Letter to Shareholders

2003 turned out to be another difficult year for businesses in Singapore and the region. The first six months was a particularly trying period as the combined effects of economic uncertainties, the war in Iraq, terrorism fears and the SARS outbreak adversely affected business and consumer confidence.

Despite the recovery in the second half, the Singapore economy grew by only 0.8% in 2003, marking a second straight year of sluggish growth. Malaysia, OCBC's second largest market, performed better, with estimated GDP growth of 4.5%.

Financial Results Against this backdrop, OCBC posted an encouraging set of results. Group net profit in 2003 reached a record S$954 million, an increase of 43% compared to S$667 million in 2002. The earnings growth was driven by lower provisions for loan losses, gains from the divestment of non-core assets, and higher contributions from associates.

Our top-line revenues, however, were sluggish given the weak business environment. Group operating profit before provisions and goodwill amortisation fell by 2% in 2003 to S$1,338 million. Net interest income declined by 5% as a result of lower interest margins in a competitive and low interest rate environment. The lower interest margins were partially offset by loan growth of 5.4%, achieved mainly through the strong expansion of housing and car loans. Fee and commission income was flat for the year, affected by the poor investment sentiments in the first half. Most importantly, we were disciplined in managing our expenses, and our cost base was little changed from 2002.

We have made substantial progress in strengthening the Group's credit processes since the second half of 2002. As a result, provisions declined from S$501 million in 2002 to S$225 million in 2003. Our non-performing loans ("NPLs") as a percentage of total loans improved from 8.1% to 6.9%. Our cumulative provision coverage also improved from 62.4% to 67.0% of NPLs.

Divestments of non-core assets during the year contributed a total net gain of S$126 million. This comprised: S$72 million from the disposal of shares in Fraser and Neave Limited ("F&N"); S$36 million from the sale of the development site at Mount Emily Road; S$14 million from sale of an associate's stake in Raffles Hotel; and S$4 million from disposal of shares in WBL Corporation Limited.

Our capital base remains strong, with the Group's total capital adequacy ratio at 21.8% and our Tier-1 ratio at 12.6% as at the end of 2003. Our credit ratings remain strong as well, with Moody's rating at Aa3, S&P at A and Fitch at A+, all unchanged from the prior year.

Dividends The Board has recommended a final dividend of 12 cents per share for ordinary shareholders for the second half, bringing the total distribution for 2003 to 23 cents per share (excluding the special gross dividend of 63.8 cents paid in July 2003). This is a 15% increase compared to the 20 cents paid for 2002.

In 2003 we adopted a policy of targeting a minimum payout of 25% of our core earnings. Consistent with this policy, the estimated net dividends of S$231 million for 2003 represent 28% of our core earnings (excluding the gains from disposal of non-core assets).

New Horizons Update We announced the New Horizons strategy in February 2003. This is a three-year plan to build OCBC into a high performance bank, with increasing market share in Singapore and Malaysia, which will then enable us to expand overseas by transferring successful customer-product solutions to other markets in Asia. We have made significant progress in the first year of New Horizons, which we briefly summarise here.

Customers: In 2003, our consumer and small and medium-sized enterprise ("SME") customers increased by 12% and 7% respectively. We conducted market research and customer satisfaction surveys to help us identify priority segments in the consumer market, and to tailor our marketing campaigns more effectively. We also introduced additional measures to benchmark customer service quality. In Malaysia, the focus throughout the year was on building up the infrastructure to acquire customers. We increased our Malaysia consumer banking sales force by 45%.

Our SME business model in Singapore and Malaysia was revamped so that we can grow the business more effectively while managing risks prudently. During the year, we introduced 11 new SME lending programmes that target specific SME segments or products, and achieved good results.

Product Strengths: We launched more than 50 new products during the year, including structured deposits, unit trusts, different bancassurance offerings, innovative loans and enhanced transactional banking products. We were the first bank in Asia to offer a cashflow lending product to SMEs, and the first bank in Singapore to introduce an SGS-linked structured deposit product. New products contributed about 6% of total revenues in the respective segments, short of our 2005 target of 15% but a significant improvement on 2002.

