

Financial Statements

for the year ended 31 december 2003

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Annual Report

for the year ended 31 december 2003

The Directors take pleasure in presenting the Financial Statements for the year ended 31 December 2003.

PRINCIPAL ACTIVITIES

The principal activity of the Bank of South Pacific Limited (BSP) is the provision of commercial banking and finance services throughout Papua New Guinea. BSP is a company listed on the Port Moresby Stock Exchange (POMSoX), incorporated under the Companies Act of Papua New Guinea, and is an authorised Bank under the Banks and Financial Institutions Act of Papua New Guinea. Its registered office is at Douglas Street, Port Moresby.

OPERATING PROFIT

For the year ended 31 December 2003, the profit after tax was K39.981 million (2002: K85.830 million loss after write off of goodwill on acquisition).

The operating profit after tax before abnormal items, was K39.981 million (2002: K54.727 million).

DIVIDENDS

No dividends have been declared/payable in respect of the year ended 31 December 2003 (2002: K18.059 million full dividend).

DIRECTORS AND OFFICERS

The following were directors of the Bank of South Pacific Limited during the year ended 31 December 2003:

N N Beangke	J G Jeffery
T E Fox	Garth McIlwain
Gerea Aopi	Vai Reva
Sir Nagora Bogan	N R Smith
Dr Ila Temu	

Details of directors' tenure and directors and executives' remuneration during the year are provided in Note 26 of the Notes to the Financial Statements.

AUDITORS

Details of amounts paid to the auditors for audit and other services are shown in Note 5 of the Notes to the Financial Statements.

DONATIONS

Donations made by the company during the year amounted to K62,132.

INTERESTS REGISTER

Transactions recorded in the Interests Register are disclosed in Note 25 of the Notes to the Financial Statements.

For, and on behalf of, the Directors.

Dated and signed in Port Moresby this 25th day of March 2004.

GARTH McILWAIN
Managing Director

T.E. FOX
Director

Statement by the Directors

for the year ended 31 december 2003

In the opinion of the Directors of Bank of South Pacific Limited:

- a) The Income Statement is drawn up so as to exhibit a true and fair view of the results of the business of the Company for the year ended 31 December 2003.
- b) The Balance Sheet is drawn up so as to exhibit a true and fair view of the state of affairs of the Company as at 31 December 2003.
- c) The Statement of Cash Flows is drawn up so as to exhibit a true and fair view of the movements in cash of the Company for the year ended 31 December 2003.
- d) The Statement of Changes in Equity is drawn up so as to exhibit a true and fair view of the changes in equity for the year ended 31 December 2003.

ADDITIONAL STATUTORY INFORMATION

The results of the Company's operations during the financial year have, in the opinion of the Directors, not been materially affected by items of an abnormal nature, other than those disclosed in the financial statements.

In the opinion of the Directors, no circumstances have arisen that make adherence to the existing method of valuation of assets or liabilities of the Company misleading or inappropriate.

No contingent liability has arisen since the end of the financial year, which continues to exist at the date of this report, other than those, disclosed in the financial statements.

At the date of this report the Directors are not aware of any circumstances that would render the values attributed to current assets in the financial statements misleading.

No contingent liability other than that disclosed in the notes to the attached financial statements has become enforceable, or is likely to become enforceable, within a period of twelve months from the date of this report, that will materially affect the Company in its ability to meet obligations as and when they fall due.

Dated and signed at Port Moresby this 25th day of March 2004.

GARTH McILWAIN
Managing Director

T.E. FOX
Director

Income Statement & Balance Sheet

for the year ended 31 december 2003

Income Statement

<i>All amounts are expressed in K'000</i>	Note	2003	2002
Interest income	1	209,990	154,417
Interest expense	1	(61,870)	(37,958)
Net interest income		148,120	116,459
Fee and commission income	2	26,649	20,759
Other income	3	68,515	58,281
Net operating income		243,284	195,499
Bad and doubtful debts (expense)/recovery	4	8,112	3,823
Other operating expenses	5	(191,054)	(137,705)
Operating profit/(loss) before tax and abnormal items		60,342	61,617
Abnormal items net of applicable tax	7	-	(140,557)
Operating profit/(loss) before tax and after abnormal items		60,342	(78,940)
Income tax expense	6	(20,361)	(6,890)
Operating profit/(loss) from ordinary activities after tax		39,981	(85,830)
Earnings per share - basic & diluted (in toea per share)	29	9	(23)

Balance Sheet

<i>All amounts are expressed in K'000</i>	Note	2003	2002
Assets			
Cash and balances with central banks	8	146,380	173,615
Treasury bills	9	698,142	496,113
Amounts due from other banks	10	101,762	133,359
Loans and advances to customers	11	705,306	702,635
Property, plant and equipment	12	174,947	171,834
Investment securities	13	-	20,286
Deferred tax assets	14	9,965	12,128
Income tax recoverable		-	5,314
Other assets	15	68,415	63,855
Total assets		1,904,917	1,779,139
Liabilities			
Amounts due to other banks	16	5,704	1,807
Amounts due to customers	17	1,623,645	1,552,161
Other borrowed funds	18	10,000	15,000
Other liabilities	19	63,098	47,875
Provision for income tax		2,742	-
Other provisions	20	18,988	15,800
Total liabilities		1,724,177	1,632,643
Shareholders Equity			
Ordinary shares	21	182,915	182,422
Retained earnings/(accumulated losses)	22	(21,991)	(43,913)
Other reserves	22	19,816	7,987
Total shareholders' equity		180,740	146,496
Total equity and liabilities		1,904,917	1,779,139

The attached notes form an integral part of these financial statements

Statement of Changes in Shareholders Equity & Cash Flow Statement

for the year ended 31 december 2003

Statement of Changes in Shareholders Equity

<i>All amounts are expressed in K'000</i>	Notes	Share capital	Reserves	Retained earnings/ (accumulated losses)	Total
Balance as at 1 January 2002		17,919	10,281	49,234	77,434
Tax effect transfer to deferred income tax liability - revaluation reserve		-	(2,294)	-	(2,294)
Net profit/(loss)		-	-	(85,830)	(85,830)
Final dividend paid for 2001		-	-	(7,317)	(7,317)
Issue of ordinary shares		164,503	-	-	164,503
Balance at 31 December 2002	21 & 22	182,422	7,987	(43,913)	146,496
Net profit/(loss)		-	-	39,981	39,981
Final dividend paid for 2002		-	-	(18,059)	(18,059)
Issue of ordinary shares		493	-	-	493
Revaluation of property		-	11,829	-	11,829
Balance at 31 December 2003		182,915	19,816	(21,991)	180,740

Cash Flow Statement

<i>All amounts are expressed in K'000</i>	Note	2003	2002
Cash flow from operating activities			
Interest received		209,191	165,251
Fees and other income		102,186	76,563
Interest paid		(60,798)	(40,515)
Amounts paid to suppliers and employees		(148,807)	(105,788)
Operating cash flow before changes in operating assets	28	101,772	95,511
Decrease/(increase) in loans		5,441	(8,767)
Decrease/(increase) in bills receivable and other assets		(14,002)	(13,389)
(Decrease)/increase in deposits		71,485	(293,880)
(Decrease)/increase in bills payable and other liabilities		11,071	(11,320)
Net cash flow from operations before income tax		175,767	(231,845)
Income taxes paid		(15,212)	(4,216)
Net cash flow from operating activities		160,555	(236,061)
Cash flow from investing activities			
Decrease/(increase) in Government securities		(181,744)	318,097
Expenditure on property, plant & equipment		(21,067)	(78,512)
Proceeds from disposal of property, plant & equipment		1,363	2,009
Acquisition of PNGBC - net cash inflow	7	-	96,956
Net cash flow from investing activities		(201,448)	338,550
Cash flow from financing activities			
Issue of share capital		-	94,775
Proceeds/(Repayment of) from borrowings		(5,000)	15,000
Dividends paid		(18,056)	(7,317)
Net cash flow from financing activities		(23,056)	102,458
Effect of exchange rate movements on cash and cash equivalents		1,220	1,765
Net increase/(decrease) in cash and cash equivalents		(62,729)	206,712
Cash and cash equivalents at the beginning of the year		305,167	98,455
Cash and cash equivalents at the end of the year	24	242,438	305,167

The attached notes form an integral part of these financial statements

Accounting Policies

for the year ended 31 december 2003

The principal accounting policies adopted in the preparation of these financial statements are set out below:

A BASIS OF PRESENTATION AND GENERAL ACCOUNTING POLICIES

The financial statements of the Bank of South Pacific Limited are prepared in accordance with International Financial Reporting Standards and interpretations of these standards issued by the Standards Interpretations Committee. They are prepared on the basis of the historical cost convention, as modified by the revaluation of certain non-current assets and financial instruments.

Estimates and assumptions have been used to achieve conformity with generally accepted accounting principles in the preparation of these financial statements. These assumptions and estimates affect balances of assets and liabilities, contingent liabilities and commitments at the end of the reporting period, and amounts of revenues and expenses during the reporting period. Whilst the estimates are based on management's best knowledge of current events and conditions, actual results may ultimately differ from those estimates.

The financial statements are presented in Papua New Guinea Kina, expressed in thousands of Kina, as permitted by Papua New Guinea Accounting Standards.

B DERIVATIVE FINANCIAL INSTRUMENTS AND ACCEPTANCES

Forward foreign exchange contracts entered into for trading purposes are initially recognised at cost and subsequently re-measured at fair value based upon the forward rate. Gains and losses on such contracts are taken to the Income Statement.

Acceptances comprise undertakings by the bank to pay bills of exchange drawn on customers. The bank expects most acceptances to be settled simultaneously with the reimbursement from the customers. Customer acceptances are accounted for as off-balance sheet transactions and are disclosed as contingent liabilities and commitments.

The bank does not actively enter into or trade in complex forms of derivative financial instruments such as currency and interest rate swaps and options.

