Financial Review

Financial Review

Bank Danamon, as a universal bank, derives its earnings firstly, from providing a comprehensive range of financial services and products to all major segments in the market using a unique business model for each segment, and secondly from trading and investing activities in financial markets as part of its day-to-day activities in managing the entire business portfolio.

The bank places emphasis on the development of high yield loan assets and the use of a combination of third party deposits and structured funding for effective management of the maturity profile of its balance sheet in accord with enterprise risk management parameters.

The operating environment for the most part of 2006 was challenging, marked by weak consumer purchasing power, slower economic growth, high inflation and high interest rates. Weak purchasing power was clearly evident from the sharp drop in new car and motorcycle sales of 40% and 13%, respectively, during the year.

The challenging macro economic condition impacted the real sector as well as the financial sector, with a decline in consumer confidence affecting the demand for credit and a general increase in non-performing loans in the banking sector as a whole. As SBI rates increased and competition escalated for third party deposits the cost of funds also increased.

Notwithstanding the challenging operating environment, Bank Danamon completed 2006 with a solid performance in terms of revenue and earnings.

To provide a clearer picture of the Bank's performance on a normalised (like-for-like) basis, we have included in this analysis references to normalised NPAT, and selected ratios to reflect the bank's fundamental core business performance, net of one-off non recurring items.

Consolidated Key Financial Data
In Rp billion, except ratios in %

	2005	2006	△YoY
Operating Results			
Normalised Net Interest Income	4,603	5,645	22.6%
Normalised Fee Income	1,080	1,358	25.7%
Normalised Operating Income	5,683	7,003	23.2%
Normalised Operating Expenses	(2,909)	(3,428)	17.8%
Normalised Pre-Provisions Operating Profit	2,774	3,575	28.9%
Cost of Credit	(814)	(1,332)	63.6%
Net Profit Before Tax	1,960	2,243	14.4%
Goodwill & Minority Interest	(206)	(202)	(1.9%)
Income Tax	(559)	(652)	16.6%
Normalised NPAT	1,195	1,389	16.2%
Non Recurring Items (After Tax)	808	(63)	(107.8%)
Reported NPAT	2,003	1,325	(33.8%)
Balance Sheets			
Total Assets	67,803	82,073	21.0%
Total Loans	36,757	42,986	16.9%
Total Government Bonds	14,102	18,702	32.6%
Total Deposits	47,089	57,834	22.8%
Total Equity	8,589	9,442	9.9%
Profitability Ratios			
Net Interest Margin	8.9	9.3	0.4
Normalised Cost to Income	51.1	48.9	(2.2)
Normalised ROAA	1.8	1.9	0.1
Normalised ROAE	15.2	16.5	1.3
Reported ROAA	3.1	1.8	(1.3)
Reported ROAE	24.2	15.1	(9.1)
Asset Quality Ratios			
Non Performing Loans / Total Loans	2.6	3.3	0.7
Loan Loss Allowance / Total Loans	2.8	3.3	0.5
Loan Loss Allowance / Non Performing Loans	145.7	141.7	(4.0)
Liabilities Ratios			
Loan to Deposit Ratio	80.8	75.5	(5.3)
Deposits to Total Liabilities	79.8	79.9	0.1
Loans to Total Funding	66.6	63.3	(3.3)
Capital Ratios			
Capital Adequacy Ratio	22.7	20.4	(2.3)
Tier 1 Capital	16.7	15.5	(1.2)
Equity/Assets	12.7	11.5	(1.2)

Net Income

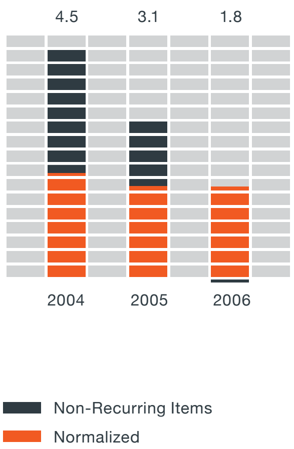
Bank Danamon reported a net profit after tax of Rp 1,325 billion in 2006, a variance of 34% compared to the previous year's profit of Rp 2,003 billion due to the absence of non-recurring items. Extraordinary items were made up from the extraordinary gain on sale of government bonds, coupled with loan recoveries, provision release and write backs. Excluding non-recurring items, normalized net profit after tax rose 16% to Rp 1,389 billion in 2006.

