# Financial Review

## Group Summary

The results for the year ended 31 December 2002 reflect a strong performance with profit before tax up 16 per cent from $1,089 million to $1,262 million. Revenue momentum has been sustained despite tough market conditions, pressure on margins and a low interest rate environment. Costs have been reduced by $28 million without cutting investment in growth businesses and in re-engineering the Bank. Provisions for bad debts and contingent liabilities were $19 million lower, mainly due to tight control on risk in Wholesale Banking where new provisions were lower and recoveries were higher than in 2001.

The results were adversely impacted by increased Consumer Banking bad debts from bankruptcies in Hong Kong, the economic deterioration in Argentina in the first quarter and the difficult economic environment in Zimbabwe, but benefitted from a gain on the unwinding of a swap relating to the preference shares repurchased in December.

In February 2002 the Urgent Issues Task Force of the Accounting Standards Board (UITF) issued guidance on the application of accounting standards to capital instruments that have characteristics of both liabilities and shareholders' funds. The Group has complied with these requirements and as a result has reclassified its Trust Preferred Securities and Step-up Callable Perpetual Trust Preferred Securities from 'minority interests – non-equity' to 'liabilities' and moved the cost of this capital from 'minority interests – non-equity' to 'interest payable'. The prior year has been restated as follows:

| | 2001 | |
|---|---|---|
| | Net interest income $ million | Profit before tax $ million |
| As previously published | 2,959 | 1,148 |
| Transfer from minority interests to interest payable on: | | |
| €500 million issued March 2000 | (37) | (37) |
| £300 million issued May 2001 | (22) | (22) |
| As published 31 December 2002 | 2,900 | 1,089 |

If the changes caused by UITF33 had not applied, the Group's net taxable profit for 2002 would have been $1,337 million.

Revenue has grown by three per cent to $4,539 million and reflects strong momentum in Consumer Banking outside of Hong Kong. Total Group revenue has felt the impact of three significant factors in 2002. Firstly, the deliberate action taken to trade revenue to improve the risk profile of the business. Secondly, the deteriorating conditions and hyper-inflationary environment in Zimbabwe depressed revenue by $64 million. Thirdly, the Group unwound certain interest rate swaps hedging the $659 million of preference shares which were repurchased in December with a gain of $57 million.

Net interest income increased by six per cent driven largely by volume growth, lower funding costs and better spreads in Consumer Banking and strong earnings on asset and liability management in Wholesale Banking. The Group also benefitted by $57 million from the unwinding of interest rate swaps relating to the Group's preference shares which were repurchased in December. The Group's average interest earning assets rose by $2.9 billion compared to 2001, an increase of three per cent. Overall the average net interest margin was 3.1 per cent compared to 3.0 per cent in 2001.

Net fees and commissions receivable have increased by one per cent to $991 million compared to $977 million in 2001. The focus on a more sophisticated product set within Global Markets generated higher fees in the Americas and the United Kingdom. In Other Asia Pacific, India and MESA growth was largely in unsecured lending in Consumer Banking, offsetting the impact of bankruptcy containment actions in Hong Kong.

Dealing profits have fallen by $50 million or eleven per cent. Hong Kong, India and MESA performed well, increasing revenue by $22 million through strong trading. However, in addition to the hyper-inflationary adjustment and translation losses relating to Zimbabwe, lower spreads and reduced volumes in a number of countries led to a fall in revenue.

Total operating expenses were reduced by $28 million to $2,557 million compared to $2,585 million in 2001. The benefits of the centralisation and operational efficiency programmes continue and the integration of Grindlays has led to higher than targeted cost synergies. This improvement is despite a $41 million charge in Latin America as a result of refocusing the strategy, and has been achieved while continuing to invest for future growth. The cost income ratio for 2002 was 53.6 per cent, compared to 55.8 per cent in 2001 on a normalised basis.

The net provisions for bad and doubtful debts and contingent liabilities were $19 million lower than 2001 at $712 million. Wholesale Banking improved its position year on year by $292 million, despite a $75 million charge for Argentina. This was achieved through a pro-active focus on risk management and a strong performance on recoveries. Hong Kong bankruptcies accounted for much of the rise in Consumer Banking's bad debts with a charge of $287 million in 2002 compared to $121 million in 2001.

Post tax return on equity (normalised) was 13.4 per cent, up from 12.0 per cent in 2001. This has been achieved through growing high return businesses, cost efficiency and active capital management.

## Consumer Banking

Consumer Banking remains of prime importance to the Bank. Revenue has increased by nine per cent from $2,222 million in 2001 to $2,416 million in 2002, and costs have been reduced by five per cent to $1,190 million. The total debt charge has increased by $273 million to $603 million mainly due to the bankruptcy situation in Hong Kong. This reduced the operating profit by two per cent from $638 million to $623 million.

The following table provides an analysis of operating profit before tax by geographic segment for Consumer Banking. All regions excluding Hong Kong reported increased operating profit.

| | | | | | | | | | 2002 |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Consumer Banking Total $million |
| Revenue | 1,013 | 313 | 156 | 285 | 204 | 213 | 137 | 95 | 2,416 |
| Costs | (422) | (106) | (79) | (177) | (114) | (104) | (124) | (64) | (1,190) |
| Charge for debts | (434) | (35) | (22) | (58) | (38) | (16) | (3) | 3 | (603) |
| Operating profit | 157 | 172 | 55 | 50 | 52 | 93 | 10 | 34 | 623 |

| | | | | | | | | | 2001 |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Consumer Banking Total $million |
| Revenue | 1,040 | 250 | 139 | 210 | 190 | 179 | 131 | 83 | 2,222 |
| Costs | (474) | (95) | (77) | (171) | (132) | (108) | (122) | (75) | (1,254) |
| Charge for debts | (226) | (17) | (11) | (35) | (19) | (15) | (3) | (4) | (330) |
| Operating profit | 340 | 138 | 51 | 4 | 39 | 56 | 6 | 4 | 638 |

Hong Kong profits have fallen overall by 54 per cent from $340 million to $157 million. However, profits before bad debts have increased by four per cent. Market conditions continue to be difficult with rising unemployment, reduced margins and the bankruptcy problem affecting the whole industry. This has impacted revenue and bad debts. Revenue has fallen by three per cent largely because the Group took decisive and early action to mitigate bankruptcy risk in its unsecured portfolio. Revenues from cards and personal loans fell by twelve per cent, while revenues from Mortgages and Wealth Management grew by eight per cent. Growth in Mortgages was from improved margins and volume growth. Wealth Management delivered strong growth in fee-based income, partially offset by declining margins as a result of the low interest rate environment in response to lower revenues. Costs in Hong Kong have been strongly managed and have been reduced by $52 million.