Retail sales of wealth management products in Singapore and Malaysia rose to a record S$5.2 billion in 2003, from S$3.9 billion in 2002. Our sales volume for treasury and structured products doubled from S$1.5 billion to S$3.0 billion. Total bancassurance sales premiums amounted to S$1.0 billion and OCBC remains the bancassurance market leader in Singapore. We achieved total unit trust sales of S$1.2 billion, growing more than four-fold over 2002 in Malaysia, and placing OCBC among the top distributors in Singapore.

OCBC's online cash management platform, *Velocity@ocbc*, was rated best-in-class in Singapore by *Global Finance* magazine for the third consecutive year. The number of corporate customers using *Velocity@ocbc* increased by 39%, while transaction volumes more than doubled.

OCBC gained market leadership in the new HDB home loan market with a 56% share based on caveats lodged, and in the private home loan market, with 21% share of new loans in Singapore.

Risk Management: We continued to grow our loan book prudently. In 2003, our domestic loans market share in Singapore increased from 19.9% to 20.7%, while our Malaysia loans market share increased from 4.7% to 4.9%. We also continued to maintain a highly liquid liability base, backed by diversified sources of funds, including a strong and stable customer deposit base and a healthy level of regulatory liquid assets.

Our NPLs and provisions were reduced by 12% and 55% respectively compared to 2002. We also established a new credit risk review team which emphasises credit process during their portfolio reviews. This team, which is part of our internal audit function, conducted 21 credit risk reviews Bank-wide in 2003. More than 500 bank officers involved in business banking credit have undergone credit process training during the year. We have also begun work on unit-by-unit self assessments as we work towards achieving our target of 100% "pass" audits with tighter controls.

Productivity: We are in the process of transforming our branches in Malaysia to centralise processing activities to the extent possible. This project is expected to be completed in the fourth quarter of 2004. Another major project is underway to centralise our operations in two locations – in Singapore and in Malaysia, with each backing the other as disaster recovery centre.

A quality awareness training programme was rolled out bank-wide in 2003. During the year, we embarked on five cross-functional process improvement projects, including projects covering letter of credit ("LC") issuance, mortgage loan processing, and new product approval processes. The results are encouraging. With the new LC issuance process, we are now close to achieving 6-sigma for same day turnaround for LC applications, despite an extended 6 p.m. cut-off time, making OCBC the most efficient LC issuing bank in Singapore. The re-engineering of our mortgage loan processes has resulted in our sales executives being better equipped and more efficient in responding to customers' needs. Our new product approval time is expected to be reduced by more than 50%, paving the way for faster product innovation. Altogether, we estimate that these process improvement projects will lead to S$30 million in revenue increases and/or cost savings every year.

Employee Commitment: To develop and reward talent, we have enhanced our career development programmes and further differentiated our incentive compensation programmes. Training for staff has been stepped up, including performance coaching and career best workshops. Our average training days per staff was 5.3, exceeding our initial target of 5 days. We introduced a Deferred Share Plan for senior managers, which helped increase the percentage of our employees who own OCBC shares to 10%, from 6% previously, a good start on our 30% target. We also began a process to fill job vacancies through increasing internal transfers, achieving a significant improvement over 2002.

Overseas Expansion: Strengthening our Malaysia business is an integral part of the New Horizons strategy as it will prepare the Group for further overseas expansion. In 2003, we implemented various measures to accelerate cross-border business development and the sharing of experiences. This began by an alignment of the organisation structure Group-wide. We also began executing our plans to increase market share in Malaysia, which focussed on enhancing our capabilities in sales and distribution, product development, processing and overall operational efficiency.

For the year, OCBC Malaysia's net profit rose 6.6% to RM205 million (S$94 million), driven by higher fee and commission income and lower provisions. Housing loans and wealth management did well, with housing loans surging by 24% to RM4.7 billion, and unit trust sales rising four-fold. We obtained central bank approval to distribute life insurance products and launched three of such products during the year, achieving strong sales. We have an existing strategic tie-up with Great Eastern Life Assurance (Malaysia) Berhad to distribute their mortgage reducing term assurance and single premium endowment products. We also placed greater emphasis on our Islamic Banking products and services in line with the growing importance of Malaysia as a regional Islamic financial centre.