Basic Earnings per Share (EPS) was Rp 268.9 as compared to Rp 407.7 in 2005, while ROAA and ROAE stood at 1.8% and 15.1%, respectively.

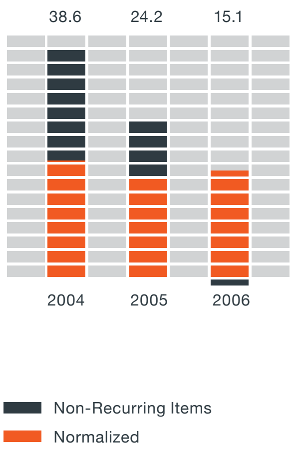
Reported Net Income and Normalized Net Income

Rp billion	2005	2006	△YoY
Normalized Net Income	1,195	1,389	16%
Non Recurring Items	808	(63)	(108%)
Reported Net Income	2,003	1,325	(34%)

Return on Average Assets
In %



Return on Average Equity
In %



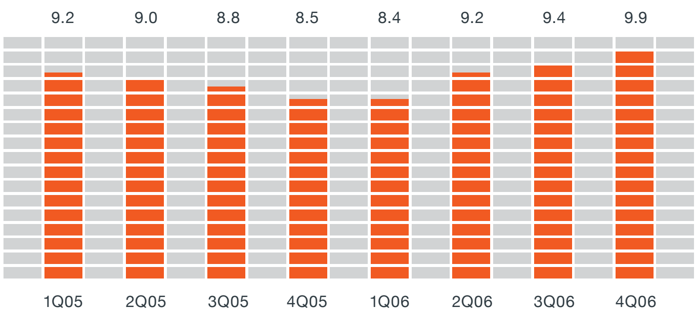
Net Interest Income

Net interest income increased by 23% to Rp 5,645 billion in 2006 supported by an expansion of earning assets and progressive improvement in net interest margin through the year. Interest income rose by 34% to Rp 10,896 billion in 2006 from Rp 8,129 billion in 2005 on the back of 22% earning assets growth and improved earning asset yield.

Loans grew by 17% and contributed over 60% of total interest income in 2006, while government bonds contributed 18% of interest income. The bank's strategy to continue to grow its high yielding businesses improved asset yield from 14.3% in 2005 to 16.6% in 2006.

Interest expense rose by 49% to Rp 5,251 billion in 2006 from Rp 3,526 billion in 2005 in line with higher interest rates during the most part of 2006 as well as a growing funding base. Despite the higher cost of funds, net interest margin widened to 9.3% from 8.9% in the previous year.

Net Interest Margin
In %



Fee Income (Non-Interest Income)

Normalized fee income rose by 26% to Rp 1,358 billion owing to the increase in credit related fees and the consolidation of Adira Insurance and Adira Quantum starting in the second quarter of 2006. Credit card business and lending contributed to over 44% of the increase in fee income in 2006 partly due to the acquisition of the American Express Card franchise. Overall, fee income contributed about 19% of operating income both in 2005 and the year in review.

Operating Expenses

Normalized operating expenses increased by 18% to Rp 3,428 billion compared to Rp 2,909 billion in the previous year. The increase was partly driven by business expansion in the mass-market sector as well as the consolidation of Adira Insurance, Adira Quantum and the American Express Card.

Salaries and employee benefits, which accounted for 55% of total normalized operating expenses, rose by 12% to Rp 1,888 billion due to salary adjustments in response to the high inflation environment during the year and an additional 2,408 head count for business expansion. General and administrative expenses increased by 19% to Rp 1,468 billion as 75 DSP SEMM units were added during the year.

