


# Always There For You

DAEGU BANK ANNUAL REPORT  
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We are here for each of our Customers to provide Comprehensive, Convenient and Customized financial services.

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thinking



supporting



leading

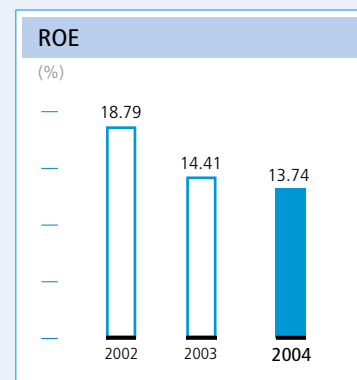
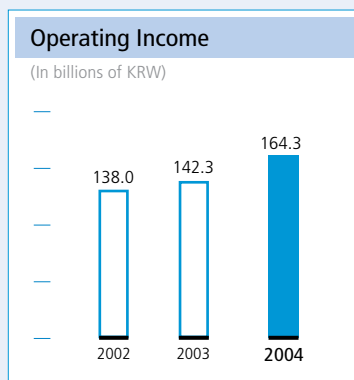
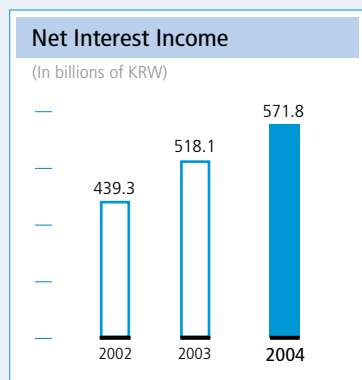


Daegu Bank, the first Korean regional bank, serves as many as 3.5 million customers, who account for approximately 60% of the total population of Daegu, the third largest city, and its vicinity of North Gyeongsang Province. We have successfully established the foundations for emerging as "the best leading regional bank with 50% regional market share." We are committed to playing the leading role as the representative regional bank that fulfills its love for the region and develops hand in hand with the local community. In the years to come, we will strive to provide comprehensive, convenient and customized financial services to the local community by constantly identifying the specific customer needs of the region and respecting customer rights.

# Financial Highlights

	In billions of KRW		In millions of US\$	
	2004	2003	2004	2003
Operating revenues	1,233.1	1,213.4	1,181.3	1,013.0
Net interest income	571.8	518.1	547.8	432.6
Operating income	164.3	142.3	157.4	118.8
Net income	123.5	110.8	118.3	92.5
Pre-provision income	397.5	342.1	380.8	285.7
Total assets	18,584.9	16,909.0	17,805.1	14,116.7
Total liabilities	17,635.9	16,071.3	16,895.8	13,417.3
Total shareholders' equity	949.1	837.7	909.2	699.4
Return on assets (ROA)	0.70%	0.67%		
Return on equity (ROE)	13.74%	14.41%		
Net interest margin (NIM)	3.40%	3.30%		
Loans to deposit ratio	79.45%	75.13%		
Cost income ratio	44.65%	42.68%		
BIS capital adequacy ratio	10.66%	10.58%		
Substandard & below credits ratio	1.46%	2.29%		

\* The Korean Won amounts are translated into U.S. dollar at the rate of W1,043.8 and W1,197.8 per U.S. \$1.00, the prevailing exchange rate on December 31, 2004 and 2003, respectively.





## CEO's Message



Lee Hwa-eon  
Chairman of the Board and CEO

### Letter to Our Shareholders

We will ensure higher levels of shareholder value to our stockholders through transparent and efficient management, while providing maximum satisfaction to our customers through friendlier and more diverse services. Meanwhile, we will strive to attain a deep trust from the local community through contribution and social services to the region.

# CEO's Message



## DEAR SHAREHOLDERS,

The domestic economy in 2004 showed signs of slowdown with the height of the rise in oil prices and appreciation of the won amidst contraction of corporate investments and depressed consumption due to the surge in credit delinquencies and increase in household debts. In addition, the bipolarization of the economy became particularly eminent with increasing gaps in the growth among sectors and classes in the cities where economic vitality and growth potential deteriorated.

The financial environment surrounding the bank sector last year was also adverse. Amidst increasing customer sensitivity to interest rates and financial products due to the continued low interest rates, the domestic financial market was clouded by competition threats from the acquisition of domestic banks by foreign financial institutions and bank consolidation and universal banking of commercial banks.

Despite such adverse conditions, Daegu Bank has been able to achieve satisfactory performance in many areas. In particular, we have realized a net income exceeding KRW 100 billion for three consecutive years, recording KRW 123.5 billion in 2004 even while provisioning an additional KRW 224.5 billion annually for bad loans, which is attributable to its unwavering dedication to local community-oriented and profitability-centered management. As a result of such superior business performance, we have been able to attain the highest rating in the domestic banking industry for two consecutive years in the CAMELS ratings by the financial supervision authorities.

In particular, our bank was selected as "the most admirable bank," ahead of other large domestic financial institutions, among "30 most respected Korean companies" last year announced by Dong-a Ilbo and IBM Business Consulting Services. In this respect, we have been able to solidify our position as a true bank of excellence, while, at the same time, enhancing our prestige as a credible bank that faithfully fulfills corporate social responsibilities.

It is no doubt that such solid business performance and the resultant maintenance of our position as a superior bank are largely due to our shareholders' interest in and support for the development of Daegu Bank. In this respect, I would like to take this opportunity to convey my gratitude.

In 2005, financing and operation of capital is expected to be difficult due to the continued underlying environment of low economic growth and low interest rates. At the same time, problems in household debts still linger on as an unresolved issue. Furthermore, full-scale financial war among domestic and foreign banks for market control is expected to unfold.



In order to actively respond to such changes in the financial environment and firmly maintain our position as the pivotal regional financial institution, we have set our management goals for 2005 as "Environment Change Response Management" with "VIC 2005" as our management slogan representing the 3 ideas of vision, innovation and challenge. All of us here at Daegu Bank will focus our energy and wisdom to vigorously strive to achieve such goals.

In terms of financial performance, DGB plans to enhance its productivity and efficiency by improving its management and revenue structure and pursuing performance-based responsibility management and management innovation. At the same time, DGB aims to become a bank that shares dreams and prosperity with the local community by further reinforcing its greatest strengths of networking abilities in the regional markets of the highly dynamic and potential North Gyeongsang Province. DGB is committed to becoming a model bank of community-focused management acknowledged both domestically and globally through the practice of transparent and clean ethical management, as well as environment-friendly management that thinks ahead for the future of the region.

Once again this year, we will ensure higher levels of shareholder value to our stockholders through transparent and efficient management, while providing maximum satisfaction to our customers through friendlier and more diverse services. Meanwhile, we will strive to attain a deep trust from the local community through contribution and social services to the region. Furthermore, we will devote our efforts to living up to the expectations of our shareholders.

I invite you all to witness our resolution and determination this year and ask for continued assistance and support. I wish you all prosperity in your endeavors and health and good fortunes to your families.

Thank you.

Lee Hwa-eon  
Chairman of the Board & CEO





## **;** always **thinking...**

We will maintain our strong competitiveness and brand value unrivaled by any other banks in the Daegu-North Gyeongsang Province by further reinforcing our greatest strengths in networking capacities and local community oriented management in the regional market. We always think about the regional economic and industrial development.





# Ethical Management

*We believe that the basis for becoming a true “small but strong bank,” “community focused bank” to all constituents of society including our employees, customers, shareholders and local citizens lies in the practice of corporate ethical management.*

Based on our management philosophy of "Sharing dreams and prosperity with the local community," Daegu Bank strives to play a leading role in the financial market as a pivotal regional financial institution that provides comprehensive financial services meeting diverse customer needs. In addition, Daegu Bank adopts honesty and credibility as the basic philosophy in conducting business activities so as to achieve our objective of maximizing customer satisfaction and shareholder value through fair and transparent management and contributing to the development of local communities and national economy. As such, we believe that the basis for becoming a true “small but strong bank,” “community focused bank” to all constituents of society including our employees, customers, shareholders and local citizens lies in the practice of corporate ethical management. In this respect, all of us here at Daegu Bank actively practice ethical management.

In order to set forth the responsibilities and obligations related to ethical management, Daegu Bank established and implemented the Code of Ethics in December 14, 2000. The code of ethics establishes detailed guidelines on the decision-making and behavior of employees in actual business activities. The ethics code strives to play a leading role in establishing a sound corporate culture of our bank, improving the image of employees to local citizens and customers and creating a new regional cultural trend.

**PERSE** signifies dark grayish blue and represents the color of DGB. In Latin, it embodies the meaning of importance on basics and principles. In addition, the word incorporates the following 5 key behavioral guidelines of DGB’s employees.

<b>P</b> (Principle)	‘Adherence to basics and principles’
<b>E</b> (Etiquette)	‘Etiquette towards others’
<b>R</b> (Regard)	‘Behavior considerate of other people’s viewpoints’
<b>S</b> (Service)	‘Incorporation of local community social service activities into everyday life’
<b>E</b> (Exploration)	‘Restless quest for new challenges’

DGB devotes its efforts to the development of the Bank and improvement of customer services in accordance to its resolution to “give back to the local community through better services and social works by incorporating PERSE into everyday life with the dignity and pride as an employee of a respected bank.”

Our code of ethics were established and implemented under such principles to allow us to conduct various ethical management practice programs and activities to date.

## Future Plans

Daegu Bank plans to expand ethical management culture and ethical management practice programs based on the ethical management activities that are currently being implemented. In addition, we plan to instill a firm belief on ethical management performance to our stakeholders, while developing ethical management practice activities in connection to performance. In order to actively encourage the participation of the local community in ethical management practices, we will expand the implementation of various cooperative ethical management programs, while reinforcing ethical management practice education and our regular monitoring and evaluation of ethical management practices.



# Vision & Strategy

## Management Philosophy

- DGB is realizing the philosophy of the bank that is "Sharing dreams and prosperity with the local community"

Since its establishment in 1967, DGB has played a crucial role in the development of the regional economy and financial market. At the same time, the Bank has successfully established the foundations for emerging into the leading regional bank. In the years to come, DGB will strive to realize knowledge-based and emotional management at the bank-wide level so as to promptly respond to changes in the financial market and macroeconomic environment. As such, DGB is committed to playing a leading role in the economic and financial development of the Daegu-North Gyeongsang Province in its capacity as the representative regional bank that fulfills its love for the region and develops hand in hand with the local community.

DGB's management philosophy is rooted in "sharing dreams and prosperity with the local community." In this respect, the Bank devotes its efforts to the sustained economic and financial development of the Daegu-North Gyeongsang Province by playing a pivotal role in the regional innovation system together with corporations, universities, research institutes and the local governments in the region. Furthermore, DGB strives to provide convenient financial services to the local community by constantly identifying the specific customer needs of the region and respecting customer rights. Moreover, DGB is committed to fulfilling its social responsibilities as a corporate citizen of the region through active social contribution and services to the local community.

## Vision

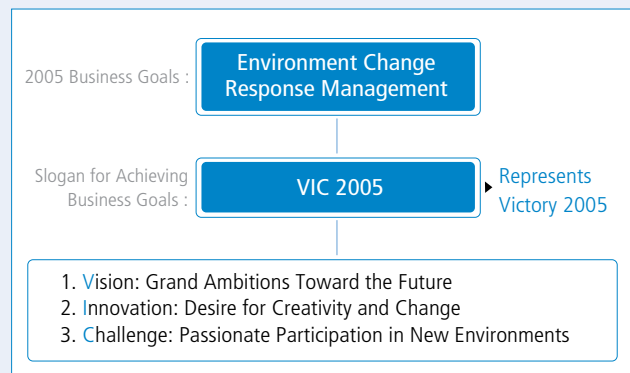
- DGB pursues the corporate vision of "the best leading regional bank with 50% regional market share."

DGB's vision lies in developing into "the best leading regional bank with 50% regional market share" and, at the same time, a "bank hand in hand with the local community." Its vision of "the best leading regional bank with 50% regional market share" contemplates DGB's goal of establishing its position as the leading bank in the regional financial market, as well as achieving business performances befitting a leading

regional bank. Meanwhile, "bank hand in hand with the local community" collectively refers to successfully expanding community-focused management, performing active regional contribution activities, faithfully fulfilling its role as the advanced information bank of the region, and enhancing its stature as the native bank beloved by local citizens.

## 2005 Business Goals

DGB has adopted "environment change response management" as its 2005 business goal, aimed at proactively responding to the changes in the financial environment and preserving its position as the main financial institution in the region. At the same time, the Bank plans to focus the energy and wisdom of all constituents on realizing its slogan of "VIC 2005," which represents the three meanings of vision, innovation and challenge, for achieving such business goal.



## 2005 Business Strategy

DGB plans to implement the following tasks to achieve its vision of "the best leading regional bank with 50% regional market share."

### Core Implementation Tasks



Bank consolidation among financial institutions and universal banking in line with deregulation has emerged as an important trend in the global financial market of today. Domestically, the progress of universal banking, coinciding with bank consolidation, has surfaced as the main trend in the financial sector pursuant to the rapid deregulation of business scopes within the industry. In particular, competition with prominent foreign financial institutions has become an inevitable reality due to the full-scale entry of foreign banks into the domestic financial industry. As such, the need to secure world-class competitiveness and establish global standard has become essential as ever before.

Based on such recognition, DGB's management policies in 2005 are as follows:

**First**\_profit-oriented management towards world-class regional bank

**Second**\_community-focused management hand in hand with the local community

**Third**\_performance-based responsibility management

**Fourth**\_knowledge management corresponding to the ubiquitous era

**Fifth**\_open culture and management

Based on the business goal of "environment change response management," DGB plans to solidify its business foundations through marketing activities for both its existing core revenue businesses and new profit businesses. In addition, the Bank also plans to expand its horizons of growth for high value-added new businesses and core customers. Furthermore, DGB will further increase its brand value by upgrading its community-focused management, while reinforcing its relationship by fully utilizing its strengths in business network.

# Core Competencies of DGB

DGB has played a leading role in the development of the Daegu-North Gyeongsang Province since its establishment in 1967. In particular, DGB successfully overcome the adversities of the financial sector restructuring amidst the 1997 financial crisis without any support of public funds. In 2004, the Bank achieved net earnings of KRW 123.5 billion, exceeding KRW 100 billion for three consecutive years, so as to solidify its position as the true representative regional bank of Korea.

Behind such superior business performance lie DGB's unique core strengths that differentiate it from other banks.

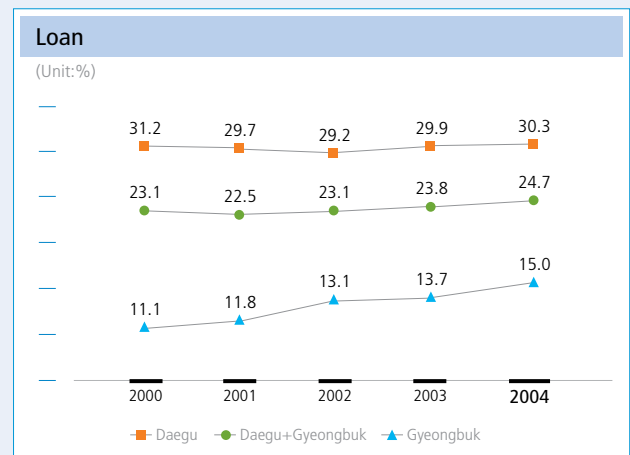
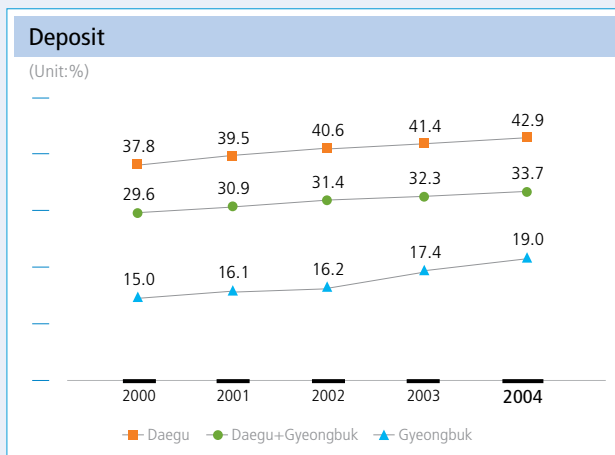
As of the end of 2004, DGB maintains the largest market share as a single financial institution reaching 42.9% in the Daegu region, based on deposits, on the back of its well developed human and physical networks, continued support and devotion to the region, and solid relationship with households and corporations of the region. Such high market share has also greatly contributed to the increase in the Bank's low-cost deposits, leading the superb profitability of DGB. Low-cost deposits have allowed the Bank to maintain the highest levels of NIM (Net Interest Margin) in Korea as the payment accounts of public institutions,

corporations, schools and hospitals in the Daegu region under DGB are in fact the Bank's low-cost deposits.