Singapore has increased operating profit by 25 per cent and significantly increased its market share in secured and unsecured lending. This has been driven by lower funding costs, the successful launch of the innovative MortgageOne housing loan solution which offers debt consolidation, Liquidity Management and Wealth Management, and through leveraging Standard Chartered's Qualifying Full Banking licence.

### Consumer Banking continued

Other Asia Pacific increased profits twelve-fold from $4 million to $50 million. This was mainly due to the Group's investments in Taiwan and Thailand. Thailand benefited from higher volume and margin in credit cards and personal loans. Revenue in Taiwan increased substantially due to increased volumes from a successful mortgage campaign together with lower funding costs.

MESA increased operating profit by 66 per cent to $93 million and India by 33 per cent to $52 million. This was due to the growth in the business and the success of the Grindlays integration. In India, the mortgage portfolio doubled in size aided by the successful launch of MortgageOne.

Africa delivered operating profit of $10 million, an increase of $4 million from 2001. This was despite an extremely difficult environment in Zimbabwe. Improved fees and commissions contributed to this performance.

The Americas and the United Kingdom have increased profit from $4 million to U$34 million, mainly due to cost efficiencies arising from restructuring in 2001.

An analysis of revenue by product is set out below:

| | 2002 $million | 2001 $million |
|---|---|---|
| Cards/Personal Loans | **1,082** | 985 |
| Wealth Management/Deposits | **815** | 774 |
| Mortgages/Auto Finance | **492** | 395 |
| Other | **27** | 68 |
| | **2,416** | 2,222 |

There has been strong revenue growth in Credit Cards and Personal Loans of ten per cent, and they continue to make impressive returns. Lending outside of Hong Kong grew 20 per cent. Bankruptcy containment actions taken in Hong Kong offset growth elsewhere.

Wealth Management has performed well with revenues up by five per cent over 2001. This has been driven by growth in unit trust, treasury and bancassurance products which offset the impact of the lower interest rate environment.

Mortgages and Auto Finance revenue increased by 25 per cent. Mortgage outstandings grew by nine per cent aided by the successful implementation of MortgageOne Account in Singapore, Malaysia and India and E-Mortgage in Hong Kong. Margins improved in 2002.

Total costs in Consumer Banking have fallen by $64 million (five per cent) to $1,190 million, with $52 million of the reduction in Hong Kong. These savings are after taking account of accelerated investment in new sales platforms, rebranding and distribution channels. The MortgageOne product has been successfully rolled out and E-Mortgage developed in Hong Kong.

The net debt charge increased from $330 million to $603 million. This was largely driven by personal bankruptcies in Hong Kong. The data from the Official Receiver's Office shows that although petition rates appear to have stabilised they remain high and volatile. The charge off period for credit cards has been reduced from 150 days past due to 120 days past due in Hong Kong as a consequence of the market environment. Elsewhere the growth in bad debts reflects higher volumes, changes in the business mix and economic conditions.

Outside Hong Kong, trading profit growth of 56 per cent required incremental risk weighted assets of $2.4 billion, a 22 per cent increase, indicating that growth in Consumer Banking need not be capital intensive.

### Wholesale Banking

The Wholesale Banking business continues to be repositioned to focus on products which offer higher returns. The Group has deliberately traded revenue to improve the risk profile of the business and this is reflected in the results of 2002. Overall revenues fell by three per cent. However, operating profit has risen by 35 per cent due to the substantial reduction in the charge for debts. The debt charge has improved due to lower provisions and improved recoveries.

The following table provides an analysis of operating profit before tax by geographic segment:

| | Asia Pacific | | | | | | | | 2002 |
|---|---|---|---|---|---|---|---|---|---|
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Wholesale Banking Total $million |
| Revenue | 403 | 172 | 78 | 287 | 190 | 288 | 195 | 510 | 2,123 |
| Costs | (200) | (103) | (64) | (229) | (76) | (92) | (104) | (343) | (1,211) |
| Charge for debts, contingent liabilities and commitments | 6 | (6) | 9 | (3) | – | 3 | – | (118) | (109) |
| Amounts written off fixed asset investments | – | – | – | – | – | – | – | (8) | (8) |
| Operating profit | 209 | 63 | 23 | 55 | 114 | 199 | 91 | 41 | 795 |

| | Asia Pacific | | | | | | | | 2001 |
|---|---|---|---|---|---|---|---|---|---|
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Wholesale Banking Total $million |
| Revenue | 402 | 190 | 98 | 319 | 165 | 257 | 224 | 528 | 2,183 |
| Costs | (205) | (110) | (54) | (233) | (77) | (99) | (104) | (309) | (1,191) |
| Charge for debts, contingent liabilities and commitments | (31) | (34) | (119) | (51) | (8) | (24) | (10) | (124) | (401) |
| Operating profit | 166 | 46 | (75) | 35 | 80 | 134 | 110 | 95 | 591 |

Most regions have improved their results through focusing more closely on Global Markets, reduced costs and improved debt charges. Malaysia has generated an additional $98 million, MESA $65 million and Hong Kong $43 million. In MESA and India the improved performance was in part due to the integration of the Grindlays acquisition and higher volume growth and improved margins in Global Markets. In Africa, the reduction in revenue of $29 million was driven by hyper-inflationary adjustments in Zimbabwe.

The profit in the Americas and the United Kingdom has fallen from $95 million to $41 million. This is mainly due to a $75 million charge taken against Argentina in the first quarter of 2002, and costs associated with repositioning the business.

An analysis of revenue by product is set out below:

| | 2002 $million | 2001 $million |
|---|---|---|
| Trade and Lending | 775 | 849 |
| Global Markets | 973 | 914 |
| Cash Management | 315 | 355 |
| Custody | 60 | 65 |
| | 2,123 | 2,183 |

Trade and Lending revenues have fallen by nine per cent from $849 million to $775 million. The reduction in business is in line with the strategy to trade revenue for risk and to concentrate resources on Global Markets. This, together with weak market demand, has had an impact on results.

Global Markets revenue has increased by six per cent to $973 million. Asset and liability management is a significant component within Global Markets and the positions taken generated substantial revenues in the low interest rate environment, particularly in the first half of 2002. Revenue growth was also generated as the Group focused on higher return business.

Cash Management balances have grown significantly by 16 per cent but revenues have not improved as margins have declined as a result of the low interest rate environment. The reduction in Custody revenues by eight per cent reflects the decrease in equity activity as this business is driven by volume and equity values. However, partially offsetting this was additional revenue from winning new mandates.