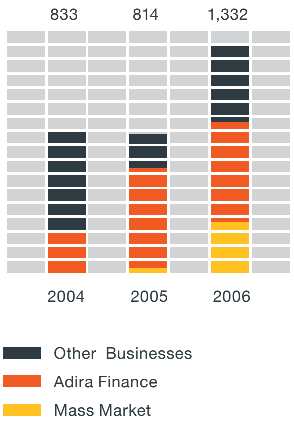
Despite the business expansion, the normalized cost to income ratio improved to 48.9% compared to 51.1% in 2005.

Cost of Credit

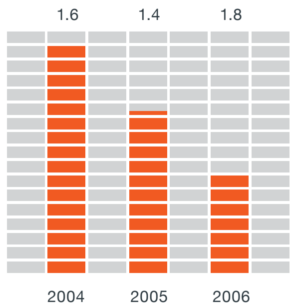
Cost of credit, which includes provision expenses, net write-off and loss on sale of repossessed assets in the consumer auto financing business, amounted to Rp 1,332 billion in 2006 compared to Rp 814 billion in the previous year. This increase was due to a growing and maturing mass market loan portfolio as well as higher non performing loans on the back of the unfavorable operating environment.

The fuel price hike, slower economic growth, high inflation and high interest rates continuing from 2005 into the first half of 2006 adversely impacted the credit quality of loans as reflected by higher non-performing loans in several businesses. However, as the operating environment improved towards the end of year the cost of credit decreased by 23% in the last quarter of 2006 to Rp 263 billion from Rp 343 billion in the previous quarter.

Normalised Cost of Credit
In Rp billion



Cost of Credit/Earning Assets
In %



Financial Position

Total assets at year end increased by 21% to Rp 82,073 billion supported by 17% loan growth and 33% increase in the government bonds portfolio.

Funding rose by 23% to Rp 67,918 billion supported by strong deposit growth. Shareholders' equity increased by 10% to Rp 9,442 billion at the end of year due to increased retained earnings.

	2005		2006		
	Rp billion	**% Total**	**Rp billion**	**% Total**	**△YoY**
Cash	640	0.9%	833	1.0%	30%
Marketable securities	2,490	3.7%	6,031	7.3%	142%
Government bonds	14,102	20.8%	18,702	22.8%	33%
Loans (gross)	36,757	54.2%	42,986	52.4%	17%
Fixed Assets	1,480	2.2%	1,575	1.9%	6%
Others	12,334	18.2%	11,946	14.6%	(3%)
Total Assets	**67,803**	**100.0%**	**82,073**	**100.0%**	**21%**

Outstanding Loans

Bank Danamon achieved loan growth of 17% in 2006 despite the challenging operating environment. Over 56% of the growth was derived from high yielding mass market and consumer auto financing businesses. This compares favorably year-on-year growth of 14% for the banking sector as a whole.

Mass market loans grew by 71% to Rp 6,228 billion and accounted for 14% of the bank's loan book, up from 10% a year ago.

Consumer loans grew by 7% to Rp 16,763 billion supported by the growth in motorcycle loans. Credit card receivables increased by 40% in 2006 following the acquisition of the American Express Card business. As such, consumer loans accounted for 39% of the total loan book. Within the consumer loan portfolio, motorcycle loans made up 54%, car loans 24%, housing loans 7%, credit cards 7% and other consumer loans 8%.

SME loans grew by 11% to Rp 8,354 billion and accounted for 19% of the loan portfolio. Commercial loans expanded by 18% to Rp 5,536 billion, representing 13% of total loan book in 2006. Corporate loans rose by 18% to Rp 6,104 billion, representing the remaining 15% of the total loan book.