Another core strength of DGB is its competitive edge in customer information. In fact, its well-managed network and non-financial information accumulated through operations in a single market for 38 years are advantages unique to DGB, which are revealed as superiority in asset quality and delinquency.

In addition, DGB retains an enormous potential market of the North Gyeongsang Province beyond its business foundations in Daegu. In particular, amidst the recent recession of the domestic economy, the industrial districts in Gumi and Pohang are enjoying the economic boom driven by buoyant exports, providing substantial opportunities for DGB.

Under the challenging business environment with sluggish economic growth and prolonged low interest rates, as well as overheated competition among banks, DGB is committed to achieving the vision of "the best leading regional bank with 50% market share" based on such core capacities.







## 2004 Highlights

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### — Gold Prize of the Dasan Finance Awards

DGB was awarded the gold prize of Korea's most prestigious Dasan Finance Awards in the banking category, bestowed to individuals and financial companies that have contributed to the development of the domestic financial industry. The Dasan Finance Awards was established by the Korea Economic Daily to identify individuals and financial companies that have contributed to the development of the financial industry in Korea via development financial products or improvement of service quality. As such, the award aims to contribute to the continued development of the domestic financial industry and has, to date, been recognized as the most prestigious prize in the financial sector.

DGB is the largest supplier of capital as a single financial institution in the region that lends 70% of total loans to local small and medium enterprises. Accordingly, the Bank is recognized for its role in greatly contributing to the development of the regional economy and in improving the soundness of its asset management including becoming a clean bank without the injection of public funds subsequent to the financial crisis in 1997.

### — Inclusion in the KOSPI 200 Index

On March 29, 2004, the Korea Stock Exchange included DGB stocks into the KOSPI 200 index. The KOSPI 200 is a stock price index developed as the underlying index for derivatives products (index futures and index options) traded on the KRX-Futures Market and is comprised of 200 blue-chip stocks listed on the KRX-Stock Market that represents the overall market and industry groups that they belong to.

The initial advantage of inclusion in the KOSPI 200 is the increased supply and demand of issues. In particular, positive effects in the supply and demand of DGB issues are expected with its inclusion in various funds that benchmark KOSPI 200 including index funds, arbitrage funds and exchange traded funds (ETF). DGB has already been recognized as a shareholder-oriented company with its inclusion in the Korea Dividend Stock Price Index (KODI) in July 2003, while also being selected as a superior company in corporate governance structure with its inclusion in the Korea Corporate Governance Stock Price Index (KOGI) in December of the same year.

### — Development of Small Business Credit Evaluation System

DGB developed and operates the small business credit evaluation system for small-sized businesses including private companies and corporations with total assets of under KRW 1 billion. The system has upgraded the Bank's credit risk management by systemizing credit information covering small businesses, which have previously been excluded. In turn, it has promoted loan support and enhanced efficient credit risk management. The system will also allow for expansion of credit loans to sound small businesses by assigning appropriate credit rating to small-sized companies, which have previously been excluded from credit evaluations. Furthermore, it has allowed DGB to secure transparency in loan screenings by quantifying credit risks of small businesses.





## 2004 Highlights

### Inclusion in the MSCI Index

In 2004, DGB was newly included in the MSCI Korea Index, the most widely used international equity benchmarks. MSCI indices are model portfolio benchmarks prepared and announced by Morgan Stanley Capital International that are recognized as the benchmark indices for investment standards of global funds around the world. With its inclusion in the MSCI index, which provides the fundamentals for devising investment strategies of over 1,500 institutional investors around the world, DGB has once again been recognized as Korea's representative financial institution. In addition, positive effects on DGB's stock price are also expected due to the direct benefits of foreign investments.

### Commencement of BANKON Service

BANKON is a mobile banking service that allows customers to conduct everyday banking businesses over mobile phones equipped with banking IC chips that stores customer account information. BANKON is an upgraded mobile banking service that provides banking services such as inquiries of deposit and loan balances, money transfers, loan principle repayment, CMS money payment, GIRO payment, CD-ATM machine cash withdrawals and credit card services, as well as transportation card functions. As such, customers do not need to carry separate cash cards, transportation cards or bankbooks.

The BANKON service provided by DGB basically supports multi-banking services so as to allow unrestricted access to major banking businesses such as money transfers and balance inquiries at existing affiliated banks of LG Telecom including Kookmin Bank, Korea First Bank, Industrial Bank of Korea and Korea Exchange Bank by simply replacing the banking IC chip.

### Selection in "30 Most Respected Companies in Korea" and No. 1 Ranking in the Financial Sector by Donga Ilbo and IBM BCS Korea

DGB was selected as one of the "30 most respected companies in Korea" for its innovation, ethics and contribution to society. Donga Ilbo and IBM Korea (BCS) jointly selected the 30 respected Korean companies and released the outcome of survey for the first time in Korea. Among 200 domestic listed companies (KOSPI 200 companies), they applied five major checkpoints such as shareholders, company staff, customers, society, environment, and 52 core performance indices. IBM BCS Korea is the Korean branch of the worldwide renowned consulting firm, IBM BCS.

The survey comprehensively evaluated the financial performance, management innovation, transparent management, employee and customer satisfaction, social contribution and environment-friendliness of major listed companies in Korea over three years from 2001 to 2003. As a regional medium standing company, DGB outperformed large financial institutions including Kookmin Bank to seize the sixth spot in the overall survey (first in the financial sector). In particular, DGB was selected as the most exemplary company among regional banks for its community-focused management, as well as receiving high marks for active social contribution activities.

### Presidential Commendation for Merits in Supporting the Daegu Summer Universiade 2003

DGB received the honor of being awarded the presidential commendation for its merits in the active support for the successful hosting of Daegu Summer Universiade 2003. DGB participated as the official sponsor bank of the Universiade, providing financial contributions and free office space to the organizing



committee through the DGB Universiade Support Corps. In addition, the Bank also actively provided human and physical support for the international sports games including lodging to the North Korean cheering party in its training facilities, admission ticket sales, temporary branch in the athlete's village, organization and operation of North Korean delegation supporters and free game admission to students and customers.

The BPR system will ultimately allow branch employees to concentrate on marketing and high-value added activities so as to provide differentiated products and services by reflecting customer needs, which, in turn, allow for comprehensive customer asset management covering financial products, real estate and taxes.

### — PERSE Promulgation Ceremony

DGB held the ceremony for the promulgation of PERSE, the 5 key behavior guidelines of employees, amidst the participation of head office employees and branch staff via intra-bank Parangsae broadcast. DGB's has embarked on practicing the PERSE behavior guidelines with its selection as the overall sixth rank among the 30 most respected Korean companies (first in the financial sector) by Donga Ilbo and IBM BCS Korea in June 2004. PERSE signifies dark grayish blue and represents the color of DGB. In Latin, it embodies the meaning of importance on basics and principles.

### — Completion of BPR System Development

DGB completed the development of the BPR system covering all business activities for the first time as a regional bank. The BPR system will allow for the change in paradigm from business-orientation to customer-orientation by increasing the portion of marketing activities in branch business activities from 30% to 53%. It will also enable branches to transmit related documents using scanners in complex business areas such as corporate loans and foreign exchange so as to allow experts in specialized departments to promptly process the work. As a result, customers will be able to receive accurate and standardized services.

### — Strategic Alliance with Franklin Templeton Investment Corp.

DGB established a strategic alliance with Franklin Templeton, a world prominent asset management company focusing on long-term value investments. The strategic alliance was devised to reinforce DGB's competitiveness in the asset management business and establish customer profits as its utmost priority amidst trends of specialization, universal banking and bank consolidation in the financial environment. The alliance is a part of the Bank's plan to reinforce its private banking business so as to, ultimately, emerge as a leading asset management bank by allowing DGB to secure diversity in product composition and diversify asset management portfolios of high value customers.



# Board of Directors & Management

Business leaders with experience, vision and  
a commitment to the success of our customers

Lee, Hwa-eon ▶  
Chairman of the Board & Chief-Executive Officer



Huh, Byung-joon ▲  
Director & Standing Auditor  
*Former Director of Examination, FSS*



Lee, Kyung-jae ▶  
Outside Director  
*Former CEO,  
Industrial Bank of Korea*



Kwon, Sang-jang ▶  
Outside Director  
*Chairman, Korea Futures Forum*



Seo, Jung-suk ▲  
Outside Director  
*Chairman, Daegu District Bar Association*



Lee, Young-sae ▲  
Outside Director  
*President, Daegu Cyber University*







**Lee, Sang-bae** ▲  
 Senior Executive Vice-President  
 Head of Retail Banking Operation Division  
*Former Head of Business Support Division*



**Kim, Geon-sik** ▲  
 Executive Vice-President  
 Head of Management Planning Division  
*Former Head of Corporate Banking Division*



**Ha, Chun-soo** ▲  
 Executive Vice-President  
 Head of Corporate Banking Division  
*Former Head of IT&System Division*



**Hong, Woo-pyo** ▶  
 Executive Vice-President  
 Head of IT & System Division  
*Former Head of Capital Market Business Division*



**Lee, Kyu-young** ▶  
 Executive Vice-President  
 Head of Business Support Division  
*Former General Manager of Strategic Planning Team*



**Yu, Chang-shub** ▲  
 Executive Vice-President  
 Head of Retail Banking Planning Division  
*Former General Manager of Management Performance Team*



**Park, Hwi-joon** ▶  
 Executive Vice-President  
 Head of Capital Market Business Division  
*Former Head of American Express Korea*



## **always** supporting...

To share dreams and prosperity with the local community, we devote our efforts to the sustained economic and financial development of the Daegu-North Kyeongsang province. We will strive to attain a deep trust from the local community through contribution and social services to the region. All of us here at DGB will focus our energy and wisdom to vigorously strive to support the regional economic development.

# Review of Operations

*The overall economy of the region showed signs of improvement in line with the recovery of exports centering on electronics in Gumi, iron & steel in Pohang and machinery & transportation equipment in Daegu.*

## Review of 2004

Despite booming exports, the domestic economy in 2004 saw a slowdown in domestic demand as a result of the contraction in consumer confidence due to excessive growth in household debts. In turn, the economy grew by only 4.7% annually, while annual average consumer prices surged by 3.6% due to the rise in international oil prices and the cow disease crisis. Meanwhile, current balance were higher than expected, reaching US\$ 27.0 billion (US\$ 13.2 billion in the first half and US\$ 13.8 billion in the second half), owing to booming exports as a result of the increase in import demand from developed countries and China. In particular, exports of transportation equipment, electronics, petrochemicals, iron & metals and textiles showed recovery in business.

Similar to the domestic economy, the Daegu-North Gyeongsang province experienced a deepened contraction in domestic demand. However, the overall economy of the region showed signs of improvement in line with the recovery of exports centering on electronics in Gumi, iron & steel in Pohang and machinery & transportation equipment in Daegu. The industrial output of the Daegu region in 2004 increased 3.3% (0.4% in 2003) over the previous year as a result of expansion of machinery & equipment and automobile component output. In case of the North Gyeongsangbuk Province, output rose by 15.0% annually (11.1% in 2003) owing to the upturn in the business of electronic components, visual & audio communications, iron & steel, machinery and automobiles.

Exports, based on customs clearances, of the Daegu-North Gyeongsang Province in 2004 increased by 14.3% over 2003, totaling US\$ 3,155.02 million, propelled by the boom in machinery and iron & steel exports despite the sluggish textile

sector. The North Gyeongsang Province alone recorded exports of US\$ 33,951.24 million, increasing 35.3% year over year as a result of the increase in exports of iron & steel, metals, electrical, electronics, machinery and precision equipment.

The ratio of dishonored bills in the region fell slightly compared to 2003, driven by recovery in exports despite continued capital shortages from depressed domestic demand. In particular, the ratio of dishonored bills in the Daegu region declined by 0.05% points from 0.71% in 2003 to 0.66%, while the North Gyeongsang Province recorded a decrease of 0.06% points to 0.33% in 2004 from 0.39% in the previous year.

With respect to the construction business of the region, building permits (total floor area basis) in 2004 of the Daegu area fell considerably by 26.3% to 5.99 million m<sup>2</sup> year over year as a result of the frozen apartment sales market stemming from the sharp decline in the real estate business subsequent to the government's comprehensive real estate measure of October 29, 2003. In case of the North Gyeongsang Province, the overall construction sector was sluggish due to the effects of the depressed real estate market. However, the housing construction market was relatively strong compared to the Daegu region with total floor area of housing permits growing 2.4% to 6.70 million m<sup>2</sup>, owing to the gradual recovery centering on residential buildings subsequent to the second half of 2004. In terms of price levels, consumer prices in the Daegu region rose by 2.9% (average of all cities: 3.6%) over the previous year in 2004 due to stable rent and agricultural product prices including onions and cabbages. On the other hand, the North Gyeongsang Province saw higher increases in consumer prices at 3.4% year over year due to the rise in pork and oil (kerosene) prices.





## Review of Operations

In the industrial activities of the regional economy, the textiles industry in 2004 showed signs of slight improvement compared to the previous year despite sluggish business due to the structural recession in the textiles business. By regions, production and exports of textiles in the Daegu area during 2004 fell by 11.2% and 0.2%, respectively, while decreasing by 8.1% and 6.7%, respectively in the North Gyeongsang Province.

The automobile components industry of the region recorded a large increase in production, output and exports owing to the surge in automobile exports despite depressed domestic demand. In particular, component exports increased by 45.3% over 2003 as a result of the expansion in direct exports based on quality with the transformation of automobile components companies in the Daegu-North Gyeongsang Province into global enterprises. During 2004, industrial production in the Daegu and North Gyeongsang Province rapidly increased by 24.7% and 14.0%, respectively, year over year.

The housing construction industry showed signs of stagnation with the decline in speculation demand for residential buildings due to the government's comprehensive real estate measure of October 29, 2003. In the 2004 Business Survey Index (BSI) conducted by the Daegu & Gyeongbuk branch of Bank of Korea, the index of the region's housing construction industry remained low at 50.

Despite the fierce competition among nationwide distributors including department stores and hyper-marts, the region's distribution sector portrayed an overall slump in business as a result of the eminent slowdown in sales of large-sized distributors due to the contraction in consumption stemming from excessive household debts. In case of the region's large retailers, sales in the Daegu area increased by only 2.7% to KRW 2,641.4 billion in 2004, while the North Gyeongsang Province showed sales increase of 5.7% year over year to total KRW 817.9 billion.

The machinery industry showed booming production activities owing to the significant increase in both exports of general machinery to China, U.S. and Europe, and domestic demand from production facilities expansion in related industries including semiconductors and automobiles. In particular, production and exports of the machinery industry in Daegu grew by 13.7% and 34.3% year over year, respectively, while increasing by 7.1% and 109.6%, respectively in the North Gyeongsang Province.

The region's steel industry centering on the Pohang area improved with the surge in exports to China and output adjustments stemming from restructuring of steel companies in industrialized countries. POSCO, the largest steel maker in the region, recorded net earnings of KRW 3.8 trillion in 2004, an increase of 93% year over year, as a result of the rapid improvement of business due to strong steel prices. Accordingly, production and exports of the steel industry in the North Gyeongsang Province increased by 9.4% and 56.3% over 2003, respectively.

The electronics industry centering on the Gumi region boomed with the special demand from 2004 Olympic Games in Athens, commencement of digital broadcasting and rapid increase in wireless communications equipment exports. The industry led the overall business recovery of the region's industry. As such, production and exports of the electronics sector in the North Gyeongsang Province grew by 24.2% and 30.0% over 2003, respectively.







## — Outlook for 2005

Despite signs of recovery in domestic demand, Korea's economy in 2005 is expected to record a growth rate at the 4% level as a result of the fall in world economic growth, surge in oil prices, rise in international interest rates, slowdown in IT industry and appreciation of KRW. Current balance is expected to show a surplus of US\$ 20 billion (Export growth rate of 14.1% and import increase rate of 18.3% based on KDI forecast), decreasing from US\$ 27 billion in 2004, owing to the decline in the growth of world economy and Won exchange rates. Consumer prices is expected to be affected by the levels of oil price surges, rising 2.9% in case of stable oil prices and 3% in case of unstable oil prices. Private consumption in 2005 is expected to grow 2.5% over the previous year (-0.8% in 2004) with the recovery in consumer confidence due to the continued adjustment of household debts and lowered special consumption tax. Facilities investment is also expected to increase by 8.3% over 3.8% in 2004.