C INTEREST INCOME AND EXPENSE

Interest income and expense are recognised in the Income Statement on an accrual basis using the effective yield method. The income arising from the various forms of instalment credit has been determined using the effective interest method.

Interest income includes coupons earned on inscribed stock and accrued discount and premium on treasury bills.

D FEE AND COMMISSION INCOME

Fees and commissions are generally recognised on an accrual basis when the service has been provided. All

non-refundable front-end loan fees and other risk related fees that constitute cost recovery are taken to income when levied.

E BORROWING EXPENSES

Expenses associated with the borrowing of funds are charged to the Income Statement in the period in which they are incurred.

F LOANS AND PROVISIONS FOR LOAN IMPAIRMENT

Loans are originated by providing funds directly to the borrower and are recognised when cash is advanced to borrowers.

All loans and advances receivable are subject to continuous management review. A specific provision for loan impairment is established if there is objective evidence that the bank will not be able to collect all amounts due under the terms of loans. The amount of the provision approximates the difference between the carrying amount and the recoverable amount, which is the current best estimate of the present value of expected future cash flows arising from the asset. All bad debts are written off against the specific provision for loan impairment in the period in which they are classified as irrecoverable. Subsequent recoveries are credited to the provision for loan losses in the income statement.

General provisions for impairment are maintained to cover non-identifiable possible losses and latent risks inherent in the overall portfolio of loans and advances. The provisions are determined having regard to the level of risk weighted assets, economic conditions, the general risk profile of the credit portfolio, past loss experience and a range of other criteria. The amount necessary to bring the provisions to their assessed levels, after write-offs, is charged to the Income Statement.

G GOODWILL

Goodwill represents the excess of the cost of any acquisition over the fair value of the share of net assets acquired at the date of acquisition. Goodwill is reported in the balance sheet as an intangible asset and is amortised using the straight line method over its estimated useful life.

In determining the estimated useful life of goodwill, management considers various factors including existing market share, potential growth opportunities, and other factors inherent in the acquired business. This assessment is reviewed at each balance date, so that any indication of impairment with implications for the recoverability of goodwill can be tested, and adjustments to the carrying value of goodwill made if necessary.

During the prior year, a significant amount of goodwill arose on a major acquisition, the recoverable amount of which was determined to be materially lower than its book value. Accordingly, the amount was taken to the Income Statement. Note 7 to these Financial Statements provides further details on the transaction.

H COMPUTER SYSTEMS DEVELOPMENT COSTS

Costs incurred to develop and enhance the bank's computer systems are capitalised to the extent that benefits do not relate solely to revenue that has already been brought to account and will contribute to the future earning capacity of the economic entity. These costs are amortised over the estimated economic life of four years using the straight line method. Costs associated with maintaining computer software programs are recognised as an expense when incurred.

I PROPERTY, PLANT AND EQUIPMENT

All property is stated at revalued amount less accumulated depreciation. Plant and equipment is stated at cost less accumulated depreciation. Depreciation is assessed from the month of acquisition. The Directors have determined that all bank properties will be revalued within a cycle of 3 years. Revaluation increments are credited to the premises revaluation reserve, whilst revaluation decrements are debited to the Income Statement unless they relate to the reversal of a pre-valuation revaluation increment of the same property.

The following basis and method of depreciation is used:

Class of asset	Method	Rate
Property (excluding land)	Straight line basis	2-3% p.a
Plant and equipment	Straight line basis	10 - 25% pa

Gains or losses on disposals (being the difference between the carrying value at the time of sale or disposal and the proceeds received) are taken into account in determining operating profit for the year. Where the carrying value of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Repairs and maintenance are taken into account in determining operating profit when the expenditure is incurred.

J LEASES

Bank is lessee

All leases entered into by the bank are operating leases. Total payments made are charged to the Income Statement reflecting the pattern of benefits derived from the leased assets.

Bank is lessor

Finance leases are included in Loans and Advances to Customers (Note 11) and are accounted for under the finance method whereby income is taken to account over the life of the lease in proportion to the outstanding investment balance.

K CASH AND CASH EQUIVALENTS

For the purpose of the cash flow statement, cash and cash equivalents comprises notes and coins, and balances due to and from other banks.

L PROVISIONS

Provisions are created when a legal or constructive obligation arises as a result of a past event, it is probable that an outflow of economic value will be required to settle the obligation, and the amount of the obligation can be reliably estimated.

Long service leave entitlements represent the pro-rata statutory entitlement for all existing staff members based on length of service up to balance sheet date.

Provision for annual leave, leave fares and other entitlements are based upon the bank's personnel policies, contractual obligations and services rendered by employees up to balance sheet date.

M EMPLOYEE BENEFITS

Post employment benefits - defined contribution plans

A defined contribution plan is a pension plan under which the bank pays fixed contributions into a separate fund, and there is no recourse to the bank for employees if the fund has insufficient assets to pay employee benefits relating to service up to the balance sheet date.

The bank pays contributions to publicly or privately administered superannuation plans on a mandatory, contractual or voluntary basis in respect of services rendered up to balance sheet date by all Papua New Guinean staff members. The contributions are at the current rate of seven per cent of employees' gross salary. Once the contributions have been paid, the bank has no further payment obligations for post-employment benefits from the date an employee ceases employment with the bank.

N DEFERRED INCOME TAXES

The liability method is used to account for deferred income tax arising from temporary differences between the tax bases of assets and liabilities and their carrying values in the financial statements.

The major temporary differences relate to depreciation of property, plant and equipment, employee provisions, tax losses carried forward, provisions for bad and doubtful debts and lease receivables.

Deferred income tax is calculated using tax rates ruling at balance sheet date. Deferred income tax assets are recognised only if it is probable that future profits will be available against which temporary differences can be utilised.

Income tax payable on profits, based on the Papua New Guinea Income Tax Act, is recognised as an expense in the period in which the profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Accounting Policies

for the year ended 31 december 2003 (continued)

O BORROWINGS (SUBORDINATED DEBT) AND RELATED BORROWING COSTS

Certain interest bearing liabilities arising from sources other than depositors and other banks, are subordinated in respect of repayment, to all other classes of liabilities, including depositors' funds and other banks funds, and are classified as borrowings on the balance sheet. These borrowings are in the form of unsecured, subordinated fixed term debt, with interest payable half-yearly and principal repayable in full on or before maturity. They are carried on the balance sheet at their principal amount.

The interest on unsecured debt is recognised in the income statement as interest expense in the period it is incurred.

P INVESTMENTS

Investments are classified into the following categories: trading, held-to-maturity and available-for-sale. Investments that are acquired principally for the purpose of generating a profit from short-term fluctuations in price are classified as trading investments. During the period the bank did not hold any investments in this category. Investments with fixed maturity that the management has the intent and ability to hold to maturity are classified as held-to-maturity. Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; Management determines the appropriate classification of its investments at the time of the purchase and re-evaluates such designation on a regular basis.

All purchases and sales of investments are recognised on the trade date, which is the date that the bank commits to purchase or sell the asset. Cost of purchase includes transaction costs. Trading and available-for-sale investments are subsequently carried at fair value, whilst held-to-maturity investments are carried at amortised cost using the effective yield method. Realised and unrealised gains and losses arising from changes in the fair value of trading investments are included in the Income Statement in the period in which they arise.

Q FOREIGN CURRENCY

Foreign exchange held and amounts payable or receivable in foreign currencies have been translated into Papua New Guinea Kina at the mid-market exchange rates applicable at balance sheet date.

Foreign currency transactions are recorded at the exchange rates in effect at the date of the transaction. Monetary assets and liabilities arising from trading transactions or overseas borrowings are translated at closing rates. Gains and losses due to currency fluctuations on these items are included in the Income Statement.

R SHARE CAPITAL

Share issue costs

External costs directly attributable to the issue of new shares, other than on a business combination, are deducted from equity net of any related income taxes.

Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are declared.

Dividends for the year, declared after the balance sheet date, are dealt with in the subsequent events note.

S FIDUCIARY ACTIVITIES

The bank acts in a fiduciary capacity to the Central Bank in respect of the disbursement and collection of funds relating to the Central Bank's agricultural support scheme loans. The bank returns all funds and income to the Central Bank. Accordingly, all transactions pursuant to these arrangements are excluded from these financial statements.

T COMPARATIVES

Comparative figures have been adjusted to conform to changes in presentation in the current year.

Interpretation of comparative figures

The business combination that occurred with the bank's acquisition of Papua New Guinea Banking Corporation in the prior year has implications for comparisons between the current and prior year balances. The acquisition was effected at the start of April 2002. The results for the prior year incorporate only nine months of returns from the significantly larger operations from the date of acquisition. The results of the current year reflect the first full year of returns from the enlarged operations following the business combination.

Financial Risk Management

for the year ended 31 december 2003 (continued)

A BANK OPERATIONS, RISKS AND STRATEGIES IN USING FINANCIAL INSTRUMENTS

All business operations must deal with a variety of operational and financial risks. The business activities of a bank expose it to very critical and specific risks, which are principally related to the bank's primary financial intermediary role in the financial markets, including the use of financial instruments including derivatives. These market risks (risk of an advance event in the financial markets that may result in loss of earnings) include liquidity risk, foreign exchange risk, interest rate risk and credit risk.

The bank accepts deposits from customers at both fixed and floating rates and for various periods and seeks to earn above average interest margins by investing these funds in high quality assets. These margins are achieved and increased by consolidating short-term funds and lending for longer periods at higher rates whilst maintaining sufficient liquidity to meet all claims that might fall due.

The bank also seeks to raise its interest margins by obtaining above average returns, net of provisions, through lending to commercial and retail borrowers with a range of credit standing. In addition to directly advancing funds to borrowers, the bank also enters into guarantees and other commitments such as letters of credit, performance bonds, and other bonds.