Costs have risen by $20 million. Costs in 2002 include $45 million staff redundancy and other costs associated with repositioning the business. Investment to enhance product capability has been funded by other underlying cost efficiencies within the Wholesale Banking business.

The significant improvement in the charge for debts reflects the risk management initiatives over the last two years and strong recoveries.

### Risk

Risk is inherent in the Group's business and the effective management of that risk is seen as a core competence within Standard Chartered. Through its risk management structure the Group seeks to manage efficiently the eight core risks: credit, market, country and liquidity risk arise directly through the Group's commercial activities whilst business, regulatory, operational and reputational risk are a normal consequence of any business undertaking. The key element of risk management philosophy is for the risk functions to operate as an independent control working in partnership with the business units to provide a competitive advantage to the Group.

Ultimate responsibility for the effective management of risk rests with the Group's Board of Directors who control and manage through the Audit and Risk Committee. The Audit and Risk Committee reviews specific risk areas, such as country risk exposures, large credit exposures, market and liquidity limits. It also guides and monitors the activities of the Group Asset and Liability Committee and the Group Risk Committee.

All of the Group's executive directors are members of the Group Risk Committee that is chaired by the Group Executive Director for Risk (GED Risk). This Committee has responsibility for determining the Group Risk appetite and strategy, monitoring and controlling Group risk exposure, setting Group standards and policies for risk measurement and management, and also delegating authorities and responsibilities to various sub-committees.

The GED Risk manages an independent risk function which:
- Recommends Group standards and policies for risk measurement and management;
- monitors and reports Group risk exposures for country, credit, market and operational risk;
- approves market risk limits and monitors exposure;
- sets country risk limits and monitors exposure;
- chairs credit committee and delegates credit authorities subject to oversight;
- validates risk models; and
- recommends risk appetite and strategy.

Individual Group executive directors are accountable for risk management in their businesses and support functions and for countries where they have governance responsibilities. This includes:
- Implementing the policies and standards as agreed by the Group Risk Committee across all business activity;
- managing risk in line with the appetite levels agreed by the Group Risk Committee; and
- developing and maintaining appropriate risk management infrastructure and systems to facilitate compliance with risk policy.

The GED Risk, together with Group Audit, provides independent assurance that risk is being measured and managed in accordance with the Group's standards and policies.

### Credit Risk

Credit risk is the risk that a counterparty will not settle its obligations in accordance with agreed terms.

Credit exposures include individual borrowers, connected groups of counterparties and portfolios on the banking and trading books.

Clear responsibility for credit risk is delegated from the Board to the Group Risk Committee. Policies for managing credit risk are determined by the Group Risk Committee which also delegates credit authorities through the GED Risk to independent Risk Officers at the Wholesale Banking and Consumer Banking business levels. Specific procedures for managing credit risk are determined at the business levels with specific policies and procedures being adapted to different risk environment and business goals. The Risk Officers are located in the businesses to maximise the efficiency of decision-making, but have an independent reporting line into the GED Risk.

Within the Wholesale Banking business, credit analysis includes a review of facility detail, credit grade determination and financial spreading/ratio analysis. There is a clear segregation of duties with loan applications being prepared separately from the approval chain. Significant exposures are reviewed and approved centrally through a Group Credit Risk Committee. This Committee receives its authority and delegated responsibilities from the Group Risk Committee.

The businesses, working with the Risk Officers, take responsibility for managing pricing for risk, portfolio diversification and overall asset quality within the requirements of Group policies and the business strategy.

For Consumer Banking, standard credit application forms are generally used which are processed in central units using manual or automated approval processes as appropriate to the customer, the product or the market. As with Wholesale Banking, origination and approval roles are segregated.

## Loan Portfolio

The following table sets out by maturity the amount of customer loans net of provisions:

| | 2002 | | | | 2001 | | | |
|---|---|---|---|---|---|---|---|---|
| | One year or less $million | One to five years $million | Over five years $million | Total $million | One year or less $million | One to five years $million | Over five years $million | Total $million |
| Consumer Banking: | | | | | | | | |
| Mortgages | 1,977 | 4,399 | 14,012 | 20,388 | 2,372 | 4,136 | 12,241 | 18,749 |
| Other | 4,798 | 3,197 | 1,218 | 9,213 | 4,907 | 2,756 | 1,003 | 8,666 |
| Total | 6,775 | 7,596 | 15,230 | 29,601 | 7,279 | 6,892 | 13,244 | 27,415 |
| Wholesale Banking | 22,035 | 4,077 | 1,764 | 27,876 | 20,289 | 3,309 | 2,460 | 26,058 |
| General Provisions | | | | (468) | | | | (468) |
| Net loans and advances to customers | 28,810 | 11,673 | 16,994 | 57,009 | 27,568 | 10,201 | 15,704 | 53,005 |

The Group's loans and advances to customers is predominantly a short-term portfolio with 51 per cent having a maturity of one year or less. The long-term portfolio, i.e. with a maturity of over five years, primarily relates to the Consumer Banking retail mortgages portfolio.

The following table sets out an analysis of the Group's net loans and advances as at 31 December 2002 and 31 December 2001 by borrowers' business or industry and geographical distribution:

| | 2002 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
| Loans to Individuals | | | | | | | | | |
| Mortgages | 13,045 | 3,813 | 2,031 | 779 | 283 | 20 | 35 | 382 | 20,388 |
| Other (see note below) | 2,573 | 1,524 | 575 | 1,684 | 882 | 1,537 | 231 | 207 | 9,213 |
| Consumer Banking | 15,618 | 5,337 | 2,606 | 2,463 | 1,165 | 1,557 | 266 | 589 | 29,601 |
| Agriculture, forestry and fishing | 5 | 7 | 59 | 35 | 15 | 14 | 62 | 365 | 562 |
| Construction | 58 | 38 | 37 | 18 | 4 | 157 | 25 | 7 | 344 |
| Commerce | 1,251 | 777 | 147 | 572 | 19 | 784 | 283 | 1,151 | 4,984 |
| Electricity, gas and water | 269 | 40 | 12 | 178 | 23 | 50 | 35 | 109 | 716 |
| Financing, insurance and business services | 1,645 | 586 | 404 | 489 | 209 | 638 | 47 | 1,921 | 5,939 |
| Loans to Governments | – | 41 | 552 | 66 | – | 13 | – | 273 | 945 |
| Mining and quarrying | – | 19 | 51 | 26 | 23 | 134 | 20 | 536 | 809 |
| Manufacturing | 1,019 | 399 | 201 | 2,020 | 887 | 1,242 | 299 | 2,256 | 8,323 |
| Commercial real estate | 1,012 | 665 | 18 | 112 | – | – | 6 | 6 | 1,819 |
| Transport, storage and communication | 405 | 112 | 77 | 217 | 113 | 178 | 107 | 1,577 | 2,786 |
| Other | 31 | 39 | 37 | 194 | – | 116 | 18 | 214 | 649 |
| Wholesale Banking | 5,695 | 2,723 | 1,595 | 3,927 | 1,293 | 3,326 | 902 | 8,415 | 27,876 |
| General provisions | | | | | | | | (468) | (468) |
| Total loans and advances to customers | 21,313 | 8,060 | 4,201 | 6,390 | 2,458 | 4,883 | 1,168 | 8,536 | 57,009 |
| Total loans and advances to banks | 2,507 | 2,027 | 394 | 2,703 | 212 | 1,792 | 218 | 6,148 | 16,001 |