In the forecast of the region's major economic indicators in 2005, exports on the basis of custom clearances is expected increase in the 20% levels, slowing down from 38% in 2004 due to the recession in industrialized countries, fall in Won exchange rates and high oil prices. Dishonored bill ratio of the region is expected remain at previous year levels around 0.60% in Daegu and 0.30% in North Gyeongsang province as a result of the recovery in domestic demand despite slowdown in exports. Consumer prices are expected to rise 2.6~2.9% in Daegu and 2.9~3.2% in North Gyeongsang Province, while unemployment rate is expected to record 3.9~4.3% in Daegu and 2.4~2.6% in North Gyeongsang Province.

*With the systematic implementation of the post Milano project plan, the region's textile industry will hopefully be able to recover from the structural depression through technological innovation.*

With respect to industry outlook of the region, the textile sector is expected to undergo difficulties in production activities as a result of the increase in raw material prices due to the rise in oil prices in the textile material and cotton & silk sectors. Meanwhile, recovery is expected in the clothing industry as clothing consumption is anticipated to gradually pick up subsequent to 2005.

Recently, textiles companies in the region are attempting to initiate new changes for overcoming the chronic structural recession in the industry. In particular, leading textiles companies in the region including Hyosung and Kolon are restructuring their businesses by reducing low value-added yarn businesses and expanding the production of differentiated high value-added products (tire cords, spandex, etc.), while companies in the chemical fiber industry pursuing business transformations into high-tech electronics material production facilities or automobile components companies are increasing. In addition, more and more textiles companies in the Daegu region are also increasing their investments in research and development including establishment of R&D centers or exclusive R&D organizations. In this respect, the region's textiles companies are materializing their efforts to overcome the depressed business conditions without the assistance of central or local government policies. As a result of such active efforts for change, R&D investments in the textiles sector has expanded. With the systematic implementation of the post Milano project plan, the region's textile industry will hopefully be able to recover from the structural depression through technological innovation.



## Review of Operations

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The region's automobile components industry in 2005 is expected to see a slowdown in automobile export growth (30.3% in 2004 and 3.8% in 2005 according to Samsung Economic Research Institute) due to demand contraction from continued high oil prices, operations of Hyundai Motor's Alabama factory (200,000 units annually), sluggish demand in industrialized countries and rise in Won exchange rates. However, favorable business conditions are expected to continue in 2005 when considering the fact that automobile sales is anticipated to remain at 3.4 million units annually and direct exports of automobile components companies in the region are increasing.

Despite the effects of the government's comprehensive real estate measure (October 29, 2003) and the downturn phase of the housing business cycles, the region's construction industry is expected avoid a rapid fall in business due to the early execution of the government's large-scale public investments, housing sales in the metropolitan area of Pangyo and recovery of domestic demand. However, the industry in the region is anticipated to show a weak steady or slight decline trends.

Within the distribution sector of the region, department store and discount store sales are expected to increase over 2004 with rapid improvement of private consumption than anticipated. However, structural problems of customer deviation to large discount stores are expected to continue for traditional markets and supermarkets. Overall, the distribution sector is expected to show a distinct recovery subsequent to the second half of 2005.

During 2005, the machinery industry of the region is expected to be affected by the decline in automobile sales growth, weak construction market and slowdown in the production of the farm machinery industry. However, favorable trends in the industry is expected to be maintained owing to the continued export growth of general machineries, reduced procurement costs of intermediate materials from fall in Won exchange rates, and technological advantage over China.

With respect to the electronics & telecommunications industry within the region, exports growth of mobile phones, white goods (refrigerator, washing machine, air conditioner, microwave oven, etc.) and digital home appliances is expected to continue into 2005. However, the growth rate is expected to slow down somewhat compared to the previous year as a result of the economic recession in industrialized countries and intensified competition in the export market with Japan and China. Nevertheless, the electronic & telecommunications sector in the Gumi region will clearly remain as the growth engine of the region in 2005.

The region's steel industry centering on POSCO in Pohang is expected to boom up throughout the year of 2005, driven by strong international steel prices. While actively expanding production through the construction of 10 million ton capacity ironworks in India, Brazil and China, POSCO is currently making large-scale investments for the construction of FINEX facilities, which will lead the boom in the region's steel industry.

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*The electronic & telecommunications sector in the Gumi region will clearly remain as the growth engine of the region in 2005.*

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*POSCO is currently making large-scale investments for the construction of FINEX facilities, which will lead the boom in the region's steel industry.*

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## Retail Banking

### Deposits

The market environment for retail banking in 2004 saw intensified competition as ever before as a result of the expansion of market risk due to continued underlying low interest rates and economic recession, slowdown in real estate market growth and aggressive marketing of domestic financial institution.

Daegu Bank's deposits increased 3.3% in 2004, while trust accounts declined by 7.7% with the deviation of capital towards high-return financial instruments due to the reinforcement of the Trust Business Act. The capital financing market in 2004 saw a distinct movement to investment products such as equity-linked deposits and beneficiary certificates due to the effects of sluggish economy stemming from depressed domestic demand.

Daegu Bank operates a total of 187 branches and offices as of the end of 2004. During 2004, the Bank expanded a net of 1 business establishment over 2003, reducing 3 branches and opening 1 office in Daegu and expanding 2 branches and 1 office in the North Gyeongsang Province.

In 2005, the Bank plans to close 4 branches and open 6 new branches while closing 2 branches and establishing 4 branches and 1 office in 2004. Such plan conforms with Daegu Bank's management philosophy of emerging into a native bank of the region in harmony with the local citizen by realizing regional love and development through community and human-oriented management.

Low-cost Deposit	(In Billions of KRW, Average Balance)		
	2002	2003	2004
Low-cost deposit	4,938.7	5,406.1	5,500.6
Deposits in Won	10,224.0	11,725.7	11,714.5
Percentage of low-cost deposits	48.3	46.1	47.0
Total deposits	13,479.3	14,920.0	15,258.3
Percentage of low-cost deposits	36.6	36.2	36.1

Total deposits of Daegu Bank in 2004 for the Daegu-North Gyeongsang Province recorded KRW 15,258.3 billion, an increase of 2.1% over 2003. This can be attributed to the rise in bank accounts by 3.3% over 2003 to total KRW 13,976.6 billion, comprising 91.6% of total deposits. Daegu Bank is solidifying its position as the leading regional bank in the Daegu-North Gyeongsang Province with the continued improvement in the growth of total deposits.

Deposits in won during 2004 declined by KRW 11.2 billion over the previous year due to low interest rate conditions. However, it is expected to increase by 3.5% year over year to KRW 12,130 billion in 2005 with rise in interest rates anticipated due to expectations of economic recovery.

In 2005, deposits in won is expected to increase as a result of (1) the Bank's reinforcement of customer management through the strengthening of community-oriented management and sales capacities including CRM, BPR and SSP, (2) full-scale attraction of public institutions to Daegu & North Gyeongsang Province due to government decentralization, and (3) reinforcement of sales in the North Gyeongsang Province.

Last year, Daegu Bank reinforced its foundation for profitability through low cost capital financing by expanding its retail customer base, attracting businesses of institutional organizations and securing maximum number of various payment accounts. As a result, the Bank's low cost deposits increased 1.75% over 2003.

to reach KRW 5,500.6 billion. While the share of low cost deposits in total deposits fell slightly over 2003, the Bank maintains the highest percentage within the banking industry.



## Review of Operations

### Bancassurance

DGB generated new revenue sources from commission income subsequent to its bancassurance business commencement in September 2003. In order to solidify its new revenue model, the Bank concluded business cooperation agreements with 10 prominent domestic insurance companies so as to establish a structure for selling 36 products that meets the needs of diverse customer groups including pension insurances, savings insurances, driver's insurances and accident insurances. As a result, the Bank recorded KRW 17.2 billion in initial insurance premiums paid for 15,000 insurance contracts in 2004. DGB posted commission income of KRW 6.2 billion in 2004 which is the largest among domestic regional banks.

In the future, the bancassurance business is expected to further expand and grow in line with the government's second and third phase of the deregulation in the scope bancassurance products. In particular, with the sales of automobile and guarantee type insurances in the second phase of bancassurance deregulation, DGB is expected to attain revenues of KRW 6.5 billion in 2005 based on convenient branch and human networks of the Daegu-North Gyeongsang Province area where the Bank secures numerous quality customers. In an effort to expand non-interest income, DGB will strategically nurture bancassurance business as a primary source of commission income.



### Credit Card Business

2004 was a year for overcoming the overall slump in the credit card market. It was also a year in which other impediments to economic growth emerged due to the severe contraction in domestic demand. In looking at Daegu Bank's credit card business results vis-a-vis 2004 plans, the Bank realized a performance of 620 thousand members over its original goal of 600 thousand, sales of KRW 2.7 trillion over KRW 3.2 trillion, fee income of KRW 92.7 billion over KRW 98.7 billion, bad debt provisions of KRW 39.4 billion over KRW 61.5 billion and net income of KRW 23.7 billion over KRW 1.6 billion.

The Bank's 2005 business plan aims to realize 700 thousand members, sales of KRW 2.5 trillion, bad debt provisions of KRW 23.0 billion and net profits of KRW 30.2 billion. In particular, its membership expansion plan focuses on securing platinum customers with high growth potential centering on check cards without credit limits. Meanwhile, the Bank's mid-to-long-term plan aims to facilitate the renewal of its credit card business in preparation for the recovery of domestic demand market by focusing on target marketing centering on high quality customers with proven credibility.

Mutual harmony between increases in receivables and risk management is like the two sides of a coin in that its balance is crucial for the growth in credit card business. In this respect, Daegu Bank plans to minimize the inflow of delinquent members by improving its credit scoring system (CSS) currently being used and additionally applying credit bureau (CB) of credit information agencies. In addition, the Bank is also improving its asset quality through the reinforcement of behavior scoring system (BSS) standards.



## Consumer Finance

As of the end of 2004, the balance of household loans increased by KRW 109.5 billion over 2003 to KRW 3,051.5 billion, while interest on household loans rose by KRW 4.7 billion to KRW 222.8 billion. Mortgage loans reached KRW 1,184.6 billion, making up 38.8% of total household loans. Meanwhile, delinquencies of household loans maintained fair levels, falling by KRW 5.4 billion or 0.23% points in delinquency rate year over year to KRW 37.5 billion and 1.23%, respectively.

The objective of retail loans in 2004 aimed at enhancing the Bank's market confidence by generating stable revenue sources and improving both delinquency and non-performing loan ratios through increases in high quality assets. In order to improve internal-driven growth and asset quality based on credit risk, the Bank expanded sound loans, prevented delinquent loans in advance, reinforced post-management of delinquent loans and strengthened sales capacities through improved loan processes.

First, major activities for expanding sound loans included target marketing for attracting new sound loans and development and sales of new products centering on sound mortgages (DGB Long-term Mortgage Loan, DGB Korea Housing Finance Corporation Mortgage Loan, special loans to high profit stores based on agreement with Daegu Credit Guarantee Foundation). In addition, the Bank also secured stable revenue sources and expanded its market share by implementing expanded credit limits and prime rate measures for quality customers above a certain credit rating so as to reinforce its competitiveness over other banks. Furthermore, Daegu Bank reinforced its group loan processing functions by introducing the housing sales management system.

Second, activities for preventing delinquent loans included (1) reinforcement of credit risk management through expanded utilization of credit bureau, (2) improvement of customer information on debtor of household credit loans, (3) reinforcement of post management of potential delinquent customer groups and collateral, (4) reinforcement of certain housing mortgages such as villas, (5) implementation and improvement of soundness review

system for professionals, (6) development of prior monitoring model for self-employed households and implementation of its management program, and (7) reinforcement of credit risk management through review and maintenance of stability on CSS model.

Third, in order to reinforce post management of delinquent loans, the Bank reduced outstanding delinquent loans by (1) expanding the concentration of delinquent loans on the head office, (2) assisting in the normalization of delinquent loans through promotion of in-house credit recovery program, individual work-outs and bad bank system, and (3) implementing comprehensive measures for reducing branch delinquencies (on-site visits by head office employees to delinquent customers, head office employee dispatches to branches for delinquency management, etc.).

Fourth, the Bank increased the efficiency of branch business activities and reinforced its marketing functions through the improvement of various processes including loan process integration (integration of CSS system and account department loan effectuations), improvement of interest rate simulation process of CSS loans, processing of batch implementation of CSS automatic loan extensions by head office, and implementation of tuition loans via Internet.

In 2005, the consumer finance segment plans to focus on improving asset quality and expanding sound loans by (1) expanding stable assets through increase in low risk household loans including the expansion of loans to employees of government institutions and financially sound companies, (2) increasing non-loan revenue including fee income through customer expansion, (3) developing early warning system for household loans, (4) minimizing delinquent loans through the reinforcement of delinquency forecast functions such as review of particular groups (customer and collateral), and (5) preventing the conversion of potential delinquent assets into long-term delinquencies.





# Review of Operations

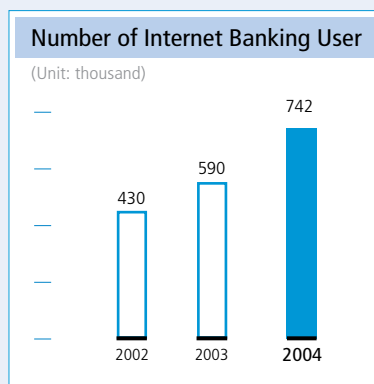
## e-Banking

Daegu Bank established various infrastructures for expanding the use of electronic banking so as to respond to the diverse need of customers by improving the IT environment of branches, developing process improvement support systems, developing and expanding new digital banking services, upgrading financial information system and reinforcing IT system security.

Daegu Bank recognizes that the expansion of customers using e-banking is an essential means for not only reinforcing its sales capacities, but also preventing customer deviations and deepening customer relationships. As such, the Bank has continued its activities for expanding the foundations of e-banking over the past years. As a result, the Bank achieved a notable growth in the number of customers using its Internet banking services from 590 thousand in 2003 to 742 thousand (25.3% increased) in 2004. In addition, the number of phone banking service subscribers has reached 1.38 million (10.2% increased) in 2004 from 1.25 million in the previous year. Based on such growth in the number of electronic banking subscribers, electronic banking transactions including Internet banking, phone banking and ATM constitutes 53.6% of total banking transaction of the Bank's customers.

Daegu Bank responds to the diverse needs of customers through automated machines including 672 CDs, 762 ATMs, 139 bankbook keeping machines and 187 utilities bill teller machines. In the future, the Bank plans to establish a diverse infrastructure for e-banking.

In 2004, the monthly average of e-banking transactions increased by 1,887 thousand over the previous year to reach 18.3 million transactions. In this respect, automated e-banking has contributed to the reduction of banking transaction processing costs by allowing the Bank to appropriately respond to rising work load without increasing the branch staff. In 2005, Daegu Bank plans to devote its efforts to promote advanced banking through the establishment of a next generation e-banking system.



Number of Automated Machines as of the end of 2004

	Category		Number of Machines
	C	D	
Automated Machine	A T M		762
	C D		672
Machine	Bankbook Keeping Machine		139
	Utilities Bill Teller Machine		187



## Corporate Banking

The domestic economy in 2004 grew by only 4.7% annually as a result of the deepened depression in domestic demand due to contractions in consumer confidence from excessive household debts despite booming exports. However, DGB was able to realize a solid growth of 8.23% over 2003 in total assets with loans to small and medium enterprises (SME) increasing 11.8% year over year as a result of its stable management of capital centering on sound SMEs.

In 2004, the Bank extended its business foundations by expanding transactions with companies that play a crucial role in the economic growth of the Daegu-North Gyeongsang Province. In addition, DGB also devoted its efforts to secure in advance potential high quality customers by providing support to prominent technology-based companies. Accordingly, the Bank was able to strengthen its relationship with such companies and provide differentiated services so as to enhance the loyalty of its corporate customers.

The share of DGB's corporate loans in total loans rose slightly in 2004 as a result of the increase in the demand for capital of corporations due to the growth of the regional economy. Owing to such expansion in corporate capital demands, total loans realized a steady growth of 7.21% over 2003.

