

Despite some specific, exceptional challenges, Asia Financial Group underlying strengths and the healthy economic environment ensured a generally satisfactory result. The Group produced a profit for the year of HK\$184.6 million, a 23.1% decline from 2004.

A Healthy Economic Environment

The global economy remained strong during the year, with trade and investment flows between China and the rest of the world playing an important part. However, concerns about heavy increases in commodity prices, especially energy, and the possibility of rising interest rates had a dampening affect on financial markets, which can influence our Group's year-on-year profits.

Hong Kong saw strong GDP growth of above 7% during the year, thanks in particular to export growth, as well as consumption and investment. Inflation remained low, unemployment continued to decline, and incomes and asset prices generally rose mildly. The government's fiscal position improved sufficiently to allow some minor tax cuts for the following financial year. We are pleased to see that consumer and investor confidence was positive.

Weaker Investment Returns and Exceptional Operational Challenges

All parts of the Group enjoyed fundamentally acceptable operational performance in 2005. However, weakness in year-on-year market values in our investment portfolios had a negative impact on our bottom line. Asia Commercial Bank had to make individual impairments for two exceptional bad loans, while Asia Insurance was exposed to a couple of events overseas, including Hurricane Katrina in the USA. In addition, the competitive environment was by no means easy in either the banking or insurance sectors.

The year-on-year value of our strategic holdings was less volatile than in 2004, however the foreign exchange movements were slightly unfavourable. Our trading portfolio's performance reflected concerns in world equities markets about rising interest rates and oil prices, which led to a relatively stagnant market for our good quality, blue-chip holdings during the reporting period (for example the Hang Seng Index ended the year only 5% up). However, our returns exceeded such benchmarks as the Hang Seng and Dow Jones Indexes.

Operating expenses increased partly as a result of expansion of our compliance functions.

Asia Commercial Bank saw a decrease in profit of 17.4% in 2005. Margins tightened significantly during the course of the year as funding costs rose faster than general interest rates, resulting in a decline in net interest income. The Bank's result also suffered from an increase in impairment allowance. While collective impairments fell, we were affected by individual impairments for two particular exceptional bad loans that affected a number of local banks and foreign banks in Hong Kong.

The Hong Kong banking sector remained extremely competitive during 2005, putting pressure on Asia Commercial Bank's more price-sensitive loans markets. However, the bank saw more positive performance in other retail loans products and benefited from stronger fee income. Profits from joint ventures also made a positive contribution. Total operating expenses for the Bank fell.

Asia Insurance saw a decline in profit of 23.3% to HK\$87.9 million in 2005. As with the holding company, this partly reflected a decline in investment gains owing to the flatness of the equities markets' year-on-year performance. It was also due to a drop in underwriting profit of 18.2%, partly because of exposure to external events like Hurricane Katrina in the US and partly as a result of fierce competition in certain lines of business.

Apart from these exceptional setbacks, Asia Insurance's core business remained fundamentally strong and profitable, with the company comfortably maintaining its position as an industry leader in Hong Kong.

Both Asia Commercial Bank and Asia Insurance ended the year with strong levels of reserves and provisions.

More details of the performance and prospects of the two subsidiaries appear in the management discussion and analysis.

Staff

The Group had a total of 566 employees at the end of 2005, an increase of 2% compared with the end of 2004. While remaining conscious of the need to manage costs carefully, we also sought to ensure that our salaries and conditions remained in line with the market and with the need to be able to attract and retain good quality people. We also continued to ensure that adequate resources were made available for training. The directors and I wish to take the opportunity to thank all our staff within the group for their dedication and hard work during 2005.

Management Strategy During the Year

The results for 2005 were impacted by exceptional events. However, the strength of the underlying operating results of the Group reflected the management's priorities of preserving investments and operational profits rather than increasing exposure to risk, while keeping a firm hold on costs.

At all times, management strategy has been driven by a determination to protect and further shareholders' long-term interests. With this in mind, management continued to examine new possible opportunities for the Group in Hong Kong as well as the Mainland and elsewhere.

Outlook and Strategy for the Future

After concerns about interest rates and oil prices last year, prospects for the global economy in 2006 look generally good. Despite its worrying deficits and debt situations, the US remains resilient. Japan is clearly returning to strength. China, while it may slow down to some extent, is likely to continue its rapid development as an exporter and an investment location, and as an increasingly important consumer market.

This is all good news for Hong Kong. Owing to rising rentals and some shortages of business premises and skills, we may see an upturn in inflation from last year's very low base. Service exports and private consumption are both expected to remain strong, and economists are predicting overall economic growth of a healthy 5%.

These trends point to a good year to come for Asia Financial Group and its clients.

As in the past, management will focus on investments and business expansion in areas where we can best take advantage of our core strengths. In doing so, we will also continue to seek appropriate alliances and partnerships where these can bring such benefits as economies of scale.

After much thought and analysis during 2005, management decided that the time was right to renew the Group's strategic direction by focusing more on those parts of its activities where it has its greatest strengths and prospects for growth. In February 2006 we entered into an agreement with JCG Holdings Limited (now known as "Public Financial Holdings Limited") to dispose Asia Commercial Bank. I strongly believe that by reallocating assets into more productive areas, we will put the Group on the path to greater long-term returns. We aim to focus on expanding our insurance business and to explore opportunities in the related field of healthcare. A more detailed explanation of our plans will appear in a separate circular to shareholders.

Looking ahead, I believe Asia Financial Group will enjoy another successful year in 2006 and I hope to report good interim results in six months' time.

Robin Y.H. Chan

Chairman

Hong Kong
27th March, 2006