### Loan Portfolio continued

| | 2001 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
| Loans to Individuals | | | | | | | | | |
| Mortgages | 12,560 | 3,005 | 1,784 | 698 | 142 | 38 | 16 | 506 | 18,749 |
| Other (see note below) | 3,368 | 1,172 | 519 | 1,111 | 721 | 1,462 | 155 | 158 | 8,666 |
| Consumer Banking | 15,928 | 4,177 | 2,303 | 1,809 | 863 | 1,500 | 171 | 664 | 27,415 |
| Agriculture, forestry and fishing | 8 | 16 | 69 | 64 | 103 | 16 | 80 | 281 | 637 |
| Construction | 56 | 57 | 40 | 39 | 22 | 104 | 16 | 68 | 402 |
| Commerce | 936 | 554 | 223 | 605 | 45 | 703 | 245 | 928 | 4,239 |
| Electricity, gas and water | 318 | 34 | 28 | 188 | 80 | 29 | 40 | 248 | 965 |
| Financing, insurance and business services | 1,836 | 558 | 309 | 532 | 124 | 312 | 40 | 1,468 | 5,179 |
| Loans to Governments | – | – | 309 | 19 | 5 | 12 | 1 | 576 | 922 |
| Mining and quarrying | – | 2 | 28 | 35 | 15 | 139 | 32 | 726 | 977 |
| Manufacturing | 1,005 | 510 | 277 | 2,261 | 553 | 1,037 | 288 | 2,410 | 8,341 |
| Commercial real estate | 681 | 1 | 26 | 202 | – | – | 3 | 13 | 926 |
| Transport, storage and communication | 313 | 247 | 75 | 88 | 103 | 192 | 38 | 1,173 | 2,229 |
| Other | 64 | 672 | 18 | – | 10 | 73 | 15 | 389 | 1,241 |
| Wholesale Banking | 5,217 | 2,651 | 1,402 | 4,033 | 1,060 | 2,617 | 798 | 8,280 | 26,058 |
| General provisions | | | | | | | | (468) | (468) |
| Total loans and advances to customers | 21,145 | 6,828 | 3,705 | 5,842 | 1,923 | 4,117 | 969 | 8,476 | 53,005 |
| Total loans and advances to banks | 1,227 | 2,315 | 607 | 3,184 | 398 | 1,704 | 325 | 9,818 | 19,578 |

Under 'Other Loans to Individuals', $1,487 million (2001: $2,112 million) relates to the cards portfolio in Hong Kong and $3,378 million (2001: $3,757 million) relates to the total cards portfolio.

Approximately 52 per cent (2001: 52 per cent) of total loans and advances to customers relate to Consumer Banking lending, predominantly personal residential mortgages. The Wholesale Banking portfolio is well diversified across both geography and industry. The Group does not have any significant concentration to industries of special interest such as Telecommunications, Aviation and Tourism. Exposure to each of these industries is less than five per cent of Wholesale Banking loans and advances to customers.

### Problem Credits

The Group employs a variety of tools to monitor the portfolio and to ensure the timely recognition of problem credits.

In Wholesale Banking, accounts are placed on Early Alert when they display signs of weakness. Such accounts are subject to a dedicated process involving senior risk officers and representatives from a specialist recovery unit, which is independent of the business units. Account plans are re-evaluated and remedial actions are agreed and monitored until complete. Remedial actions include, but are not limited to, exposure reduction, security enhancement, exit of the account or immediate movement of the account into the control of the specialist recovery unit.

In Consumer Banking, an account is considered to be in default when payment is not received on the due date. Accounts that are overdue by more than 30 days (60 days for mortgages) are considered delinquent. These are closely monitored and subject to a special collections process.

In general, loans are treated as non-performing when interest or principal is 90 days or more past due.

### Consumer Banking

Provisions are derived on a formulaic basis depending on the product:

- Mortgages: a provision is raised where accounts are 150 days past due based on the difference between the outstanding value of the loan and the forced sale value of the underlying asset.
- Credit cards: a charge off is made for all balances which are 150 days past due or earlier as circumstances dictate. In Hong Kong charge off is currently at 120 days.
- Other unsecured Consumer Banking products: a charge off is made at 150 days past due.
- Other secured Consumer Banking products: a provision is raised at 90 days past due for the difference between the outstanding value and the forced sale value of the underlying asset. The underlying asset is then re-valued periodically until disposal.

It is current practice to provision and write off exposure in respect of Hong Kong bankruptcies at the time the customer petitions for bankruptcy.

The Small and Medium Enterprises (SME) portfolio is provisioned on a case by case basis.

The following table sets out the non-performing portfolio in Consumer Banking:

| | | | | | | | | | 2002 |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
| Loans and advances – Gross non-performing | 118 | 111 | 176 | 68 | 41 | 27 | 15 | 18 | 574 |
| Specific provisions for bad and doubtful debts | (45) | (18) | (24) | (16) | (8) | (7) | (8) | (1) | (127) |
| Interest in suspense | (1) | (3) | (22) | (10) | (7) | (7) | (7) | (1) | (58) |
| Net non-performing loans and advances | 72 | 90 | 130 | 42 | 26 | 13 | – | 16 | 389 |
| Cover ratio | | | | | | | | | 32% |

| | | | | | | | | | 2001 |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
| Loans and advances – Gross non-performing | 164 | 115 | 168 | 68 | 39 | 78 | 18 | 21 | 671 |
| Specific provisions for bad and doubtful debts | (70) | (15) | (20) | (24) | (11) | (52) | (5) | (13) | (210) |
| Interest in suspense | – | (2) | (20) | (8) | (6) | (15) | (7) | – | (58) |
| Net non-performing loans and advances | 94 | 98 | 128 | 36 | 22 | 11 | 6 | 8 | 403 |
| Cover ratio | | | | | | | | | 40% |

In 2001, gross non-performing loans and advances for Other Asia Pacific have been restated. $58 million of gross non-performing loans in Standard Chartered Nakornthon Bank (SCNB) subject to a Loan Management Agreement (LMA) are now reported in Wholesale Banking.