DGB also improved asset quality and prevented long-term delinquencies through the reinforcement of prior delinquency prevention activities. Furthermore, the Bank efficiently managed its assets by avoiding excessive concentrations in asset positions and reflecting various risk factors including industry forecasts in its asset management. As a result, the delinquency rate of corporate customers fell from 1.45% in 2003 to 1.15% in 2004. Moreover, NPL coverage ratio for corporate loans significantly increased to 139.4% from 70.9% in 2004.

Meanwhile, DGB recorded the lowest levels of credit loan ratio within the banking industry by maintaining conservative asset management strategies despite its rising trends due to improved credit evaluation techniques. In addition, DGB's delinquency ratio was significantly lower than that of other banks in the region: delinquency ratio of 1.3% for DGB vs. average delinquency ratio of 2.9% for other banks in Daegu and North Gyeongsang Province. Owing to such conservative asset management, DGB retains a sound asset quality.

In the future, DGB plans to continuously reinforce its share in the corporate loan market in the North Gyeongsang Province area, as well as strengthen its market activities, through the attraction 1,000 target new corporate customers. In addition, the Bank plans to expand its corporate loans by approximately 10.5% over 2004 by strengthening its corporate banking business through the attraction of companies moving into new industrial complexes.

### Corporate Loan Portfolio

(In billions of KRW)

	2002		2003		2004		
	Amount	%	Amount	%	Amount	%	YOY
Manufacturing	2,956.2	49.8	3,224.6	55.0	3,481.5	52.4	8.0
Construction	384.3	6.5	392.2	6.7	530.2	8.0	35.2
Wholesales & Retail	602.5	10.2	890.3	15.2	1,000.4	15.0	12.4
Finance & Insurance	221.9	3.7	76.4	1.3	79.2	1.2	3.7
Real estate & Leasing	103.2	1.7	500.5	8.5	572.6	8.6	14.4
Restaurant & Lodging	708.7	11.9	289.4	4.9	301.3	4.5	4.1
Others	962.5	16.2	495.1	8.4	686.6	10.3	38.7
Total Corporate Loan	5,939.3	100.0	5,868.5	100.0	6,651.8	100.0	13.3

\*Loans in Won

# Review of Operations

## Capital Market Business

The capital market in 2004 saw numerous financial institution experiencing difficulties in capital operations as depressed domestic demand worsened due to the contraction in consumer confidence from excessive household debts despite booming exports.

The bond market in the first half of 2005 is expected to start off on a temporary rise due to increases in the amount of government bond issuances for early execution of fiscal budget. However, the market is anticipated to stabilize as low interest rates are expected to be maintained by the government for stimulating the economy. In the second half of 2005, market rates are expected to gradually rise as economic indicators are expected to improve as a result of the government's economic stimulation. As such, DGB plans to focus its bond operations on identifying and investing in short-term trading bonds and investment bonds, while reinforcing its risk management.

Within the stock market, price fluctuations are expected in the first half of 2005 due to the slowdown in export growth from strong won exchange rates amidst expectations of active economic stimulus by the government for domestic demand recovery. However, bullish market is expected in the second half owing to the recovery of the IT market from increased demand for IT products, expectations of stable economic recovery, stable stock supply and demand, improved corporate competitiveness, and equity preference from low interest rates. Accordingly, DGB plans to structure its equity portfolio centering on profit performance based blue chip stocks and turnaround stocks, while gradually expanding its equity operations according to market conditions.

(In Billions of KRW, Bank Account)

Securities Investments	Total	Trading Securities	Investment Securities	AFS	
				AFS	HTM
Bond (in Won)	5,183.9	571.4	4612.6	1817.5	2795.1
Government	1,863.7	146.0	1717.8	237.3	1480.5
Municipal	451.9	0.0	451.9	20.2	431.7
Debenture	1,465.6	365.0	1100.6	922.2	178.4
Public Corporate	30.1	-	30.1	10.4	19.7
Corporate	324.6	10.2	314.5	217.3	97.2
Others	1,048.0	50.2	997.8	410.2	587.6
Bond (in Fcy)	52.8	-	52.8	42.4	10.4
Stock	49.1	25.5	23.6	23.6*	-
Beneficial Certificate (stock)	4.4	-	4.4	4.4	-
(stock)	-	-	-	-	-
Others	18.8	-	18.8	18.8	-
Total	5,309.0	596.9	4712.1	4712.1	2805.4

\*Equities swapped from debt to troubled companies : 16.3 bn Won (book value 11.9 bn Won) + Equity holdings on subsidiary 7.3 bn Won



## International Banking & Foreign Exchange

Recently, domestic banks have continued to specialize and expand its businesses to improve market competitiveness in line with the trends of bank consolidation and universal banking in the financial industry. In particular, the international banking sector is seeking various ways to generate revenues under the common paradigm of globalization of capital.

Daegu Bank's foreign currency assets in 2004 totaled US\$ 758 million, achieving steady growth every year in both business profits and size. Its importance is increasing when considering the growth potential of international banking business in the future. As of the end of 2004, the Bank's foreign currency liquidity ratio recorded 106.21%, exceeding the 80% criteria set by financial supervisory authorities.

In 2004, Daegu Bank focused its international banking operations on increasing profits and developing new revenue models through diverse business activities including investments in foreign currency securities, foreign currency syndicated loans, foreign exchange dealing and derivative products. Furthermore, the Bank also continued to contribute to the reinforcement of support to its branches in foreign currency businesses such as import-export and foreign currency remittances.

Daegu Bank has implemented a business concentration system by business segments as a means to enhance business profits. Accordingly, the Bank's investment business unit was able to structure a sound investment portfolio through continued participation in foreign currency securities investments and syndicated loans. In the foreign exchange dealing area, the Bank

has secured a stable revenue source through reinforced marketing activities for developing new business lines including the promotion of corporate desks. With respect to capital, the Bank secured capital efficiency through a competitive credit line and financing of mid-to-long-term capital at low interest rates based on the confidence of international financial markets in its solid internal growth. Moreover, the Bank continued to develop new revenue sources by expanding its fee income through the improvement of annual payment import letter of credit operations.

Additionally, the Bank held foreign exchange risk seminars for medium standing companies so as to actively provide support to its branches with regard to foreign exchange business activities. The Bank also published a international banking & foreign exchange market information magazine for its branches and business customers. At the same time, Daegu Bank established the Internet Buy & Sell system (IBS) system so as to diversify its revenue base and further reinforce its competitiveness in international banking.

In 2005, Daegu Bank plans to strengthen its role in the international banking business to secure the deposits, loans and revenues that accompany the continually growing international banking and foreign exchange businesses. In particular, the Bank plans to extend its operations of exclusive corporate desks so as to expand new customers and foreign exchange income. In addition, the Bank also plans to promote its investment business by actively seeking various forms of investment tools, while simultaneously achieving an optimal foreign exchange portfolio structure and foreign exchange risk management by establishing effective capital financing and operations plans based on ALM strategies.

# Review of Operations

## Trust Business

Trust deposits of the overall banking industry in 2004 dropped approximately 17.65% compared to the end of 2003 as a result of the sluggish domestic economy, continued low interest rates and full-scale entry of foreign banks. Amidst such environment, the Bank's trust business saw a fall in deposits over 2003 with the reduction in the scope of its trust management due to the revision of the Trust Act. However, the magnitude of the decrease was minimized as the average balance of trust deposits reached KRW 1.28 trillion due to the sales of various specified money trust products in line with the preference of customers.

DGB pursued an asset management strategy of minimizing credit and market risks through adequate portfolio positions and durations. Accordingly, the Bank was able to invest in investment grade companies so as to give customers a stable return. In addition, the Bank also generated maximum profits by minimizing interest rate fluctuation risks through hedging strategies using derivative products. Furthermore, the compliance activities of the Investment Strategy Committee and portfolio company reviews were reinforced to allow for optimal asset management performance.

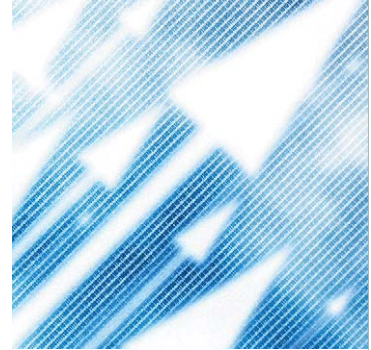


While direct comparison with other banks is difficult due to the discrepancies in fund establishment dates, DGB realized an overall high trust dividend payout vis-a-vis bank time deposits. The yield of new open-type money trust, DGB's core trust product maintained stable and sustained levels of approximately 4.31% (12 months).

In 2005, the Bank plans to actively respond to changes in the market environment by reinforcing both marketing to core customers and asset risk management in order to establish the foundations for solid trust business amidst expectations of slight rise in interest rates stemming from increase in exports and recovery of domestic demand.

	(In Billions of KRW)		
	2002	2003	2004
Assets	1,515.6	1,391.8	1,164.3
Securities	(1,199.0)	(1,120.1)	(1,052.8)
Liabilities	1,515.6	1,391.8	1,164.3
Money in trust	(1,445.0)	(1,336.4)	(1,103.4)
Revenues	123.5	109.6	90.8
Interest revenues	(101.1)	(95.4)	(76.4)
Expenses	109.6	92.6	76.4
Interest expenses	(81.2)	(73.3)	(62.5)
Trust fees & commissions	13.9	17.0	14.4





## — Risk Management

Daegu Bank comprehensively identifies and efficiently manages risks related to the Bank's business activities so as to ensure the soundness and stability of management, as well as stable revenue. Accordingly, the Bank sets permissible risk limits by each business unit (credit risk, market risk, liquidity risk, etc.) for approval by the Board Risk Management Committee. In turn, the Bank optimizes risk and returns through the risk limit management system that reinforces prior risk management.

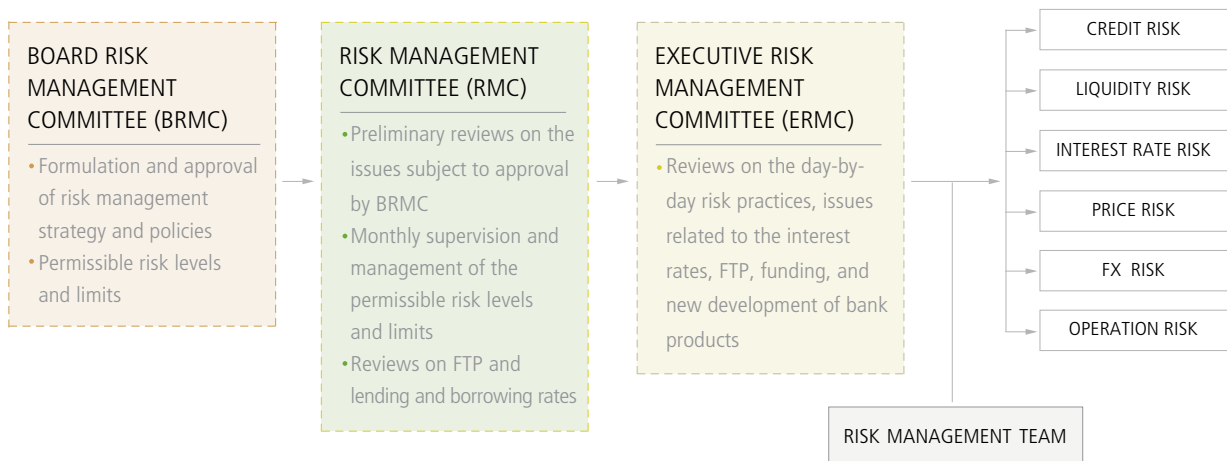
Credit risk management involves various activities related to the efficient management of potential losses from noncompliance of financial or contractual obligations involving loan, marketable securities, money and derivative transactions. Daegu Bank introduced and operates the Credit Scoring System (CSS) and Credit Risk Management System (CRMS) for managing risks related to household and corporate loans, respectively.

Market risk management involves various activities related to the efficient management of risks that potentially reduces interest income and investment asset values due to fluctuations in market conditions including interest rates, stock prices and foreign exchange rates. In this respect, Daegu Bank systematically manages interest rate risks, stock price fluctuation risks and foreign exchange risks through the development and implementation of the Travis securities management and Market Risk Management (MRM) systems.

Meanwhile, liquidity risk management involves various activities related to the efficient management of risks arising from payment defaults and missed investment opportunities caused by unexpected changes in cash positions. To cope with such uncertainties, Daegu Bank has been managing an ALM system since 1996 and plans to redevelop the system in 2004~2005.

In particular, Daegu Bank comprehensively identifies the risks inherent in the Bank's overall operations and applies an efficient integrated risk management by measuring and controlling individual risks including credit, market, liquidity and operational risks in a consistent manner.

### ■ STRUCTURE OF RISK MANAGEMENT





## **always** leading...

We are committed to fulfilling its social responsibilities as a corporate citizen of the region through the services to the local community. DGB has had a long tradition of finding the delicate balance between its economic profitability and its social responsibility in order to lead the regional economic and industrial advancement.



## Corporate Social Responsibility

# “ *Sharing Dreams and Prosperity with the Local Community* ”

### Corporate citizenship

As a regional bank with business foundations in the Daegu-North Gyeongsang Province, community-focused management is our fundamental management philosophy for achieving the ultimate vision of leading regional bank. Contributing to the development of the region and reinforcing relationships with the local community is based on the recognition that local community development is in fact the development of our bank. It is also our strategy for securing competitive advantage, as well as our survival strategy to establish a solid business foundation based on the local community and local citizens. Community-focused management incorporates a strategy of coexistence aimed at “sharing dreams and prosperity with the local community,” while maximizing our image as a close and convenient bank that contributes to the region. In order to realize such management philosophy, we aim to establish human and physical networks within the region, while enhancing our image as a close and convenient bank that contributes to the region.

Local community management is also a community-focused strategy for achieving our vision of leading regional bank that develops hand in hand with the local community. In this respect, Daegu Bank implements various programs for collective development with the community by (1) establishing strong community-focused business foundations through business activities focused on local customers and community, (2) building and expanding human networks through the systematization of customers and employees, (3) providing support for the promotion of culture, sports, scholarships and welfare of the region, (4) actively conducting regional contribution projects for promoting the welfare of local citizens and sharing with the local community, and (4) pursuing organized, systematic and continued voluntary community service and contribution activities by employees.

### Social Contribution

Daegu Bank formed the DGB Service Corps centering on voluntary participation of our employees in order to establish “community-focused management” as a corporate culture by enhancing the image of our management of “community-focused management” and inspiring pride in employees. Our DGB Service Corps goes beyond simple donation activities to perform spiritual and cultural activities in which employees directly participate so as to share our profits obtained through our business activities with the community.

DGB Service Corps conducts various activities in social welfare, culture & arts, sports and environment preservation. Its major activities in 2004 include the “DGB community love, great happiness campaign”, underclothes donations, blood donations for children with fatal diseases, snow disaster damage relief support, donation of supplies and sales activities for “Beautiful Saturday” events, assistance to children in need, sponsorship and voluntary services for welfare facilities, support for free meal centers, financial contributions to the DGB Love Fund, nature preservation of Shin River, Geumho River and Palgong mountain, and professional football day with local citizens.





# Corporate Social Responsibility

## Local Community Contribution Activities

Daegu Bank formed and operates the "Community Love Task Force", an exclusive community-focused social contribution organization in order to fulfill our corporate social responsibilities and our role as a corporate citizen that shares and develops with the local community by providing community services to the local community and giving back corporate profits to the region.

Daegu Bank takes the initiative in disaster relief of the region including fund raising support and disaster relief unit dispatches for various disasters in the region. We are at the forefront of various disaster relief support activities through employee dispatches and financial support for various disasters within the region including damage recovery support for regions affected by typhoon Lusa in 2002, on-site support for Daegu subway fire disaster in 2003 and snow disaster relief support in 2004.

Daegu Bank is committed to creating a good environment for living by conducting systematic and continuous social contribution activities for social welfare, culture & arts, scholarship programs, volunteer services and environment preservation. In addition to the in-house volunteer activities, we actively participate in community chest drives of external organizations including local governments.



## Social Welfare

Daegu Bank incorporates social service work into our everyday business activities by establishing one-to-one relationship with social welfare facilities in which individual employees, departments and branches of the bank separately support more than a single facility. We provide support for the needy by performing diverse social service activities including assistance to youth-headed families, support for children in need, sisterhood relationship with elderly people living alone, support for children with fatal diseases, blood donation activities and visits to social welfare facilities.