The bank also enters into transactions denominated in foreign currencies. This activity generally requires the bank to take foreign currency positions in order to exploit short term movements in the foreign currency market. The Board places limits on the size of these positions. The bank also has a policy of using offsetting commitments for foreign exchange contracts, effectively minimising the risk of loss due to adverse movements in foreign currencies.

Risk in the bank is managed through a system of delegated limits. These limits set the maximum level of risk that can be assumed by each operational unit and the bank as a whole. The limits are delegated from the Board of Directors to executive management and thence to the respective operational managers.

The risk management framework establishes roles, responsibilities and accountabilities of the Asset and Liability Committee, the Credit Committee and the Executive Committee, the specific management committees charged with the responsibility for ensuring the bank has appropriate systems, policies and procedures to measure, monitor and report on risk management. The framework also includes policies and procedures which detail formal feedback processes to these management committees, to the Audit and Compliance Committee of the Board, and ultimately to the Board of Directors.

B CAPITAL ADEQUACY

The Bank is required to comply with various prudential standards issued by the Bank of Papua New Guinea (BPNG), the official authority for the prudential supervision of banks and similar financial institutions in Papua New Guinea. One of the most critical prudential standards is the capital adequacy requirement. All banks are required to maintain at least the minimum measure of capital to risk-weighted assets to absorb potential losses. The BPNG follows the prudential guidelines set by the Bank of International Settlements under the terms of the Basel Accord. The minimum ratio of base capital to risk weighted assets set by the BPNG in the prior year, was 10%, until 1 October 2003. On this date, the BPNG issued revised prudential standard 1/2003, Capital Adequacy, that prescribes ranges of overall capital ratios to measure whether a bank is under, adequately, or well capitalised, and also introduces the leverage capital ratio (see below for details). In all months, the bank complied with the prevailing prudential requirements for total capital and leverage capital. As at 31 December 2003, the bank's total capital adequacy ratio and leverage capital ratio satisfied the capital adequacy criteria for well-capitalised.

The measure of capital used for the purposes of prudential supervision is referred to as base capital. Total base capital varies from the balance of capital shown on the balance sheet and is made up of tier 1 capital (core) and tier 2 capital (supplementary), after deducting the value of investments in other banks and financial institutions. Tier 1 capital is obtained by deducting from equity capital and audited retained earnings (or losses), intangible assets including deferred tax assets. Tier 2 capital cannot exceed the amount of tier 1 capital, and can include subordinated loan capital, specified asset revaluation reserves, un-audited profits (or losses) and a small percentage of general loan loss provisions. The Leverage Capital ratio is calculated as Tier 1 Capital divided by Total Assets.

Risk weighted assets are derived from on-balance sheet and off-balance sheet assets. On balance sheet assets are weighted for credit risk by applying weightings (0, 20, 50 and 100 per cent) according to risk classification criteria set by the BPNG. Off-balance sheet exposures are risk weighted in the same way after converting them to on-balance sheet credit equivalents using BPNG specified credit conversion factors.

Financial Risk Management

for the year ended 31 december 2003 (continued)

B CAPITAL ADEQUACY (continued)

The bank's capital adequacy level is as follows:

<i>All amounts are expressed in K'000</i>	Balance sheet / notional amount		Risk-weighted amount		
	2003	2002	2003	2002	
Balance sheet assets (net of provisions)					
Currency	58,418	56,980	401	360	
Loans and advances	722,077	836,873	612,193	609,856	
Investments and short term securities	698,142	516,398	-	68	
All other assets	427,734	381,651	270,116	260,283	
Off balance sheet items	268,632	273,710	25,049	23,940	
Total	2,175,003	2,065,612	907,759	894,507	
Capital Ratios		Capital (K'000)	Capital Adequacy Ratio		
		2003	2002	2003	2002
a) Before Dividend	Tier 1 capital	148,841	122,911	16.40%	13.74%
	Tier 1 + Tier 2 capital	187,371	154,445	20.64%	17.26%
b) After Dividend	Tier 1 capital	148,841	104,852	16.40%	11.72%
	Tier 1 + Tier 2 capital	187,371	136,386	20.64%	15.25%
(c) Leverage Capital Ratio				7.83%	-

C CREDIT RISK AND ASSET QUALITY

The bank incurs risk with regards to loans and advances made to customers and other monies or investments held with financial institutions. Credit risk is the likelihood of future financial loss resulting from the failure of clients or counter-parties to meet contractual obligations to the bank as they fall due.

Credit risk is managed by analysing the risk spread across various sectors of the economy and by ensuring risk is diversely spread by personal and commercial customers. Individual exposures are measured using repayment performance, reviews and statistical techniques. Comprehensive credit standards and approval limits have been formulated, approved by the Credit and Business Risk sub-committee of the Board and implemented. The Credit Committee (which reports to the Board through the Executive and Managing Director) is responsible for the development and implementation of credit policy and loan portfolio review methodology. The Credit Committee is the final arbiter of risk management and loan risk concentration.

As indicated in Accounting Policy F - Loans and provision for loan impairment, the bank has in place processes that identify, assess and control credit risk in relation to the loan portfolio, to assist in determining the appropriateness of provisions for loan impairment. These processes also enable assessments to be made of other classes of assets that may carry an element of credit risk. The bank assigns quality indicators to its credit exposures to determine the asset quality profile.

Large credit exposures are also monitored as part of credit risk management. These are classified as balances of individual accounts or groups of related counter-parties that exceed 10% of the capital base. Included in large exposures are significant exposures to the Government and statutory bodies. As at 31 December 2003, the three largest exposures totaled

K94.207 million, accounting for over 90% of the exposure to the sector. From October 2003, the Bank of Papua New Guinea introduced a revised prudential standard for asset quality. The revised standard specifies more detailed criteria for the classification of loans into various grades of default risk and corresponding loss provision levels as a consequence of those gradings. Since its introduction, BSP has complied with the new requirement at all times.

Credit related commitments

These instruments are used to ensure that funds are available to a customer as required. The bank deals principally in the credit related commitments set out below.

Guarantees and standby letters of credit, which represent irrevocable assurances that the bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same risk as loans.

Documentary and trade letters of credit are written undertakings by the bank on behalf of a customer, authorising a third party to draw drafts on the bank for specified amounts under specified terms and conditions. They are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a conventional loan.

Commitments to extend credit represent undrawn portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. Whilst the potential exposure to loss equates to the total undrawn commitments, the likely amount of loss is less than the total commitment since the commitments to extend credit are contingent upon customers maintaining specific credit standards. The bank monitors the term to maturity of these commitments because longer term commitments generally carry a greater degree of credit risk than shorter term commitments.

Financial Risk Management

for the year ended 31 december 2003 (continued)

C CREDIT RISK AND ASSET QUALITY (continued)

Economic sector risk concentrations

Economic sector risk concentrations within the customer loan portfolio are as follows

<i>All amounts are expressed in K'000</i>	2003	%	2002	%
Commerce, finance and other business	365,011	52	344,246	49
Private households	79,637	11	128,292	18
Government and public authorities	8,159	1	58,035	8
Agriculture	48,308	7	55,807	8
Transport & communication	90,124	13	50,538	7
Manufacturing	66,502	9	36,034	5
Construction	47,565	7	29,683	5
Net loan portfolio balance	705,306	100	702,635	100

D LIQUIDITY RISK

Liquidity risk is the risk of being unable to meet financial obligations as they fall due. Liquidity policy is set by the Board, through the Asset and Liability Committee, to ensure that the bank has sufficient funds available to meet all its known and potential obligations.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of banking activities. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

Short-term mismatch of asset and liability maturity at 31 December 2003

The maturity profile of material Assets and Liabilities at 31 December 2003 is shown in the following schedule. The mismatching of maturity of assets and liabilities indicates an apparent negative net "current" asset position. However, as stated in the preceding paragraph, mismatched positions are established and managed to exploit profit opportunities that arise from them, particularly in a normal yield curve environment. Accordingly, this mismatched maturity position is considered manageable by the bank, and does not impair the ability of the bank to meet its financial obligations as they fall due. The Directors are also of

the view that the bank is able to meet its financial obligations as they fall due for the following additional reasons:

- The bank complies with the Minimum Liquid Asset Ratio ("MLAR") and Cash Reserve Requirement ("CRR") set by the regulatory authority, the Bank of Papua New Guinea ("BPNG"). The MLAR is the minimum ratio of liquid assets to total customer deposits considered by the regulator as sufficient to support exceptional liquidation by depositors, of their funds. All commercial banks are required to hold a minimum of 25% of the value of total customer deposits in the form of prescribed liquid assets. As at 31 December 2003, the bank's Liquid Asset Ratio was approximately 52%, significantly in excess of the minimum requirement (2002: 38%).

The CRR specifies that a bank must hold an amount equal to 3% of its total customer deposits in the form of cash in an account maintained at the BPNG. The bank complies with this daily requirement on an ongoing basis. The balance of the CRR account is shown in Note 8, Cash and Balances with Central Bank, and Note 23, Contingent Liabilities and Commitments.

Financial Risk Management

for the year ended 31 december 2003 (continued)

D LIQUIDITY RISK (continued)

Maturity of assets and liabilities

All amounts are expressed in K'000

As at 31 December 2003	Up to 1 month	1-3 months	3-12 months	1-5 years	over 5 years	Total
Assets						
Cash and central bank assets	97,924	-	-	48,456	-	146,380
Treasury bills	162,952	235,050	300,140	-	-	698,142
Due from other banks	82,812	18,750	200	-	-	101,762
Loans and advances	167,710	39,850	47,117	302,679	147,950	705,306
Investments	-	-	-	-	-	-
Total assets	511,398	293,650	347,457	351,135	147,950	1,651,590
Liabilities						
Due to other banks	5,704	-	-	-	-	5,704
Due to customers	1,450,996	77,626	94,333	675	15	1,623,645
Other borrowings	-	-	-	10,000	-	10,000
Other liabilities	9,035	54,063	-	-	-	63,098
Other provisions	1,187	-	4,831	-	12,970	18,988
Total liabilities	1,466,922	131,689	99,164	10,675	12,985	1,721,435
Net liquidity gap	(955,524)	161,961	248,293	340,460	134,965	(69,845)
As at 31 December 2002						
Total assets	834,039	88,330	95,646	313,854	194,138	1,526,007
Total liabilities	1,387,746	173,899	44,127	16,469	10,402	1,632,643
Net liquidity gap	(553,707)	(85,569)	51,519	297,385	183,736	(106,636)

E FOREIGN EXCHANGE RISK

Foreign exchange risk is the risk to earnings caused by a change in foreign exchange rates on open currency positions. The objective of foreign exchange risk management within the bank is to minimise the impact on earnings of any such movement.