The relatively low Consumer Banking cover ratio reflects the fact that Standard Chartered classifies all exposure which is 90+ days past due as non-performing, whilst provisions on unsecured lending are only raised at the time of charge-off (see details relating to the raising of provisions above).

### Wholesale Banking

Loans are designated as non-performing as soon as payment of interest or principal is 90 days or more overdue, or where sufficient weakness is recognised that full payment of either interest or principal becomes questionable. Where customer accounts are recognised as non-performing or display weakness that may result in non-performing status being assigned, they are passed to the management of a specialist unit, which is independent of the main businesses of the Group.

For loans and advances designated non-performing, interest continues to accrue on the customer's account but is not included in income.

Where the principal or a portion thereof, is considered uncollectable and of such little realisable value that it can no longer be included at its full nominal amount on the balance sheet, a specific provision is raised. In any decision relating to the raising of provisions, the Group attempts to balance economic conditions, local knowledge and experience and the results of independent asset reviews.

Where it is considered that there is no realistic prospect of recovering the principal of an account against which a specific provision has been raised, then that amount will be written off. The Group reports non-performing loans on a net at risk basis two years after first raising a specific provision. Net at risk is the result of netting interest in suspense and specific provision against applicable gross outstandings. Normal account management and collection efforts are not impacted by this process.

### Wholesale Banking continued

The following table sets out the non-performing portfolio in Wholesale Banking:

**2002**

| | Asia Pacific: Hong Kong $million | Asia Pacific: Singapore $million | Asia Pacific: Malaysia $million | Asia Pacific: Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
|---|---|---|---|---|---|---|---|---|---|
| Loans and advances – Gross non-performing | 121 | 101 | 192 | 810 | 22 | 97 | 80 | 608 | 2,031 |
| Specific provisions for bad and doubtful debts | (28) | (28) | (100) | (69) | (15) | (41) | (36) | (244) | (561) |
| Interest in suspense | (13) | (14) | (34) | (19) | (5) | (13) | (30) | (19) | (147) |
| Net non-performing loans and advances | 80 | 59 | 58 | 722 | 2 | 43 | 14 | 345 | 1,323 |

**2001**

| | Asia Pacific: Hong Kong $million | Asia Pacific: Singapore $million | Asia Pacific: Malaysia $million | Asia Pacific: Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
|---|---|---|---|---|---|---|---|---|---|
| Loans and advances – Gross non-performing | 252 | 120 | 275 | 963 | 43 | 284 | 87 | 498 | 2,522 |
| Specific provisions for bad and doubtful debts | (60) | (36) | (126) | (122) | (29) | (121) | (47) | (200) | (741) |
| Interest in suspense | (18) | (11) | (23) | (14) | (10) | (33) | (29) | (29) | (167) |
| Net non-performing loans and advances | 174 | 73 | 126 | 827 | 4 | 130 | 11 | 269 | 1,614 |

Included in Other Asia Pacific are net non-performing loans of $690 million (2001: $739 million) in Standard Chartered Nakornthon Bank (SCNB) which are subject to a Loan Management Agreement (LMA). Refer to note 19 on page 77. In 2001 gross non-performing loans for Other Asia Pacific have been restated to include $58 million of gross non-performing loans subject to the LMA which were previously reported under Consumer Banking.

### Wholesale Banking Cover Ratio

Corporate loans and advances to customers against which provisions have been outstanding for two years or more are written down to their net realisable value. The following table shows the cover ratio after adjusting for the cumulative amounts written down. The non-performing loans recorded in SCNB are excluded from the cover ratio calculation as they are the subject of a Loan Management Agreement with a Thai government agency. Refer to note 19 on page 77.

**2002**

| | Total $million | Adjustment for cumulative amounts written down $million | Exclude LMA $million | Adjusted total $million |
|---|---|---|---|---|
| Loans and advances – Gross non-performing | 2,031 | 1,652 | (781) | 2,902 |
| Specific provisions for bad and doubtful debts | (561) | (1,136) | 91 | (1,606) |
| Interest in suspense | (147) | (516) | – | (663) |
| Net non-performing loans and advances | 1,323 | – | (690) | 633 |
| Cover ratio | | | | 78% |

| | 2001 | | | |
|---|---|---|---|---|
| | Total $million | Adjustment for cumulative amounts written down $million | Exclude LMA $million | Adjusted total $million |
| Loans and advances – Gross non-performing | 2,522 | 1,574 | (828) | 3,268 |
| Specific provisions for bad and doubtful debts | (741) | (1,108) | 89 | (1,760) |
| Interest in suspense | (167) | (466) | – | (633) |
| Net non-performing loans and advances | 1,614 | – | (739) | 875 |
| Cover ratio | | | | 73% |

Net non-performing loans have decreased by $291 million to $1,323 million at 31 December 2002 on the back of strong recoveries as work-out strategies initiated in earlier years take effect. Net non-performing loans are covered by collateral and on-going work-out strategies. The Wholesale Banking adjusted cover ratio also shows significant improvement year-on-year and now stands at 78 per cent (2001: 73 per cent).

## Group

The following table sets out the movements in the Group's total specific provisions against loans and advances:

| | 2002 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
| Provisions held at 1 January 2002 | 130 | 51 | 146 | 146 | 40 | 173 | 52 | 213 | 951 |
| Exchange translation differences | 2 | 1 | – | (3) | – | (1) | (4) | 6 | 1 |
| Amounts written off and written down | (501) | (52) | (45) | (126) | (67) | (135) | (7) | (98) | (1,031) |
| Recoveries of amounts previously written off | 14 | 5 | 10 | 13 | 13 | 1 | – | 9 | 65 |
| Other | – | – | – | (6) | – | 3 | – | – | (3) |
| New provisions | 502 | 59 | 45 | 115 | 104 | 40 | 9 | 138 | 1,012 |
| Recoveries/provisions no longer required | (74) | (18) | (32) | (54) | (67) | (33) | (6) | (23) | (307) |
| Net charge against profit | 428 | 41 | 13 | 61 | 37 | 7 | 3 | 115 | 705 |
| Provisions held at 31 December 2002 | 73 | 46 | 124 | 85 | 23 | 48 | 44 | 245 | 688 |

| | 2001 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Asia Pacific | | | | | | | | |
| | Hong Kong $million | Singapore $million | Malaysia $million | Other Asia Pacific $million | India $million | Middle East & Other South Asia $million | Africa $million | Americas, UK & Group Head Office $million | Total $million |
| Provisions held at 1 January 2001 | 227 | 90 | 71 | 292 | 53 | 209 | 52 | 152 | 1,146 |
| Exchange translation differences | (3) | (2) | – | 6 | (1) | (2) | (5) | (5) | (12) |
| Amounts written off and written down | (359) | (96) | (64) | (230) | (54) | (106) | (9) | (83) | (1,001) |
| Recoveries of amounts previously written off | 8 | 7 | 11 | 10 | 8 | 1 | 1 | 5 | 51 |
| Other | – | – | (2) | (18) | 7 | 32 | – | 16 | 35 |
| New provisions | 318 | 71 | 154 | 140 | 68 | 66 | 20 | 157 | 994 |
| Recoveries/provisions no longer required | (61) | (19) | (24) | (54) | (41) | (27) | (7) | (29) | (262) |
| Net charge against profit | 257 | 52 | 130 | 86 | 27 | 39 | 13 | 128 | 732 |
| Provisions held at 31 December 2001 | 130 | 51 | 146 | 146 | 40 | 173 | 52 | 213 | 951 |