## Culture & Arts

Daegu Bank is reinforcing its support for various culture and arts programs to promote the culture of the region. In particular, we provide support for various cultural and arts events in the region including the Gyeongju Culture Expo, Dalgubeol Festival and Cheongdo cow fights. We also provide exhibition space for culture & arts through the gallery located in our headquarters. In addition, we publish the "Folk & Culture" magazine for free distribution. Since 2002, we have instilled dreams and hopes in children by holding children's sketching contests, which have developed into the largest children's cultural event in our region with the simultaneous holding of the event in Gumi and Pohang area in 2004.





### Scholarship Programs

In December 1990, Daegu Bank established the Daegu Bank Scholarship & Culture Foundation (financial contribution: KRW 5 billion) to provide support to youngster who will lead the future of the regional society. Through the foundation, we provide scholarships every year to selected middle school, high school and college students in the Daegu-North Gyeongsang Province. In December 2004, we contributed an additional KRW 2 billion to the foundation due to the recent continuation of low interest rate environment so as to expand its scholarship program. In addition, we are constantly devoting our efforts to the development of education in the Daegu-North Gyeongsang Province by providing financial support to various educational institutions for improving the education environment of the region.

### Sports Promotions

Daegu Bank contributes to the Sports Promotion Fund of the City of Daegu and North Gyeongsang Province every year in order to contribute to the cultivation of sound minds through the promotion of sports to local citizens, while developing the athletics of the region. We also played a leading role in the establishment of the Daegu professional football club through capital contributions, while actively supporting various advertising sponsorships of the club.

Daegu Bank also sponsors various sporting events for local citizens including inline marathons for the disabled, Saturday bowling tournaments, health runs and nationwide football tournaments. In addition, we are contributing to the promotion of sports in the region through the sports clubs (tennis club and rifle club) within our bank. In 2004, we hosted the "Professional Football Day with the Local Citizens" to provide free admission to the community. Furthermore, we are contributing to the promotion of the profession football club through the volunteer services and cheering of DGB Service Corps at official matches.

### Areas of Activities

Activity	Major Areas of Activities
Labor Service Activity	<ul style="list-style-type: none"> <li>- Various international and sporting event support activities</li> <li>- Farm village and business partner onsite experience activities</li> <li>- Sisterhood relationship establishment activities with social welfare facilities and the elderly living alone</li> <li>- Meal support to free meal distribution centers</li> </ul>
Environment-friendly Activity	<ul style="list-style-type: none"> <li>- I love Shin River and Geumho River campaigns</li> <li>- Nature preservation activities (Ap Mountain, Palgong Mountain, Seongam Mountain)</li> <li>- Wood sign attachments of major hiking routes and parks</li> <li>- Clean Street Promotion Campaign (Green City)</li> <li>- Migratory bird feeding events</li> </ul>
Social & Cultural Activity	<ul style="list-style-type: none"> <li>- Various cultural event activities support</li> <li>- Cultural relic PR and cleanup activities</li> <li>- Various invitational art performances</li> </ul>
Donation & Contribution Activity	<ul style="list-style-type: none"> <li>- Aid to youth-headed families and elderly people living alone</li> <li>- Assistance campaigns for children in need</li> <li>- Contribution activities through DGB Love Fund</li> <li>- Assistance to the disabled and children with fatal diseases</li> <li>- Sponsorships for social welfare facilities</li> <li>- Support for various social service organizations</li> </ul>



# Shareholder Relations

## IR Activities

Investor confidence towards the financial sector plummeted during the process of restructuring on financial institutions subsequent to the 1997 financial crisis as reflected in the significantly undervalued stock price of Daegu Bank vis-a-vis intrinsic value. Our IR activities begin under the basic recognition that our intrinsic value must receive fair market value. In particular, the importance of IR has emerged as such recognition coincides with our management philosophy of realization of shareholder value through management transparency at a time when improvement of governance structure and accounting policy transparency is required. As such, we established the Investor Relations Team within the planning & coordination division for the first time as a regional bank in 1999 to commence active IR activities to institutional and general investors including analysts and portfolio managers.

We began conducting full-fledged IR activities in October 26, 2001 by holding a large-scale investor relations conference for over 150 domestic and foreign analysts, portfolio managers and reporters in Seoul. Since then, we have hosted a series of over 20 investor relations conferences including corporate road shows, small group meetings, one-on-one meetings and institutional investor visits. In addition, we also established an IR corner within our Internet homepage so as to provide transparent and prompt investment information to both institutional and individual investors. We have met with a total of 777 investors through 132 meetings and 644 domestic and foreign investors through 151 meetings in 2002 and 2003, respectively. In 2004, we held a total of 178 one-on-one meetings and conferences to meet 658 analysts and investors. Furthermore, we enhanced our image as a leading bank in the market by holding frequent invitational IR meetings and conference calls in our bank.

- Regular Quarterly IR Conferences
- Overseas IR Activities (Non-Deal Roadshows, Conference Calls, etc)
- One-on-One Meetings with Visiting Investors
- Reinforcement of Cyber IR

## Future IR Strategy

We believe that our stock price is still substantially undervalued with respect to our asset quality, our solid local community-based competitiveness and stable revenue structure. Accordingly, we will pursue future IR activities focusing on the following so as to maintain reasonable stock price levels by inducing long-term stable market participations of domestic and foreign investors.

We are building the foundations for renewed growth for realizing our visions of "The Best leading regional bank with 50% regional market share" by securing a financial structure and management system of international standards based on market principles and transparency, and attaining global competitiveness able to respond to entry of any foreign or large commercial banks into our regional market. Our IR activities will facilitate the role of shareholder value management in attaining such vision.

### Contact Information of the IR Team is as follows :

- Telephone : 82-53-740-2050
- E-mail : jinsok@dgb.co.kr
- URL: www.dgb.co.kr

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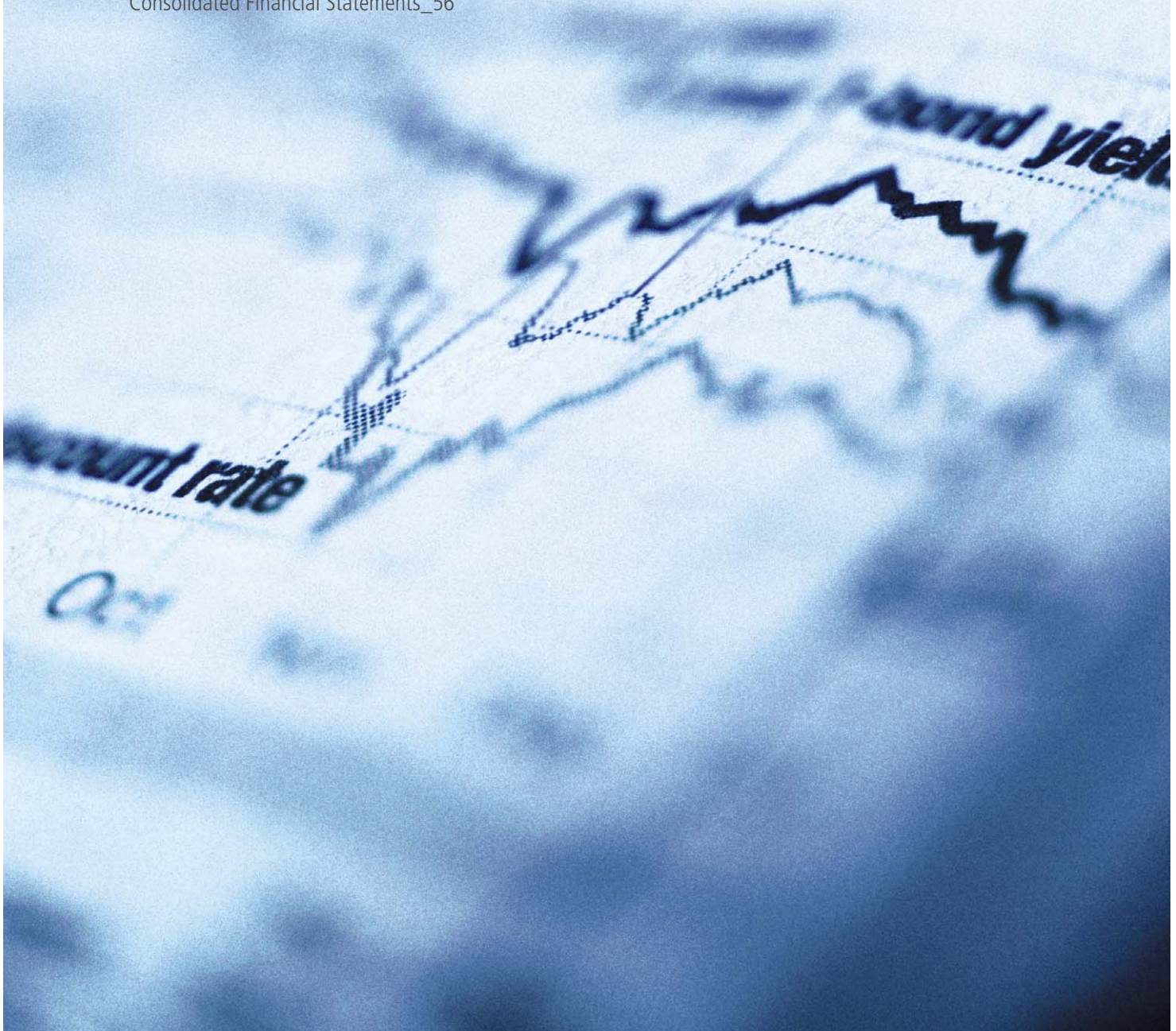
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# Management's Discussion & Analysis

## Selected Financial Information

(In billions of KRW, except for income per share)

	2000	2001	2002	2003	2004	Change
Operating revenues	1,136.3	1,144.1	1,160.8	1,213.4	1,233.1	1.6%
Interest income	962.4	974.6	984.3	1,011.3	1,014.5	0.3%
Operating expenses	1,071.4	988.7	1,022.8	1,071.1	1,068.7	-0.2%
Interest expenses	621.5	633.3	545.0	493.1	442.6	-10.2%
Provision for loan losses	179.5	81.7	165.1	209.5	203.2	-3.0%
Net interest income	340.9	341.3	439.3	518.1	571.8	10.4%
Operating income	64.9	155.4	138.0	142.3	164.3	15.5%
Net income	15.6	30.7	131.2	110.8	123.5	11.5%
Pre-provision income	179.4	124.3	309.7	342.1	397.5	16.2%
Total assets	13,028.8	14,551.5	16,020.5	16,909.0	18,584.9	9.9%
Loans	6,593.4	8,144.9	8,867.0	10,137.4	11,374.0	12.2%
Securities	3,231.8	4,129.1	4,660.9	5,214.1	5,309.1	1.8%
Total liabilities	12,496.3	13,991.1	15,275.3	16,071.3	17,635.9	9.7%
Deposits	9,061.0	10,455.5	11,737.3	12,648.7	13,262.8	4.9%
Borrowings	2,751.1	2,682.8	2,493.3	2,500.9	3,125.5	25.0%
Total shareholders' equity	532.4	560.4	745.2	837.7	949.1	13.3%
Capital stock	602.1	602.1	660.6	660.6	660.6	0.0%
Earnings per share (Won)	131	257	1027	839	935	11.4%
Return on assets (%)	0.13%	0.23%	0.88%	0.67%	0.70%	0.03%p
Return on equity (%)	2.94%	5.91%	18.79%	14.41%	13.74%	-0.67%p
Net interest margin (%)	3.53%	3.14%	3.15%	3.30%	3.40%	0.10%p
Loan loss provision to SBLs (%)	46.63%	55.27%	71.11%	74.97%	105.50%	30.53%p
SBLs to total credit (%)	8.69%	3.73%	2.28%	2.29%	1.46%	-0.83%p
BIS capital adequacy ratio (%)	11.69%	11.01%	10.85%	10.58%	10.66%	0.08%p
Tier I capital ratio (%)	7.65%	7.56%	7.84%	8.22%	8.65%	0.43%p
Tier II capital ratio (%)	4.06%	3.46%	3.02%	2.37%	2.02%	-0.35%p
Cost income ratio (%)	48.40%	44.80%	44.60%	42.68%	44.65%	1.97%p

2004 Annual Report of Daegu Bank may contain forward-looking statements provided to assist in the understanding of plans or objectives of the DGB's management for future operations, products or services, and forecasts of its revenues, earnings or other measures of economic performance. Forward-looking statements speak only as of the date they are made. The Bank does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made or to reflect the occurrence of unanticipated events.

## — OVERVIEW

DGB is emerging into the best leading regional bank which is small but strong and prospering with the Region. As a means to become a small but strong bank, the Bank has improved its profitability comparable to leading banks in the world. DGB also has the highest BIS ratio in the banking industry and the lowest level of delinquency rate in Korea. In addition, DGB continues to restructure its organization in an efficient way. In order to prosper with the region, DGB has reinforced its community-focused management and continues to extend active community services. The Bank also faithfully performs its role as the innovative information bank of the region and heightens its position as the regional community's bank.

DGB places top priority in its business strategy on the regional community in an age of globalization and integration in the financial industry. In tandem with the global trend of universal banking, the Bank concentrates its core competencies on banking businesses and provides total financial services through strategic alliances with other financial institutions. Particularly, in addition to prudent asset quality management, DGB has steered its business emphasis on expanding its horizons of growth for high value-added new businesses and core customers. The Bank will further increase its brand value by upgrading its community-focused management, while reinforcing its relationship by fully utilizing its strengths in business network.

## — ANALYSIS OF OPERATING RESULTS

Summary Income Statement	(In billions of KRW)			
	2002	2003	2004	Change
Net interest income (a)	439.3	518.1	571.8	10.4%
Non-interest income (b)	100.6	95.6	92.2	-3.6%
<b>Total income (c=a+b)</b>	<b>539.9</b>	<b>613.7</b>	<b>664.0</b>	<b>8.2%</b>
General & administrative expenses (d)	236.8	261.9	296.5	13.2%
Provision expenses (e)	165.1	209.5	203.2	-3.0%
<b>Operating income (f=c-d-e)</b>	<b>138.0</b>	<b>142.3</b>	<b>164.3</b>	<b>15.5%</b>
(Operating income before provisioning)	303.1	351.8	367.5	4.5%
Non-operating income (g)	-6.8	-27.0	8.7	-
Income before taxes (h=f+g)	131.2	115.2	173.0	50.2%
Income taxes (i)	0.0	4.4	49.5	n.m.
<b>Net income (j=h-i)</b>	<b>131.2</b>	<b>110.8</b>	<b>123.5</b>	<b>11.5%</b>

In 2004, most of domestic banks suffered from decrease in deposits and reported deterioration in net interest income due to low market interest rates and resulting net interest margin falls. It is noteworthy that DGB posted a 7.2% growth in total loans and a 5.0% increase in total deposits in 2004. In addition, the Bank managed to improve net interest margin on the back of active inducement of low-cost deposits. With steady growth in net interest income, total income rose 8.2% to KRW 664 billion, and operating income jumped 15.5% to KRW 164.3 billion in 2004. Moreover, substantial improvement in non-operating performance caused pretax income to shoot up by 50.1% to KRW 173.0 billion. Net income increased 11.5% to KRW 123.5 billion in 2004. Solid customer relationship within its dedicated region and superior risk management capability has made this notable operating performance possible.

# Management's Discussion & Analysis

Net Interest Income		(In billions of KRW)		
	2002	2003	2004	Change
Cash & due from banks	39.5	20.8	4.5	-78.4%
Securities	300.6	296.2	295.8	-0.1%
Loans	628.3	687.8	709.9	3.2%
Others	15.9	6.5	4.2	-35.5%
<b>Interest income (a)</b>	<b>984.3</b>	<b>1,011.3</b>	<b>1,014.5</b>	<b>0.3%</b>
Deposits	364.4	356.8	310.9	-12.9%
Borrowings	123.8	97.5	100.1	2.7%
Debentures	28.2	26.9	26.5	-1.5%
Others	28.5	12.0	5.1	-57.4%
<b>Interest expenses (b)</b>	<b>545.0</b>	<b>493.2</b>	<b>442.6</b>	<b>-10.2%</b>
<b>Net interest income (c=a-b)</b>	<b>439.3</b>	<b>518.1</b>	<b>571.8</b>	<b>10.4%</b>

In 2004, net interest income jumped 10.4% to KRW 571.8 billion, compared to KRW 518.1 billion, primarily due to substantial decrease in interest expenses.

