

The second half of last year witnessed the gradual improvement of the Hong Kong economy. The Mainland and Hong Kong Closer Economic Partnership Arrangement ("CEPA") has given the economy a new boost. The tourism and restaurant businesses have turned around and so has the property market. The employment situation has continued to improve, not to mention the gradual blossoming of economic activities on the back of a swift rebound of the retail consumer market brought about by the increasing numbers of mainland visitors to Hong Kong travelling under the "individual travels" arrangement. The overseas economies have generally stabilized as this year began to unfold and Hong Kong has started benefitting from the official implementation of CEPA, which means zero import tariff for the sale of a number of Hong Kong products in the mainland. This has facilitated the return of manufacturers who had previously moved up north. In the light of Hong Kong's superb position, foreign businesses have actively explored the use of CEPA incentives for investment opportunities in Hong Kong. The local industries tended to have been given a dose of new life. Statistics have indicated that local exports have risen 25 months in a row, setting the longest continuous increase record for the past 13 years. The value of the overall exports has risen some 16 percent for the first six months of this year. The export industry has flourished mainly because of the good performance of the markets in Europe, America, Japan and South East Asia. It is generally believed that strong growth momentum will persist. Following the interactive effect caused by the various trades and businesses, Hong Kong's economy as a whole boasted a full recovery for the first half of this year. All kinds of indicators have shown various degrees of progress. This is a period exhibiting the most vitality after the financial turmoil of 1997.

Although the economy has markedly improved, the impact has yet to be felt by the banking sector. As such, the results for the first half of this year, as compared with those of the corresponding period last year, can only be described as a slight improvement. The Bank's unaudited, consolidated results for the first half of 2004 improved somewhat compared with those for the previous corresponding period. Net interest income rose 2.08 percent to HK\$353.291 million. Operating profit before provisions increased 19.42 percent to HK\$252.219 million. Provisions newly made for bad and doubtful debts for the first half of this year fell 3.97 percent to 84.966 million from 88.478 million for the corresponding period last year. However, the provisions written back during the period declined 33.10 percent to 33.149 million from 49.55 million for the corresponding period last year. As such, provisions for bad and doubtful debts for the first half of this year rose 33.11 percent to 51.817 million. Profit attributable to shareholders amounted to HK\$175.86 million, an increase of 19.13 percent. As of 30 June 2004, total customers' deposits decreased 0.59 percent to HK\$32.399 billion compared with the corresponding figure as of 31 December 2003. Total loans and advances to customers (after provisions for bad and doubtful debts) increased 2.50 percent to HK\$20.229 billion. Total assets amounted to HK\$40.158 billion, an increase of 0.54 percent. As of 30 June 2004, unadjusted capital adequacy ratio rose 7.31 percent to 20.55 percent against the corresponding ratio of 31 December 2003. Average liquidity ratio for the first half of 2004 dropped 0.73 percent to 53.23 percent against the corresponding ratio for the first half of 2003. As of 30 June 2004, loan-to-deposit ratio stood at 54.51 percent, an increase of 2.99 percent against the corresponding ratio as of 31 December 2003. Earnings per share for the first half of 2004 amounted to HK\$0.40, an increase of HK\$0.06 per share over the corresponding figure for the first half of 2003. The increase in profit is due mainly to the rebound of the economy from the trough. Business activities of the various trades and industries tended to have gradually picked up, leading to a steady increase in the need to borrow and the desire to invest. Total customers' deposits decreased slightly in comparison with the corresponding figure at the end of 2003 because deposit rates still tended to be low. As far as loan quality is concerned, the Bank has consistently abided by its prudent credit risk management policy by actively undertaking debt collection efforts. It is expected that, in the light of the current improving economic environment, loan quality would be markedly improved.

The local economy has shifted into a rising mode. Deflation, which has plagued the territory for years, can be expected to be behind us in a few months. Gross domestic product for this year has been forecasted to grow up to 7 percent. Although US interest rates have just started to rise, the American presidential election towards the end of this year will have its impact on the international political landscape for the next four years. In the light of Hong Kong's sound foundation and network of global trading partners, not to mention a more stable development of the economy facilitated by mainland China's macroadjustment policy, the local economy stands to benefit even more from plans to foster closer cooperation in the Pan Pearl River Delta area (comprising nine provinces and two Special Administrative Regions). Such plans will pave the road for a brighter future with huge potential for business opportunities.

The recovery of the economy will help the local government to gradually reduce its fiscal deficit. The recent successful issues of the retail bonds which are backed by the revenues from five tunnels and the Lantau Link owned by the government and of the HK\$20 billion government bonds, as well as such proposals as those for the merger of the Kowloon-Canton Railway Corporation and the MTR Corporation and for the listing of the Airport Authority that are in the pipeline, are all beneficial to the government's finances. The goal to cut the fiscal deficit can thus be expected to be achieved sooner. Large public infrastructural projects have continued to be implemented. The Hong Kong Disneyland will commence business next year, while all the major enterprises concerned have climbed on the bandwagon to expand their operations. All these are conducive to lowering the unemployment rate. It is expected that the current robust market condition will continue.

Your board appointed Mr Kevin Wai Hung Chu, Senior Manager heading the Bank's Corporate and Commercial Banking Department, an Executive Director on 1 June 2004. I, on behalf of your board, would like to welcome Mr Chu as a new board member to join us in charting the development of the Bank.

We will continue to stride forward by devoting our efforts to both the development of our comprehensive array of business lines and the sharpening of our competitive advantage.