Of the amounts written off and the recoveries of amounts previously written off:

| | 2002 $million | 2001 $million |
|---|---|---|
| Covered by specific provisions | 786 | 817 |
| Not covered by specific provisions | 245 | 184 |
| Recoveries of loans previously written off | (65) | (51) |
| | 966 | 950 |

## Country Risk

Country risk is the risk that a counterparty is unable to meet its contractual obligations as a result of adverse economic conditions or actions taken by governments in the relevant country.

This covers the risk that:

- The sovereign borrower of a country may be unable or unwilling to fulfil its foreign currency or cross-border contractual obligations; and/or
- a non-sovereign counterparty may be unable to fulfil its contractual obligations as a result of currency shortage due to adverse economic conditions or actions taken by the government of the country.

The Group Risk Committee approves country risk policy and procedures and delegates the setting and management of country limits to the Group Head, Credit and Country Risk.

The businesses and country Chief Executive Officers manage exposures within these set limits and policies. Countries designated as higher risk are subject to increased central monitoring.

The following table based on the Bank of England Cross Border Reporting (C1) guidelines shows the Group's cross border assets, including acceptances, where they exceed one per cent of the Group's total assets. Cross border assets exclude facilities provided within the Group. They comprise loans and advances, interest bearing deposits with other banks, trade and other bills, acceptances, amounts receivable under finance leases, certificates of deposit and other negotiable paper and investment securities where the counterparty is resident in a country other than that where the cross border asset is recorded. Cross border assets also include exposures to local residents denominated in currencies other than the local currency.

| | | | | 2002 |
|---|---|---|---|---|
| | Public sector $million | Banks $million | Other $million | Total $million |
| USA | 1,084 | 1,729 | 2,462 | 5,275 |
| Germany | – | 2,363 | 234 | 2,597 |
| Hong Kong | 16 | 181 | 1,842 | 2,039 |
| Korea | 12 | 1,334 | 407 | 1,753 |
| Singapore | 1 | 190 | 1,361 | 1,552 |
| France | 4 | 1,202 | 323 | 1,529 |
| Italy | 488 | 613 | 374 | 1,475 |
| Australia | 359 | 988 | 59 | 1,406 |

| | | | | 2001 |
|---|---|---|---|---|
| | Public sector $million | Banks $million | Other $million | Total $million |
| USA | 1,637 | 1,330 | 1,750 | 4,717 |
| Germany | – | 3,546 | 119 | 3,665 |
| Hong Kong | 8 | 167 | 1,685 | 1,860 |
| Korea | 5 | 1,214 | 203 | 1,422 |
| Singapore | 25 | 310 | 1,485 | 1,820 |
| France | – | 1,281 | 409 | 1,690 |
| Italy | 396 | 1,047 | 239 | 1,682 |

### Argentina

Standard Chartered has net exposure (net of cash collateral and export credit agency guarantees ) of $211 million (2001: $380 million) against which provisions of $136 million (2001: $56 million) are held. This provides a cover ratio of 64 per cent (2001: 15 per cent). The following table shows the breakdown of this exposure:

| | 2002 $million | 2001 $million |
|---|---|---|
| Banks: | | |
| Foreign owned banks | 79 | 174 |
| Government owned banks | 21 | 34 |
| Local banks | 41 | 93 |
| Corporates | 63 | 79 |
| Government bonds | 7 | – |
| Total exposure after cash collateral and export credit agency cover | 211 | 380 |
| Provisions held | (136) | (56) |
| Net at risk | 75 | 324 |
| Cover ratio | 64% | 15% |

### Other Latin American Exposure

In addition to Argentina, the Group has exposure to a number of other Latin American countries. The following table shows cross border assets based on the Bank of England Cross Border Reporting (C1) guidelines (net of specific provisions where appropriate).

| | 2002 | | | 2001 | | |
|---|---|---|---|---|---|---|
| | Banks $million | Non-banks $million | Total $million | Banks $million | Non-banks $million | Total $million |
| Brazil | 195 | 78 | 273 | 607 | 168 | 775 |
| Chile | 120 | 43 | 163 | 171 | 115 | 286 |
| Colombia | 155 | 45 | 200 | 178 | 150 | 328 |
| Peru | 18 | 218 | 236 | 48 | 299 | 347 |
| Venezuela | 6 | 46 | 52 | 21 | 112 | 133 |
| Others | 8 | 8 | 16 | 35 | 11 | 46 |

Local currency exposure to local residents in these countries totals $165 million (2001: $212 million).

## Market Risk

The Group recognises market risk as the exposure created by the potential changes in market prices and rates. Market risk arises on financial instruments, which are either valued at current market prices (mark-to-market) or at cost plus any accrued interest (non-trading basis). The Group is exposed to market risk arising principally from customer driven transactions.

Market risk is supervised by the Group Risk Committee, which agrees policies and levels of risk appetite in terms of Value at Risk (VaR). A Group Market Risk Committee sits as a specialist body to provide business level management, guidance and policy setting. Policies cover the trading book of the Group and also market risks within the non-trading books. Limits by location and portfolio are proposed by the business within the terms of the agreed policy. Group Market Risk agrees the limits and monitors exposures against these limits.

Group Market Risk augments the VaR measurement by regularly stress testing aggregate market risk exposures to highlight potential risk that may arise from extreme market events that are rare but plausible. In addition, VaR models are back tested against actual results to ensure pre-determined levels of accuracy are maintained.

Additional limits are placed on specific instrument and currency concentrations where appropriate. Factor sensitivity measures are used in addition to VaR as additional risk management tools. Option risks are controlled through revaluation limits on currency and volatility shifts, limits on volatility risk by currency pair and other underlying variables that determine the options' value.