Driven by increase in Interest income inched up to KRW1,014.5 billion in 2004 by 0.3% from KRW 1,011.3 billion in the previous year. In line with low market interest rates, interest income from cash and due from banks plummeted to KRW 4.5 billion in 2004 from KRW20.8 billion in 2003. Meanwhile, in response to prolonged low interest rate environment, DGB extended corporate loans to local SMEs with solid growth potential. As a result, interest income from loans, contributing most to interest income, rose 3.2% to KRW 709.9 billion in 2004, accounting for 70.0% of total interest income.

On the other hand, interest expenses dropped by 10.2% to KRW 442.6 billion, compared to KRW 493.2 billion in the previous year. Despite a 4.9% increase in deposits, lower market interest rates made interest on deposits drop by 12.9% to KRW 310.9 billion last year. Meanwhile, interest on borrowings nudged up 2.6% to KRW100.1 billion as the year-end balance of borrowings jumped 25.0% to KRW 3,125.5 billion to actively respond such

market environment changes as the deposit decrease due to falling market interest rates.

NIM & NIS		(%)		
	2002	2003	2004	Change
NIM	3.15	3.30	3.40	0.10%p
NIS	4.14	4.07	4.15	0.08%p
Avg. Loan rates	7.81	7.25	6.89	-0.36%p
Avg. Deposit rates	3.67	3.18	2.74	-0.44%p

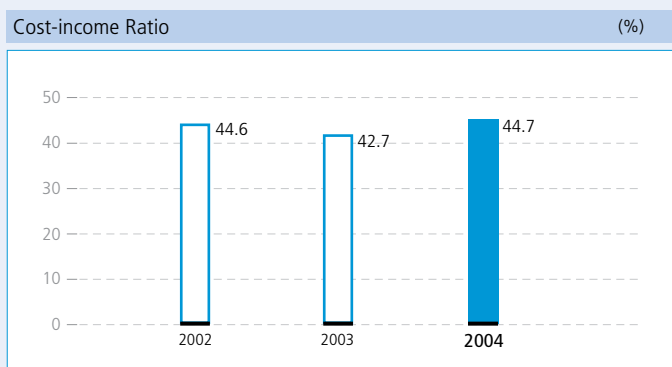
Through low-cost financing and efficient asset allocation, DGB continued improving net interest margin (NIM) for two consecutive years. DGB maintained its NIM at significantly higher level than the industry average. The Bank's NIM gained 10 basis points to 3.40% in 2004, subsequent to an increase of 15 basis points in 2003. Net interest spread (NIS) also increased by 8 basis points to 4.15% last year.

Non-interest Income and Expenses		(In billions of KRW)		
	2002	2003	2004	Change
Fees and commissions	131.3	137.2	141.6	3.2%
Gain on securities	10.6	14.5	9.5	-34.5%
Gain on derivative instruments	7.0	17.5	33.6	91.7%
Others	27.7	32.2	33.9	5.3%
<b>Non-interest income</b>	<b>176.5</b>	<b>201.4</b>	<b>218.6</b>	<b>8.5%</b>
Fees and commissions	15.7	17.0	18.6	9.4%
Loss on securities	13.0	12.6	7.8	-38.1%
Loss on derivative instruments	7.8	22.8	32.8	43.8%
Others	39.4	53.4	67.2	25.9%
<b>Non-interest expenses</b>	<b>75.9</b>	<b>105.8</b>	<b>126.4</b>	<b>19.5%</b>
<b>Non-interest income, net</b>	<b>100.6</b>	<b>95.6</b>	<b>92.2</b>	<b>-3.6%</b>
G&A expenses	236.8	261.9	296.5	13.2%
Provision expenses	165.1	209.5	203.2	-3.0%



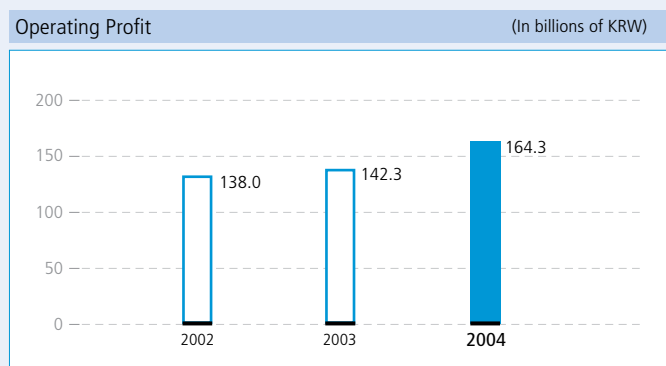
Upon the Bank's efforts to diversify income sources, non-interest income increased 8.5% to KRW 218.6 billion in 2004. Despite falling commission income on credit cards, total fee and commission income rose 3.2% to KRW 141.6 billion, powered by bancassurance and beneficiary certificates. While gain on securities fell by 34.5% to KRW 9.5 billion, gain on derivative instruments almost doubled to KRW 33.6 billion.

Non-interest expenses jumped 19.5% to KRW 126.4 billion last year because of increases in loss on derivative instruments and other miscellaneous expenses. Therefore, net non-interest income declined to KRW 92.2 billion in 2004, a 3.6% drop over KRW 95.6 billion in 2003.

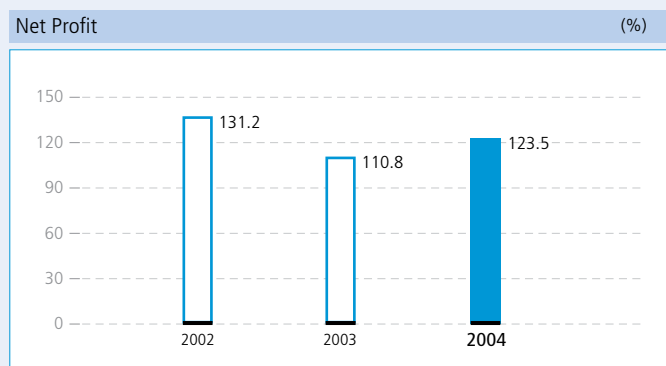


G&A expenses increased 13.2% to KRW 296.5 billion due to hike in salaries and administration expenses. In particular, temporary increases in wages and incentive payments were attributable to the overall growth in G&A expenses. Therefore, the cost-income ratio edged up by 2.0%p to 44.7% in 2004, but the Bank anticipates the cost-income ratio to come back to the normal level in 2005. In addition, in accordance with the improvement in asset quality and effective credit risk management, loan loss provision expenses dropped by 3.0% to 203.2 billion in 2004.

## Net Income



Subsequent to 2003, the Bank recorded a 15.5% increase in operating income to KRW 164.3 billion in 2004, compared to KRW 142.3 billion the year before. In addition, pretax profit surged 50.2% to KRW 173.0 billion due to steady growth in net interest income and vastly improved non-operating performance.



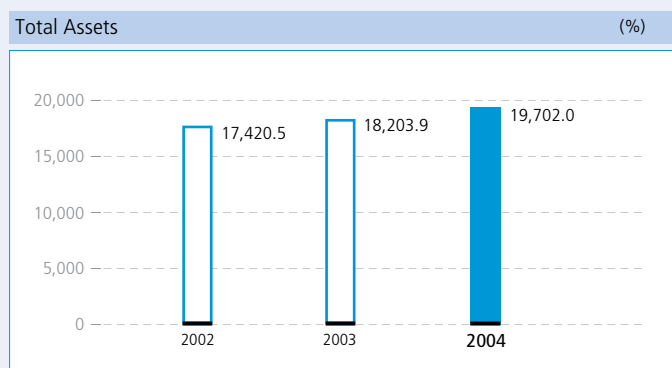
However, as the effective tax rate soared from a mere 3.8% in 2003 to 28.6% in 2004, net income increased at relatively lower growth rate of 11.5% to KRW 123.5 billion.

# Management's Discussion & Analysis

## BALANCE SHEET ANALYSIS

In 2004, the Bank took actions relating to both the asset and liability sides of the balance sheet in order to enhance asset quality and defensively position itself for a low interest rate environment. While assets were reallocated, the Bank adjusted its funding structure to further reduce funding costs.

### 1. Assets



As of December 31, 2004, the Bank's total assets increased by 8.2% to KRW 19,702.0 billion. The primary reason for the increase was loan growth backed by increase in both deposits and borrowings during the year.

	2002	2003	2004	% of total
By industry				
Manufacturing	3,556.0	3,616.3	3,837.8	35.2%
Construction	357.2	493.1	587.6	5.4%
Wholesale and retail	858.9	1,012.4	1,157.7	10.6%
Restaurants & hotels	198.8	311.4	318.0	2.9%
Finance & insurance	314.6	111.1	123.3	1.1%
Real estate & leasing	223.6	461.7	546.0	5.0%
Others	715.3	900.2	944.5	8.7%
Household	3,327.4	3,446.6	3,395.4	31.1%
Total loans in Korean Won	9,551.8	10,352.8	10,910.3	100.0%

Amidst adverse operating conditions, the Bank was able to secure high quality corporate customers with future growth potential. As a result, DGB actively extended loans to corporate clients by 8.8% to KRW 7,515 billion in 2004, compared to KRW 6,906 billion in 2003, on the back of rapid demand growth for capital in the manufacturing, and wholesale and retail sectors. Over 90% of total loans are denominated in Korean Won.

	2002	2003	2004	Change
Cash & due from banks	1,561.7	660.5	634.3	-4.0%
Trading securities	284.4	340.0	596.9	75.6%
Investment securities	4,376.5	4,874.2	4,712.2	-3.3%
Loans	8,867.0	10,137.4	11,374.0	12.2%
Other assets	930.8	897.0	1,267.5	41.3%

Subsequent to 2003, DGB continued reallocating its assets in an effort to enhance income-generating capacity in 2004. Securities and loans were mainly attributable to steady asset growth in 2004, increasing 1.8% to KRW 5,309.1 billion and 12.2% to KRW 11,374.0 billion, respectively. Meanwhile, the year-end balance of low income-generating cash and due from banks further declined from KRW 1,561.7 billion in 2002 and KRW 660.5 billion in 2003 to KRW 634.3 billion in 2004. This fundamental change in the Bank's asset portfolio is positive in terms of future earnings momentum.

## 2. Funding Sources

	(In billions of KRW)			
	2002	2003	2004	Change
Deposits	11,737.3	12,648.7	13,262.8	4.9%
Borrowings	2,493.3	2,500.9	3,125.5	25.0%
Debentures	327.7	285.0	285.0	0.0%
Other liabilities	717.0	636.7	962.6	51.2%

DGB's primary sources of funding are deposits and borrowings, accounting for over 90% of total funding. Despite prolonged underlying low interest rates, deposits rose 4.9% to KRW 13,262.8 billion due to ongoing efforts to increase deposit accounts and strengthen community-focused marketing activities. In particular, responding actively to market environment changes, DGB expand borrowings to lower funding cost.

	(In billions of KRW)		
	2002	2003	2004
Low-cost deposits	4,938.7	5,406.1	5,500.6
Deposits in Won	10,224.0	11,725.7	11,714.5
% of low-cost deposits	48.3	46.1	47.0
Total deposits	13,479.3	14,920.0	15,258.3
% of low-cost deposits	36.6	36.2	36.1

Separately, the Bank's low-cost deposits continued growing to KRW 5,500.6 billion in 2004, an increase of 1.8% over the previous year. The percentage of low-cost deposits over total deposits gained 0.9%p to 47.0% in 2004, representing among the highest in the domestic banking industry.

## ASSET QUALITY

	(In billions of KRW)		
	2002	2003	2004
Total credits	9,551.8	10,352.8	10,910.3
Substandard or below loans	217.7	236.9	159.5
SBL ratio (%)	2.28	2.29	1.46
Loan Loss Coverage Ratio (%)	71.1	74.9	105.5

Total credits of the Bank increased by KRW 557.5 billion won, or 5.4%, to KRW 10,352.8 billion in 2004. Of total credits, KRW 159.5 billion was classified as "substandard or below", and the Bank's SBL ratio improved 83 basis points to 1.46% in 2004, compared to 2.29% in 2003. Accordingly, the Bank reduced the provision for loan loss by 5.2% to 168.3 billion won. With the decrease in substandard and below loans and prudent provisioning, loan loss coverage ratio jumped by 30.6%p to 105.5% in 2004. Overall, DGB maintained its excellent asset soundness.

## CAPITAL ADEQUACY

	(In billions of KRW)			
	2002	2003	2004	Change
Total equity capital	976.6	1,024.7	1,097.8	7.1%
Core capital	705.4	795.6	891.0	12.0%
Supplementary capital	272.0	230.0	207.6	-9.7%
Risk-weighted assets	9,001.0	9,683.1	10,297.9	6.3%
BIS capital ratio (%)	10.85	10.58	10.66	0.08%p
Tier I capital ratio (%)	7.84	8.22	8.65	0.43%p
Tier II capital ratio (%)	3.02	2.37	2.02	-0.35%p
Equity to Asset Ratio	4.45	4.88	5.04	0.16%p

In 2004, while the Bank's supplementary capital declined, total equity capital increased 7.1% to KRW 1,097.8 billion on the back of a 12.0% increase in core capital. The expansion of core capital and effective management of risk-weighted assets boosted tier I capital ratio by 43 basis points to 8.65% in 2004. Meanwhile, as tier II capital ratio decreased 35 basis points to 2.02%, BIS capital ratio inched up 8 basis points to 10.66% in 2004.

# INDEPENDENT AUDITORS' REPORT

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To the Board of Directors and Stockholders of Daegu Bank, Ltd.

We have audited the accompanying non-consolidated balance sheets of Daegu Bank, Ltd. (the "Bank") as of December 31, 2004 and 2003, and the related non-consolidated statements of income, appropriations of retained earnings and cash flows for the years then ended (all expressed in Korean won). These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the Republic of Korea. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such non-consolidated financial statements present fairly, in all material respects, the financial position of the Bank as of December 31, 2004 and 2003, and the results of its operations, the appropriations of its retained earnings and its cash flows for the years then ended, in conformity with financial accounting standards generally accepted in the Republic of Korea

Without qualifying our opinion, we draw attention to the following :

As discussed in Note 23 to the accompanying non-consolidated financial statements, the Bank transferred loans with recourse to Korea Asset Management Corporation. ₩7.9 billion and ₩39.7 billion of such transferred loans remain unsettled as of December 31, 2004 and 2003, respectively. Additional gains or losses may be recorded upon the final settlement of the loans with Korea Asset Management Corporation in accordance with the recourse provisions.

As discussed in Note 23 to the accompanying non-consolidated financial statements, the Bank has ₩ 90 billion in debt securities issued by LG Card as of December 31, 2004 and an impairment loss has been recorded in the amount of ₩17.2 billion, or 19%. Additional gains or may be recorded depending on the result of corporate restructuring by LG Card.

As described in Note 2 to the accompanying non-consolidated financial statements, the accompanying non-consolidated financial statements have been prepared in accordance with Statements of Korea Accounting Standards (SKAS) No. 1 through No. 10 and No.12 through No.13. In connection with these accounting changes, the accompanying non-consolidated financial statements of the Company as of December 31, 2004 and 2003 were not affected.

Accounting principles and auditing standards and their application in practice vary among countries. The accompanying financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries other than the Republic of Korea. In addition, the procedures and practices utilized in the Republic of Korea to audit such financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report and the accompanying financial statements are for use by those knowledgeable about Korean accounting procedures and auditing standards and their application in practice.

*Ahn Kwon K Co.*

January 20, 2005

**Notice to Readers**

This report is effective as of January 20, 2005, the auditors' report date. Certain subsequent events or circumstances may have occurred between the auditors' report date and the time the auditors' report is read. Such events or circumstances could significantly affect the accompanying financial statements and may result in modifications to the auditors' report.