The bank accepts foreign currency denominated transactions and therefore has exposure to movements in foreign currency. The bank has a policy to offset these transactions by minimising daily exposure. This is done through hedging material exposures as they arise. As foreign exchange contracts generally consist of offsetting commitments, they involve only limited foreign exchange risk to the bank and material loss is not envisaged.

Currency concentration of assets, liabilities, and off-balance sheet items

All amounts are expressed in K'000

As at 31 December 2003	US	AUS	EURO	PGK	Other	Total
Assets						
Cash and central bank assets	1,209	621	188	143,985	377	146,380
Treasury bills	-	-	-	698,142	-	698,142
Due from other banks	27,683	55,509	113	14,653	3,804	101,762
Loans and advances	5,445	-	-	696,952	2,909	705,306
Other assets	3	111	-	253,212	1	253,327
Total assets	34,340	56,241	301	1,806,944	7,091	1,904,917
Liabilities						
Due to other banks	-	-	-	5,704	-	5,704
Due to customers	1,158	50,761	-	1,570,659	1,067	1,623,645
Other borrowings	-	-	-	10,000	-	10,000
Other liabilities	4	866	-	83,950	8	84,828
Total liabilities	1,162	51,627	-	1,670,313	1,075	1,724,177
Net on-balance sheet position	33,178	4,614	301	136,631	6,016	180,740
Off-balance sheet net notional position	31,511	(3,806)	-	-	12,722	40,427
Credit commitments	-	-	-	207,794	-	-

Financial Risk Management

for the year ended 31 december 2003 (continued)

E FOREIGN EXCHANGE RISK (continued)

All amounts are expressed in K'000

As at 31 December 2002	US	AUS	EURO	PGK	Other	Total
Total assets	77,224	65,451	1,014	1,631,284	4,166	1,779,139
Total liabilities	9,495	51,684	-	1,571,418	46	1,632,643
Net on-balance sheet position	67,729	13,767	1,014	59,866	4,120	146,496
Off-balance sheet net notional position	11,976	1,171	62,654	-	5,797	81,598
Credit commitments	-	-	-	198,960	-	198,960

F OPERATIONAL RISK

Operational risk is the potential exposure to unexpected financial or non-financial losses arising from the way in which the bank and its subsidiaries conducts its business. Operational risk is managed through formal policies, documented procedures, business practices and compliance monitoring. An independent internal audit function also conducts regular reviews to monitor compliance with policy and regulatory environment and examines the general standard of control.

G INTEREST RATE RISK

Interest rate risk in the balance sheet arises from the potential for a change in interest rate to have an adverse effect on the revenue earnings in the current reporting period and future years. As interest rates and yield curves change over time the bank may be exposed to a loss in earnings due to the effects of interest rates on the structure of the balance sheet. Sensitivity to interest rates arises from mismatches in the re-pricing dates, cash flows and other characteristics of the assets and their corresponding liability funding. These mismatches are actively managed as part of the overall interest rate risk management process governed by the Assets and Liabilities Committee (ALCO), which meets regularly to review the effects of fluctuations in the prevailing levels of market interest rates on the financial position and cash flows of the bank. The objective of interest rate risk control is to minimise these fluctuations in value and net interest income over time, providing secure and stable sustainable net interest earnings in the long term. The table below illustrates the interest sensitivity of assets and liabilities at the balance date.

Shown in the following tables are the balance sheet structure and contractual maturity profile of assets and liabilities as at 31 December 2003 and the effective ruling rates. Given this information, and assuming the financial assets and liabilities at 31 December 2003 were to remain until maturity or settlement without any action by the bank to alter the resulting interest rate expense, an immediate and sustained 1% change in market interest rates would change net interest income by K0.93 million in the succeeding year.

Interest sensitivity of assets, liabilities and off balance sheet items - re-pricing analysis

All amounts are expressed in K'000

As at 31 December 2003	Up to 1 month	1-3 months	3-12 months	1-5 years	over 5 years	Non interest bearing
Assets						
Cash and central bank assets	146,380	-	-	-	-	-
Treasury bills	698,142	-	-	-	-	-
Due from other banks	-	101,762	-	-	-	-
Loans and advances	634,775	70,531	-	-	-	-
Other assets	-	-	-	-	-	253,327
Total assets	1,479,297	172,293	-	-	-	253,327
Liabilities						
Due to other banks	-	5,704	-	-	-	-
Due to customers	1,623,645	-	-	-	-	-
Other borrowings	-	-	10,000	-	-	-
Other liabilities	-	-	-	-	-	84,828
Total liabilities	1,623,645	5,704	10,000	-	-	84,828
Interest sensitivity gap	(144,348)	166,589	(10,000)	-	-	-

Financial Risk Management

for the year ended 31 december 2003 (continued)

G INTEREST RATE RISK (continued)

Interest sensitivity of assets, liabilities and off balance sheet items - re-pricing analysis

All amounts are expressed in K'000

As at 31 December 2002	Up to 1 month	1-3 months	3-12 months	1-5 years	over 5 years	Non interest bearing
Assets						
Cash and central bank assets	173,615	-	-	-	-	-
Treasury bills	496,113	-	-	-	-	-
Due from other banks	-	133,359	-	-	-	-
Loans and advances	632,372	70,263	-	-	-	-
Investments	-	-	20,286	-	-	-
Other assets	-	-	-	-	-	253,131
Total assets	1,302,100	203,622	20,286	-	-	253,131
Liabilities						
Due to other banks	-	1,807	-	-	-	-
Due to customers	1,552,161	-	-	-	-	-
Other borrowings	-	-	15,000	-	-	-
Other liabilities	-	-	-	-	-	63,675
Total liabilities	1,552,161	1,807	15,000	-	-	63,675
Interest sensitivity gap	(250,061)	201,815	5,286	-	-	-

Effective interest rates as at 31 December 2003

Amounts are expressed in % p.a.

	2003	2002
Assets		
Cash and central bank assets	12.50	12.00
Treasury Bills	18.10	14.97
Due from other banks	12.00	12.00
Loans and advances	12.68	12.66
Investments	-	11.28
Liabilities		
Due to other banks	12.00	12.00
Due to customers	3.27	3.22
Other borrowed funds	20.10	16.97

H FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

There is no material difference between the fair value and carrying value of the financial assets and liabilities of Bank of South Pacific Limited.

Derivative financial instruments

In the normal course of trading, the bank enters into forward exchange contracts. The bank does not actively enter into or trade in, complex forms of derivative financial instruments such as currency and interest rate swaps and options.

Exposures in foreign currencies arise where the bank transacts in foreign currencies. This price risk is minimised by entering into counterbalancing positions for material exposures as they arise. Forward and spot foreign exchange contracts are used.

Forward exchange contracts outstanding at 31 December 2003, stated at the face value of the respective contracts are:

All amounts are expressed in respective FCY'000 and K'000

As at 31 December 2003		USD	AUS	EURO	GBP	Other	Total
Selling	FCY	13,948	1,318	-	1,635	52,954	
	Kina	46,493	3,295	-	9,692	3,030	62,510
Buying	FCY	(4,495)	-	-	(1,198)	-	
	Kina	(14,982)	-	-	(7,101)	-	(22,083)
As at 31 December 2002		USD	AUS	EURO	GBP	Other	Total
Selling	FCY	18,314	5,233	277	135	81,539	
	Kina	73,846	11,976	1,170	8,721	4,068	99,781
Buying	FCY	(2,775)	-	-	(717)	(69,100)	
	Kina	(11,191)	-	-	(4,635)	(2,357)	(18,183)

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

1 NET INTEREST INCOME

<i>All amounts are expressed in K'000</i>	2003	2002
Interest income		
Cash and short term funds	2,932	1,699
PNG Public Securities: Treasury bills and inscribed stock	102,512	60,106
Loans and advances	103,684	92,415
Other	862	197
	209,990	154,417
Less:		
Interest expense		
Customer deposits	58,465	36,683
Other banks	757	926
Other borrowings	2,648	349
	61,870	37,958
	148,120	116,459

2 NET FEE AND COMMISSION INCOME

<i>All amounts are expressed in K'000</i>	2003	2002
Fee and commission income		
Credit related	9,452	7,273
Trade and international related	4,657	3,871
Electronic banking related	2,619	2,582
Other	10,063	7,184
	26,791	20,910
Less:		
Fee and commission expenses		
Agencies	38	66
Other	104	85
	142	151
	26,649	20,759

3 OTHER INCOME

<i>All amounts are expressed in K'000</i>	2003	2002
Dividend income - available for sale securities	8	8
Foreign exchange related	63,379	53,872
Other	5,128	4,401
	68,515	58,281
Included in other income:		
Profit/(loss) on sale of fixed assets	23	(1,511)
Foreign exchange related income includes gains and losses from spot and forward contracts and translated foreign currency assets		

4 BAD AND DOUBTFUL DEBTS (EXPENSE)/RECOVERY

<i>All amounts are expressed in K'000</i>	2003	2002
Bad debts (written off)/recovered - net	(2,014)	776
Net credit/(charge) to doubtful debts provision	10,126	3,047
	8,112	3,823