## Value at Risk

The Group measures the potential impact of market prices and rates using Value at Risk (VaR) models. These are described in more detail in note 51 to the accounts on page 101.

The total VaR for trading and non-trading books combined as at 31 December 2002 was $12.4 million. Of this total, $11.3 million related to interest rate risk and $1.0 million to foreign exchange risk. The corresponding figures as at 31 December 2001 were $13.9 million and $1.5 million respectively (refer table in note 51 to the accounts on page 101).

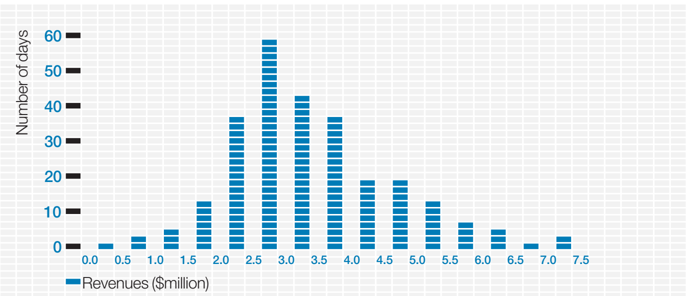
The average total VaR for trading and non-trading books during the year was $15.2 million (2001: $13.4 million) with a maximum exposure of $21.5 million. The average level of risk was higher in 2002 than the prior year due to higher market volatility post September 11, 2001.

The total VaR for market risks in the Group's trading book was $2.7 million at 31 December 2002, compared to $3.5 million a year earlier. Of this total, $1.6 million related to interest rate risk and $1.1 million to foreign exchange rate risk. The corresponding figures at 31 December 2001 were $2.1 million and $1.5 million respectively.

VaR for interest rate risk in the non-trading books of the Group totalled $10.1 million at 31 December 2002, compared to $11.6 million a year earlier.

The Group has no significant trading exposure to equity or commodity price risk.

The average daily revenue earned from market risk related activities, including asset and liability management was $3.4 million, compared with $3.3 million during 2001. An analysis of the frequency distribution of daily revenues shows that there were no days with negative revenues during 2002. The most frequent result was daily revenue of between $2.5 million and $3.0 million with 58 occurrences. The highest daily revenue was $7.1 million.




**Daily Distribution of Market Risk Revenues**
Year to 31 December 2002

## Foreign Exchange Exposure

The Group's foreign exchange exposures comprise trading and structural foreign currency translation exposures.

Foreign exchange trading exposures are principally derived from customer driven transactions. The average daily foreign exchange trading revenue during 2002 was $1.2 million.

## Interest Rate Exposure

The Group's interest rate exposures comprise trading exposures and structural interest rate exposures. Interest rate risk arises on both trading positions and non-trading books.

Structural interest rate risk arises from the differing re-pricing characteristics of commercial banking assets and liabilities, including non-interest bearing liabilities such as shareholders' funds and some current accounts.

The average daily interest rate revenue from market risk related activity during 2002 was $2.2 million.

## Derivatives

Derivatives are contracts whose characteristics and value derive from underlying financial instruments, interest and exchange rates or indices. They include futures, forwards, swaps and options transactions in the foreign exchange and interest rate markets. Derivatives are an important risk management tool for banks and their customers because they can be used to manage the risk of price, interest rate and exchange rate movements.

The Group's derivative transactions are principally in plain vanilla instruments, where the mark-to-market values are readily determinable by reference to independent prices and valuation quotes or by using standard industry pricing models. The total off-balance sheet credit risk to derivatives at 31 December 2002 was $9,783 million (2001: $7,517 million) based on net replacement cost.

The Group enters into derivative contracts in the normal course of business to meet customer requirements and to manage its own exposure to fluctuations in interest and exchange rates. Only offices with sufficient product expertise and appropriate control systems are authorised to undertake transactions in derivative products.

The credit risk arising from a derivative contract is calculated by taking the cost of replacing the contract, where its mark-to-market value is positive, together with an estimate for the potential change in the future value of the contract, reflecting the volatilities that affect it. The credit risk on contracts with a negative mark-to-market value is restricted to the potential future change in their market value. The credit risk on derivatives is therefore usually small relative to their notional principal values. For an analysis of derivative contracts see notes 46 and 47 to the accounts on pages 96 to 98.

The Group applies a potential future exposure methodology to manage counterparty credit exposure associated with derivative transactions.

Please refer to note 51 to the accounts on page 101 for further information on market risk.

## Liquidity Risk

The Group defines liquidity risk as the risk that funds will not be available to meet liabilities as they fall due.

Liquidity risk is managed through the Group Asset and Liability Committee (GALCO). This Committee, chaired by the Finance Director and with authority derived from the Board, is responsible for both statutory and prudential liquidity. These are managed through the provision of policies and procedures that are co-ordinated by regional and local asset and liability committees.

A range of tools are used for the management of liquidity. These comprise commitment and wholesale borrowing guidelines, key balance sheet ratios and medium-term funding requirements.

At the local level, in line with policy, the day to day monitoring of future cash flows takes place and suitable levels of easily marketable assets are maintained by the businesses.

A substantial proportion of the Group's assets are funded by customer deposits made up of current and savings accounts and other short-term deposits. These customer deposits, which are widely diversified by type and maturity, represent a stable source of funds. Lending is normally funded by liabilities in the same currency and if other currencies are used the foreign exchange risk is usually hedged.

The GALCO also manages the structural foreign exchange and interest rate exposures that arise within the Group. Polices and terms of reference are set within which Group Corporate Treasury manage these exposures on a day to day basis.

Policies and guidelines for the setting and maintenance of capital ratio levels also originate from the GALCO. Responsibilities are delegated through the regional and local asset and liability committees to the relevant businesses. Ratios are monitored centrally by Group Corporate Treasury.

### Operational and Other Risks

Operational risk is the risk of direct or indirect loss due to an event or action causing failure of technology, processes, infrastructure, personnel, and other risks having an operational risk impact. Standard Chartered seeks to minimise actual or potential losses from operational risk failures through a framework of policies and procedures that identify, assess, control, manage and report risks.

An independent Group Operational Risk function is responsible for establishing and maintaining the overall operational risk framework. The Group Operational Risk function provides reports to the Group Risk Committee.

Compliance with operational risk policy is the responsibility of all managers. In every country, a Country Operational Risk Group (CORG) has been established. It is the responsibility of the CORG to ensure appropriate risk management frameworks are in place and to monitor and manage operational risk. CORGs are chaired by Country Chief Executives.

Business units are required to monitor their operational risks using Group and business level standards and indicators. Significant issues and exceptions must be reported to the CORG. Where appropriate, issues must also be reported to Business Risk Committees and the Group Risk Committee.