# NON-CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>ASSETS</b>		
Cash and due from banks (Note 3)	₩ 634,326	₩ 660,480
Securities (Notes 2 and 4)	5,309,093	5,214,171
Loans (Notes 5, 6 and 7)	11,374,007	10,137,408
Fixed assets (Note 8)	348,848	350,744
Other	918,675	546,217
<b>TOTAL ASSETS</b>	<b>₩ 18,584,949</b>	<b>₩ 16,909,020</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities:</b>		
Deposits (Note 10)	₩ 13,262,754	₩ 12,648,704
Borrowings (Note 11)	3,125,494	2,500,867
Debentures (Note 12)	285,000	285,000
Other	962,629	636,704
<b>Total Liabilities</b>	<b>17,635,877</b>	<b>16,071,275</b>
<b>STOCKHOLDERS' EQUITY</b>		
Common stock (par value ₩ 5,000) (Authorized : 300 million shares) (Issued and outstanding : 132.1 million shares)	660,625	660,625
Capital surplus	12,328	12,328
Retained earnings	260,349	169,858
Capital adjustments		
(1) Stock options	-	628
(2) Gain (loss) on valuation of available-for-sales securities	15,770	(5,694)
<b>Total Stockholders' Equity</b>	<b>949,072</b>	<b>837,745</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>₩ 18,584,949</b>	<b>₩ 16,909,020</b>

See notes to accompanying non-consolidated financial statements.

# NON-CONSOLIDATED STATEMENTS OF INCOME

YEARS ENDED DECEMBER 31, 2004 AND 2003

Korean won (in millions,  
except for income per share)

	<b>2004</b>	2003
<b>OPERATING REVENUES</b>		
Interest on due from banks	₩ 4,479	₩ 20,850
Interest on trading securities	11,934	18,738
Interest on available-for-sale securities	88,880	88,114
Interest on held-to-maturity securities	195,026	189,316
Interest on loans	709,944	687,793
Interest - other	4,218	6,535
Total interest income	1,014,481	1,011,346
Fees and commissions	127,213	119,691
Gain on disposal of trading securities	8,725	13,858
Gain on valuation of trading securities	289	-
Dividend on trading securities	72	199
Dividend on available-for-sale securities	390	433
Gain on foreign currency transactions	33,871	30,701
Trust account commission fees	14,369	17,508
Other	33,641	19,661
Total operating revenue	<u>1,233,051</u>	<u>1,213,397</u>
<b>OPERATING EXPENSES</b>		
Interest on deposits	(310,894)	(356,767)
Interest on borrowings	(100,090)	(97,541)
Interest on debentures	(26,540)	(26,860)
Interest - other	(5,126)	(12,024)
Total interest expense	(442,650)	(493,192)
Commission charges	(18,591)	(16,954)
Loss on disposal of trading securities	(7,796)	(11,395)
Loss on valuation of trading securities	(0)	(1,213)
Loss on foreign currency transactions	(26,762)	(17,093)
Provision for loan losses	(203,183)	(210,252)
Salaries	(121,354)	(107,455)
Depreciation	(23,318)	(24,723)
Amortization of intangible assets	(4,095)	(3,759)
Other general and administrative expenses	(147,730)	(125,967)
Other	(73,256)	(59,107)
Total operating expenses	<u>(1,068,735)</u>	<u>(1,071,110)</u>

(Continued)

# NON-CONSOLIDATED STATEMENTS OF INCOME (CONTINUED)

YEARS ENDED DECEMBER 31, 2004 AND 2003

Korean won (in millions,  
except for income per share)

	<b>2004</b>	2003
OPERATING INCOME	164,316	142,287
NON-OPERATING INCOME	46,335	48,822
NON-OPERATING EXPENSE	(37,607)	(75,852)
INCOME BEFORE INCOME TAXES	173,044	115,257
INCOME TAXES (Note 17)	(49,522)	(4,429)
NET INCOME	₩ 123,522	₩ 110,828
NET INCOME PER SHARE-BASIC (Note 18)	₩ 935	₩ 839
NET INCOME PER SHARE-DILUTED (Note 18)	₩ 935	₩ 839

See notes to accompanying non-consolidated financial statements.

# NON-CONSOLIDATED STATEMENTS OF APPROPRIATIONS OF RETAINED EARNINGS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>RETAINED EARNINGS BEFORE APPROPRIATIONS</b>		
Unappropriated retained earnings (undisposed accumulated deficit) carried over from prior year	₩ 181	₩ 284
Net income	123,522	110,828
Total	123,703	111,112
<b>TRANSFER FROM RESERVES</b>		
Reserve for business rationalization	746	-
<b>APPROPRIATIONS OF RETAINED EARNINGS</b>		
Legal reserve	(12,400)	(11,200)
Voluntary reserve for recapitalization	(12,400)	(11,200)
Other reserve	(63,300)	(55,500)
Cash dividends (Note 26)	(36,334)	(33,031)
Total	(124,434)	(110,931)
<b>UNAPPROPRIATED RETAINED EARNINGS CARRIED OVER TO THE SUBSEQUENT YEAR</b>	₩ 15	₩ 181

See notes to accompanying non-consolidated financial statements.

# NON-CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	₩ 123,522	₩ 110,828
Additions of expenses not involving cash outflows (Note 27)	267,627	325,228
Deductions of revenues not involving cash inflows (Note 27)	(255,822)	(322,431)
Changes in assets and liabilities resulting from operations (Note 27)	(113,154)	143,642
Net cash provided by operating activities	22,173	257,267
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Cash inflows from investing activities :		
Disposal of trading securities	9,331,283	4,514,242
Disposal of available-for-sale securities	2,133,266	1,765,917
Disposal of held-to-maturity securities	520,114	1,277,586
Disposal of property and equipment	896	3,693
Decrease in other receivables	36,619	74,438
Sub-total	12,022,178	7,635,876
Cash outflows for investing activities :		
Acquisition of trading securities	(9,586,971)	(4,568,575)
Acquisition of available-for-sale securities	(2,022,653)	(1,781,142)
Acquisition of held-to-maturity securities	(427,356)	(1,768,337)
Acquisition of property and equipment	(22,906)	(28,336)
Acquisition of intangible assets	(3,743)	(6,713)
Increase in other assets	(362,728)	(40,793)
Sub-total	(12,426,357)	(8,193,896)
Net cash used in investing activities	(404,179)	(558,020)

(Continued)



# NON-CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

YEARS ENDED DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Cash inflows from financing activities :		
Increase in borrowings in Korean won	118,125	14,478
Increase in borrowings in foreign currency	77,797	112,087
Increase in debentures	-	6,000
Increase in other liabilities	384,696	-
Sub-total	580,618	132,565
Cash outflows for financing activities :		
Repayment of borrowings in Korean won	-	-
Repayment of debentures	-	(46,000)
Payment of cash dividends	(33,031)	(33,031)
Decrease in other liabilities	-	(72,292)
Sub-total	(33,031)	(151,323)
Net cash provided by (used in) financing activities	547,587	(18,758)
<b>NET INCREASE (DECREASE) IN CASH</b>	165,581	(319,511)
<b>CASH AT THE BEGINNING OF THE YEAR</b>	328,755	648,266
<b>CASH AT THE END OF THE YEAR (Note 27)</b>	₩ 494,336	₩ 328,755

See notes to accompanying non-consolidated financial statements.

Notes to Non-Consolidated Financial Statements are not enclosed intentionally. Therefore, investors, shareholders and other stakeholders should review notes to financial statements in order to properly understand the Bank's important accounting policies and details on operating performance and financial conditions. Notes to financial statements can be found on 'NON-CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT' (<http://www.dgb.co.kr>)

# INDEPENDENT AUDITORS' REPORT

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To the Stockholders and Board of Directors of Daegu Bank, Ltd.

We have audited the accompanying balance sheets of trust account (the "Trust") of Daegu Bank, Ltd as of December 31, 2004 and 2003, and the related statements of operations and cash flows for the years then ended (all expressed in Korean won). These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the Republic of Korea. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Trust as of December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended, in conformity with financial accounting standards generally accepted in the Republic of Korea.

Accounting principles and auditing standards and their application in practice vary among countries. The accompanying financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries other than the Republic of Korea. In addition, the procedures and practices utilized in the Republic of Korea to audit such financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report and the accompanying financial statements are for use by those knowledgeable about Korean accounting procedures and auditing standards and their application in practice.

*Ahn Kwon & Co.*

January 20, 2005

**Notice to Readers**

This report is effective as of January 20, 2005, the auditors' report date. Certain subsequent events or circumstances may have occurred between the auditors' report date and the time the auditors' report is read. Such events or circumstances could significantly affect the accompanying financial statements and may result in modifications to the auditors' report.

# TRUST ACCOUNT OF BALANCE SHEETS

DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>ASSETS</b>		
Securities (Notes 2 and 3)	₩ 1,052,805	₩ 1,120,077
Loans (Notes 2, 4 and 7)	55,856	149,855
Allowance for loan losses (Notes 2 and 5)	(3,560)	(3,339)
Lending to bank accounts (Note 6)	47,201	96,105
Other assets	11,999	29,069
<b>TOTAL ASSETS</b>	<b>₩ 1,164,301</b>	<b>₩ 1,391,767</b>
<b>LIABILITIES</b>		
Money trusts (Notes 2 and 8)	₩ 1,103,425	₩ 1,336,381
Borrowings	-	785
Special reserve (Notes 2 and 9)	7,221	5,619
Other liabilities	53,655	48,982
<b>TOTAL LIABILITIES</b>	<b>₩ 1,164,301</b>	<b>₩ 1,391,767</b>

See notes to accompanying financial statements.

# TRUST ACCOUNT OF STATEMENTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>REVENUES :</b>		
Interest on securities	₩ 65,383	₩ 80,338
Interest on loans and bills discounted	7,750	12,086
Interest on due from bank account (Note 6)	3,272	2,863
Interest on bonds purchased under resale agreements	-	146
Revenues on securities	7,520	6,409
Gain on derivatives transaction	1,623	863
Commissions	331	222
Reversal of special reserve	32	129
Reversal of allowance for loan losses	4,387	4,445
Other revenues	505	2,116
Total revenues	₩ 90,803	₩ 109,617
<b>EXPENSES :</b>		
Expenses on money trust	₩ (62,458)	₩ (73,137)
Interest on borrowings	-	(188)
Commissions	(83)	(149)
Expenses on securities	(5,246)	(12,955)
Losses on derivatives transactions	(2,920)	(1,854)
Contributions to the Credit Guarantee Fund	(113)	(189)
Insurance fees on deposits	(1,001)	(876)
Taxes and dues	(18)	(86)
Provision for special reserve (Note 2)	(1,634)	(1,457)
Provision for loan losses (Note 2)	(2,571)	(1,684)
Other expenses	(390)	(54)
Total expenses	₩ (76,434)	₩ (92,629)
TRUST FEES (Note 2)	₩ 14,369	₩ 16,988

See notes to accompanying financial statements.

# TRUST ACCOUNT OF STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Expenses not involving cash outflows (Note 10)	₩ 9,452	₩ 16,124
Revenues not involving cash inflows (Note 10)	(11,939)	(10,982)
Changes in assets and liabilities resulting from operations (Note 10)	(45,631)	(1,785)
Total	(48,118)	3,357
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Cash outflows for financing activities	(785)	(11,015)
Total	(785)	(11,015)
<b>NET DECREASE IN CASH</b>	(48,903)	(7,658)
<b>CASH AT BEGINNING OF THE YEAR</b>	96,104	103,762
<b>CASH AT END OF THE YEAR (Note 10)</b>	₩ 47,201	₩ 96,104

See notes to accompanying non-consolidated financial statements.

Notes to Trust account of Financial Statements are not enclosed intentionally. Therefore, investors, shareholders and other stakeholders should review notes to financial statements in order to properly understand the Bank's important accounting policies and details on operating performance and financial conditions. Notes to financial statements can be found on 'TRUST ACCOUNT OF FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT' (<http://www.dgb.co.kr>)



# INDEPENDENT AUDITORS' REPORT

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To the Board of Directors and Stockholders of Daegu Bank, Ltd.

We have audited the accompanying consolidated balance sheets of Daegu Bank, Ltd. (the "Bank") and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of income, stockholders' equity and cash flows for the years then ended (all expressed in Korean won). These consolidated financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the Republic of Korea. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Bank and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for the years then ended, in conformity with financial accounting standards generally accepted in the Republic of Korea.

Without qualifying our opinion, we draw attention to the following :

As discussed in Note 23 to the accompanying consolidated financial statements, the Bank transferred loans with recourse to Korea Asset Management Corporation. ₩7.9 billion and ₩39.7 billion of such transferred loans remain unsettled as of December 31, 2004 and 2003, respectively. Additional gains or losses may be recorded upon the final settlement of the loans with Korea Asset Management Corporation in accordance with the recourse provisions.

As discussed in Notes 5 and 23 to the accompanying consolidated financial statements, the Bank has ₩90 billion in debt securities issued by LG Card as of December 31, 2004 and 19% of such debt securities was recognized as impairment loss. Additional gains or losses may be recorded depending on the actual results of corporate restructuring of LG Card.

As described in Note 2 to the accompanying consolidated financial statements, the Bank adopted Statements of Korea Accounting Standards (SKAS) No.1 through No.10, No.12 and No.13. In connection with adoption of these accounting standards, the accompanying consolidated financial statements of the Company for the years ended December 31, 2004 and 2003 were not affected.

Accounting principles and auditing standards and their application in practice vary among countries. The accompanying financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries other than the Republic of Korea. In addition, the procedures and practices utilized in the Republic of Korea to audit such financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report and the accompanying financial statements are for use by those knowledgeable about Korean accounting procedures and auditing standards and their application in practice.

*Ahn Kwon K Co.*

February 19, 2005

**Notice to Readers**

This report is effective as of February 19, 2005, the auditors' report date. Certain subsequent events or circumstances may have occurred between the auditors' report date and the time the auditors' report is read. Such events or circumstances could significantly affect the accompanying financial statements and may result in modifications to the auditors' report.

# CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>ASSETS</b>		
Cash and due from banks (note 3)	₩ 634,326	₩ 660,480
Securities (Notes 2 and 4)	5,794,948	5,582,772
Loans (Notes 5, 6 and 7)	11,416,601	10,215,431
Fixed assets (Note 8)	348,848	350,744
Other assets	923,389	555,196
<b>TOTAL ASSETS</b>	<b>19,118,112</b>	<b>17,364,623</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities:</b>		
Deposits (Note 10)	13,784,129	13,113,748
Borrowings (Note 11)	3,125,495	2,500,867
Debentures (Note 12)	285,000	285,000
Other liabilities	974,416	627,263
<b>Total liabilities</b>	<b>18,169,040</b>	<b>16,526,878</b>
<b>STOCKHOLDERS' EQUITY</b>		
Common stock (par value ₩5,000) (Authorized - 300 million shares) (Issued and outstanding - 132.1 million shares)	660,625	660,625
Consolidated capital surplus	12,328	12,328
Consolidated retained earning	260,349	169,858
Consolidated capital adjustments		
(1) Stock options	-	628
(2) Loss on valuation of available-for-sales securities	15,770	(5,694)
<b>Total stockholders' equity</b>	<b>949,072</b>	<b>837,745</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>₩ 19,118,112</b>	<b>₩ 17,364,623</b>

See notes to accompanying consolidated financial statements.

# CONSOLIDATED STATEMENTS OF INCOME

YEARS ENDED DECEMBER 31, 2004 AND 2003

Korean won (in millions, except for income per share)

	<b>2004</b>	2003
<b>OPERATING REVENUES</b>		
Interest on due from banks	₩ 4,479	₩ 20,850
Interest on traded securities	37,196	44,481
Interest on available-for-sale securities	88,880	88,114
Interest on held-to-maturity securities	195,026	189,316
Interest on loans	714,872	694,617
Interest - other	4,217	6,346
Total interest income	1,044,670	1,043,724
Commission income	127,444	119,819
Gain on disposition of trading securities	9,233	14,577
Dividend on trading securities	87	216
Dividend on available-for sale securities	390	433
Gain on foreign exchange	33,871	30,701
Fee and commissions from trust account	6,841	8,921
Other	34,709	20,817
Total operating revenue	1,260,216	1,239,208
<b>OPERATING EXPENSES</b>		
Interest on deposits	(335,014)	(378,164)
Interest on borrowings	(100,090)	(97,541)
Interest on finance debentures issued	(26,540)	(26,860)
Other	(3,666)	(10,954)
Total interest expense	(465,310)	(513,519)
Commission expenses	(18,622)	(16,991)
Loss on disposition of traded securities	(9,521)	(13,987)
Loss on valuation of traded securities	-	(3,941)
Loss on foreign exchange	(26,762)	(17,093)
Bad debt expenses	(201,695)	(207,429)
Salaries	(121,354)	(107,455)
Depreciation	(23,318)	(24,723)
Amortization of intangible asset	(4,095)	(3,759)
Other selling and administrative expenses	(147,735)	(125,975)
Other	(77,488)	(62,049)
Total operating expenses	(1,095,900)	(1,096,921)

(Continued)

# CONSOLIDATED STATEMENTS OF INCOME (CONTINUED)

YEARS ENDED DECEMBER 31, 2004 AND 2003

Korean won (in millions, except for income per share)

	<b>2004</b>	2003
OPERATING INCOME	164,316	142,287
NON-OPERATING INCOME	46,335	48,822
NON-OPERATING EXPENSE	(37,608)	(75,852)
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST	173,043	115,257
INCOME TAXES (Note 17)	(49,521)	(4,429)
INCOME BEFORE MINORITY INTEREST	123,522	110,828
MINORITY INTEREST	-	-
CONSOLIDATED NET INCOME	₩ 123,522	₩ 110,828
BASIC NET INCOME PER SHARE (Note 18)	₩ 935	₩ 839
DILUTED NET INCOME PER SHARE (Note 18)	₩ 935	₩ 839

See notes to accompanying consolidated financial statements.



# CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

YEARS ENDED DECEMBER 31, 2004 AND 2003

Description	Korea won (in millions)					Total
	Capital Stock	Capital Surplus	Retained Earnings	Capital Adjustment	Minority Interest	
I. JANUARY 1, 2003	₩ 660,625	₩ 12,328	92,440	₩ (20,189)	-	₩ 745,204
Consolidated net income	-	-	110,828	-	-	110,828
Dividends	-	-	(33,031)	-	-	(33,031)
Losses on sale of treasury stock	-	-	(379)	379	-	-
Losses on valuation of available-for sale securities	-	-	-	14,564	-	14,564
Stock options	-	-	-	180	-	180
II. DECEMBER 31, 2003	₩ 660,625	₩ 12,328	₩ 169,858	₩ (5,066)	-	₩ 837,745
I. JANUARY 1, 2004	₩ 660,625	₩ 12,328	₩ 169,858	₩ (5,066)	-	₩ 837,745
Consolidated net income	-	-	123,522	-	-	123,522
Dividends	-	-	(33,031)	-	-	(33,031)
Losses on valuation of available-for sale securities	-	-	-	21,463	-	21,463
Stock options	-	-	-	(627)	-	(627)
II. DECEMBER 31, 2004	₩ 660,625	₩ 12,328	₩ 260,349	15,770	-	₩ 949,072

See notes to accompanying consolidated financial statements.

# CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	Korean won (in millions)	
	2004	2003
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	₩ 123,522	₩ 110,828
Additions of expenses not involving cash outflows (Note 27)	268,393	328,283
Deductions of revenues not involving cash inflows (Note 27)	(257,556)	(325,130)
Changes in assets and liabilities resulting from operations (Note 27)	2,784	203,632
Net cash provided by operating activities	137,143	317,613
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Cash inflows from investing activities :		
Disposal of traded securities	9,331,283	4,514,242
Disposal of available-for sale securities	2,133,266	1,765,917
Disposal of held-to-maturity securities	520,114	1,277,586
Disposal of property and equipment	896	3,693
Decrease in other receivables	36,232	73,581
Decrease in other assets	387	-
Sub-total	12,022,178	7,635,019
Cash outflows for investing activities :		
Acquisition of traded securities	(9,702,760)	(4,628,160)
Acquisition of held-to-maturity securities	(427,355)	(1,781,142)
Acquisition of available-for sale securities	(2,022,653)	(1,768,337)
Acquisition of property and equipment	(22,906)	(28,336)
Acquisition of intangible assets	(3,743)	(6,713)
Increase in other assets	(361,758)	(40,792)
Sub-total	(12,541,175)	(8,253,480)
Net cash used in investing activities	(518,997)	(618,461)

(Continued)

# CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

YEARS ENDED DECEMBER 31, 2004 AND 2003

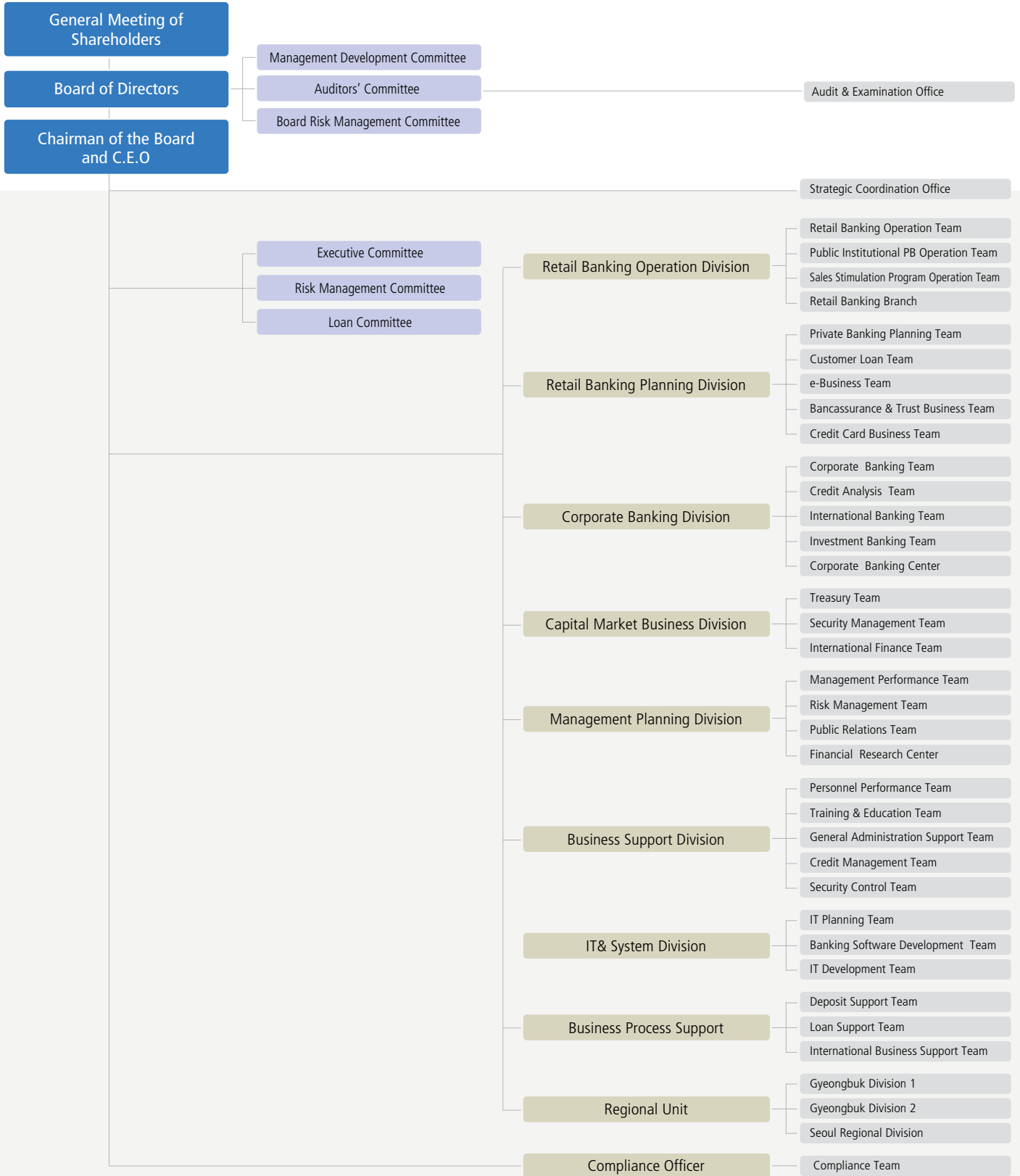
	Korean won (in millions)	
	2004	2003
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Cash inflows from financing activities		
Increase in borrowings in Korean won	118,910	14,478
Increase in borrowings in foreign currency	77,797	112,087
Increase in debentures	-	6,000
Increase in other liabilities	384,544	-
Sub-total	581,251	132,565
Cash outflows for financing activities		
Repayment of borrowings in Korean won	(785)	-
Repayment of debentures	-	(46,000)
Payment of cash dividends	(33,031)	(33,031)
Decrease in other liabilities	-	(72,197)
Sub-total	(33,816)	(151,228)
Net cash provided by (used in) financing activities	547,435	(18,663)
<b>NET INCREASE (DECREASE) IN CASH</b>	165,581	(319,511)
<b>CASH AT THE BEGINNING OF THE YEAR</b>	328,755	648,266
<b>CASH AT THE END OF THE YEAR (Note 27)</b>	₩ 494,336	₩ 328,755

See notes to accompanying non-consolidated financial statements.

Notes to Consolidated Financial Statements are not enclosed intentionally. Therefore, investors, shareholders and other stakeholders should review notes to financial statements in order to properly understand the Bank's important accounting policies and details on operating performance and financial conditions. Notes to financial statements can be found on 'CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT' (<http://www.dgb.co.kr>)

# Organization Chart

As of May 02, 2005



# History

1960s	Oct. 07, 1967	Business begun with paid-in capital of ₩150 million.
	Oct. 20, 1969	Main Branch moved to a newly constructed building.
1970s	May 12, 1972	Bank listed on the Korea Stock Exchange.
	Oct. 01, 1973	"Class-A" foreign exchange business begun.
	Jan. 04, 1975	Bank enlisted to handle budgetary funds for the City of Daegu.
	Nov. 30, 1978	Operation of the Daegu Bank Computer Center begun.
	Oct. 23, 1979	New York Office established.
1980s	Feb. 07, 1983	On-line banking services opened at all business units.
	Apr. 26, 1985	Paid-in capital increased to ₩35 billion.
	May 28, 1985	Construction of new Main Branch Building completed.
	Oct. 22, 1985	Daegu Leasing Co. established as a subsidiary.
	Sep. 19, 1987	Paid-in capital increased to ₩50 billion.
	May 05, 1988	Paid-in capital increased to ₩100 billion.
	Jun. 27, 1989	Paid-in capital increased to ₩150 billion.
	Jul. 21, 1989	Paid-in capital increased to ₩165 billion by transferring 15 billion from capital reserve.
	Oct. 11, 1989	Construction of new Computer Center Building completed.
	Dec. 07, 1989	Tokyo Office established.
1990s	Sept. 09, 1991	Operation of an integrated on-line service begun.
	Dec. 27, 1991	Dae-Eun Scholarship Foundation established.
	May 02, 1994	Daegu Banking Institute established as a subsidiary.
	Jun. 24, 1995	Paid-in capital increased to ₩210 billion.
	Jul. 21, 1995	Hong Kong Office established.
	Aug. 08, 1996	Daegu Bank Finance Co. established as a subsidiary.
	Feb. 27, 1997	Paid-in capital increased to ₩220.5 billion through stock dividends.
	Jul. 19, 1997	Paid-in capital increased to ₩316.5 billion.
	Feb. 21, 1998	Hong Kong Office closed.
	Oct. 24, 1998	Paid-in capital increased to ₩482.1 billion.
	Nov. 30, 1998	Paid-in capital increased to ₩502.1 billion.
	Nov. 30, 1998	Tokyo Office closed.
	Dec. 31, 1998	New York Office closed
	Jun. 17, 1999	US\$50 million in overseas convertible bonds issued
Nov. 05, 1999	Daegu Leasing Co. closed (Subsequently incorporated into Korea Non-Bank Lease Financing Co.)	
Nov. 20, 1999	Paid-in capital increased to ₩602.1 billion	
2000s	Jul. 05, 2000	Daegu Credit Information Co. established as a subsidiary
	Jun. 23, 2001	Operation of Credit Risk Management System begun
	Jul. 07, 2001	Cyber Dokdo branch opened
	May 17, 2002	Conversion of US\$50 million in CBs to equity capital completed
	Jun. 02, 2002	Bank designated "Model of Corporate Governance" by Korea Stock Exchange
	Dec. 01, 2002	Computer backup system put online.
	Jul. 08, 2003	Awarded Prime Minister's Citation for DGB Service Corps' merits in community service
	Sept. 16, 2003	Accredited BS7799 for Internet banking system
	Oct. 18, 2003	Awarded Korea Management Innovation Association's Grand Prize in the leadership category
	Jan. 06, 2004	Awarded the Dasan Finance Awards' Gold Prize in the banking category
	Jun. 21, 2004	DGB is selected in 30 most respected companies in Korea and ranked first in the financial sector by Donga Ilbo and IBM Business Consulting Services (BCS) Korea
	Sept. 08, 2004	DGB proclaims PERSE ethical behavior guidelines
	Nov. 22, 2004	DGB completes development and begins application of BPR system for the first time as a regional bank in Korea

# Corporate Data

## Major Stockholders

(As of December 31, 2004)

Name	Stocks	Ownership
SAMSUNG LIFE INSURANCE AND OTHER RELATED COMPANIES	9,724,694	7.36
SSB - SMALL CAP	8,492,500	6.43
FRANKLIN TEMPLETON INVESTMENT CORP	7,013,416	5.31
MSIL - SR INV(L) Ltd.	4,014,470	3.04
TEMPLETON INVESTMENT TRUST MANAGEMENT CO., LTD	2,986,858	2.26
NATIONAL PENSION CORPORATION	2,091,640	1.58
DONGIL INDUSTRY CO. LTD. AND OTHER RELATED COMPANIES	2,008,683	1.52
NTC - GOV SPORE	1,898,980	1.44
PENSION FONDS PGGM	1,713,680	1.30
INCOME FUND OF AMERICA	1,607,950	1.22
STICHTING SHELL PENSION	1,560,000	1.18
STICHTING PENSION FUNDS	1,509,030	1.14
SAUDI ARABIAN MONETARY	1,425,220	1.08
PVC - VKF INVESTMENTS LTD	1,419,980	1.07
VANGUARD INTER-NATIONAL	1,400,000	1.06
BONYL/BONYE-MERLLNCH IN	1,386,300	1.05
CHASE MANHATTAN BANK(IRE)	1,340,910	1.01

(Note) Preferred stocks owned by KDIC(Korea Deposit Insurance Corporation) are out of consideration.

## Subsidiaries

Daegu Credit Information Co., Ltd.

- 527-4, Bisan-dong, Seo-gu, Daegu 703-040, Korea
- Tel: 82-53-573-7700, Fax: 82-53-608-1400
- President: Kim Chan-soo
- The Bank's ownership: 53.32%

Korea Non-Bank Lease Financing Co., Ltd.

- Yuwon Bldg. 6Fl., Seosomun-dong 75-95, Chung-gu, Seoul, Korea
- Tel: 82-2-398-4118, Fax: 82-2-398-4198
- President: Kim Jong-soo
- The Bank's ownership: 22.29%

## Domestic Network (As of December 31, 2004)

Area	Number of Retail Branches	Number of Corporate Branches
Daegu	133	3
Gyeongbuk	49	3
Seoul	3	1
Busan	1	-
Ulsan	1	-

(Note) Headquarters included as a branch in the Daegu area.

## Number of employees 2,016 (As of December 31, 2004)





— **International Banking Team**

Mailing Address: 118, Suseong-dong, Suseong-gu, Daegu, 706-712, Korea  
E-mail: dg5252@empal.com  
Tel: 82-53-740-2559  
Fax: 82-53-740-6910  
SWIFT: DAEBKR22  
Telex: K28306 DAEGUBK  
Tel: General Manager | 82-53-740-2541  
Correspondent Banking | 82-53-740-2545  
Import | 82-53-740-2543  
Export | 82-53-740-2543  
Money Transfer & Check Collection | 82-53-740-2545

— **International Finance Team**

Mailing Address: 70, Sogong-dong, Jung-gu, Seoul 100-070, Korea  
SWIFT: DAEBKR22SEL  
Telex: K28306 DAEGUBK  
Fax: 82-2-775-7484  
Tel: Correspondent banking 82-2-754-2269  
Offshore Investment 82-2-318-0689  
FX Trading 82-2-752-2897

— **International Business Support Team at Headquarters, Daegu**

Mailing Address: 118, Suseong-dong 2-ga, Suseong-gu, Daegu 706-712, Korea  
SWIFT: DAEBKR22  
Fax: 82-53-756-2095  
Telex: K54334 DAEGUBK  
Tel: Import: 82-53-740-2978  
Export: 82-53-740-2986  
Money Transfer & Check Collection: 82-53-740-2946  
Foreign Trade Finance & Local L/C: 82-53-740-2960

— **International Business Support Team at Seoul**

Mailing Address: 70, Sogong-dong, Jung-gu, Seoul 100-070, Korea  
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Telex: K28306 DAEGUBK  
Fax: 82-2-757-8695  
Tel: Import / Export 82-2-757-8696



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