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

5 OTHER OPERATING EXPENSES

<i>All amounts are expressed in K'000</i>	2003	2002
Administration	43,055	27,121
Auditors remuneration	698	543
Computing	15,585	7,216
Depreciation	24,645	17,067
Amortisation of computer development	749	962
Amortisation of deferred acquisition costs	1,069	777
Non-executive Directors costs	243	403
Non-lending losses	7,204	5,946
Loss on premises revaluation	6,180	-
Fixed asset write off	1,936	-
Premises and equipment	16,310	14,453
Staff costs		
Defined contribution plans	2,318	1,818
Statutory benefit contributions	4,782	3,300
Wages and salaries	55,267	48,818
Other	11,013	9,281
	73,380	63,217
	191,054	137,705

6 INCOME TAX EXPENSE

<i>All amounts are expressed in K'000</i>	2003	2002
Current tax	16,284	(2,856)
Deferred tax	(3,815)	10,999
Current year	12,469	8,143
Prior year adjustments	5,517	334
Tax credit in respect of settlement of PNGBC tax obligations at acquisition	2,375	(1,587)
	20,361	6,890
Tax calculated at 30% of profit before tax (2002: 25%)	18,320	(19,735)
Expenses not deductible for tax	531	35,432
Deductible expenses not recognised for accounting purposes	(182)	(132)
Adjustment to deferred taxes for change in tax rate	-	(2,404)
Tax credit in respect of Community Service Obligations Act	(6,200)	(5,018)
Tax credit in respect of settlement of PNGBC tax obligations at acquisition	2,375	(1,587)
Prior year under provision	5,517	334
	20,361	6,890

Further information about deferred taxes is presented in Note 14.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

7 ABNORMAL ITEMS

<i>All amounts are expressed in K'000</i>	2003	2002
Write off of goodwill on acquisition of PNGBC Limited	-	140,557
Tax applicable	-	-
	-	140,557

Acquisition of Papua New Guinea Banking Corporation Limited in 2002

In December 2001, the Independent Public Business Commission under the Papua New Guinea Government's privatisation program, accepted a bid by the Bank of South Pacific Limited for the purchase from it, of Papua New Guinea Banking Corporation Limited. On April 9 2002, the Bank effected the settlement transaction for the purchase of Papua New Guinea Banking Corporation Limited from the Government of Papua New Guinea. The goodwill of K140,557 represents the excess of the consideration paid of K230,904 over the net assets acquired of K90,347. There was a net cash flow on acquisition of K96,956, represented by the surplus of cash acquired over the portion of the consideration discharged by cash.

The directors had determined that reliable assessments of the future economic benefits flowing from the goodwill could not be made because of the high levels of risk and uncertainty surrounding the critical decision factors. Accordingly, the amount was written off in 2002 as allowed in these circumstances, by the relevant accounting standards, IAS 22: Business Combinations and IAS 36: Impairment of Assets.

8 CASH AND BALANCES WITH CENTRAL BANK

<i>All amounts are expressed in K'000</i>	2003	2002
Notes and coins	58,419	57,890
Money market placements	-	22,000
Balances with central bank other than statutory deposit	39,505	17,168
Included in cash and cash equivalents	97,924	97,058
Statutory deposits with central bank	48,456	76,557
	146,380	173,615

9 TREASURY BILLS

<i>All amounts are expressed in K'000</i>	2003	2002
Treasury bills - face value	750,000	500,000
Discount for interest receivable	(51,858)	(3,887)
	698,142	496,113

Treasury bills are debt securities issued by the Bank of Papua New Guinea for a term of three months, six months or a year. Treasury bills are classified as assets held for trading and carried at fair value.

10 AMOUNTS DUE FROM OTHER BANKS

<i>All amounts are expressed in K'000</i>	2003	2002
Items in the course of collection	27,695	34,442
Placements with other banks	74,067	98,917
Included in cash and cash equivalents	101,762	133,359

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

11 LOANS AND ADVANCES TO CUSTOMERS

All amounts are expressed in K'000

	2003	2002
Loans originated by the bank		
Overdrafts	162,379	163,406
Leases	10,133	13,174
Term loans	497,597	491,001
Mortgages	88,256	98,239
Gross loans and advances net of reserved interest	758,365	765,820
Less allowance for losses on loans and advances	(53,059)	(63,185)
	705,306	702,635

Allowance for losses on loans and advances

Movement in allowance for losses on loans and advances:

Balance at 1 January	63,185	9,840
Balance of provisions acquired on amalgamation	-	56,392
Provision for loan impairment	7,290	1,508
Loans written off against provisions/writeback of provisions no longer required	(17,416)	(4,555)
Balance at 31 December	53,059	63,185

Loans and advances to customers includes finance lease receivables, analysed as follows:

Investment in finance leases receivable

Not later than 1 year	1,554	6,127
Later than 1 year and not later than 5 years	10,628	8,597
Later than 5 years	-	2,325
	12,182	17,049
Unearned future finance income	(2,049)	(3,875)
Net investment in finance leases	10,133	13,174

The net investment in finance leases is analysed as follows:

Not later than 1 year	1,354	5,018
Later than 1 year and not later than 5 years	8,779	6,419
Later than 5 years	-	1,737
	10,133	13,174

12 PROPERTY, PLANT AND EQUIPMENT

All amounts are expressed in K'000

	Capital WIP	Premises	Equipment	Total
At 31 December 2002				
Cost	16,507	103,064	104,979	224,550
Accumulated depreciation	-	(12,231)	(40,485)	(52,716)
Net book amount	16,507	90,833	64,494	171,834
Year ended 31 December 2003				
Opening net book amount	16,507	90,833	64,494	171,834
Additions	20,850	628	28,542	50,020
Disposals	(29,643)	(1,269)	(132)	(31,044)
Adjustments: - Revaluation increases	-	16,898	-	16,898
- Revaluation decreases	-	(6,180)	-	(6,180)
- Write offs	-	-	(1,936)	(1,936)
Depreciation charge	-	(3,633)	(21,012)	(24,645)
Closing net book amount	7,714	97,277	69,956	174,947
At 31 December 2003				
Cost	7,714	105,401	129,502	242,617
Accumulated depreciation	-	(8,124)	(59,546)	(67,670)
Net book amount	7,714	97,277	69,956	174,947

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

13 INVESTMENT SECURITIES

<i>All amounts are expressed in K'000</i>	2003	2002
Securities - held-to-maturity		
Inscribed stock - issued by Bank of Papua New Guinea	-	20,286
Movement for the year in investment securities:		
At 1 January	20,286	-
Securities acquired on amalgamation	-	14,970
Additions	-	15,000
Disposals (redemptions)	(20,286)	(9,970)
	-	20,000
Interest receivable	-	286
At 31 December	-	20,286

14 DEFERRED TAX ASSET

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 30% applicable from 1 January 2003 (2002: 25%). Deferred income taxes are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable. At 31 December, the net benefit reflects the estimated future tax benefits at applicable income tax rates of the following:

<i>All amounts are expressed in K'000</i>	2003	2002
Specific allowance for losses on loans and advances	11,072	12,807
General allowance for losses on loans and advances	4,851	5,425
Employee related provisions	5,369	4,738
Prepaid expenses	(314)	(281)
Other provisions	327	34
Depreciation and amortisation	(3,022)	(7,669)
Revalued assets	(7,363)	(2,294)
Deferred expenditure	(955)	(197)
Other	-	(435)
	9,965	12,128

The movements on the deferred income tax accounts are as follows:

At 1 January	12,128	540
Deferred tax balances acquired on acquisition of PNGBC	-	18,379
Tax expense - change in tax rate	-	2,404
Tax losses utilised during the year	-	(11,128)
Specific allowance for losses on loans and advances	(1,735)	(837)
General allowance for losses on loans and advances	(573)	75
Employee related provisions	631	964
Depreciation and amortisation	4,647	(2,315)
Prepaid expenses	(33)	(84)
Other provisions	293	(5)
Deferred expenditure	(758)	(73)
Revalued assets	(5,069)	4,208
Other	434	-
At 31 December	9,965	12,128

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

15 OTHER ASSETS

<i>All amounts are expressed in K'000</i>	2003	2002
Items in transit and other assets	29,333	36,497
Accrued income	25,798	8,991
Deferred acquisition costs	3,802	4,400
Computer development costs	950	1,699
Prepayments	8,511	12,258
Accounts receivable	21	10
	68,415	63,855

16 AMOUNTS DUE TO OTHER BANKS

<i>All amounts are expressed in K'000</i>	2003	2002
Items in the course of collection	5,704	1,80

17 AMOUNTS DUE TO CUSTOMERS

<i>All amounts are expressed in K'000</i>	2003	2002
Demand/current	1,174,800	1,128,950
Term	448,845	423,211
	1,623,645	1,552,161

18 OTHER BORROWED FUNDS

<i>All amounts are expressed in K'000</i>	2003	2002
Loan capital		
Subordinated loan	10,000	15,000

The loan capital qualifies as tier 2 capital under current capital adequacy guidelines issued by the Bank of Papua New Guinea. The indebtedness is subordinated to all other classes of liabilities, and is repayable on or before maturity on 30 September 2007. Interest is payable every six months on 1 April and 1 October each year.