Breakdown of loans by segments

	2005		2006		
	Rp billion	**% Total**	**Rp billion**	**% Total**	**△ YoY**
Corporate	5,181	14%	6,104	15%	18%
Commercial	4,690	13%	5,536	13%	18%
Small & medium enterprises	7,550	21%	8,354	19%	11%
Consumer	15,686	42%	16,763	39%	7%
Mass Market	3,650	10%	6,228	14%	71%
Total (gross)	**36,757**	**100%**	**42,986**	**100%**	**17%**

The ratio of non-performing loans (NPL) to total loans increased to 3.3% in 2006 from 2.6% a year earlier. NPL in the mass market segment increased to 2.8% at year end from 1.9% a year earlier partly reflecting a maturing loan portfolio. Net NPL remained zero with provision coverage reaching 142% (after taking into account the collateral value) as of December 31, 2006.

Government Bonds

The portfolio of government bonds increased by 33% to Rp 18,702 billon. As such, government bonds now account for 23% of the bank's assets compared to 21% in 2005.

The bank increased the level of fixed rate government bonds in the portfolio towards the end of 2006 to Rp 10,898 billion or 58% of the total bonds. Average duration held was 3.4 years at the end of 2006 as compared to 1.8 years in 2005.

Breakdown of government bonds portfolio

	2005		2006		
	Rp billion	**% Total**	**Rp billion**	**% Total**	**△ YoY**
Held to Maturity	7,880	56%	6,687	36%	(15%)
Available for Sale	6,060	43%	11,058	59%	82%
Trading	162	1%	957	5%	491%
Total	**14,102**	**100%**	**18,702**	**100%**	**33%**
Fixed Rate	5,475	39%	10,898	58%	99%
Variable Rate	8,627	61%	7,804	42%	(10%)
Total	**14,102**	**100%**	**18,702**	**100%**	**33%**

Total Funding and Customer Deposits

A strong growth in deposits caused funding to increase by 23%. Current and savings accounts rose by 18% and 14% respectively. Meanwhile time deposits surged by 26%. Altogether they made up 85% of total funding.

The remaining 15% of funding comprised long-term (structured) funding, including senior bonds, subordinated debts, securities sold under repurchase agreements and other borrowings. Bank Danamon and its subsidiaries continue to raise long-term funding to reduce the asset liability maturity mismatch.

The Loan to Funding Ratio decreased to 63% from 67% a year earlier and the Loan to Deposit Ratio also declined from 81% at the end of 2005 to 76% in 2006.

Breakdown of Total Funding

	2005		2006		
	Rp billion	**% Total**	**Rp billion**	**% Total**	**△ YoY**
Total Deposits	47,089	85%	57,834	85%	23%
Current Account	4,538	8%	5,337	8%	18%
Savings	8,552	16%	9,713	14%	14%
Time Deposits	33,999	62%	42,784	63%	26%
Long-Term Funding	8,116	15%	10,084	15%	24%
Total Funding	**55,205**	**100%**	**67,918**	**100%**	**23%**

Capital

The bank's capital adequacy ratio (CAR) with market risk charge remains strong at 20.4% as of December 31, 2006 as compared to 22.7% a year earlier. Tier-1 and Tier-2 capital ratio stood at 15.5% and 6.9% as of December 31, 2006, compared to 16.7% and 8.4% on December 31, 2005.

Capitalization, as measured by the equity to asset ratio, stood at 11.5% at the end of 2006 as compared to 12.7% a year earlier due to asset expansion.

Rp billion	2005	2006	△YoY
Tier 1 Capital	7,933	8,371	5%
Tier 2 Capital	3,976	3,702	(7%)
Investment	(1,144)	(1,096)	(4%)
Total Capital after Investment	**10,765**	**10,977**	**2%**
Risk Weighted Assets (inc. market risk)	47,466	53,825	13%

Capital Adequacy Ratio	**22.7%**	**20.4%**	**(2.3%)**
Tier 1 Ratio	16.7%	15.5%	(1.2%)
Tier 2 Ratio	8.4%	6.9%	(1.5%)

Responsibility for Financial Reporting

This Annual Report and the accompanying financial statements and related financial information are the responsibility of the Management of Bank Danamon and have been approved by members of the Board of Directors and the Board of Commissioners whose signatures appear below:

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