Enhancing Shareholder Value: Our New Horizons target is to achieve 12% ROE by 2005, and deliver annual earnings per share growth of 10% or more. For 2003, we achieved 10.0% return on ordinary shareholders' funds. Excluding the non-core gains, our ROE was 8.7%, up from 7.4% in 2002. Our core EPS growth was 20%, indicating good progress towards our longer term goal.

Much was accomplished on the capital management front. As part of our efforts to restructure our Tier 1 capital and utilise lower-cost capital, we raised a total of S$895 million of Tier 1 preference shares during the year. We paid a special cash dividend of S$0.4975 per share (S$0.6378 gross) in July 2003, and at the same time gave shareholders the option to elect to receive preference shares in lieu of cash. We also cancelled 0.94% of our shares in conjunction with our F&N share divestment.

During the year we reduced our stakes in F&N and WBL Corporation to below 10% to comply with regulatory guidelines. We also sold a development property site at Mount Emily Road through a public tender. Our associate, Raffles Investments, sold its remaining stake in Raffles Hotel.

Following the recent decision by Robinsons not to sell its retail business, we will review our options with regard to our stake in Robinsons, taking into account the regulatory guidelines on divestments of non-core assets, and our shareholders' interests.

Challenges Ahead 2004 is expected to be a better year as many leading indicators, including the stock market indices, continue to pick up. The Government projects Singapore's GDP growth this year to improve to 3 – 5%, while Malaysia's GDP is expected to grow by 5.5 – 6%. Globally, there are signs of a synchronised global economic recovery led by the US, Japan and Europe, with China continuing to be a growth engine for Asia. If there are no major shocks to the global or regional economies, such a scenario bodes well for our revenues, particularly if domestic employment prospects improve.

In today's fast changing financial services industry, it is not sufficient to rely on traditional lending activity for our revenue. We continue to seek to reduce our reliance on interest income, and develop skills in designing and marketing new financial products and services to meet our customers' needs so as to grow our non-interest income.

While size is not necessarily a measure of quality, it nevertheless confers significant economies of scale. We will grow, organically and through joint ventures, alliances and acquisitions in Singapore and elsewhere, but at a time and in a manner of our choice. In the meantime we will continue to invest in our people and our infrastructure, making further improvements to our information systems and refining our risk management skills. We will push forward aggressively in Malaysia, organising to take full advantage of our traditional strengths there. We will also strengthen our culture of customer focus and make service excellence a hallmark that will increasingly distinguish OCBC from other financial institutions over time.

We remain committed to restructuring our capital to make it more efficient. The disposal of non-core assets will continue, not just in response to the requirements of the monetary authority, but also to support growth in our core business and to enhance shareholder value.

A Word of Thanks Looking back on 2003, we feel a sense of satisfaction. In spite of the difficult environment, we launched our New Horizons strategy and made good progress in building OCBC into a high performance bank. We were able to stay the course in pursuing our longer term strategic goals, and we came through with solid financial results for the year.

Clearly, these achievements would not have been possible without the support of our customers, whom we thank for their continuing loyalty to OCBC. We also thank all our colleagues for their hard work throughout a difficult year. With their dedication and commitment, we are well on our way towards building OCBC into the financial institution that will deliver on its purpose, which is to help individuals and businesses across communities achieve their aspirations by providing innovative financial services.

Our appreciation also goes to our fellow Board members for contributing their invaluable time and expertise. Mr Lee Seng Wee, who served eminently as Chairman for eight years, stepped down on 1 July 2003. We are pleased that he remains on the Board as a non-executive Director and continues to share his wealth of experience. On behalf of the Board, we express our deep gratitude to Mr Lee for his many years of leadership, and for his tireless work in furthering OCBC's interests.

Finally, we wish to thank you, our shareholders, for your continued support.

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CHEONG CHOONG KONG
Chairman

DAVID CONNER
Chief Executive Officer

11 February 2004