Interest rate: actual rate for 182-day treasury bills issued by Bank of Papua New Guinea at the commencement of the interest period + 2%

19 OTHER LIABILITIES

<i>All amounts are expressed in K'000</i>	2003	2002
Creditors and accruals	9,496	10,299
Items in transit and all others	53,602	37,576
	63,098	47,875

20 OTHER PROVISIONS

<i>All amounts are expressed in K'000</i>	2003	2002
Staff related	17,873	15,687
Provision for non lending loss	1,090	90
Provision for dividend payable	2	-
Other	23	23
	18,988	15,800

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

21 ORDINARY SHARES

<i>Number of shares in '000s, Book value in K'000</i>	Number of shares	Book value
At 31 December 2001/1 January 2002	17,016	17,919
Issue of shares - capital raising	14,581	94,775
Issue of shares - consideration for business acquisition	10,711	69,620
Issue of shares - remuneration of employees	45	108
At 31 December 2002/1 January 2003	42,353	182,422
Issue of shares - remuneration of employees	62	493
Share split (1/10)	381,730	-
At 31 December 2003	424,145	182,915

On 28 August 2003, BSP successfully listed on the Port Moresby Stock Exchange. On 31 October 2003, BSP applied for and received approval for Port Moresby Stock Exchange to effect a 1/10 share split where each old share was divided into 10 new shares.

The issued capital of Bank of South Pacific Limited comprises ordinary shares. Following is a summary of principal shareholders as at 31 December 2003 and their respective percentage holdings.

Major shareholders: % shareholding	2003	2002
Independent Public Business Corporation	25.25	25.29
Motor Vehicles Insurance Limited	12.50	12.52
Credit Corporation (PNG) Limited	11.45	11.47
Petroleum Resources Kutubu Limited	10.88	10.90
Public Officers Superannuation Fund Board	10.88	10.90
National Superannuation Fund Limited	10.02	10.03
Teachers Savings & Loans Society Limited	5.77	5.78
Defence Force Retirement Benefits Fund Board	4.86	4.87
Sir George Constantinou	0.82	0.82
Lamin Trust Fund	0.72	0.72
Evangelical Lutheran Church of PNG Superannuation Board	-	0.49
	93.15	93.79
All Others	6.85	6.21
	100.00	100.00

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

22 RESERVES AND RETAINED EARNINGS/(ACCUMULATED LOSSES)

<i>All amounts are expressed in K'000</i>	2003	2002
Reserves comprise:		
Revaluation reserve	17,181	5,352
Capital reserve	635	635
General reserve	2,000	2,000
	19,816	7,987
MOVEMENT IN RESERVES FOR THE YEAR:		
Revaluation reserve		
At 1 January	5,352	7,646
Adjustment for deferred tax liability	(5,069)	(2,294)
Net gains from changes in fair value of property, plant and equipment	16,898	-
At 31 December	17,181	5,352
Capital reserve		
At 1 January	635	635
No movement for the year	-	-
At 31 December	635	635
General reserve		
At 1 January	2,000	2,000
Movement for the year	-	-
At 31 December	2,000	2,000
MOVEMENT IN RETAINED EARNINGS FOR THE YEAR:		
Retained earnings/(losses)		
At 1 January	(43,913)	49,234
Net profit/(loss) for the year	39,981	(85,830)
Dividend for prior year	(18,059)	(7,317)
Interim dividend for current year	-	-
At 31 December	(21,991)	(43,913)

23 CONTINGENT LIABILITIES AND COMMITMENTS

<i>All amounts are expressed in K'000</i>	2003	2002
Off balance sheet financial instruments		
Standby letters of credit	3,415	12,195
Guarantees and indemnities issued	44,620	42,618
Trade letters of credit	12,803	19,937
Commitments to extend credit	207,794	198,960
	268,632	273,710

LEGAL PROCEEDINGS

A number of legal proceedings against the bank were outstanding as at 31 December 2003. No provision has been made as existing management information and professional advice indicate that it is unlikely that any significant loss will arise. Based on information available at 31 December 2003, the bank estimates a contingent liability of K8.69million (2002: K1.6 million) in respect of these proceedings.

STATUTORY DEPOSITS WITH THE CENTRAL BANK

Cash reserve requirement - 3% of all amounts due to customers (2002: 5 %)	48,456	76,557
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COMMITMENTS FOR CAPITAL EXPENDITURE

Amounts with firm commitments, and not reflected in the accounts	4,899	27,079
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OPERATING LEASE COMMITMENTS

Not later than 1 year	3,225	3,481
Later than 1 year and not later than 5 years	1,050	1,214
Later than 5 years	1,156	1,497
	5,431	6,192

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

24 CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with less than 90 days maturity.

<i>All amounts are expressed in K'000</i>	2003	2002
Cash and balances with central bank (note 8)	146,380	173,615
Due from other banks (note 10)	101,762	133,359
Due to other banks (note 16)	(5,704)	(1,807)
	242,438	305,167

25 RELATED PARTY TRANSACTIONS

Related parties are considered to be enterprises or individuals with whom the bank is especially related because either they or the bank are in a position to significantly influence the outcome of transactions entered into with the bank, by virtue of being able to control, dominate or participate in a fiduciary capacity, in decision-making functions or processes. The bank conducted transactions with the following classes of related parties during the year:

- Directors and/or parties in which the director has significant influence
- Key management personnel and other staff and/or parties in which the individual officer has significant influence

A number of banking transactions are entered into with these related parties in the normal course of business, and include loans, deposits, property rentals, share transfers and foreign currency transactions. These transactions are carried out on commercial terms and market rates. For the year ended 31 December 2003, balances and transactions of accounts for Directors were as follows:

<i>All amounts are expressed in K'000</i>	2003
Deposits	
Opening balances	1,091
Net Movement	1,859
Closing Balance	2,950
Interest Paid	63
Loans and advances	
Opening balances	1,169
Loans issued	860
Interest	176
Charges	21
Loan Repayments	(498)
Closing Balance	1,728

Incentive-based transactions are provided for staff. Such transactions include marginal discounts on rates, and specific fee concessions. These incentives are mainly percentage-based on market rates and fees, and as such, staff accounts are always subject to underlying market trends in interest rates and fees. As at 31 December 2003, staff account balances were as follows:

<i>All amounts are expressed in K'000</i>	2003	2002
Housing loans	14,038	17,514
Other loans	1,578	2,374
Leases	-	663
	15,616	20,551
Cheque accounts	2,826	2,321
Foreign currency accounts	526	1,197
Savings accounts	340	1,101
Term deposits	-	133
	3,692	4,752

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

25 RELATED PARTY TRANSACTIONS (continued)

Interests register

The following are transactions recorded in the interests register:

Name	Nature of Interest	
N. N. Beangke	Director	Oil Search Limited ¹ , Credit Corporation(Fiji) Ltd, New Guinea Islands Produce Ltd ⁵ , PNG Coffee Exports Ltd, Credit Corporation (PNG) Ltd ^{3,5} , Baibua Ltd, Demakuri Ltd ⁵ , Bank of South Pacific Limited ¹
	Shareholder	Credit Corporation (PNG) Ltd ⁵ , New Guinea Islands Produce ⁵
	Family Trust	Niugini Nominees Ltd ⁵
T. E. Fox	Director	Kramer Group Ltd, Kramer Consultants Ltd, Kramer Pacific Ltd, PNG Institute of Directors, Teyo No. 1 Ltd, Kina Investment & Superannuation Ltd, Bank of South Pacific Limited, Zen No.33 Ltd
	Shareholder	Kramer Consultants Ltd, Teyo No. 1 Ltd, Bank of South Pacific Limited, Zen No 33 Ltd
N. R. Smith	Director/shareholder	Bank of South Pacific Limited ³ , N & R Smith Ltd ⁵
	Committee member	Commercial Bankers Association, Consultative Implementation and Monitoring Council, Institute of National Affairs ⁸
Garth McIlwain	Director	Anderson Foodland Ltd ⁶ , Tower Insurance Ltd, New Guinea Islands Produce Company Ltd ⁵ , Finance Pacific Superannuation Fund, East New Britain Supermarkets Ltd ⁶ , Rabtrad Madang Ltd, Balimore No. 21 Ltd ⁵ , Demakuri Ltd ⁵ , Bank of South Pacific Ltd ⁴ , Credit Corporation (Fiji) Ltd
	Shareholder	Bank of South Pacific Ltd
	Family Trust	Niugini Nominees Ltd ⁵
	Committee member	Papua Club Inc, Returned and Servicemens League Port Moresby
J. G. Jeffery	Director	James Barnes (PNG) Ltd ⁷ , NasFund, Employers Federation of PNG, The Tower Ltd, Bank of South Pacific Ltd, PNG Manufacturers Council, Madang Development Corporation, Madang Country Club, Rabtrad Ltd, Jayliss Ltd
Vai Reva	Director	Bank of South Pacific Ltd
	Employee	British American Tobacco (PNG) Ltd ⁷
	Committee member	PNG Business Council, Institute of National Affairs, Port Moresby Chamber of Commerce
Gerea Aopi	Director	Bank of South Pacific Ltd, Steamships Trading Company, Turanet Ltd, POMSoX Ltd, Hirad Ltd, Niu Marsh Ltd, Kumul Hotels, MRDC Ltd, Endeavour Properties Ltd, Vaio Investments Ltd, Wahinemo Ltd, Tahali Consultants Ltd, Ezytok Ltd, Institute of National Affairs
	Shareholder	Oil Search Ltd, Niu Marsh Ltd, Vaio Investments Ltd, Wahinemo Ltd, Tahali Consultants Ltd, Lihir Gold Ltd, Investment Corporation of PNG, Ezytok Ltd
	Employee	Oil Search Ltd ⁷
	Committee member	Institute of National Affairs, Business Council of PNG, National Events Council, Ela United Church Fundraising, Society of Petroleum Engineers
Dr. Ila Temu	Director	Bank of South Pacific Ltd, Placer Niugini Ltd, Kina Finance Ltd, Tipi Enterprise Ltd, Oil Search Ltd, IPBC
	Shareholder	Telstra
	Employee	Placer Niugini
Sir Nagora Bogan	Director	Bank of South Pacific Ltd, POSF Ltd ¹ , Coprez Communications Ltd ¹ , Coprez Holdings Ltd, Inventive Nook Ltd, James Cook Ltd, Niugini Cocoa Factory
	Shareholder	Coprez Holdings Ltd, Inventive Nook Ltd, James Cook Ltd, Niugini Cocoa Factory

