the execution of trade orders from customers and positions taken in order to hedge other elements of the trading book.

The Group's maximum market risk exposures in different activities are set by the Executive Committee and ALCO. Exposures are monitored against established limits and excesses are reported to Senior Management for necessary action. This reporting is independently reviewed by the internal auditors.

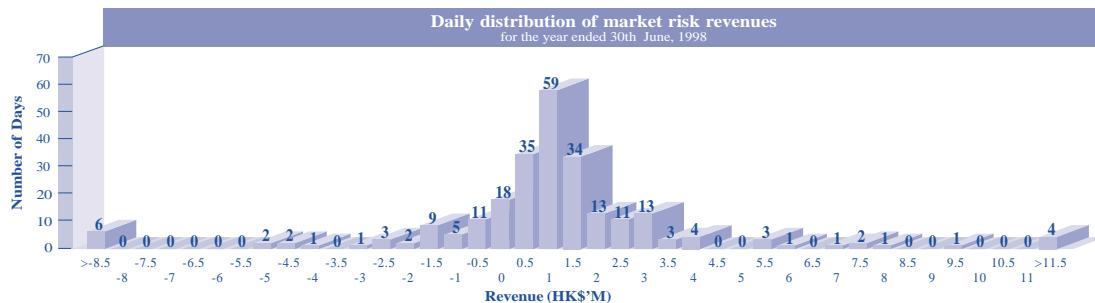
The average daily revenue earned from the Group's market risk related treasury activities for the year ended 30th June, 1999 was HK\$1.115 million and the standard deviation for such daily revenue was HK\$3.75 million.

The frequency distribution of daily revenue analysed by market-risk related treasury activities for the year ended 30th June, 1999 is shown below:

1999



1998



This shows a maximum daily loss of HK\$20 million and the next maximum daily loss of HK\$6.9 million, with 63 out of 246 days showing losses. The most frequent result was a daily revenue of between HK\$0.001 million to HK\$0.5 million with 39 occurrences. The highest daily revenue was HK\$37.7 million.

Unaudited Supplementary Financial Information

– Foreign exchange risk management

The Group's foreign exchange risk primarily arises from foreign exchange dealing, banking transactions and investments in the Group's overseas branches and subsidiaries. All foreign exchange positions are centrally managed by the Dao Heng Markets within the limits approved by the Management. Limit excesses, if any, are reported to Senior Management for necessary action.

The average daily foreign exchange trading profit for the year ended 30th June, 1999 was HK\$514,000.

The exchange rate risk of long-term foreign currency funding, to the extent that such funding is used to fund assets denominated in a different currency, is normally hedged by using interest rate and currency swaps or forward exchange agreements.

– Interest rate risk management

The Group's interest rate open positions arise from trading, investments and other normal banking activities. This risk primarily results from the timing differences in the re-pricing of interest-bearing assets and liabilities. It also relates to positions arising from non-interest bearing liabilities including current accounts, as well as from certain fixed rate loans and liabilities. The interest rate sensitive positions are managed by Dao Heng Markets under the limits approved by the Senior Management and ALCO.

The average daily revenue earned from treasury-related interest rate activities for the year ended 30th June, 1999 was HK\$601,000.

(v) Operational risk

Operational risk is the financial loss resulting from procedural errors, systems failures, frauds and other event risks.

It is the Group's policy to maintain adequate documentation of its operating procedures to facilitate training and quality performance. The systems and procedures are independently reviewed by internal auditors and approved by Senior Management. Supervisors and management exercise close supervision and control of operational activities to minimize the operational losses.



The Local Distribution Network of the Group

