

Management Discussion and Analysis

Banking

Net profit attributable to shareholders:	HK\$42.7mn	-19.2%
Total operating income:	HK\$323.4mn	-6.0%
Net interest income:	HK\$267.7mn	-7.3%
Other operating income:	HK\$55.7mn	+0.6%
Charge for bad and doubtful debts:	HK\$49.8mn	-47.0%
Loans and advances:	HK\$7.75bn	+0.8%
Customer deposits:	HK\$10.34bn	-7.9%

Net interest margin:	2.07%	(24 basis points lower than 2000)
Cost-to-income ratio:	63%	(13 percentage points higher than 2000)
Average liquidity ratio:	50%	(Average 2000: 53%)
Capital adequacy ratio:	20%	(end-2001)

Asia Commercial Bank experienced a very challenging operating environment, with fierce competition, generally weak loan demand from both the commercial and consumer sectors and very tight net interest margins during a period of higher costs.

This was the first full year of credit card operations, which helped support income from fees and commissions. The Bank also introduced Internet banking and the sale of the products of Hong Kong Life Insurance Limited, a joint venture of six local banks, during the year. Two consumer banking centres were opened as part of the planned expansion of business delivery outlets. The start-up costs in such areas as IT, marketing and personnel associated with these projects obviously affected the bottom line in 2001. This in turn explains the sharp increase in cost-income ratio. However, we are confident of positive returns from these activities in the future.

As well as expanding our consumer banking business in 2002, we plan to concentrate on productivity increases, the continued reduction of loan provisions through stronger credit control procedures, increased fee income and treasury operations, and prudent expansion of business in the Mainland. Assuming some degree of economic recovery in 2002, we expect satisfactory performance in the coming year.

Insurance

Net profit attributable to shareholders:	HK\$21.1mn	-56.5%
Underwriting profit:	HK\$26.7mn	+44.8%
Net investment loss and dividend income:	(HK\$13.0mn)	+1165.1%
Interest and other income:	HK\$45.0mn	-32.3%
Premium turnover:	HK\$449.1mn	+22.8%
Operating expenses:	HK\$53.5mn	-2.9%
Provision for bad debt:	HK\$5.7mn	N.A.

Management Discussion and Analysis (cont'd)

As the increase in underwriting profit shows, Asia Insurance's core business performed very well during 2001. The decline in net profit was the result of impairment provisions for the fall in value of strategic investments; we are hopeful that no further significant provisions will be needed in 2002.

The underwriting business benefited from both higher volumes and firmer pricing. Volumes increased for several reasons. We continued to expand our distribution network and agency force. We aggressively entered the field of professional indemnity insurance, for which we foresee very bright prospects. And we were able to increase market share as the overcrowded general insurance market in Hong Kong underwent some long overdue consolidation. On the pricing side, some premiums have finally started to return to more realistic levels, especially for such lines as motor and employee compensation coverage.

Asia Insurance maintained careful control of costs during the year, even though additional business required a small increase in staff numbers.

The Hong Kong general insurance industry remains beset with problems. There is still too much capacity in the market, and extremely high increases in reinsurance costs after the September terrorist attacks in the USA have created some uncertainties. However, Asia Insurance is in a very sound position. We hope to continue expanding our market share in traditional and speciality lines, and we expect to be able to maintain realistic pricing levels, attracting clients with high standards of service and the assurance of a Standard and Poor's A- rating. Being hopeful that no further provisions will eat into operating profit in the coming year, we expect Asia Insurance to make a significant contribution to the Group's profit growth in 2002.

Investment Services

Net loss attributable to shareholders:	(HK\$8.7mn)	N.A.
Total operating income:	HK\$61.0mn	-45.5%
Operating expenses:	HK\$49.9mn	-28.1%

The significant downturn in Asia Investment Services' results is largely a result of the effects of a major exceptional item in 2000. However, it also reflected the depressed state of the markets in 2001, which affected commission and fee income from brokering, financing and other activities. Weak corporate earnings also impaired Asia Investment Services' loans portfolio, and a significant provision for doubtful debts in 2001 resulted in the company reporting a loss.

Most markets in Asia suffered from weakness and low turnover during 2001, as it became apparent that the US and global economies were entering a slowdown and regional investors lowered their expectations of growth. In Hong Kong, in particular, retail investors were concerned about unemployment and continued negative inflation and preferred to stay in cash. As a result, Asia Investment Services' main activities, such as brokerage, futures and corporate finance, made relatively slim profits. Although the management continued to pay attention to expenses, scope for continued cost savings are relatively limited.

Management Discussion and Analysis (cont'd)

For the coming year, the fundamentals in much of the region, and especially in China, are generally positive. If regional markets reflect local as well as global factors, Asia Investment Services should see some improvement in results in the coming year.

Financial Resources

The Group's liquidity and financial resources remained in a healthy state during the year. There were no significant developments affecting either the financial resources or the capital structure of the Group.

Contingent Liabilities

As at 31st December, 2001, a corporate guarantee of HK\$355 million in aggregate was executed by the Company for banking facilities made available to the Group, which was utilised to the extent of HK\$60,000 at the balance sheet date.

An indemnity to the extent of HK\$600 million was executed by the Company in favour of a securities trading client of one of its subsidiary (the "Client") against any losses incurred by the Client, relating to that subsidiary not fulfilling its obligation to the Client or not complying with the Client's instructions in relation to certain particular securities trading transactions. As at 31st December, 2001, the Group had no transactions executed for the Client which are subject to the indemnity abovementioned.

The Securities and Futures Commission ("SFC") has conducted an investigation against Asia Financial (Assets Management) Limited ("AFAM") in respect of a breach of the Code on Takeovers and Mergers and may have a potential breach of the Securities Ordinance. In the opinion of the directors, the potential liabilities in relation to AFAM cannot be measured with sufficient reliability before the conclusion of this matter. Accordingly, no provision has been made in the financial statements.

Staff

The total number of employees of the Group was approximately 650 at the end of 2001, a 4.8% increase compared with the end of 2000. As with many companies in Hong Kong, the Group had to exercise tight control of operating costs during the year, and salary remuneration, compensation and benefits were kept closely in line with the market. However, we made every effort to ensure that we continued to offer competitive salaries and conditions in order to attract and retain good quality personnel. We also continued to ensure that adequate resources remained available for training. The dedication and hard work of our staff during 2001 is greatly appreciated.