¹Chairman, ²Deputy Chairman, ³Managing Director, ⁴Executive Director, ⁷General Manager, ⁸Councillor

⁵Company is shareholder of Bank of South Pacific Limited, or shareholder of company that is shareholder

⁶Company has commercial banking facilities with Bank of South Pacific Limited

26 DIRECTORS AND EXECUTIVE REMUNERATION

DIRECTORS REMUNERATION

Directors of the company received remuneration including benefits during 2003 as detailed below:

All amounts are in K

Name of Director	Meetings attended/ total held	Appointed/ (Resigned)	Base emolument	Bonus shares	Other compensation	Total remuneration	
						2003	2002
N. N. Beangke	7/7	-	37,500	-	-	37,500	39,500
T. E. Fox	7/7	-	30,000	-	-	30,000	32,000
Dr. Ila Temu	4/7	27/6/03	27,500	-	-	27,500	-
B. A. Flynn	-	(2/4/02)	-	-	-	-	35,000
Sir Nagora Bogan	4/7	27/6/03	25,000	-	-	25,000	-
B. J. Hanson	-	(2/4/02)	-	-	-	-	35,000
N. R. Smith	7/7	(31/12/03)	-	724,416	2,714,696	3,439,112	2,574,768
J. G. Jeffery	7/7	-	27,500	-	-	27,500	32,000
Gerea Aopi	5/7	-	27,500	-	-	27,500	14,750
Vai Reva	5/7	-	27,500	-	-	27,500	14,750
Garth McIlwain	7/7	-	-	-	776,977	776,977	713,806

EXECUTIVE REMUNERATION

The number of employees or former employees whose income from the bank was equal to or greater than K100,000 during the year, are classified in income bands of K10,000 as follows:

Remuneration K'000	2003 No.	2002 No.	Remuneration K'000	2003 No.	2002 No.	Remuneration K'000	2003 No.	2002 No.
100-110	-	1	310-320	1	2	490-500	-	2
110-120	2	-	320-330	2	1	500-510	-	1
120-130	2	4	330-340	1	1	510-520	-	2
130-140	1	1	340-350	-	2	530-540	1	-
140-150	1	-	350-360	1	5	540-550	2	-
150-160	1	-	360-370	3	3	570-580	-	1
160-170	1	-	370-380	2	4	580-590	1	-
170-180	1	-	380-390	5	4	590-600	-	-
190-200	-	1	390-400	3	3	600-610	1	-
210-220	1	-	400-410	1	3	610-620	1	1
230-240	1	-	410-420	3	1	660-670	-	1
240-250	-	-	420-430	3	-	730-740	-	1
250-260	-	-	430-440	1	2	740-750	1	-
260-269	-	2	440-450	2	1	760-770	-	1
270-280	-	1	450-460	2	-	770-780	1	-
280-290	-	-	460-470	-	-	790-800	-	1
290-300	1	1	470-480	2	-	810-820	1	-
300-310	-	1	480-490	1	1	820-830	1	-
Total							55	56

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 december 2003 (continued)

27 POST BALANCE SHEET DATE EVENTS

"Debits" Tax

The Papua New Guinea Government released its 2003 national budget in November 2002. New fiscal measures announced in the budget included the proposed introduction in 2003, of a 0.01% tax on withdrawals from savings, transaction and current accounts of bank customers ("debits" tax). The concept of the "debits" tax was for the banks to charge and collect the tax from their respective customers and periodically remit it to the Internal Revenue Commission.

The "debits" tax was not implemented in 2003, as the relevant legislation was not finalised, and the government (through the Internal Revenue Commission) and the commercial banks were still deliberating on the administrative aspects of the "debits" tax. The "debits" tax was implemented on 1 January 2004.

28 RECONCILIATION OF OPERATING CASH FLOW

All amounts are expressed in K'000

	2003	2002
Reconciliation of operating profit/(loss) after tax to operating cash flow before changes in operating assets		
Operating profit/(loss) after tax	39,981	(85,830)
Add: tax expense	20,361	6,890
Operating profit before income tax	60,342	(78,940)
Major non cash amounts		
Abnormal non-cash expense - goodwill on acquisition	-	140,557
Depreciation	24,645	17,067
Amortisation of deferred acquisition and computer development costs	1,818	1,739
Net (profit)/loss on sale of fixed assets	23	1,511
Loss on property revaluation	6,180	-
Write off fixed assets	1,936	-
Movement in forex income accrual	6,088	-
Movement in provision for doubtful debts	(8,112)	(3,823)
Increase in payroll provisions	2,499	3,362
Net effect of other accruals	6,353	14,038
Operating cash flow before changes in operating assets	101,772	95,511

29 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year. Bank of South Pacific Limited has no dilutive potential ordinary shares. Consequently, basic earnings per share equals diluted earnings per share.

	2003	2002
Net profit attributable to shareholders (K'000)	39,981	(85,830)
Weighted average number of ordinary shares in use ('000)	423,681	370,456
Basic and diluted earnings/(loss) per share (expressed in toea)	9	(23)

30 SEGMENT REPORTING

Business segments

The Bank of South Pacific Limited comprises one segment, this being the provision of banking services and products. This determination is based on the risks involved with the provision of services and products and the bank's management reporting system.

Geographical segments

The Bank of South Pacific Limited's business segment operates in Papua New Guinea.

Independent Audit Report

for the year ended 31 december 2003

SCOPE

We have audited the financial statements of Bank of South Pacific Limited for the year ended 31 December 2003. The financial report includes the Company's balance sheet as at 31 December 2003 and the related statements of income, cash flows and changes in equity for the year then ended. The Company's Directors are responsible for the financial statements. Our responsibility is to express an opinion on the financial report based on our audit to the members of the Company.

Our audit has been conducted in accordance with International Standards on Auditing. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial report is free of material misstatement. Our procedures include an assessment of the accounting principles used and significant accounting estimates made by the directors, as well as evaluating the overall financial report presentation. These procedures have been undertaken to form an opinion whether, in all material respects, the financial report is presented fairly in accordance with International Financial Reporting Standards and other generally accepted accounting practice and statutory requirements in Papua New Guinea, so as to present a view which is consistent with our understanding of the Company's financial position and performance as represented by the results of their operations and their cash flows.

We have obtained all the information and explanations we have required. We believe that our audit provides a reasonable basis for our opinion.

The audit opinion expressed in this report is formed on the above basis.

UNQUALIFIED AUDIT OPINION

In our opinion, the financial report of Bank of South Pacific Limited has been prepared in accordance with the PNG Companies Act (1997) including:

- a) giving a true and fair view of the Company's financial position as at 31 December 2003 and the results of its operations and cash flows statements for the year then ended in accordance with International Financial Reporting Standards, and comply with generally accepted accounting practice and statutory requirements of Papua New Guinea; and
- b) proper accounting records have been kept by the Company as far as appears from our examination of those records.

OTHER INFORMATION

In addition to providing audit services, we also provide Bank of South Pacific Limited taxation advice.

Dated this 25th day of March 2003.

DELOITTE TOUCHE TOHMATSU

By: Paul Barber

Registered under the Accountants Act 1996

Corporate Governance Principles

Following the amalgamation with the Papua New Guinea Banking Corporation, the introduction of a worldclass Corporate Governance regime was identified as a priority for the Board of Bank of South Pacific Limited. This statement outlines the principles adopted by the Board. In the interest of transparency, the Board has stipulated that these principles (as amended from time to time) be reproduced in the Company's Annual Report for the information of shareholders.

THE ROLE OF SHAREHOLDERS

The shareholders of the Company are responsible for voting on the election of Directors at the Annual General Meeting in accordance with the Constitution. All Directors, apart from Executive Directors, are subject to re-election by rotation no later than every three years. The Annual General Meeting also provides shareholders with the opportunity to express their views on matters concerning the Company and to vote on other items of business for resolution by shareholders.

COMMUNICATION WITH SHAREHOLDERS

The Board aims to keep shareholders informed of all major developments affecting the Company's activities and its state of affairs through distribution of the annual report, Chairman's address to the Annual General Meeting, and through announcements to the Port Moresby Stock Exchange and releases to the media.

THE BOARD OF DIRECTORS

The Board is responsible for the overall corporate governance of the Company including its strategic direction, establishing goals for management and monitoring the achievement of those goals with a view to optimising Company performance and increasing shareholder wealth.

Key functions of the board include:

- overall strategy of the company, including operating, financing, dividend, and risk management
- appointing the Managing Director and setting an appropriate remuneration package
- appointing the Company Secretary
- endorsing appropriate policy settings for management
- reviewing the performance of management
- approval of an annual strategic plan and an annual budget for the Company and monitoring results on a regular basis
- ensuring that risk management systems are in place to protect the Company's financial position and assets
- ensuring that the Company complies with the law and relevant regulations, and conforms with the highest standards of financial and ethical behaviour
- acquisition and disposals material to the business
- authority levels
- directors remuneration via the Remuneration and Nomination Committee
- approving financial statements

COMPOSITION OF THE BOARD

The maximum number of Directors, as prescribed by the Constitution approved by shareholders, is 10. The Board is currently comprised of 7 non-executive Directors, including the Chairman, and one Executive Director whom is the Managing Director. All the non-executive Directors are free from any material business or other relationship with the Company which could compromise their independence.

The Board accepts that it has a responsibility to shareholders to ensure that it maintains an appropriate mix of skills and experience, without gender bias, within its membership and consequently gives careful consideration to setting criteria for new appointments it may make in accordance with the Company's Constitution and in selecting candidates for recommendation to shareholders. It has delegated the initial screening process involved to the Remuneration and Nomination Committee which, when appropriate, seeks independent advice on possible new candidates for directorship. All Directors must be satisfied that the best candidate has been selected.