Other risks recognised by the Group include business, regulatory, legal, and reputational risks.

### Business Risk

Business risk is the risk of failing to achieve business targets due to inappropriate strategies, inadequate resources or changes in the economic or competitive environment, and is managed through the Group's management processes. Regular reviews of the performance of Group businesses by Group Executive Directors are used to assess business risks and agree management action. The reviews include corporate financial performance measures, capital usage, resource utilisation and risk statistics to provide a broad understanding of the current business position.

### Regulatory Risk

Regulatory risk includes the risk of non-compliance with regulatory requirements in a country in which the Group operates. The Group Legal and Compliance function is responsible for establishing and maintaining an appropriate framework of Group compliance policies and procedures. Compliance with such policies and procedures is the responsibility of all managers.

### Legal Risk

Legal risk includes the risk of unexpected loss from transactions not being enforceable under applicable law or regulation or from inadequate or unsound contractual documentation. The Group manages legal risk through effective use of its internal and external legal advisers and by seeking to ensure that transactions are properly authorised and documented.

### Reputational Risk

Reputational risk is defined as the risk that any action taken by the Group or its employees creates a negative perception in the external market place. This includes the Group's and/or its customers' impact on the environment. The Group Risk Committee examines issues that are considered to have reputational repercussions for the Group and issues guidelines or policies as appropriate. It also delegates responsibilities for the management of legal/regulatory and reputations risk to the business through business risk committees.

### Independent Monitoring

Group Audit is an independent group that reports directly to the GED Risk and the Audit and Risk Committee. Group Audit provides independent confirmation that Group and business standards, policies and procedures are being complied with. Where necessary, corrective action is recommended.

### Hedging Policies

Standard Chartered does not generally hedge the value of its foreign currency denominated investments in subsidiaries and branches. Hedges may be taken where there is a risk of a significant exchange rate movement but, in general, the management believes that the Group's reserves are sufficient to absorb any foreseeable adverse currency depreciation. Standard Chartered also seeks to match closely its foreign currency-denominated assets with corresponding liabilities in the same currencies. The effect of exchange rate movements on the capital risk asset ratio is mitigated by the fact that both the value of these investments and the risk weighted value of assets and contingent liabilities follow substantially the same exchange rate movements.

### Capital

Standard Chartered's policy is to maintain a conservative balance sheet and strong capital base. The Group Asset and Liabillity Committee targets Tier 1 and Total Capital ratios of seven to nine per cent and 12 to 14 per cent respectively. The Group believes that being well capitalised is important.

| | 2002 $million | 2001* $million |
|---|---|---|
| **Tier 1 capital:** | | |
| Shareholders' funds | 7,327 | 7,538 |
| Minority interests | 249 | 73 |
| Innovative Tier 1 securities | 997 | 929 |
| Unconsolidated associated companies | 31 | 22 |
| Less: | | |
| Premises revaluation reserves | (3) | (61) |
| Goodwill capitalised | (2,118) | (2,269) |
| Own shares held[†] | (57) | – |
| Total Tier 1 capital | 6,426 | 6,232 |
| **Tier 2 capital:** | | |
| Premises revaluation reserves | 3 | 61 |
| General provisions | 468 | 468 |
| Undated subordinated loan capital | 1,853 | 1,804 |
| Dated subordinated loan capital | 2,605 | 2,677 |
| Total Tier 2 capital | 4,929 | 5,010 |
| Investments in other banks | (558) | – |
| Other deductions | (4) | (19) |
| Total capital | 10,793 | 11,223 |
| Risk weighted assets | 55,931 | 53,825 |
| Risk weighted contingents | 18,623 | 15,517 |
| Total risk weighted assets and contingents | 74,554 | 69,342 |
| **Capital ratios:** | | |
| Tier 1 capital | 8.6% | 9.0% |
| Total capital | 14.5% | 16.2% |

[†] Relates to shares held in trust to fulfil the Group's obligations under employee share schemes.

| | 2002 $million | 2001* $million |
|---|---|---|
| Shareholders' funds: | | |
| Equity | 6,695 | 6,279 |
| Non Equity | 632 | 1,259 |
| Total | 7,327 | 7,538 |
| Post tax return on equity (normalised) | 13.4% | 12.0% |

* Comparative restated (see note 40).

The Group identified improving the efficiency of capital management as a strategic priority for 2002. A capital plan to achieve this has been developed. This includes several key elements. In particular, to reduce the amount of Tier 2 capital and to improve the overall capital mix within the broad target ratios.

In October 2002, Standard Chartered PLC listed on the Hong Kong Stock Exchange. The Company issued 35 million ordinary shares of $0.50 per share. The shares were issued at HK$84 per share, raising $17.5 million of share capital and $328 million of share premium.

In December 2002, the Company repurchased 659,126 Non-cumulative Preference Shares with a nominal value of $5 and issued at a price of $1,000 per Preference Share. The Shares were repurchased at $1,110 per share, together with an amount to compensate for accrued dividend. The deduction from the share premium reserve was restricted to the $328 million premium raised on the Hong Kong listing.

## Efficiency Programme

In August 2000 the Group announced an efficiency programme, the purpose of which was to improve productivity and to build an operational platform to support future growth. Excellent progress continues to be made. Headcount reductions have exceeded the original target set.

| | Achieved by end of 2002 | | Original target over three years | |
|---|---|---|---|---|
| | Headcount reduction | Headcount addition | Headcount reduction | Headcount addition |
| Centralising of processing and support operations | **2,350** | **2,200** | 2,000 | 1,000 |
| Operational efficiencies | **3,100** | **–** | 2,100 | – |
| Integration of acquisitions | **2,700** | **–** | 2,100 | – |
| | **8,150** | **2,200** | 6,200 | 1,000 |

| | Achieved | | Target | | |
|---|---|---|---|---|---|
| | | | Original | Revised | |
| | 2002 | 2001 | 2001 | 2002 | 2003 |
| Cost synergies | $million | $million | $million | $million | $million |
| Centralising of processing and support operations | **60** | 19 | 29 | 64 | 100 |
| Operational efficiencies | **90** | 60 | 29 | 80 | 90 |
| Integration of acquisitions | **115** | 70 | 50 | 100 | 115 |
| | **265** | 149 | 108 | 244 | 305 |
| Investment spend | **(110)** | (93) | (167) | (114) | (136) |
| Net Cost Benefit | **155** | 56 | (59) | 130 | 169 |
| Original Net Cost Benefit | | | (59) | 82 | 159 |

At the end of 2001 the Group increased its targets for savings from the Efficiency Programme. These higher targets have been delivered in 2002.