Nominees of the Board and shareholders must meet the "fit and proper person" criteria set and adjudged by the Bank of Papua New Guinea before they can take their place on the Board. The Board does not recognise that any office bearer or employee of an institutional shareholder by virtue of his/her position within the organisation has an automatic right to be appointed to the Board. Non-executive Directors shall retire from the Board no later than the Company's Annual General Meeting following their 69th birthday.

An integral element of the process for new Directors is an orientation program for new members of the Board.

BOARD PERFORMANCE REVIEW

A regular review is conducted of the Board's performance in meeting its responsibilities. The purpose of the review is to identify areas for improvement to ensure that the Board meets the highest standards of corporate governance and that the Board and each Director can make an appropriate contribution to the Company's objective of growing shareholder value. The review is conducted with the assistance of external consultants.

BOARD'S RELATIONSHIP WITH MANAGEMENT

The management of the business of the Company is conducted by and under the supervision of the Managing Director, and by those other officers and employees to whom the management function is properly delegated by the Managing Director.

The Board is responsible for:

- defining the limits to management's responsibilities
- approving the corporate objectives for which the Managing Director is responsible

The Board receives detailed briefings from senior management on a regular basis and opportunities are provided for the Directors to enhance their knowledge of the Company's business to assist them in assessing the performance of senior managers. Non-executive Directors meet on their own periodically to review the performance and management processes of the Company.

BOARD COMMITTEES

To assist in the execution of its responsibilities, the Board has established two Board Committees, comprised of non-executive Directors. Each committee has a formal Charter approved by the Board.

AUDIT AND COMPLIANCE COMMITTEE

The key responsibilities of the Audit and Compliance Committee include:

- the financial reporting and audit process
- the system of internal control and management of financial risks
- the systems for ensuring operational efficiency and cost control
- the systems for approval and monitoring expenditure including capital expenditure
- the processes for monitoring compliance with laws and regulations and implementation of Board decisions by management.

The Chairman of the Board is excluded from acting as Chairman of this Committee.

REMUNERATION AND NOMINATION COMMITTEE

The key responsibilities of this Committee include:

- To oversee the selection and appointment of a Chief Executive Officer and setting of an appropriate remuneration and benefits package for recommendation to the full Board
- In conjunction with the Chief Executive Officer, identify and maintain a clear succession plan for the Executive Management Team, ensuring an appropriate mix of skills and experience

as well as appropriate remuneration and benefits packages are in place and reviewed regularly.

- To review directors remuneration via the Remuneration & Nomination Committee
- To ensure that the Board itself maintains an appropriate mix of skills and experience necessary to fulfil its responsibilities to shareholders while maintaining a world class Corporate Governance regime.

BOARD AND BOARD COMMITTEE MEETINGS

Scheduled meetings of the Board are held bi-monthly and the Board meets on other occasions to deal with specific matters that require attention. Meetings of Board Committees are scheduled regularly during the year. The Board has a policy of rotating its meetings to locations where the Company has a significant presence. On these occasions the Board also visits Company operations and meets with local management and key customers.

DISCLOSURES BY DIRECTORS

The Board has in place a policy and procedures for the reporting of any matter which may give rise to a conflict between the interests of a Director and those of the Company. These arrangements are designed to ensure that the independence and integrity of the Board are maintained.

PURCHASE/SALE OF SHARES BY DIRECTORS

The Board encourages non-executive Directors to own shares in the company to further link their interests with those of all shareholders. Non-executive Directors are not eligible to participate in any employee share ownership scheme.

Directors are subject to Securities Act 1997 restrictions for buying, selling or subscribing for securities in the company if they are in possession of inside information, ie information which is not generally available and, if the information were generally available, a reasonable person would expect it to have a material effect on the price or value of the securities of the company. Directors must discuss proposed share trades with the Chairman of the Board.

Further, Directors may only trade in the securities of the company, subject to the foregoing insider trading restrictions, during each of the eight weeks following the announcements of half yearly profit and yearly profit or the date of issue of a prospectus.

In addition Directors must not trade in any other entity if inside information on such entity comes to the attention of the director by virtue of holding office as a director of the company.

PURCHASE AND SALE OF SHARES BY MANAGEMENT

Management of the company is subject to Securities Act 1997 restrictions for buying, selling or subscribing for securities in the company if they are in possession of inside information, ie information which is not generally available and, if the information were generally available, a reasonable person would expect it to have a material effect on the price or value of the securities of the company.

Further executive management may only trade in the securities of the company, subject to the foregoing insider trading restrictions, during each of the eight weeks following the announcements of half yearly profit and yearly profit or the date of issue of a prospectus.

Management should discuss proposed share trades with the Managing Director in advance, who in turn will keep the Chairman of the Board apprised.

In addition management must not trade in any other entity if inside information on such entity comes to the attention of management by virtue of holding office as an officer of the company.

INDEPENDENT ADVICE TO DIRECTORS

The Board recognises that in certain circumstances individual Directors may need to seek independent professional advice, at the expense of the company, on matters arising in the course of their duties. Any advice so received is made available to other Directors. Any Director seeking such advice is required to give prior notice to the Chairman of his or her intention to seek independent professional advice.

DIRECTORS' FEES

The maximum aggregate amount of fees that can be paid to non-executive Directors is determined by shareholders at annual general meetings of the company in accordance with the Constitution. Fees are intended to remunerate non-executive Directors for time spent on Board and Board Committee matters, including review and preparation time, meeting attendance, visits to Company operations and travel. The Chairman and Deputy Chairman spend additional time attending to their special responsibilities.

The annual fees currently being paid are as follows:

- Chairman - K35,000
- Deputy Chairman - K27,500
- Non-executive Director - K25,000
- Board committee members - K2,500 per committee

EXTERNAL AUDITORS AND CONSULTANTS

The Board has adopted a policy whereby appointment of External Auditors will be recommended by the Board to shareholders. Each term of appointment shall not exceed three (3) years.

Additionally, a duly appointed external audit firm shall not be engaged by the company to provide specialist consultancy services relating to financial, strategic and taxation matters.

RISK MANAGEMENT

The company has in place a number of arrangements to identify and manage areas of significant business risk. Each year the Board reviews the budget and the strategic plan put forward by management.

On a day to day basis the Board ensures its risk management responsibilities are met through the establishment and operation of three Management committees. The principal risk policy decision-making body in the company is the Executive Management Committee under the chairmanship of the Managing Director, and such committee establishes and delegates both relevant and specific responsibilities to an Assets and Liabilities Committee and a Credit Committee.

ETHICAL STANDARDS

Bank of South Pacific Limited acknowledges the need for Directors and employees at all levels to observe the highest standards of ethical behaviour when undertaking company business. To this end, the Board has adopted:

- A specific Code of Conduct for both Directors and members of the Executive Management team of the company and stipulates that each Director and relevant employees acknowledge in writing having read, understood and agreed to abide by such a Code, and
- A Corporate Mission; Objectives and Core Values Statement which establishes principles to guide all employees in the day to day performance of their individual functions within the company.

To ensure the maintenance of high standards of corporate behaviour on an ongoing basis, the Board further stipulates that senior management periodically undertake an appropriate communication program to reinforce both the Code and Core Value Statements. All Directors are encouraged to maintain membership of an appropriate Directors Association to keep abreast of current trends in Director's duties, responsibilities and corporate governance issues.



Branch Network

SENIOR MANAGEMENT

Managing Director
Garth McIlwain

General Manager Retail Bank
Tony Westaway

General Manager Credit & Risk
Brian Storm

General Manager Corporate & International
Robin Fleming

General Manager Paramount Banking
Aho Baliki

Acting General Manager Human Resources
Steve Grey

Chief Financial Officer
Tony Taylor

Chief Legal Officer
Paul Toua

BRANCHES

AITAPE
Branch Manager
Jacob Bigigien

ALOTAU
Branch Manager
Paul Kalai

BIALLA
Branch Manager
Peter Tikot

BOROKO
Branch Manager
Jennifer Niba

BUKA
Branch Manager
Poni Tukily

BULOLO
Branch Manager
Tony Waningu

COMMERCIAL CENTRE
Manager Operations
Mathias Manowo

DARU
Branch Manager
Thomas Tua

GOROKA
Branch Manager
Magai Kawailon

KAINANTU
Branch Manager
Kili Tambua

KAVIENG
Branch Manager
David Wasape

KEREMA
Branch Manager
Denis Konu

KIMBE
Branch Manager
Ega Renagi

KIUNGA
Branch Manager
Josephine Komoru

KOKOPO
Manager Operations
Maria Kipau

Branch Manager
Misbil Alfred

KUNDIAWA
Branch Manager
Andrew Bokame

LAE
Branch Manager
Theo Pedé

LAE COMMERCIAL

Acting Manager
Operations
Emma Harold

LAE MARKET

Branch Manager
Mathias Vinevel

LIHIR

Branch Manager
Kaser Tei

Officer in Charge
Vagi Kauri

LORENGAU

Branch Manager
Cecilia Pasum

MADANG

Branch Manager
Mark Kamjua

MAPRIK

Branch Manager
Darius Manjali

MENDI

Branch Manager
Danny Vincent

MT HAGEN

Branch Manager
Albert Burua

**MT HAGEN
COMMERCIAL**

Relationship Manager
Craig Lynch

Manager Operations
Mary Kundi

NAMATANAI

Branch Manager
Nelson Wara

POPONDETTA

Branch Manager
Mathew Yokondo

PORT MORESBY

Branch Manager
Charles Mobutuna

DOUGLAS STREET

Manager Operations
Madeleine Topelemu

RABAU

Branch Manager
Martha Baul

TABUBIL

Branch Manager
Iamo Kila

VANIMO

Branch Manager
Dennis Lamus

**WAIGANI BANKING
CENTRE**

Branch Manager
Richard Yopo

WAIGANI DRIVE

Manager Operations
Anne Baniyamai

WABAG

Branch Manager
Geoffrey Mirava

WABAG

Branch Manager
Jerry Paniu

WEWAK

Branch Manager
Ben Mursau

